



JOINT-STOCK FINANCIAL CORPORATION

SISTEMA

2014
ANNUAL REPORT

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SISTEMA TODAY

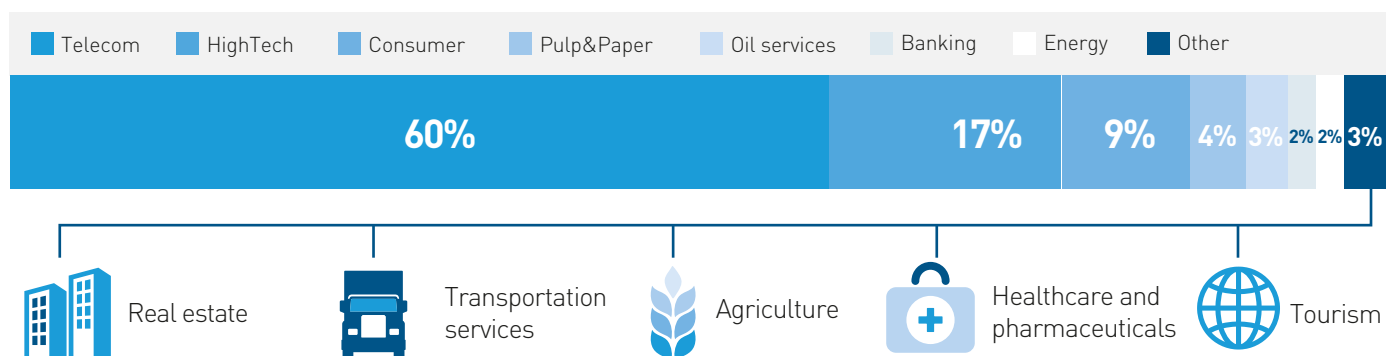
Established in 1993, today Sistema is a large private investor operating in the real sector of the Russian economy. Sistema's investment portfolio comprises stakes in predominantly Russian companies from various sectors of economy,

including telecommunications, utilities, retail, high tech, pulp and paper, pharmaceuticals, healthcare, railway transportation, agriculture, finance, mass media, tourism, etc. Sistema is the controlling shareholder in most of its portfolio

companies. Sistema's competencies focus on improvement of the operational efficiency of acquired assets through restructuring and attracting industry partners to enhance expertise and reduce financial risks.



Sectors of operations



Note: Based on aggregate income from assets

Contribution to national development



RUB 100 billion

Payments to the federal and regional budgets in 2014



Over RUB 700 million

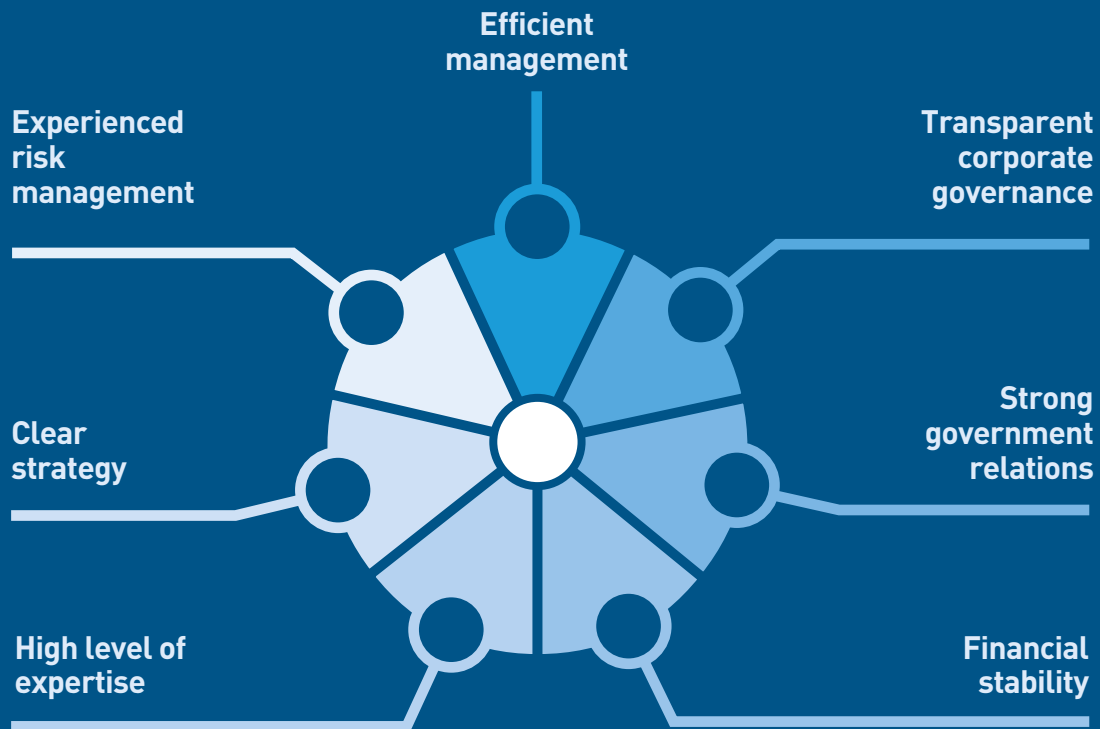
Social and charity investment in 2014



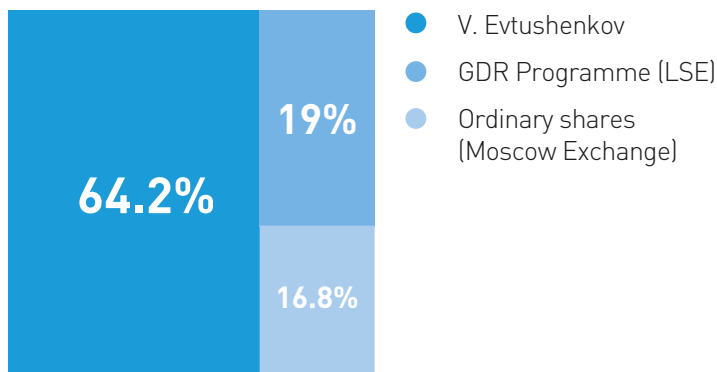
RUB 62.8 billion

Investment in existing and new assets in 2014

Shareholder value



Shareholder capital structure



Note: including the shares held by insiders, management and members of the Board of Director and ordinary shares on Sistema Group's balance sheet.

The company's shares are traded on the London Stock Exchange (LSE) as Global Depository Receipts (GDRs), with one GDR representing 20 ordinary shares. Its Global Depository Receipts are listed on the LSE under ticker symbol SSA. The company's shares are also listed on the Moscow Exchange under ticker symbol AFKS.

Financial stability

Revenue for 2014

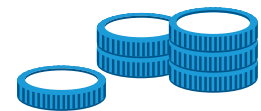
631.9 RUB billion

Adjusted OIBDA for 2014

165.2 RUB billion

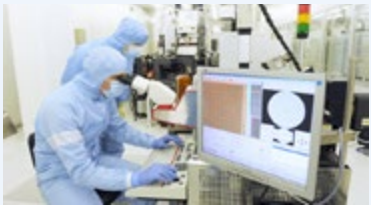
Dividends received in 2014

55.6 RUB billion



HISTORY TIMELINE

1993-1995




1993 Sistema JSFC is founded.

Sistema actively consolidates assets in the core sectors of Russia's economy, acquiring assets in telecommunications, electronics, tourism, retail, oil and gas, construction and real estate.

Sistema invests in MGTS, establishes Vimpel Communications and Sistema-Hals, as well as project management companies.

1996-2002




Sistema acquires a 40.4% stake in MTS and starts its development in partnership with Deutsche Telekom.

During VimpelCo's IPO on the New York Stock Exchange, raising US\$ 110.8 million Sistema, sells its stake in VimpelCom.

MTS completes an IPO on the New York Stock Exchange, generating US\$ 323 million.

Sistema creates an insurance holding on the basis of ROSNO and attracts a strategic partner – Allianz AG, one of the largest insurance groups in the world. As a result of this transaction, Sistema received a 49% stake in ROSNO and Allianz AG received 47.2%.

2003-2004



Sistema acquires control of Comstar (50%) and Kosmos TV (50%) in a transaction totalling approximately US\$ 35 million.

As a result of consolidation, Comstar-OTS received a 99% controlling stake in MTU-Inform, 100% stake in Telmos, 100% stake in MTU-Intelm and 55.62% stake in MGTS. This event became a milestone in the consolidation of alternative communication operators under our control to create a united digital operator.

2005



Sistema launches its IPO on the London Stock Exchange, raising US\$ 1.56 billion.

Sistema buys minority stakes in Bashkir oil and energy companies (together, the «BashTEK companies»), including Bashneft and Bashenergo, for a total amount of about US\$ 600 million.

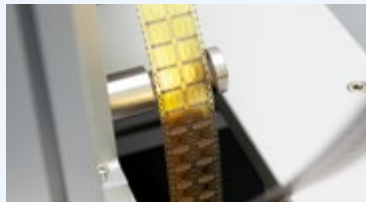
Sistema actively develops banking business and increases its stake in the Moscow Bank for Reconstruction and Development (MBRD) to 98.9%. Later, MBRD consolidated 66% of the shares in East-West United Bank.

2006



IPO of Comstar-OTS. Sistema launches an IPO for Comstar-OTS, raising US\$ 1 billion on the London Stock Exchange.

Sistema-Hals launches its IPO, raising US\$ 409 billion on the London Stock Exchange.



SITRONICS is established as a result of development and consolidation of high-tech assets by Sistema.

2007-2008



Sistema acquires a 100% stake in American Hospital Group and a 100% stake in the Medexpress chain of clinics, later merged into Medsi Group.

Sistema successfully exits from insurance business by selling 47.4% of ROSNO to Allianz, with an option for Allianz to buy the remaining 3% over the next several years.

Sistema increases its stake in SITRONICS to 60% and launches an IPO on the London Stock Exchange, raising US\$ 2.35 billion.

Sistema first acquires a 10% and then a 41% stake in Shyam Telelink Ltd and enters into a call option agreement allowing it to increase its stake from 51% to 74%. The transaction was worth US\$ 46.74 million.

2009-2010



Sistema consolidates its telecom assets and sells its 50.91% stake in Comstar-OTS to MTS in a transaction worth about US\$ 1.32 billion.

Sistema acquires controlling stakes in BashTEK companies for US\$ 2 billion, increasing its shareholding in Bashneft to 76.5%.

Sistema exits from real estate construction business. VTB Bank acquires a controlling stake in Sistema-Hals. Later, Sistema completed the sale of the remaining shares in Sistema-Hals.

Sistema buys a 49% stake in NK RussNeft in a transaction worth less than \$100 million.

2011



Sistema establishes RTI, a company consolidating Sistema's high-tech business, including Concern RTI Systems and SITRONICS.

Sistema transitions from the operating holding model to the investment company model.

Rosimushchestvo acquires 14% of SSTL for US\$ 647 million as a result of an additional issue of shares.

VAO Intourist and Thomas Cook Group Plc complete a transaction to form a joint venture based on the tour operator and retail business of Intourist. Thomas Cook purchased a 50.1% stake for a total of US\$ 45 million. Later, Thomas Cook increased its stake in the JV to 75%.

Sistema sells 24.4% of MGTS to MTS for RUB 10.56 billion, completing consolidation of its telecom assets.

Sistema makes its first investments in the agricultural sector by acquiring a 100% stake in Don-skoe for RUB 476.5 million and a 100% stake in First Cavalry Army Stud Farm for RUB 303 million. Both land clusters are located in the Rostov Region with a combined land of 39,000 hectares.

2012



Sistema acquires a 100% stake in SG-trans, the largest independent LPG transport operator in Russia, for RUB 22.77 billion.

Medsi Group commences merger of assets with the Medical Centre for the Mayor and Government of Moscow. In exchange for a 25% stake, Medsi received 3 hospitals, 3 health resorts and 3 outpatient clinics. Thus, Medsi Group became a full-service medical company.

RTI buys a 50% stake in NVision Group and increases its stake in SITRONICS to 100%. SITRONICS was delisted from the London Stock Exchange on August 23, 2012

Sistema sells power generation assets of Bashkirenergo to Inter RAO UES for RUB 11.2 billion.

Sistema and Louis-Dreyfus family members form a farming joint venture in Russia. The JV combines both parties' agricultural assets, totalling approximately 90,000 hectares.

2013



Sistema sells its 49% stake in NK RussNeft for US\$ 1.2 billion.

Sistema acquires 51% of Business-Nedvizhimost, which owns 76 properties with a total area of 178,000 sq m, from MGTS-Nedvizhimost for RUB 3.2 billion. Later, Sistema purchased the remaining 49% for RUB 3.1 billion.



Sistema invests in oil service assets by acquiring 100% of Bashneft-Service Assets (later renamed Targin) from Bashneft for RUB 4.1 billion.

The Board of Directors of Sistema approves a new incentive programme, based on share price performance and cash flow at the Corporate Centre level.

2014



In April 2014, Sistema acquired a 10.8% stake in OZON for US\$ 75 million. MTS also acquired a 10.8% stake at the same price.

In July 2014, Sistema pays RUB 19.9 billion in dividends. This translates to a dividend yield of around 5% as of the payout date.



Sistema begins investment in forestry and pulp and paper industries.

In September 2014, LLC LesInvest, part of the Group, acquired 100% shares of OJSC Segezha Pulp and Paper Mill from the Bank of Moscow and 100% of shares of LLC Derevoobrabotka-Proekt (Group of companies). The net external debt of the acquired assets is equal to zero (see p. 44). The Group of companies is the largest producer of sack paper and paper sacks in Russia and the second largest manufacturer of paper sacks in Europe.

In 2014, Sistema increased its stake in NVision Group to 100%.




Sistema expands its footprint in the retail sector. In October 2014, Sistema buys a 40% stake in the holding company which owns the assets of Concept Group, one of the leaders in the Russian retail clothing market in terms of revenue growth, in a transaction worth about RUB 1 billion. The documents signed provide for an option for Sistema to increase its shareholding in Concept Group to the controlling level within three years.

MTS-Bank issues additional shares for RUB 13.1 billion. Sistema purchased 2,474,818 ordinary shares for RUB 9.46 billion. MTS purchased 952,000 ordinary shares for RUB 3.64 billion.

In December 2014 by the court Sistema transferred all its shares in Bashneft to the Government. In February 2015 the Moscow Arbitration Court upheld the claim of the Corporation to the LLC Ural-Invest and decided to recover losses from the defendant in favor of Sistema. In March 2015 Sistema and LLC Ural-Invest signed a settlement agreement under which the fund transfers RUB 46.5 billion to the Corporation, of which RUB 4.6 billion invested in the fund charitable projects. Later on Sistema has received additional compensation of RUB 12.9 billion.

COMPANY STRUCTURE



53%

Over
104 mln
subscribers



87%

195 RUB
billion
worth of assets



50%

Over
100,000
hectares of land



99%

Over
109 mln
store visits per year



91%

80,000 km
of power
grids



100%

49
drilling rigs,
180 crews




75%

Over
6 mln
visits per year



50%

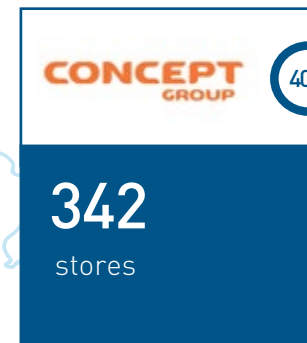
Over
34,000
of railcars under
management



74%

6 mln doses
of Hepatitis B
vaccine per year

World-wide reach of activities and diversified asset structure enable Sistema JSFC to achieve sustainable operating and financial performance.



PRESIDENT'S SPEECH



2014 was a challenging year both in corporate and macroeconomic terms. In this period, Sistema faced numerous operational and strategic pressures and I am pleased to see the Group has successfully navigated these obstacles, demonstrating the resilience of our business model and acquiring invaluable experience, which will assist us in our future development.

In addition to external macroeconomic factors, Sistema was, undoubtedly, affected by the situation surrounding Bashneft last year. Following litigation, Sistema transferred the asset to the state, subsequently obtaining cash compensation as a good-faith buyer. The events had a significant impact on our portfolio, but it did not change the essence of our business and our competencies. We are still a unique Russian company that employs efficient management, the right strategic decisions and a professional team to turn distressed and complicated assets into leaders in their respective industries.

In 2014, we have achieved solid results, with consolidated revenues growing by 7.2%. Ten out of our thirteen biggest assets increased their revenues; eleven out of thirteen achieved positive OIBDA; nine showed positive net income and paid dividends. Developing assets' share of Sistema's total revenue grew to 41% in 2014 from

32% in the previous year.

One of the key assets in our portfolio is Detsky Mir, Russia's best-known children's goods brand, demonstrated the third largest revenue and highest growth rate of all the Group's assets. Detsky Mir's value increases each year, and the company continues to retain its leading industry position, with over 330 stores across Russia.

Our company RTI develops high-tech assets in the microelectronics and defence industries, as well as smart IT systems. The initiatives we have implemented to optimise the business and increase its financial stability in 2014 have led to a considerable improvement in the Group's returns.

Last year Sistema continued to actively develop its healthcare business Medsi, which generated a 4% year-on-year revenue growth, in rouble terms, despite the closure for redevelopment of some medical facilities during the year. Medsi's strategy is currently focused on increasing its market share in the medium term, both by constructing new treatment facilities and increasing patient loyalty.

Our Indian business, SSTL, has largely delivered on its financial targets and we expect that it will near OIBDA breakeven in 2015 as we continue to reduce its reliance on Sistema. Whilst numerous regulatory challenges continue to persist, the latest licensing rounds have shown both demand and price increase in the 800 mhz spectrum that SSTL operates in. This is encouraging and may create strategic opportunities as the sector outlook improves and evolves.

In 2014, we continued our search for attractive investment opportunities in Russia, investing in the pulp and

industry. With vast felling area, low production costs, and proximity of export markets, LesInvest Group, Russia's biggest producer of sack paper and paper sacks and Europe's second largest paper sack maker, has significant growth potential. We intend to further enhance its value, create new jobs and modernize production facilities. Last year, Sistema also entered the e-commerce and fashion retail market by acquiring interests in OZON Holdings Limited and Concept Group.

With more than 20 years of experience operating in Russia, we have proved that Sistema has the capacity and expertise to create value for all the stakeholders not only during periods of growth, but also in times of volatility and uncertainty. Meeting our social responsibilities is a core element of our business strategy, and we are committed to developing our people, investing in talent and diligence, as well as fostering regional innovation and social development.

As we look into 2015, Sistema remains in a strong financial position. We have a stable and growing dividend flow from current investments, a much reduced corporate costs and a process of vigorous assessment of each opportunity on its financial merits. With these fundamentals in place, we believe Sistema is well placed to capitalise on new investment opportunities and we look forward to delivering value to the Group's shareholders in the coming year.



Mikhail Shamolin
President of Sistema

STRATEGIC REVIEW

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STRATEGY

Mission

Long-term growth of shareholder value through efficient management of the asset portfolio and achievement of high returns on investment.

High returns on investment

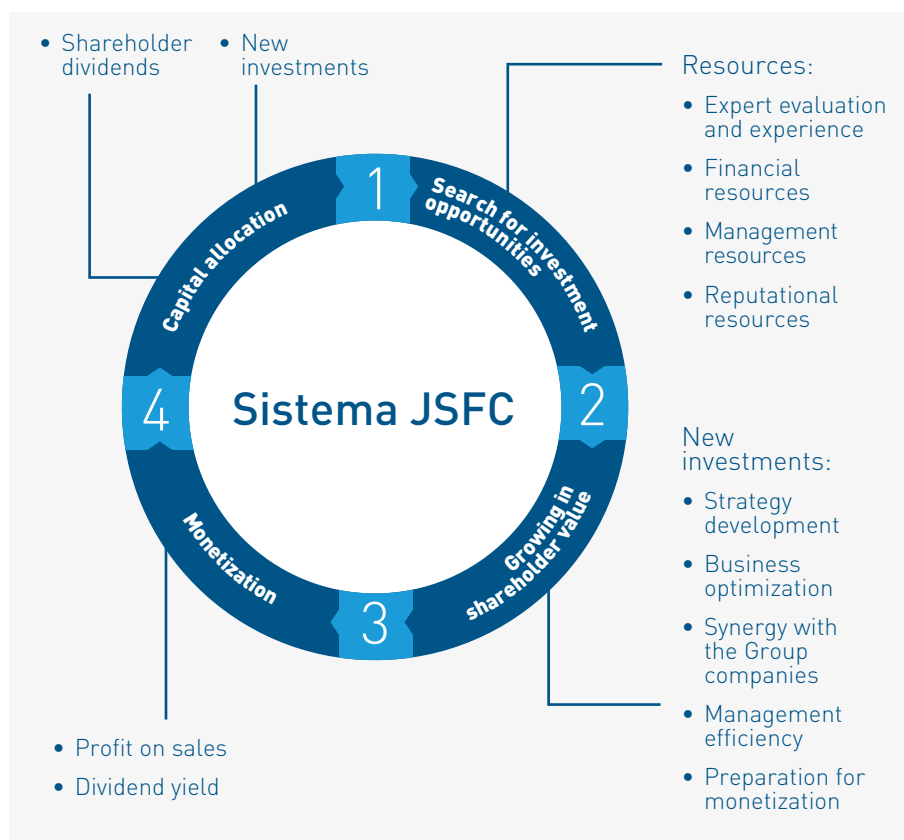
Unique expertise on the Russian market and a strong management team

Lower investment risk

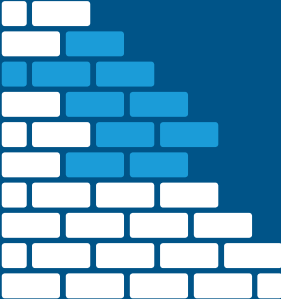



Diversified and balanced portfolio in the fundamental segments of the Russian economy and balanced contribution of assets to the total value

Value creation model

The model of Sistema as an investment company envisages creation of shareholder value through constant reinvestment of capital - accumulation of cash from incoming dividends and monetisation of assets, distribution of the received profit in form of dividends among Sistema's shareholders, reinvestment in existing assets and new investment projects in order to receive further income.



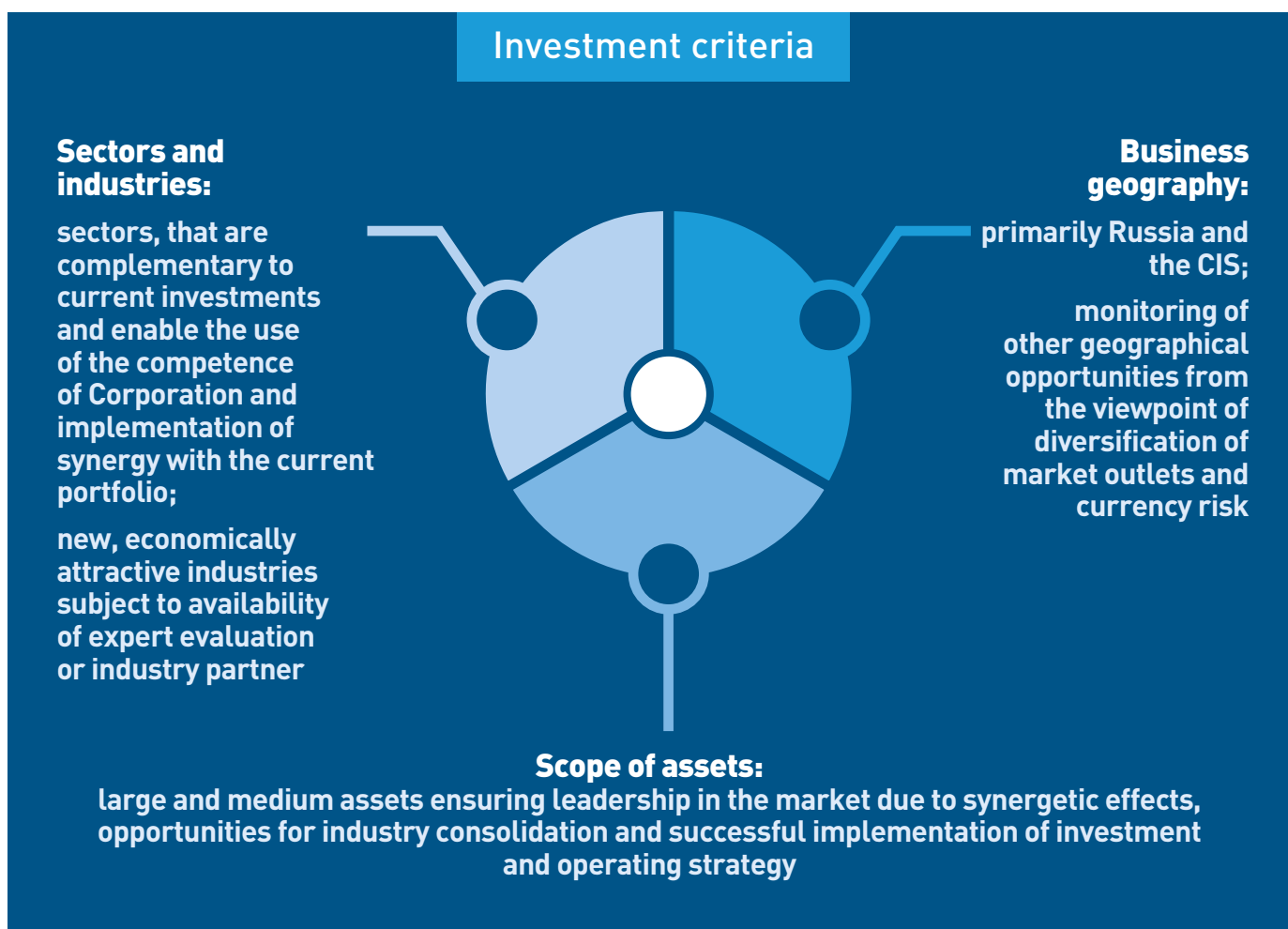
Components of successful growth

<p>Our business</p> 	<p>Our principles of operation</p> 	<p>Our strategy</p> 	<p>Our efficiency</p> 
<p>Creation of value by leveraging competencies:</p>	<p>Lean and competitive structure:</p>	<p>Science applications to create art:</p>	<p>No cash – no reward:</p>
<ul style="list-style-type: none"> • Assessment and development of business strategies for our assets without involvement in operations • Monitoring of M&A opportunities in current and new sectors • Development and implementation of asset monetisation plans • Hiring efficient management for companies under our control • Providing comprehensive support to our assets in attracting financial and other resources • Increasing operational efficiency of acquired assets through restructuring and attracting industry partners to increase expertise and share financial risks 	<ul style="list-style-type: none"> • Managing assets according to the principle of deal origination and industry expertise of portfolio managers • A team of strategic experts, macroeconomists and communication professionals 	<ul style="list-style-type: none"> • Internal rate of return on investments above weighted-average cost of capital ($IRR > WACC$) with a 5-7-year payback period • Focus on investment with a positive net cash flow • Acquiring assets with an acceptable debt level ($Debt/OIBDA < 3.0x$) for preserving the Group's stable financial situation • Keeping consolidated Debt/EBITDA at 2x • Payout to shareholders of up to 30% of profit 	<ul style="list-style-type: none"> • Remuneration of investment managers fully depends on cash generated by their portfolio for Sistema • Cash may be received from dividends or monetisation • Current dividends from MTS are not included in calculation of remuneration • Remuneration is paid after deducting the portfolio's expenses and the Central Bank's rate



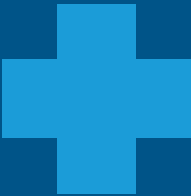
Investment strategy




Medium-term goals of Sistema as an investment company


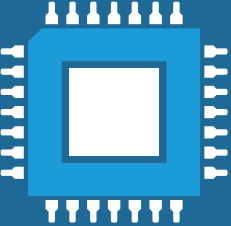
- Generating a substantial cash flow at Hold Co through portfolio monetisation and dividends from subsidiaries, as well as by finding and benefiting from unique investment opportunities in Russia
- Balancing investment portfolio with export-oriented industrial companies in Russia that may become a source of foreign currency liquidity
- Restructuring and supporting portfolio companies operating in segments that are most sensitive to changes in the economic situation
- Building industry leaders in private healthcare, high technology and microelectronics, pulp and paper industry, in order to maximise returns on shareholder capital









Sistema JSFC Investment Vision

Industry	Key industry characteristics	Strategy	Sistema JSFC investment vision
<p>Telecommunications in Russia</p> 	<ul style="list-style-type: none"> • Slowing down growth of the mobile communications market • Growing penetration of data transfer services • Growth in the OTT services segment 	<p>Develop to obtain stable dividend flow</p>	<p>Sistema JSFC views MTS as a strategic asset that is generating high dividend income.</p> <p>In order to achieve the targets on dividend flow, MTS will continue to develop actively the data transfer services, focus its marketing efforts on holding its leading positions in Russia and explore potential for synergies with other businesses of Sistema JSFC Group, including, MTS Bank and Ozon Holding, to get competitive advantages on the market.</p> <p>More about the operating strategy see p. 28</p>
<p>Children's goods retail</p> 	<ul style="list-style-type: none"> • The sector is resistant to deterioration of macroeconomic situation • Low market concentration with opportunities for consolidation • Demographic situation will continue promotion of growth of consumer expenditures on children's goods 	<p>Grow business volume to obtain dividend income; and possible partial sale given the favourable conditions</p>	<p>Sistema JSFC views Detsky Mir as a promising asset that has already achieved significant results and is able to bring in substantial returns on capital in the form of dividends or by means of partial monetization.</p> <p>Since the children's goods retail sector is resistant to economic recessions, Sistema JSFC is planning active development of the Detsky Mir chain and opening about 40 new stores in 2015.</p> <p>More about the operating strategy see p. 34</p>
<p>Private healthcare</p> 	<ul style="list-style-type: none"> • High growth rate of the Russian private healthcare services market • Government support to the sector • Low market concentration with opportunities for consolidation 	<p>Grow business volume and introduce the best practices in healthcare</p>	<p>Sistema JSFC sees a high potential of the Russian private healthcare market development and is building up the federal network providing high-quality healthcare and rehabilitation services for the country citizens.</p> <p>During the next two years, Medsi will focus its efforts on expanding business scale by constructing new medical centers, introducing new healthcare technologies and further improving of the quality of services.</p> <p>More about the operating strategy see p. 38</p>

Industry	Key industry characteristics	Strategy	Sistema JSFC investment vision
Wood processing industry 	<ul style="list-style-type: none"> • The ruble rate depreciation and large transport leverage reduce the competitiveness of importers • Rated wood cutting of Russia exceeds in three times the felling volume • Export-oriented industry with the largest great of currency returns 	Develop the asset by restructuring and optimizing of business; getting on the dividend flow in the medium term	<p>Sistema JSFC acquired assets of GC LesInvest at the end of 2014.</p> <p>Sistema JSFC is planning to ensure return on capital by optimizing of current business, improving controllability and transparency, as well as subsequently expanding production (in particular, paper sacks and plywood).</p> <p>More about the operating strategy see p. 44</p>
Electric grid business 	<ul style="list-style-type: none"> • Steady and slight growth of power consumption – by 0.4% in 2014 • In autumn 2013, tariffs of natural monopolies for 2014 were frozen • In 2014 tariff growth was limited at the rate of 3.8% 	Further develop the business after successful transition to RAB regulation of tariffs, maintain a steady dividend flow	<p>The strategy of electric grid assets is focused on growth of business by modernizing of equipment, building of modern grids using Smart Grid components and developing the region infrastructure. Sistema JSFC intends to develop the business by consolidating and subsequently modernizing of regional assets.</p> <p>The company transition to the 10-year tariff regulation using the return-on-investment (RAB) method will enable effective long-term business development planning and is aimed to improve its investment attractiveness. The company expects to invest over 29 bln. rub. in the electric grid sector of the Republic for the 10-year term.</p> <p>More about the operating strategy see p. 52</p>
Railway transportation 	<ul style="list-style-type: none"> • The segment of liquefied gases (LNG) transportation shows the highest stability in the sector • LNG transportation volume has grown by 8% in 2014, while bulk oil cargo transportation volumes by 2% in total 	Develop LNG transportation segment and maintain profitability	<p>In 2015, Sistema JSFC will focus on supporting SG-trans current business and achieving operational objectives. Maintaining of profitability will be achieved by efficient wagon fleet management and optimization of leasing agreements.</p> <p>More about the operating strategy see p. 60</p>

Industry	Key industry characteristics	Strategy	Sistema JSFC investment vision
Pharmaceuticals 	<ul style="list-style-type: none"> • The market volume has grown by 9.3% in monetary terms in 2014 • Share of foreign producers in the Russian market is over 70% • Russia has launched the programme for import substitution • Starting from 2014, the government may limit participation of foreign companies in government tenders 	<p>Expand product portfolio and establish partnership with an industry expert</p>	<p>Sistema JSFC is planning to develop the pharmaceutical business by implementing large-scale projects on launching new production lines and procurement of third-party products. Gain in product portfolio by partnership with international companies will contribute in increase of production capacity utilization, Binnopharm is also planning to upscale production by participating in the programme for import substitution.</p> <p>More about the operating strategy see p. 76</p>
High Technologies 	<ul style="list-style-type: none"> • The government demand for high-tech products is growing • Growing demand for intelligent transport systems • Development of microelectronics will be supported by the import substitution programme 	<p>Improve the economic performance of the business, develop own intellectual products and achieve a steady dividend flow in the medium term</p>	<p>In 2014, Sistema JSFC has begun restructuring JSC RTI high-tech assets in order to improve the economic performance of the business and achieve a stable dividend flow in the medium term. The main development focus will be on the segments of defense industry, microelectronics and intelligent IT systems. RTI is planning to increase its profitability by growing intellectual property share in finished products, to increase production of microchips by extending cooperation with the government and to focus on new products in the aerospace industry.</p> <p>More about the operating strategy see p. 54</p>

Industry	Key industry characteristics	Strategy	Sistema JSFC investment vision
<p>Oilfield services</p> 	<ul style="list-style-type: none"> • Industry consolidation with the biggest players • Increase of volumes of horizontal drilling • Demand for high-tech oilfield services 	<p>Develop promising segments of high-tech drilling, improve the profitability of business and potential partnership with an industry expert</p>	<p>Investments in Targin have a significant growth potential by modernization of the vehicle fleet to increase profitability, introduction of new technologies to diversify range of services and optimization of business and its structure. Sistema JSFC is planning to attract an industry partner to extend Targin expert evaluation.</p> <p>More about the operating strategy see p. 72</p>
<p>Banking sector</p> 	<ul style="list-style-type: none"> • Increased cost of funding • Tougher regulation of retail lending • For the first time in several years, corporate lending grew faster than retail lending 	<p>Develop and support the banking business, provide effective risk management</p>	<p>Sistema JSFC investment strategy in the banking business provides for growth of shareholder capital returns while maintaining the high level of MTS Bank financial stability.</p> <p>Under current economic conditions, Sistema JSFC is focused on improvement of the risk management system and growing of Bank's customer deposits. Sistema JSFC also sees a growth potential for the banking business in the synergy with MTS.</p> <p>More about the operating strategy see p. 54</p>
<p>Real estate</p> 	<ul style="list-style-type: none"> • Due to an unprecedented volume of commissioned real estate in 2014, the office real estate market now has a surplus • Subsidizing of the mortgage rate will support the residential real estate market 	<p>Construct and develop the most liquid real estate assets and monetize by leasing and sales</p>	<p>Sistema JSFC is planning construction and monetization of residential real estate assets, as well as aggregation of office real estate assets and increase in revenue from management and leasing and property management, which will be used to finance new projects and will enable to pay portfolio dividends.</p> <p>More about the operating strategy see p. 80</p>

Industry	Key industry characteristics	Strategy	Sistema JSFC investment vision
Telecommunications in India 	<ul style="list-style-type: none"> • Three largest Indian operators have taken up 58% of the market • Competition in the data transfer services segment is growing • In 2015, a new auction for several frequency bands was held, including for 800 MHz, where SSSL operates 	<p>Reduce expenditures for the business funding and resolve regulatory issues</p>	<p>In 2015, we plan to continue with financial rehabilitation of the Indian business and significantly reduce its need in financing of its operating activity on the part of Sistema JSFC. In case of resolved regulatory issues regarding frequency spectrum use, Sistema JSFC may consider opportunities of partnership with an industry expert.</p> <p>More about the operating strategy see p. 84</p>
Media assets 	<ul style="list-style-type: none"> • Rate of growth of the Russian media market is slowing down • Ownership ratio of foreign companies in any Russian mass media company has been limited to 20% • The government is stimulating telecasting of the Russian content on the part of state 	<p>Search for new promising markets and develop convergent media products in partnership with other Sistema Group companies</p>	<p>Sistema JSFC investment strategy in regard to media assets of SMM is focused on creating conditions for entry into emerging markets in the new digital environment, developing new digital services and digital media. Successful implementation of the strategy will contribute in maximum use of current competitive advantages of Sistema Group as a whole.</p> <p>More about the operating strategy see p. 88</p>
Agriculture 	<ul style="list-style-type: none"> • Export-oriented industry with a high share of currency returns • Russia became the world's third largest wheat producer in 2014 • Russia's wheat output in comparison with the previous year grew up by 13% as compared with the global growth of 1% 	<p>Expand the land bank and develop export channels</p>	<p>The strategy of agriculture business development proposes further expansion of the land bank by strategic acquisitions and partners attracting. The targeted regions are Rostov region, Stavropol territory and Krasnodar territory. Sistema JSFC is also planning to develop export channels and such segments as seeds production and sale and contracted harvest works.</p> <p>More about the operating strategy see p. 68</p>

Sistema's financial results

(US\$ millions)	FY 2014	FY 2013	Change
Revenues	16,585.0	18,502.0	(10.4%)
Adjusted OIBDA	4,438.3	5,570.2	(20.3%)
Operating income	1,738.4	3,566.6	(51.3%)
Adjusted operating income	2,146.1	2,936.7	(26.9%)
Net (loss)/ income attributable to Sistema	(4,087.6)	2,257.5	-
Adjusted net income attributable to Sistema	1,194.9	1,623.5	(26.4%)

(RUB millions)	FY 2014	FY 2013	Change
Revenues	631,865	589,251	7.2%
Adjusted OIBDA	165,171	177,400	(6.9%)
Operating income	60,876	113,588	(46.4%)
Adjusted operating income	78,353	93,527	(16.2%)
Net (loss)/ income attributable to Sistema	(232,556)	71,898	-
Adjusted net income attributable to Sistema	44,194	51,706	(14.5%)

Note: The reporting currency of the Group's US GAAP consolidated financial statements is the US dollar. Here and hereafter, the financial information in Russian roubles has been presented for the users' convenience and is not derived from audited financial statements. Financial figures in US dollars were converted to roubles using following approach: amounts from the statement of financial position – using closing rates as of the reporting dates, amounts from the income statement – using average rates of the reporting periods except for significant transactions / accruals, which were converted using exchange rate as of date of a transaction /accrual or actual rouble amounts for transactions/accruals nominated in roubles.

Following its transfer to the Russian Federation in December 2014 of shares in Bashneft, Bashneft's results are treated as a disposal, reported as discontinued operations and excluded from the Group's financial results for all periods presented. The Group's financial results for the fourth quarter and the

full year of 2014 were impacted by the rouble depreciating significantly against the US dollar.

In 2014, Sistema recognised loss from certain one-off items, which significantly impacted the company's financial results. The largest one-off items include: US\$ 5.0 billion

loss from the deconsolidation of Bashneft, US\$ 290.0 million loss from the impairment of long-lived assets in India (SSTL) and US\$92.5 million of accrued provisions for cash and deposits in Delta Bank (MTS).

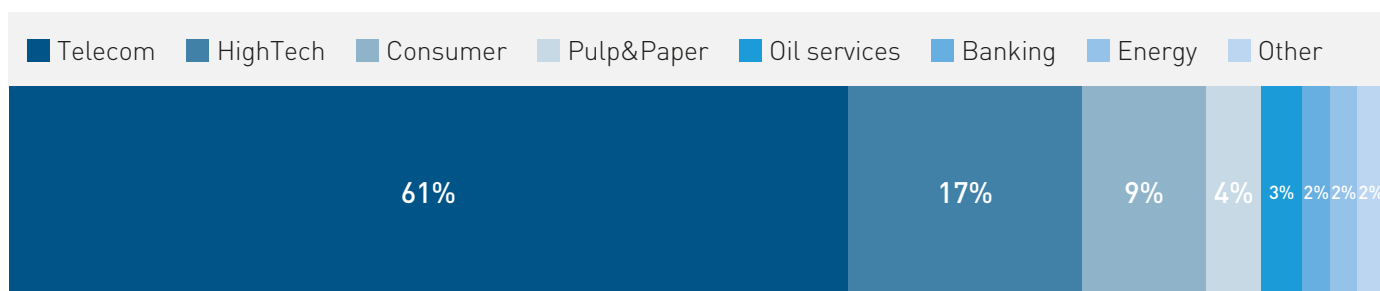
Revenues

Sistema's consolidated revenues in rouble terms increased by 7.2% year-on-year in 2014 despite the challenging economic environment, and reflect a strong contribution

from all the Group's companies, particularly from MTS, Detsky mir, as well as Targin (acquired in the third quarter of 2013) and the pulp and paper business (acquired in the third

quarter of 2014). Ten of Sistema's 13 major assets demonstrated revenue growth in 2014 in rouble terms.

Revenues by sectors*



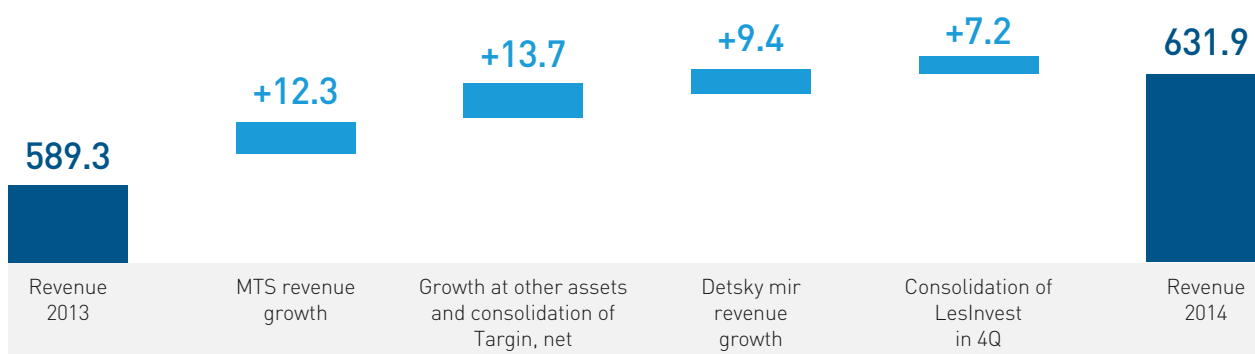
* Based on aggregate revenues of 4Q 2014

As of the fourth quarter of 2014, the Company began consolidating LesInvest into the Group's financial results. In the fourth quarter of 2014,

LesInvest already contributed RUB 7.2 billion and RUB 1.1 billion to the Group's consolidated revenue and OIBDA. The consolidation of Targin

contributed approximately RUB 16 billion to the Group's revenue growth for the full year of 2014.

Revenue analysis, RUB bln



OIBDA

The Group's adjusted OIBDA decreased by 6.9% year-on-year in rouble terms in 2014, mainly

due to accrued provisions for the loan portfolio to individuals at MTS Bank. Eleven of Sistema's 13 major

companies reported positive adjusted OIBDA in the reporting year.

OIBDA analysis, RUB bln



Net income

In 2014, adjusted consolidated net income attributable to Sistema decreased by 14.5% year-on-year in rouble terms, mainly due to US\$ 548.6 million (RUB 21.1

billion) worth of foreign exchange losses. Nine of Sistema's 13 major companies reported net income in 2014. The Group's net income includes Sistema's share in

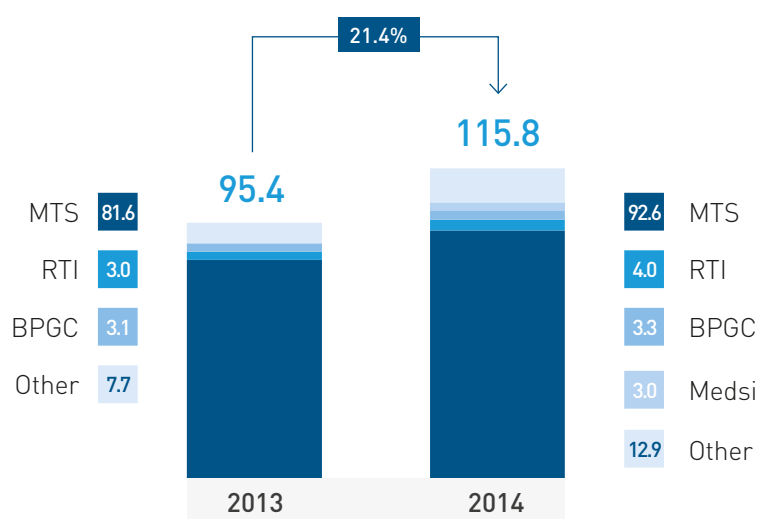
Bashneft's net profit for the period of ownership: US\$ 1.2 billion in 2014 and US\$ 1.1 billion in 2013.

Capital expenditures

Capital expenditures increased by 21.4% YoY mainly driven by MTS due to US dollar appreciation. Active construction and modernisation of medical facilities at MEDSI added RUB 3 bln to capital expenditures of the Group in 2014. Other largest contributors to the Group's CAPEX are RTI, BPGC, Detsky mir and real estate projects.

The Group's SG&A expenses grew by 6.2% YoY, which is lower than the rate of inflation. Corp Centre's SG&A increased by 4.9% YoY in 2014, mainly due to one-off optimisation costs in 4Q 2014 and non-cash accruals for incentive programme in 2014. In 2015, Sistema plans to reduce its SG&A by 25-30%.

Group's capital expenditures, RUB bln



Group's debt

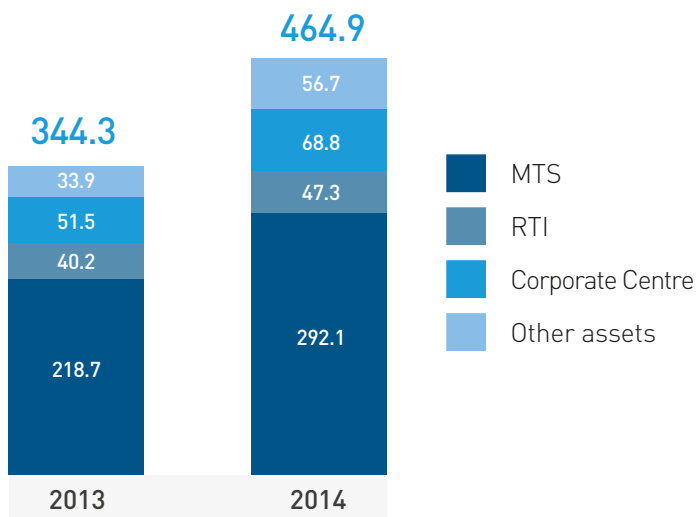
A 35% increase in consolidated debt was mainly due to the dollar appreciating against the rouble and MTS increased obligations.

MTS debt increased due to borrowing of additional funds at attractive terms

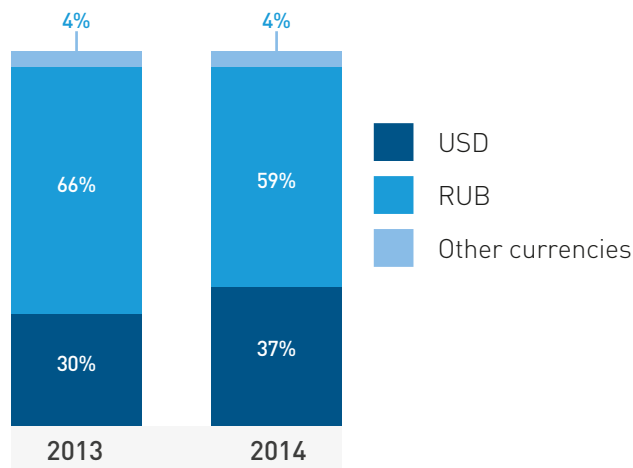
to hedge risks of low liquidity in the future on the back of market situation. In October 2014, MTS signed an agreement with Sberbank of Russia to open a non-revolving line of credit for a total amount of RUB 50 billion and maturity in September 2021.

The Group's debt currency profile remained largely stable. A large part of US dollar denominated debt relates to MTS and the Corporate Centre, obligations of Sistema's other Russian subsidiaries are largely denominated in roubles.

Group's debt, RUB bln



Group's debt by currency



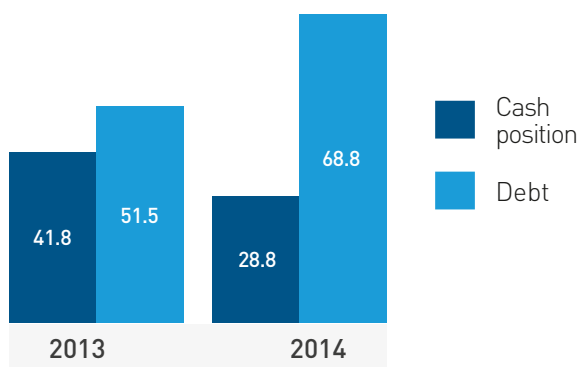
Debt at Corporate level

The Corporate Centre's debt increased due to dollar appreciation against the rouble. The Corporate Centre's obligations in US dollars are mostly represented by Eurobonds

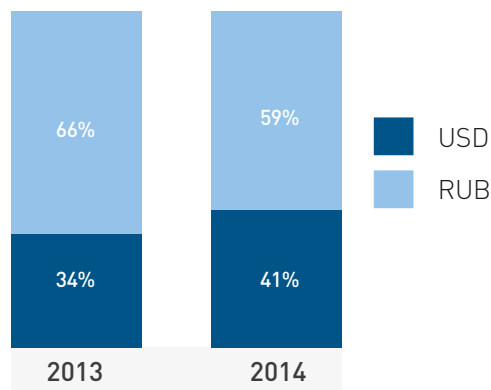
with maturity in 2019. Corp Centre's cash position amounted to RUB 28.8 bln, 70% of Sistema's cash was denominated in US dollars. Net debt at Corporate level amounted to RUB

40 bln. In 2015, Sistema plans to repay RUB 2.8 bln of rouble bonds and RUB 12.2 bln of loans from banks (RUB 8.6 bln had already been repaid after the reporting period).

Corporate Centre's debt, RUB bln



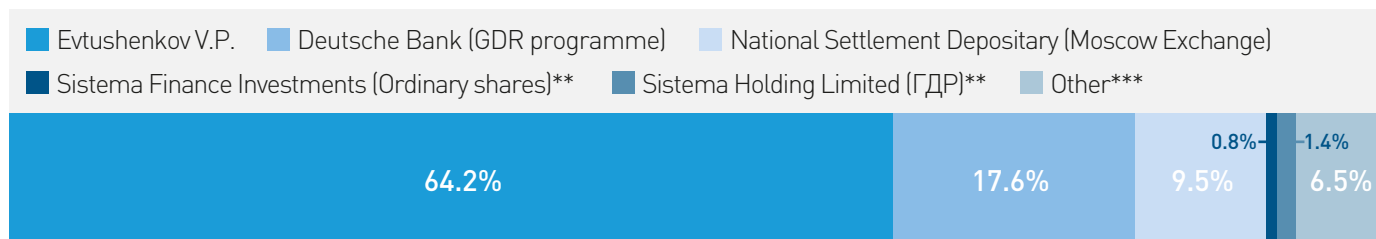
Corporate Centre's debt by currency



* Including highly liquid financial instruments

SHAREHOLDER CAPITAL AND SECURITIES

Sistema's shareholders*



Sistema has 9,650,000,000 ordinary shares outstanding, with a par value of RUB 0.09 each. The company's shareholder capital amounts to RUB 868,500,000. Sistema had its IPO in February 2005 and was listed on the London Stock Exchange under ticker symbol SSA. The company's shares are traded on the London Stock Exchange as Global Depository Receipts (GDRs) with one GDR representing 20 ordinary shares. Its ordinary shares are traded on the Moscow Exchange under ticker symbol AFKS. Sistema's free float on the London Stock Exchange is approximately 19% and 16.8% of the shares are traded on the Moscow Exchange (including positions of insiders, shares owned by management and members of the Board of Directors, and ordinary shares on Sistema's Group balance sheet).

Sistema's shares are included in the benchmark indices of the Moscow Exchange (MICEX Index and RTS Index). These are capitalisation-weighted composite indices calculated based on prices of the 50 most liquid stocks of major Russian issues from Russia's key sectors.

Sistema's shares are also included in MICEX Financial Services Index (a sector index). Sector Indices are capitalisation-weighted indices calculated based on prices of the most liquid shares of Russian issuers operating in the relevant sector, which are admitted to trading on the Moscow Exchange and are included in the Broad Market Index.

The Moscow Exchange's multi-asset indices are composite indices comprised of stocks and bonds

admitted to trading on the Moscow Exchange, that can be used as investment vehicles by Russian Pension Funds. Sistema's shares are included in equity sub-index and bond sub-index.

Sistema's GDRs are also included in MSCI Russia Index. This serves to confirm international recognition of the company and strengthen its reputation among the largest institutional investors with index strategies.

Shares of MTS, Sistema's subsidiary, are traded on the New York Stock Exchange as ADRs (ticker: MBT). Its ordinary shares are traded on the Moscow Exchange under ticker symbol MTSS. Chairman of the Board of Directors of Sistema Vladimir Evtushenkov, with 64.19% of shares, is Sistema's principal shareholder.

Number of outstanding shares amounts

9,650,000,000

Ordinary shares with nominal value of RUB 0.09

The share capital amounts RUB 868.5 million

* As of December 23, 2015

*Shares and GDRs owned by Sistema Group

*** Shares held by insiders (management, members of the Board of Directors and others)

Sistema's shareholders*

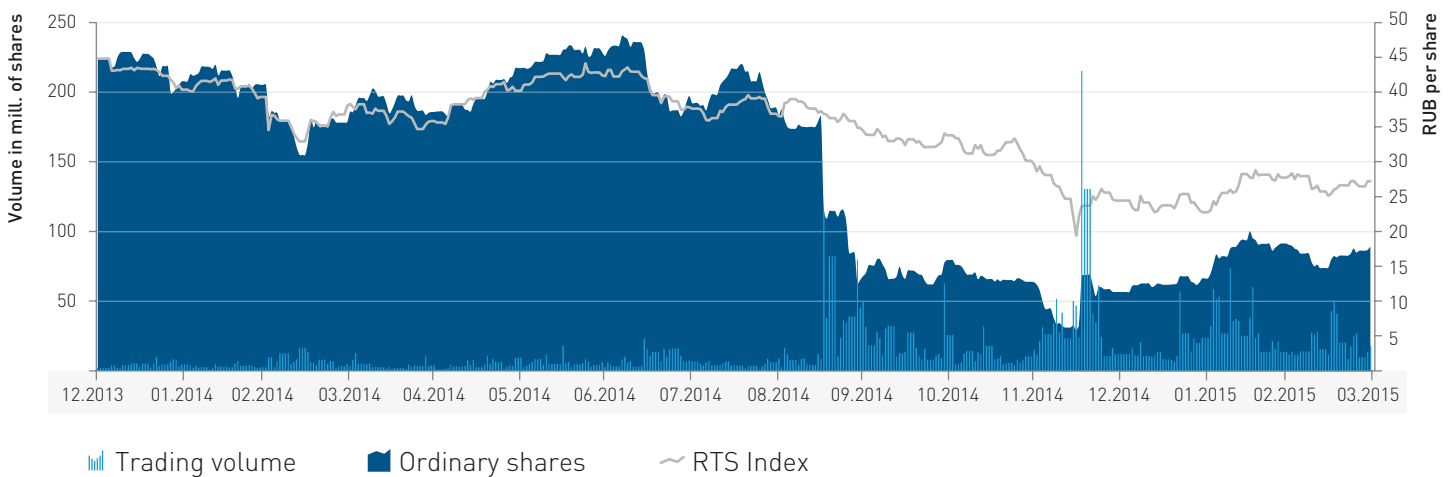
Sistema's GDRs and ordinary shares significantly decreased in the second half of 2014 due to the situation around Bashneft and changes in macroeconomic conditions. The rouble depreciated against the US dollar by 75.3% in 2014, Brent oil price fell by 44.5% in 2014.

Sistema's GDRs dropped by 83.8% between January 1, 2014 and January 1, 2014. The closing price of Sistema's GDR on the London Stock Exchange on the first trading day of 2014 was US\$ 31.25 with a market capitalisation of US\$ 15,078 million, while on the last trading day it was US\$ 5.21 with a market capitalisation of US\$ 2,514 million. Sistema's ordinary shares decreased by 74.5% in 2014, RTS index lost 45.2% for the year.

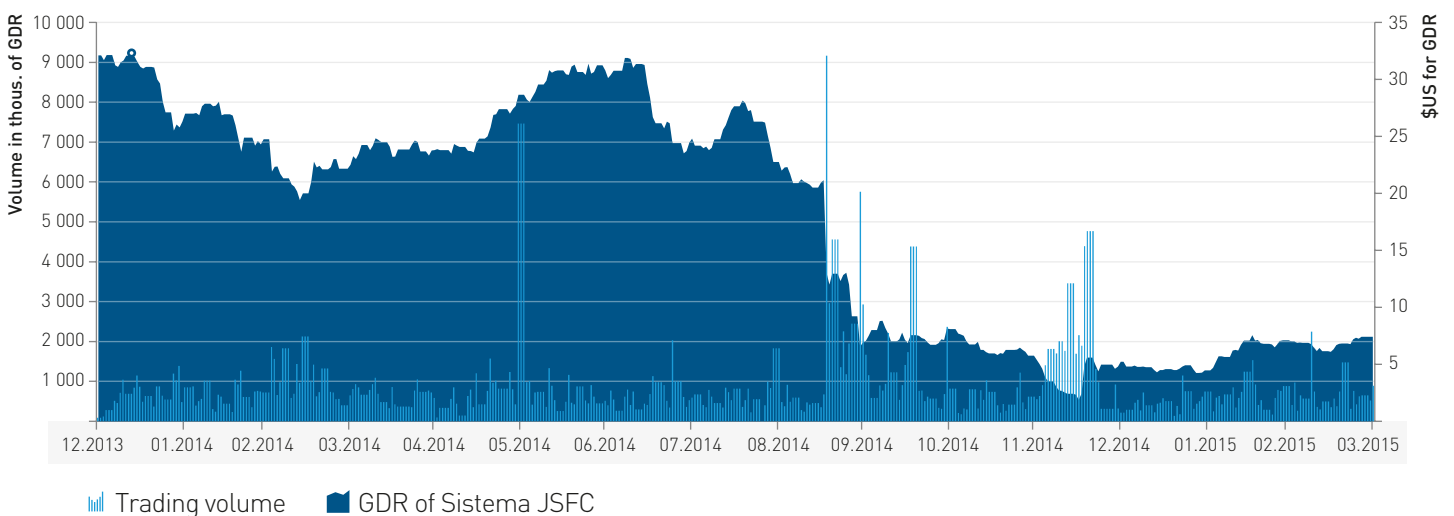
Sistema's GDRs reached a high of US\$ 32.08 on January 10, 2014 and a low of US\$ 1.88 on December 16, 2014. The average daily trading volume on the London Stock Exchange in 2014 was 997,240 GDRs.

Between January 1, 2015 and March 31, 2015, Sistema's GDRs gained 42% and its ordinary shares rose by 57%, while RTS Index was up 11.3%. The company's market capitalisation as of March 31, 2015, was USD\$ 3.6 billion.

Ordinary shares



Global depository receipts

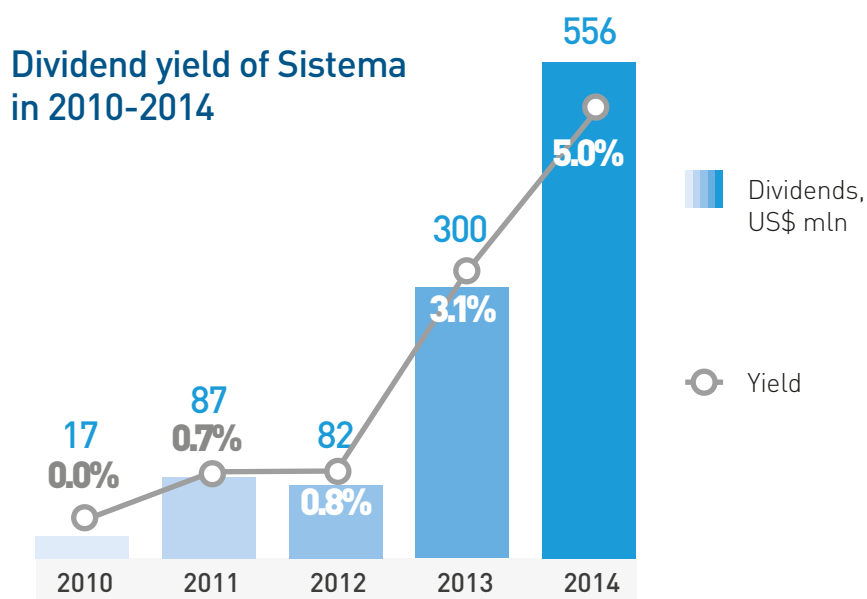


* Source: Bloomberg

Dividends

Sistema's dividend policy aims to provide a regular and sizeable dividend flow, while allowing the company to maintain the financial flexibility to take advantage of attractive investment opportunities in the future.

Dividends are declared on the basis of results from the previous financial period, and the company's dividend policy is for annual dividends to be a minimum of 10% of the corporation's consolidated net income under US GAAP (net of any special dividends paid). In addition, in the event of a large asset sale for cash, special dividends will be declared in an amount of at least 10% of the net gain from such a transaction, as determined by the Board of Directors. Under Russian law, the total amount of dividends with respect to any year may not exceed the company's annual unconsolidated net income determined in accordance with Russian Accounting Standards (RAS).



In June 2014, the Annual General Meeting of Shareholders approved the total amount of dividend payment on Sistema's shares for 2013 at RUB 19.9 billion, representing a payment of RUB 2.06 per ordinary share (RUB 41.2 per GDR). The total proposed dividend

payment has been determined on the basis of Sistema's full year 2013 US GAAP net income and the corporate centre's net gain from the sale of stake in RussNeft in July 2013. In July 2014, Sistema paid out record dividends, corresponding to dividend yield of 5%.

BOND PORTFOLIO

Debt profile at the holding company level includes rouble bonds and Eurobonds. As of December 31, 2014, Sistema had two rouble bond issues and one Eurobond issue:

- 3-series rouble bonds with a par value of RUB 19 billion maturing on November 24, 2016 and with a coupon rate of 8.75% (semi-annual payments)
- 4-series amortised rouble bonds with a par value of RUB 19.5 billion maturing on March 15, 2016 and with a coupon rate of 7.65% (semi-annual payments)

- Eurobonds issued in May 2012 with a par value of US\$ 500 million and a coupon rate of 6.95% (semi-annual payments), maturing on May 17, 2019

In 2014, Sistema repaid its 2-series rouble bond issue with a par value of RUB 20 billion.

In February 2015, Sistema completed the placement of RUB 10 billion Series BO-01 unconvertible interest-bearing bonds with a par value of RUB 1,000 at the rate of 17% per annum. Coupon payments will be made on a semi-annual basis.

The bonds mature in 15 years. In addition, bondholders have the right to redeem their bonds at the point of expiration, 18 months from the date the bonds were placed.

Placement of exchange bonds was the first market transaction in the Russian market since the turn of 2014 among BB credit rating corporate borrowers, as well as the first market transaction in the corporate segment in 2015. The successful placement showed the attractiveness of Sistema JSFC securities and interest to the current investment strategy.

OUR INVESTMENTS

MTS	28
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Sistema mass media	88

Mobile TeleSystems (MTS) is a leading telecom operator in Russia and the CIS countries. Together with its subsidiaries, MTS provides services to about 104m mobile subscribers in Russia, Armenia,

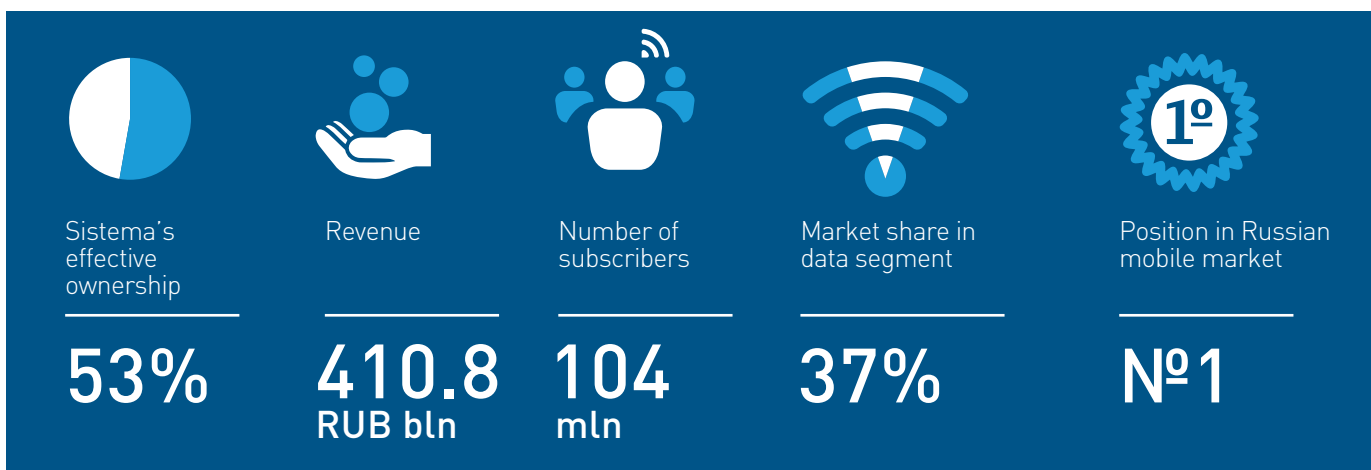
Ukraine, Turkmenistan and Uzbekistan. The company also provides fixed telephony and pay-TV services in Moscow (MGTS), in all federal districts of Russia and in Ukraine.



Management

President – A.A. Dubovskov

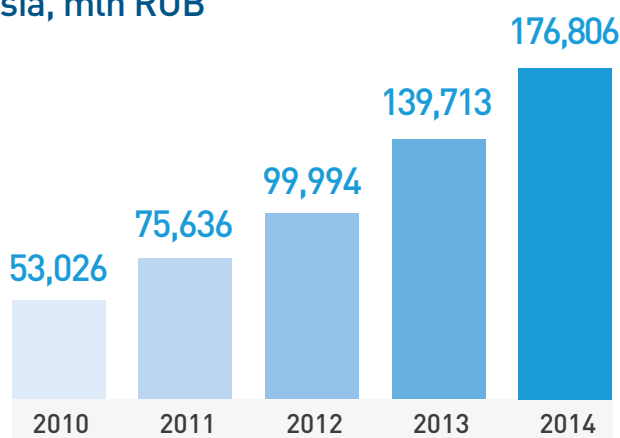
Chairman of the Board of Directors – R. Sommer



Industry*

The growth rate of the Russian telecom market slowed down in 2014 to 2.7% compared to 5% in 2013, mainly due to the decline in the growth rate of the mobile market from 5% to 3%. The penetration of OTT services (Skype, WhatsApp, Viber, etc.) continues to increase and has reached 13% in Moscow. This trend is expected to result in a further downturn in the mobile voice market as part of mobile voice usage continues to be replaced by Voice over IP (VoIP) and SMS is replaced by iMessaging.

Operators' revenues from data services in Russia, mln RUB



* According to company data and information from ACM-Consulting, TMT-Consulting, iKS-Consulting and Svyaznoy.

Data communication services continue to drive growth in the mobile business through incentives to increase smartphone and tablet penetration, promotion of packaged "voice&data" plans, development of data communication networks and distribution channels. In 2014, the penetration rate for data services in Russia reached 60%. Over the last three years, data traffic in Russia has grown sevenfold, with LTE traffic accounting for 12% of total traffic as of December 2014.

According to expert estimates, the broadband access (BBA) subscriber base in Russia totalled 28.9 mln households in 2014. The fixed BBA market in 2014 increased by 5.1%. In 2015, the BBA and pay-TV markets will remain highly competitive, with 3-4 players in every large city of Russia. The growth in the BBA subscriber base will be mainly driven by churn from competitors. According to forecasts, the number of BBA subscribers in 2015 may increase by 3.7% to 29.96 mln households.

The pay TV market in Russia grew by 6.1% in 2014 to RUB 57 bn, with the number of pay-TV subscribers rising by 8.3% to 37.8 mln. The TV market remains among the fastest growing markets due to the development of hybrid and satellite TV. In 2015, growth rates of the pay TV market and subscriber base in Russia are predicted to slow down from 4.2% to 3.8%, respectively, with a penetration rate of above 70%.

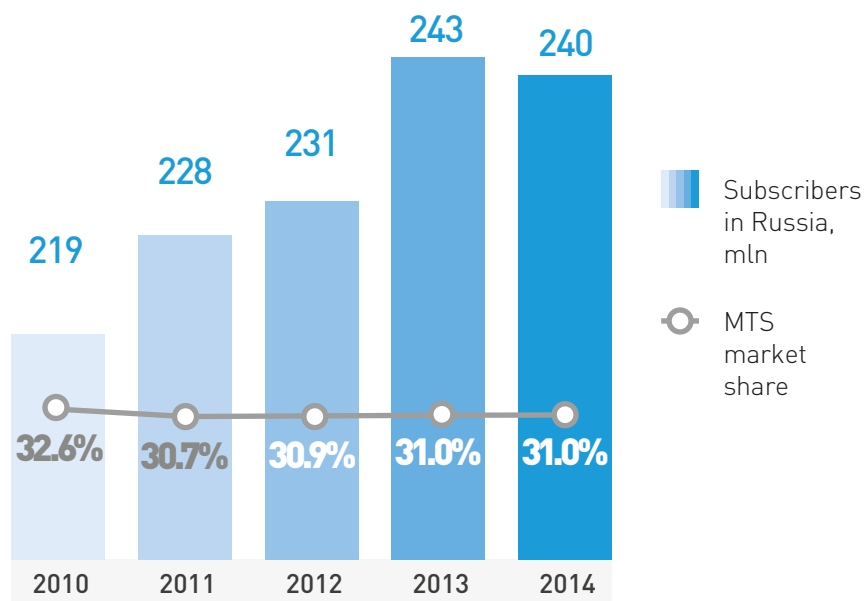
Steady growth in 2014

MTS remains the leader in total revenues and OIBDA among the Russian «Big Three» operators, with the lowest churn rate in 2014 and a 7.5% year-on-year growth in the mobile subscriber base in

* Calculated from company press releases.

** mobile subscriber base in Russia for the 2010-2013 includes MTS subscribers recorded on the basis of 6-month activity. From the 3rd quarter of 2014 MTS has moved to the account of subscribers based on 3-month activity, the data for 2014 include a 3-month MTS subscribers.

Subscriber base in Russia, m



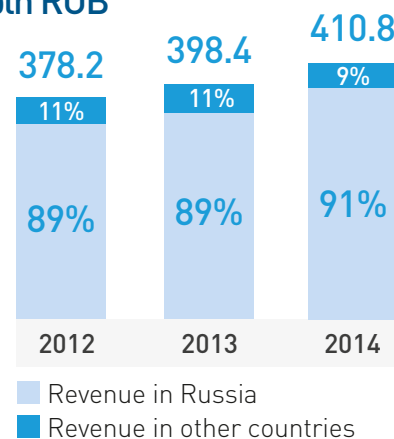
Over 2014, the sales of mobile phones and smartphones in Russia increased by 6% to 44m units with the share of smartphones in total phone sales reaching 64%. The market is characterised by a fall in the average smartphone price with an increase in the share of low cost models in total sales to 60-65%. The growth of tablet unit sales also slowed down to 33% in 2014 year-on-year compared to 125% growth in 2013; however, in monetary terms, sales remained stable.

In 4Q 2014, the financial results of telecom companies were affected by

fluctuations in the rouble exchange rate against foreign currencies and lower growth in retail lending, pushing up the costs of imported telecom equipment and international roaming and interconnect costs of telecom operators. Therefore, rates for premium international roaming and voice calls are expected to increase.

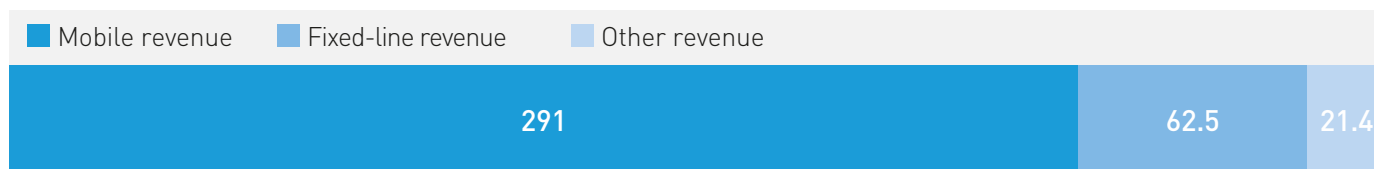
The majority of markets where MTS operates will continue to be exposed to currency risks in 2015. Besides, there is the risk of a decline in consumption in the telecom market, especially for international roaming services.

MTS revenues by geographies, bln RUB



■ Revenue in Russia
■ Revenue in other countries

MTS revenues in Russia by services, bln RUB



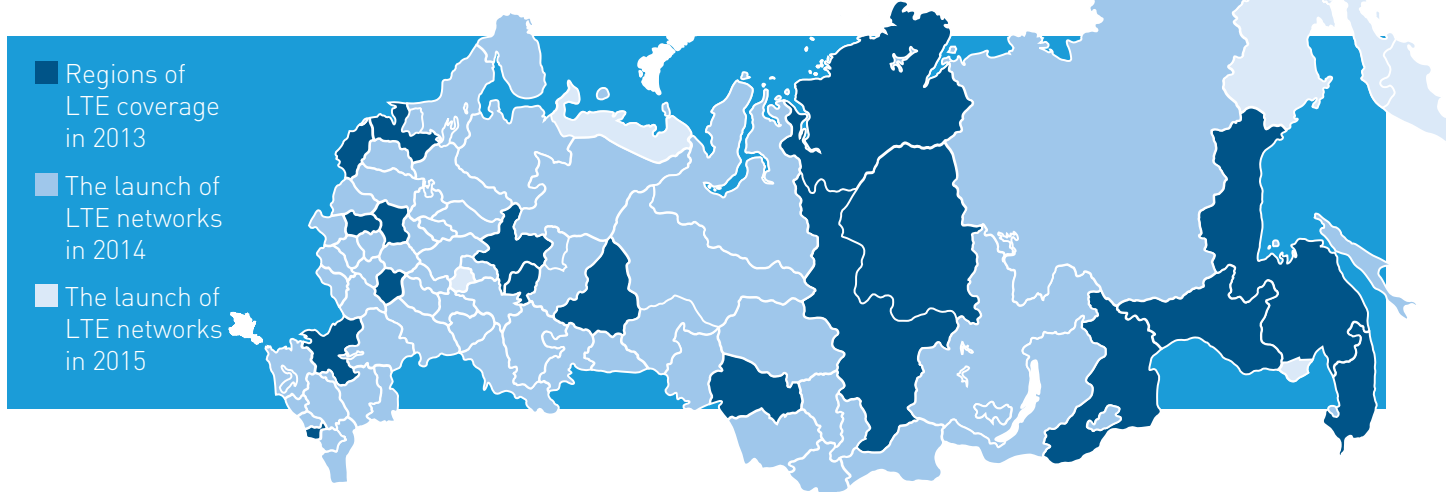
In 2014, MTS continued active investments in the construction of 3G and 4G data networks along with modernization and expansion of 3G networks in strategic regions and quality improvement projects implemented in Moscow and Saint-Petersburg. According to Speedtest data, MTS has the best data download speeds and the lowest network lag in Russia. In Moscow, according to Speedtest user measurements, MTS's LTE networks have the highest data download speeds, following the large-scale construction of networks undertaken in 2013-2014.

The 4G network was launched into commercial operation in 76 Russian regions compared to 15 regions at the end of 2013, with MTS leading in terms of the number of Russian regions covered by LTE networks as of the end of 2014.

In Moscow, MTS focused on the quality of data services, which resulted in a 10-fold growth in LTE traffic with over half of the total Internet (smartphone) traffic being generated by LTE users.

The launch of a small cell deployment project in large Russian cities will enable MTS to increase the LTE network speeds and capacity and improve radio coverage in locations where mobile Internet usage is particularly high. At the first stage, MTS will implement the project in Moscow (200 cells) and Saint Petersburg.

MTS LTE coverage map in Russia



In 2014, fixed broadband access was the main driver of growth in the subscriber base and revenues in fixed-line business, coming from new connections and increase in average monthly revenue per user (ARPU).

MGTS GPON (GigabitPON) network with digital TV signal and home Internet with the speed of up to 1 GB/s became available in 3.5 mln

apartments or 90% of households in Moscow. The number of MTS GPON users reached 1.1 bln. The number of fixed BBA and GPON TV users in the corporate segment was up 50%. Total Internet traffic in the MGTS network grew by 45% for the year.

In 2014 MGTS implemented several contracts for connecting transport hubs in the capital, student hostels, and traffic lights to high-speed data

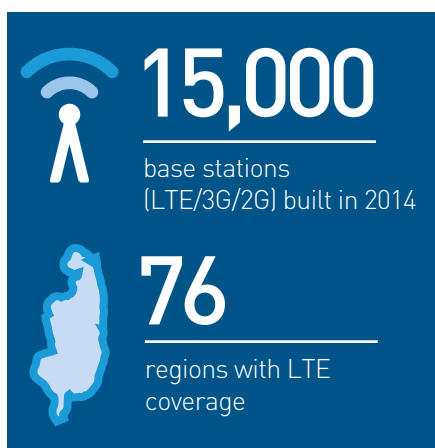
channels. MGTS also successfully implemented a video surveillance project for the elections to the Moscow Duma in September 2014.

Large-scale projects implemented in 2014 include the launch of MVNO on MTS network, which provided subscribers with access to packaged services, including fixed-line Internet, telephony and pay TV; mobile Internet and voice calls;

and mobile TV. Implementation of IMS (IP Multimedia Subsystem) was completed in Moscow, which enables the operator to launch its own OTT services.

Deterioration of macroeconomic conditions and the political situation in Ukraine in 2Q 2014 has led to a drop in the consumption of communication services by MTS-Ukraine subscribers, especially data and content delivery services. Starting from August 2014, MTS-Ukraine ceased services in the Crimea for technical reasons.

Operational strategy



infrastructure facilities, non-transport monitoring (people, trouble notification).

Development of new sales channel formats will take place at OZON Holding, the largest multi-brand player engaged in online sales of operator products. In 2015, MTS will launch its service and product offerings, sale of SIM cards and subscriber equipment, payments from MTS account using Ozone applications, etc. in real time.

Key events

- In April 2014 MTS acquired a 10.8% stake in OZON Holdings Limited, one of Russia's largest e-commerce businesses, for US\$ 75 million. Sistema also acquired a 10.8% stake in OZON at the same price.
- In May 2014, MTS became the only Russian telecom brand to be included in the BRANDZ™ Top 100 Most Valuable Global Brands for the seventh time, ranked 9th among the world's 10 most valuable telecom brands. Its brand value increased by 14.5% over the year to US\$ 12.18 bln.
- In July 2014, MTS signed a settlement agreement with the Republic of Uzbekistan to resume operations in the country, under which MTS received a 50.01% stake in UMS. The network was launched on December 1, 2014.
- In November 2014, MTS in partnership with Sistema Mass Media announced plans to launch satellite TV services under the MTS brand. The services will be available for 95% of the country's population.
- In December 2014, MTS signed a partnership agreement with VimpelCom to jointly plan, develop and use LTE networks in certain Russian regions. Under the agreement, between 2014 and 2016, MTS will develop shared mobile data networks in 19 regions, while VimpelCom will construct networks in 17 regions.

MTS will continue to actively develop data services as the most promising business segment and deploy multiband LTE networks with frequency aggregation at a later stage. In 2015, MTS plans to provide 4G network coverage in all Russian regions. Construction of micro cells will be continued in locations with massive web traffic along with installation of indoor base stations in large cities. SON (self-organizing network) implemented in Moscow since 2014 will also be deployed in other Russian regions. As for construction and modernisation of fixed-line networks based on target technologies, MTS plans to connect over 90% households with FTTB (fiber-to-building) technology.

In response to OTT market trends, from mid 2015, MTS plans to launch its own IP telephony and messaging service based on Rich Communication Suite technology (similar to Skype, Viber, WhatsApp). Work on the Big Data project - search for additional revenue opportunities and improvement of operational efficiency by using IT assets - MTS data storages - will be continued.

According to the M2M service strategies for 2015-2017, work will be carried out in the following 5 areas: motor vehicle monitoring and dispatching, insurance telematics, security and search systems, monitoring of residential and commercial properties and



According to the 2015-2018 development strategy for financial services offered by MTS and MTS Bank, the share of MTS subscribers in the bank's client portfolio is expected to expand from 2% to 7%. The key focus in the development of financial services in 2015 will be on the launch of a single digital wallet for MTS customers, development of NFC services and launch of new products: digital signature on a SIM card, virtual card, money transfer service, expansion of fee-based financial services (insurance, railway and air tickets).

The MTS strategy for foreign markets is aimed at maintaining and strengthening its leadership position in the broadband internet segment, building and upgrading networks, improving efficiency, expanding the frequency band, developing new growth points: mobile advertising, mobile commerce, M2M, Big Data.

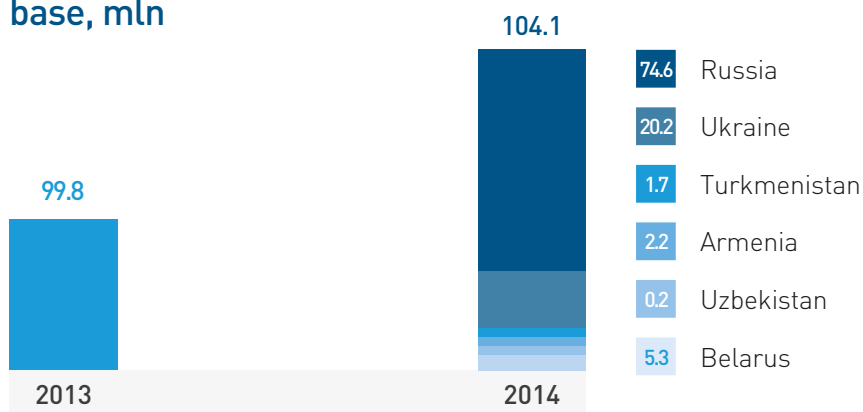
Financial results of MTS

RUB million	2014	2013	Change
Revenue	410,758	398,443	3.1%
OIBDA	171,812	176,299	(2.5%)
Operating income	98,698	114,866	(14.1%)
Net income attributable to Sistema	27,725	42,270	(34.4%)
Capital expenditures	92,599	81,575	13.5%
Net debt	230,651	188,086	22.6%

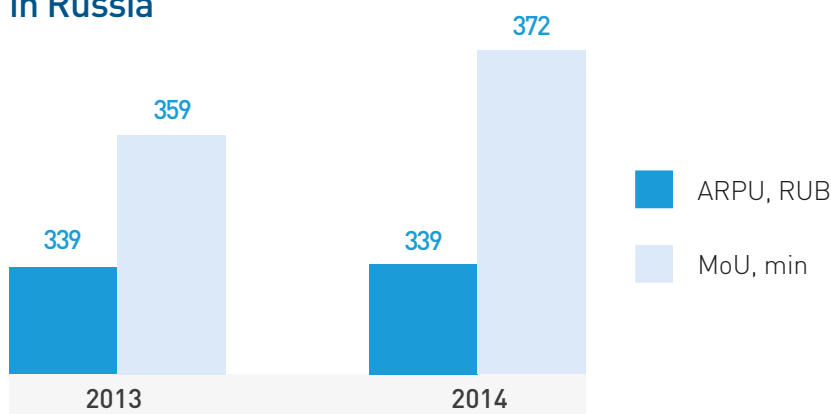
MTS retained its leading position among the Big Three operators in the Russian telecom market in 2014, both in terms of revenue and profitability. MTS' revenue in rouble terms increased by 3.1% year-on-year in 2014, as a result of the continued development of its data services and subscriber base growth. The total subscriber base increased by 4.1% to 104.1 million customers as of December 31, 2014.

In February 2015, MTS' subsidiary MTS Ukraine won a tender for a nationwide licence for 3G telecommunication services in the 1950-1965 MHz/2140-2155 MHz spectrum ranges. Granted for a term of 15 years, the licence cost UAH 2.715 billion. In accordance with the conditions stipulated in the tender papers, MTS is required to launch 3G services in all of the regional centres across Ukraine within 18 months upon allocation of the licence.

MTS mobile subscriber base, mln



Revenue per user and minutes of usage at MTS in Russia



In 2014, MTS' capital expenditures of RUB 92.6 billion slightly exceeded the target of RUB 90 billion due to prepayments to the vendors in anticipation of further depreciation of the rouble.

Key projects include the enhancement of 3G networks in Russia, roll-out of LTE/4G networks

throughout Russia, and the ongoing deployment of GPON in Moscow, as well as network modernization in other markets of operations.

MTS debt increased due to additional borrowings made on attractive terms to hedge the risks of low liquidity in the future. In October 2014, MTS signed an agreement with

Sberbank of Russia to open a non-revolving credit facility for a total amount of RUB 50bn maturing in September 2021.

The high proportion of rouble-denominated debt mitigates the risks associated with currency volatility and enhances the company's financial stability.

MTS debt profile

Debt by instruments



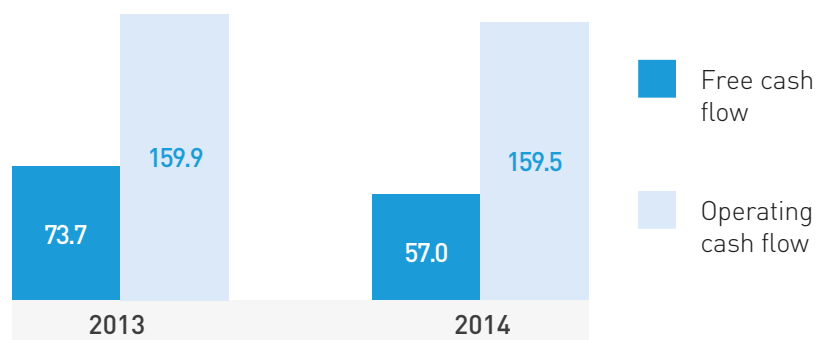
Debt by currency*



* The debt structure by currency includes risks of currency hedging in the amount of US\$ 675.3 million at the end 4th quarter of 2014

As of December 31, 2014, MTS Ukraine, a subsidiary of MTS, held US\$ 90.2 million in current accounts and deposits in Delta Bank, the fourth largest bank in Ukraine. In December 2014, Delta Bank delayed customer payments and put limits on cash withdrawals. In March 2015, the National Bank of Ukraine adopted a resolution declaring Delta Bank to be insolvent. The Group recognised a provision for cash and deposits in Delta Bank in the financial statements for 2014.

MTS Free Cash Flow, RUB bln



DETSKY MIR

The Detsky Mir Group is the largest children's goods retailer in Russia and the CIS. The Group includes the Detsky Mir retail chain in Russia and

Kazakhstan, the early development chain ELC in Russia and the online stores detmir.ru and elc-russia.ru.



Management

President – V.S. Chirakhov

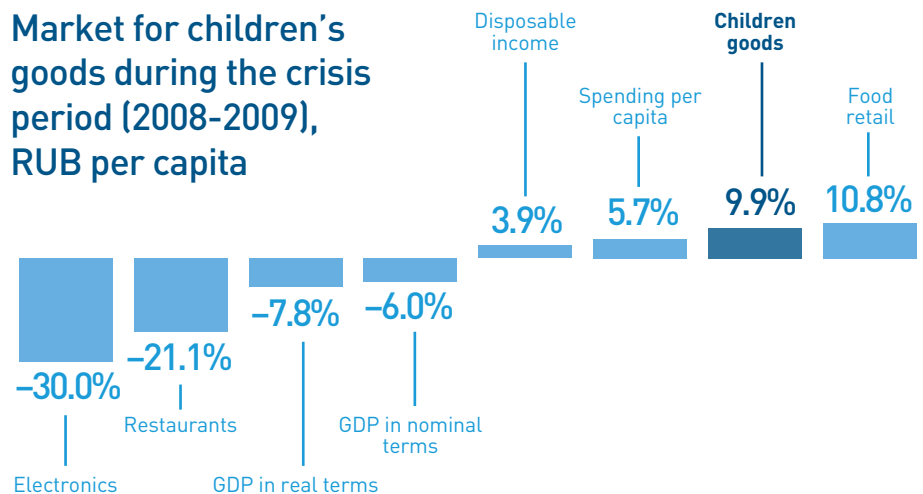
Chairman of the Board of Directors – C. A. Baxter



Industry*

In 2014, the market of children's goods kept growing despite a slowdown in Russia's economy. Similar to food retail, the market for children's goods is resistant to macroeconomic challenges, as was clearly demonstrated by the financial crisis of 2008-2009 when the population's spending on children's goods rose by 9% (outpaced only by spending on food with 11%). Replacement of so-called uncivilised retail (open-air markets, kiosks, fairs) by modern formats and market consolidation by the largest players continued in 2014. Detsky Mir retained its leadership in 2014 with its market share rising from 8.1% to 10.0%.

Market for children's goods during the crisis period (2008-2009), RUB per capita

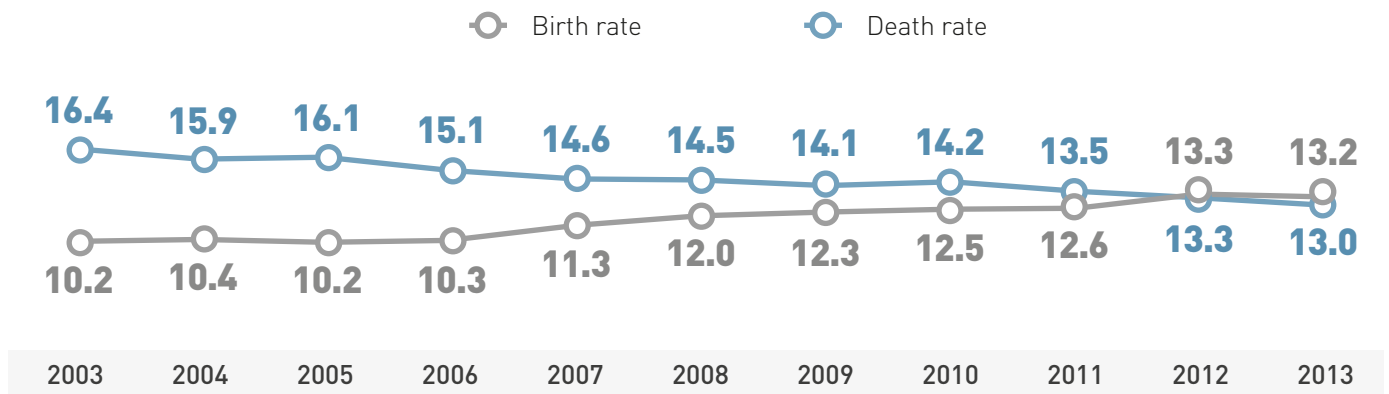


In 2014, the market for children's goods increased by 3.2% in rouble terms. In 2015, experts expect market growth to slow down to 2.7%, however, demographics will continue to drive up spending on children's goods. The government's support of family and motherhood, including the Maternity Capital Programme, contributes significantly

to a rise in birth rates. According to Rosstat, Russia had a record number of births in 2014 (1.9 million). By resolution of the Russian Government the Maternity Capital Programme was extended to 2017, which will probably have a positive effect on the birth rates in 2015-2016 through additional financial support provided to families.

* RosInter, M-Video, Synovate Comcon, X5 Retail Group, Rosstat.

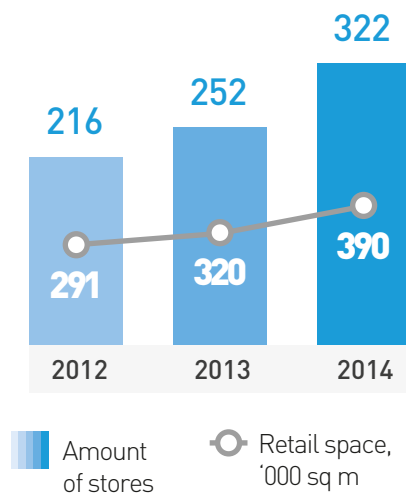
Birth and death rates convergence, % per 1,000 habitants



Steady growth in 2014

In 2014, Detsky Mir continued to improve business efficiency. Key projects implemented during the reporting year include the construction of Detsky Mir's warehouse in the Moscow region, the introduction of a unified SAP IT platform and the launch of a 7,000 sq.m. flagship store in the centre of Moscow, which became the biggest children's goods store in Russia. In 2014, the company opened 56 new Detsky Mir stores and 16 ELC stores*.

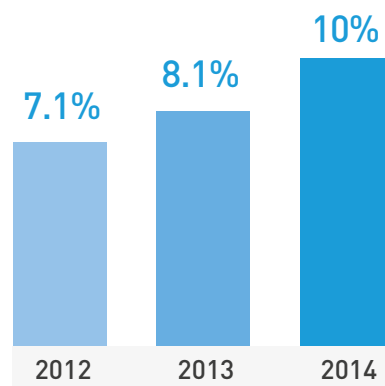
Detsky mir stores and retail space



The retail space of Detsky Mir expanded by 22% in 2014 to 390,000 m² from 320,000 a year earlier. All newly launched Detsky Mir stores

were designed in a new concept providing for a large number of play areas, which was first implemented in the Mega – Belaya Dacha mall in December 2013. Ten largest stores in the chain were remodelled to the new concept.

Detsky Mir's share in total children's retail market



The key growth segments in 2014 were toys and baby products where the market share of Detsky Mir in 2014 rose from 13.2% to 16.3% and from 9.2% to 11.9%, respectively. These two categories are expected to remain the key growth areas in 2015. Thus, according to a forecast by Synovate Comcon, in 2015 the market share of Detsky Mir in the toys category will reach 19.7% and in the baby products category it will expand to 13.1%.

Key events

- In August 2014, the flagship Detsky Mir store was opened in the centre of Moscow in Vozdvizhenka St. With a total area of 7,000 m², the store became the largest children's goods store in Russia, and also a leader in the Detsky Mir chain in terms of customer traffic and sales in two months after opening.
- In December 2014, Vladimir Chirakhov, CEO of Detsky Mir, became the company's minority shareholder, with a 1.08% stake, as part of a long-term incentive programme.
- In August and December 2014, Detsky Mir paid out RUB 2.5 bln in dividends based on performance in 2013 and 9 months of 2014.

* ELC stores – stores selling learning toys

Operational strategy

In 2015, Detsky Mir expects to see positive effects from the measures taken to improve operational efficiency: the launch of a unified SAP platform, modernisation of cashier services, opening of a new warehouse in Bekasovo and introduction of a new concept.

In July 2015, it is planned to launch the company's own warehouse for 70,000 pallets, which will significantly increase the speed of deliveries. This, in turn, will considerably increase inventory turnover and inventory management efficiency. The company will continue opening new stores in cities with a population of at least 50,000 people and replacing chains

of other retailers on the back of the deteriorating macroeconomic conditions.

In 2015, Detsky Mmir expects to open 60 new stores. The affordable price policy will remain the chain's priority in 2015 and subsequent years, which will help to attract new customer and increase loyalty among the existing clientele. Online sales will remain the key driver of Detsky Mir' development as a multi-channel retailer. All initiatives which were launched in the pilot format, namely, electronic kiosks, online application for smartphones, in-store pick-up service will be actively used to maximise the customer interaction efficiency.



Nº1

on the market for children's goods in Russia



7,000 M²

the largest toy store in Russia



123%

growth in the online store's revenue



38%

gross profit margin



1.6x

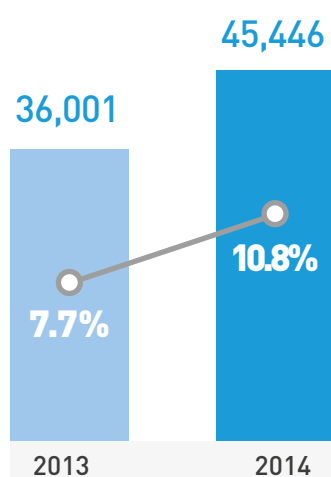
Net debt/OIBDA



Financial results of Detsky mir

RUB million	2014	2013	Change
Revenue	45,446	36,001	26.2%
OIBDA	4,910	2,771	77.2%
Operating income	4,170	2,137	95.1%
Net income attributable to Sistema	2,043	1,299	57.2%
Net debt	7,866	5,062	55.4%

Detsky mir revenue and OIBDA margin



■ Revenue, mln RUB

○ OIBDA margin

Detsky mir saw its rouble revenues increase by 26.2% year-on-year in 2014 to RUB 45.4 billion as a result of double-digit growth in like-for-like sales and high revenue growth in the stores opened in 2012 and 2013. Like-for-like sales increased by 13.6% year-on-year in rouble terms.

A minor decrease in gross margins in 2014 was due to the rouble depreciation against global currencies and the need to maintain affordable prices at our stores, which ensured additional incoming traffic.

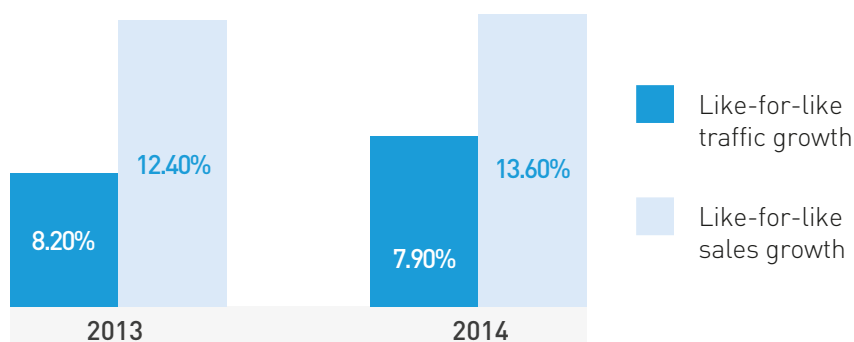
Double-digit growth of like-for-like sales resulted from a competitive price policy, marketing activities and improved merchandising.

The key driver of like-for-like sales growth was increase in traffic, i.e. inflow of new customers and higher conversion. Opening of new stores in the new format, an attractive loyalty programme and competitive prices will encourage like-for-like sales growth in the future.

Detsky mir's OIBDA in rouble terms grew by 77.2% year-on-year in 2014. The OIBDA margin increased to 10.8% in 2014 compared to 7.7% in 2013, reflecting improved operating efficiency. Detsky mir's SG&A expenses declined as a percentage of revenues to 29.4% in 2014, compared to 31.8% in the previous year.

Retailer's net debt is at a comfortable level – Net debt/OIBDA amounted to 1.6. The company's debt is denominated in roubles.

Like-for-like growth of Detsky mir



■ Like-for-like traffic growth

■ Like-for-like sales growth

MEDSI GROUP



№1 provider of private healthcare services in Russia






Medsi Group is a leading provider of private healthcare in Russia, offering a complete range of preventive, diagnostic and treatment services as well as rehabilitation services for children and adults.



Management

President – E.A. Brusilova

Chairman of the Board of Directors – M.V. Shamolin

				
Sistema's effective ownership	Revenue	Number of doctors	Patient visits per year	Healthcare facilities
75%	9.8 RUB bln	1,842	>6 mln	230,000 m²

Industry*

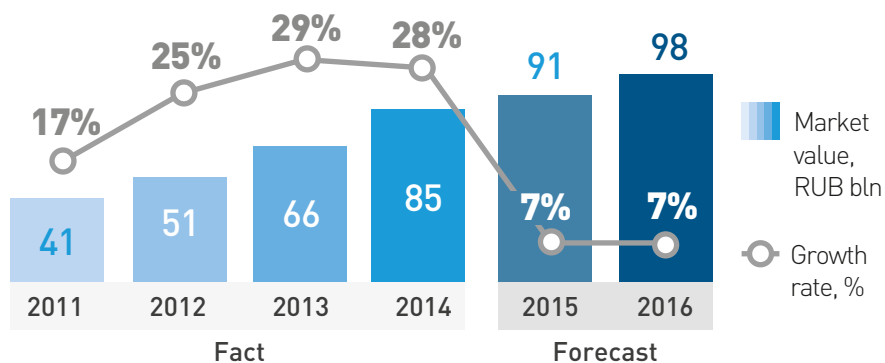
The market for private healthcare services in Russia demonstrated double-digit growth in 2014 and reached RUB 530 bln. The combined effect of structural market changes and the government's initiatives will continue to support the development of the private healthcare sector. The trend towards consolidation, and reduction in the number of public healthcare facilities, which emerged in 2013, will continue in 2015.

In 2014, the Moscow market held 28% of legal private healthcare market, which is primarily due to the fact that the VHI (voluntary health insurance) segment is much

more developed in the capital. Over the last 5 years, the private healthcare market grew more than twofold, reflecting a considerable in-

crease in the number of private clinics and a higher quality of services compared to free public healthcare and shadow healthcare services.

Private healthcare market in Russia, bln RUB



* Sources: Biznesstat, analysis of the Company.

The value of the VHI segment, which has historically been showing high growth rates, amounted to almost RUB 100 bln in 2014, up 50% from 2009. The Moscow market, which accounts for more than 60% of the total VHI market, is characterised

by a high concentration of large corporations and dynamic growth of businesses that are the main customers of insurance companies.

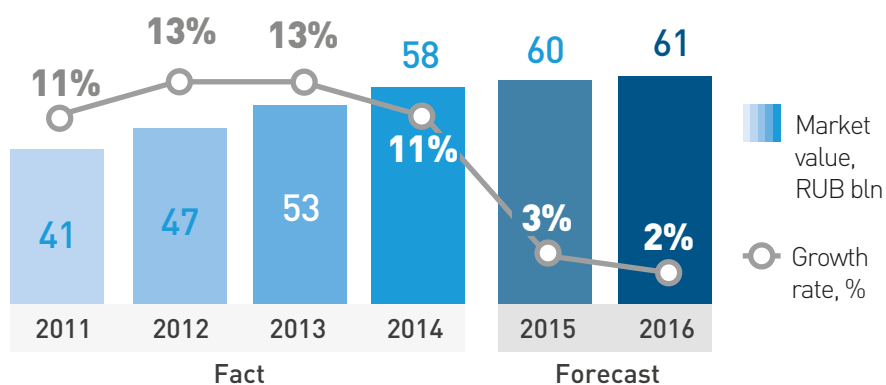
The VHI segment exhibits a strong correlation with the economic and

business environment in Russia. The economic downturn results in a reduction in the scope and options of VHI programmes and, in some cases, VHI being denied to some employees.

In the next year, the healthcare industry will mainly be shaped by ongoing reforms stimulating the public and private sectors to consolidate their efforts to further develop the healthcare market in the country. There is a tendency towards engaging private clinics to provide services under OHI (obligatory health insurance) programmes; initiatives are being proposed to enable patients to pay extra on top of the fees covered by OHI or set off their expenses against VHI and to grant certain benefits to healthcare facilities.

Moreover, the government is taking measures aimed at curbing under-the-counter payments for medical services, which currently account for about 25% of the entire healthcare market.

Voluntary medical insurance market in Russia, RUB bln



Steady growth in 2014

Medsi is the largest federal chain of clinics, serving more than 6 mln patients every year. Its market

share by revenues amounted to 2% in Russia and over 6% in Moscow in 2014.

MEDSI medical facilities

Moscow

- 1 clinical diagnostic centre
- 16 clinics
- 3 hospitals
- 2 sanatoriums
- 3 wellness centres

Regions

- 7 clinics
- 1 sanatorium (Yalta)



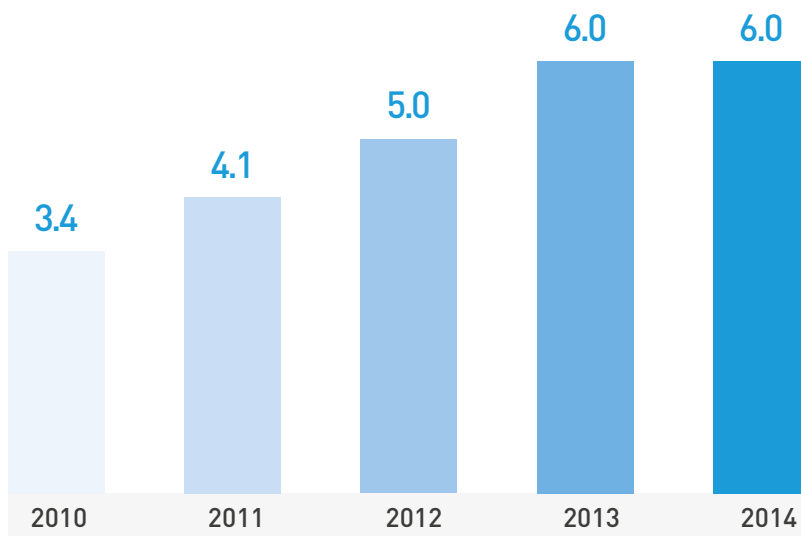
In 2014, the construction of the second flagship clinical and diagnostic centre with a total area of 22,000 m² was started at Krasnaya Presnya. The centre will offer a complete range of outpatient and diagnostic medical services, as well as inpatient treatment and rehabilitation services.

Last year, four inefficient loss-making clinics were closed in the regions; however, Medsi continued its development in Moscow by opening a new clinic for outpatient primary and diagnostic care.

After the integration with SUE Medical Centre assets was

completed in 2014, the company launched a large-scale investment programme to modernise its assets and install new high-tech equipment, introduce new medical services and modern treatment methods, and establish cross sales within the Group by providing a full range of medical services.

Patient visits growth at MEDSI, mln



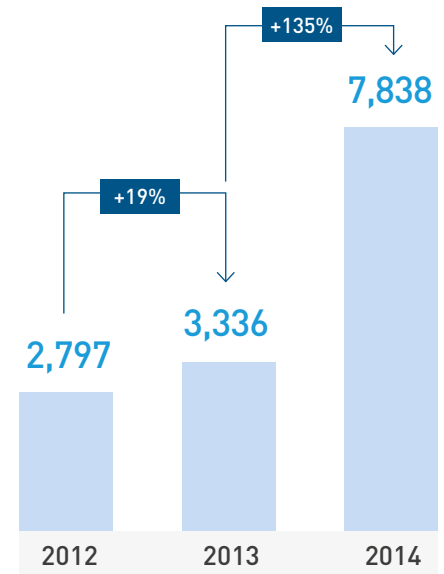
Medsi started implementation of the first reconstruction phase at the hospital in Otradnoe in collaboration with Royal Philips and works to convert one of its outpatient clinics into a modern children's healthcare centre in cooperation with Vamed.

The key initiative for the Group's business efficiency improvement in 2014 was restructuring of the management system, granting additional powers and responsibilities to key assets and at the same time optimising the motivation system. In addition, the company continued to improve business efficiency by introducing a cutting-edge unified IT system and expanding medical space in two existing clinics.

The introduction of new high-precision diagnostic equipment and modern surgical appliances resulted in substantial shifts in the quantity, quality and scope of provided medical care.

Improved efficiency of clinical hospitals is largely due to the implementation of new technologies; in particular, the company gradually transitioned to a laparoscopic approach which is now used in most surgeries, thereby increasing the patient flow and reducing the duration of their stay in the hospital. As a result, the total number of surgeries performed increased by 135%, while the occupancy rate in clinical hospitals in Otradnoe and Botkinsky proezd reached 43% and 65%, respectively. In the near future, the company will implement invasive arrhythmology and open a full-service pain management clinic.

Number of surgeries



The refurbishment of its asset base has enabled Medsi to obtain licenses and quotas for high-tech medical care (HTMC) under the state programmes from the beginning of 2015.

Key events

- In November 2014, Elena Brusilova was appointed President of Medsi Group.
- In January 2015, at the World Economic Forum in Davos, Medsi and Royal Phillips announced a new joint initiative to set up a new unique training centre on the basis of Medsi's assets.



Operational strategy

The company's strategy is focused on organic growth and selective investments in the most successful and efficient healthcare assets. The key long-term drivers for growth include investment projects scheduled for 2015, such as launching the clinical and diagnostic centre on Krasnaya Presnya, completing modernisation of the surgery, intensive care and sterilisation units in the hospital in Otradnoe, creating a radiology unit in Otradnoe, renovating the outpatient clinic in Khoroshevsky proezd and creating a specialised children's clinic on its basis.

In addition to the large-scale investment programme, the company will increase its patient flow and improve operational and management efficiency. Strong emphasis will be placed on the retail segment: the marketing promotion programme for services and clinics started in 4Q 2014 will be continued in 2015. Medsi is

currently cooperating with all major insurance companies. Maintaining and increasing the insurance flow through new products and flexible pricing, despite the challenging economic situation, is also one of the company's KPIs. Qualifying for state quotas on high-tech medical care (HTMC) and providing services under obligatory health insurance programmes at affordable rates, will present additional opportunities for Medsi.

The company's optimisation programme provides for creating an efficient and manageable business process chain. A new unified information system to be implemented in 2015-2016 will help cut the managing company's expenses through automation. In 2014, the incentive system for the operational staff and management was updated to include a variable component linked to individual performance and financial and operating KPIs.

The decline in the purchasing power caused by the deterioration of the macroeconomic environment is affecting the private healthcare segment. The most significant drop in demand is expected in the regions with a low average income per capita.

Financial results of Medsi

RUB millions	2014	2013	Change
Revenue	9,767	9,362	4.3%
OIBDA	866	1,408	(38.5%)
Operating income	382	970	(60.6%)
Net income attributable to Sistema	533	1,011	(47.3%)
Net debt	(1,003)	(4,415)	77.3%

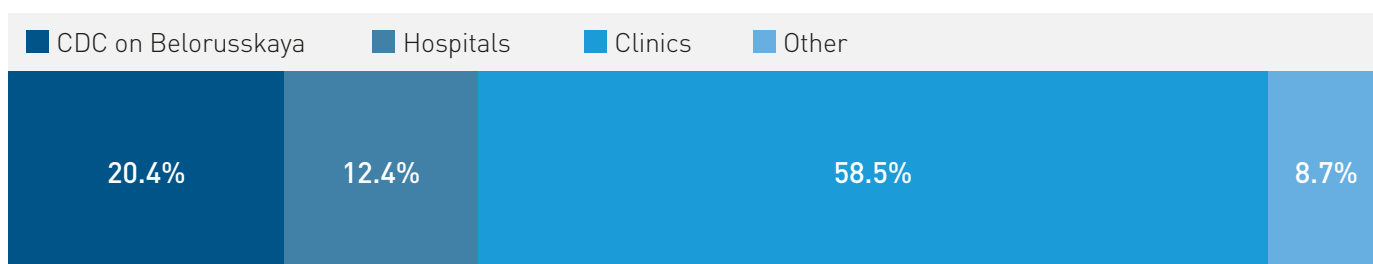
Medsì's rouble revenues grew by 4.3% year-on-year in 2014, reflecting an 0.7% rise in the number of patient visits to 6.035 million, and a 4.0% increase in the average bill in rouble terms, which totalled RUB 1,618.

The share of individual contracts in the company's revenues decreased by 2.0 p.p. to 22%, while the share represented by insurance companies and legal entities increased to 42% and 11%, respectively.

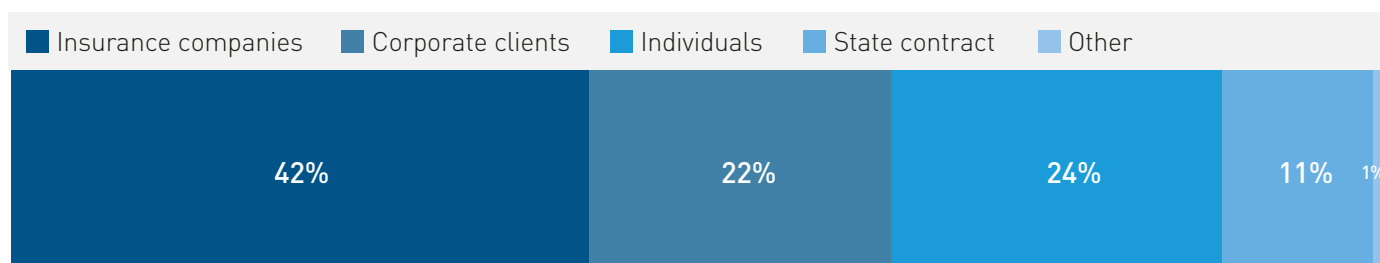
Healthcare facilities in Moscow and the Moscow region were the biggest

contributors to the Group's revenue. In 2014, they accounted for 88.1% of MEDSI's revenue. This growth was largely driven by a strong increase in the revenue generated by CDC on Belorusskaya, which increased by 12.9% (with an OIBDA margin of 45.9%) and accounted for 20.4% of the Group's total revenue in 2014.

MEDSI's revenue by assets

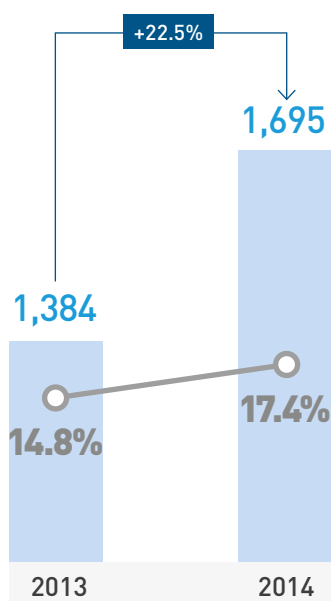


MEDSI's revenue by clients



In 2014, the Group's selling, general and administrative expenses (SG&A) rose by 22.5%, due to an increase in personnel expenses and growth of advertising and marketing expenses. Increase of personnel expenses reflected MEDSI's management system redesign and introduction of new functional areas and business units. Growth of advertising expenses resulted from the Group's stepped-up marketing activities targeting individual customers to improve utilisation rates across its medical assets and increase brand awareness. The SG&A/revenue ratio grew to 17.4% versus 14.8% in the previous year. In the reporting period, OIBDA declined by 38.5% versus 2013 to RUB 866 million, OIBDA margin was 8.9%.

SG&A expenses of MEDSI, mln RUB

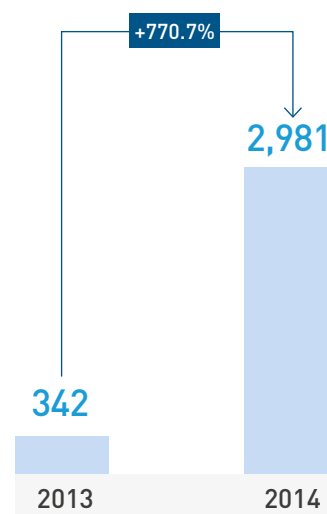


○ SG&A/Revenue
 ■ SG&A

MEDSI's CAPEX in 2014 totalled RUB 2,981.1 million, a more than eight-fold increase over the previous year.

In 2014, Medsi launched three investment projects in Moscow, including the construction of a new clinical and diagnostic centre in Krasnaya Presnya, which will include an adult and children's in-patient hospital. This new clinical and diagnostic centre is scheduled to open in the second half of 2015. The company also started the renovation of its clinics in Otradnoe and on Khoroshevskoye highway, the latter is to be converted into a specialised children's clinic.

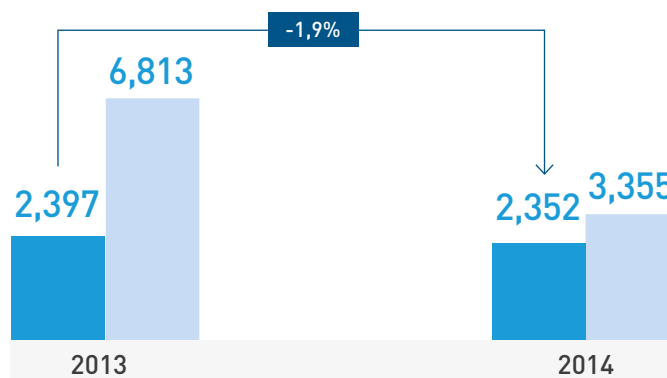
MEDSI's CAPEX, mln RUB



As of 31 December 2014, the Group's total debt stood at RUB 2,352.3 million versus RUB 2,397.3 million at the end of 2013. All liabilities of the Group are denominated in

roubles. Most of MEDSI's debt (67%) is made up by long-term liabilities with maturing in 3-5 years. As of the end of 2014, MEDSI had a net cash position of RUB 1,003 million.

MEDSI's debt, mln RUB



■ Total debt
 ■ Cash position

LESINVEST GROUP (SEGEZHA)

LesInvest Group is a vertically integrated pulp and paper company with a full cycle of timber harvesting and advanced wood processing operations.

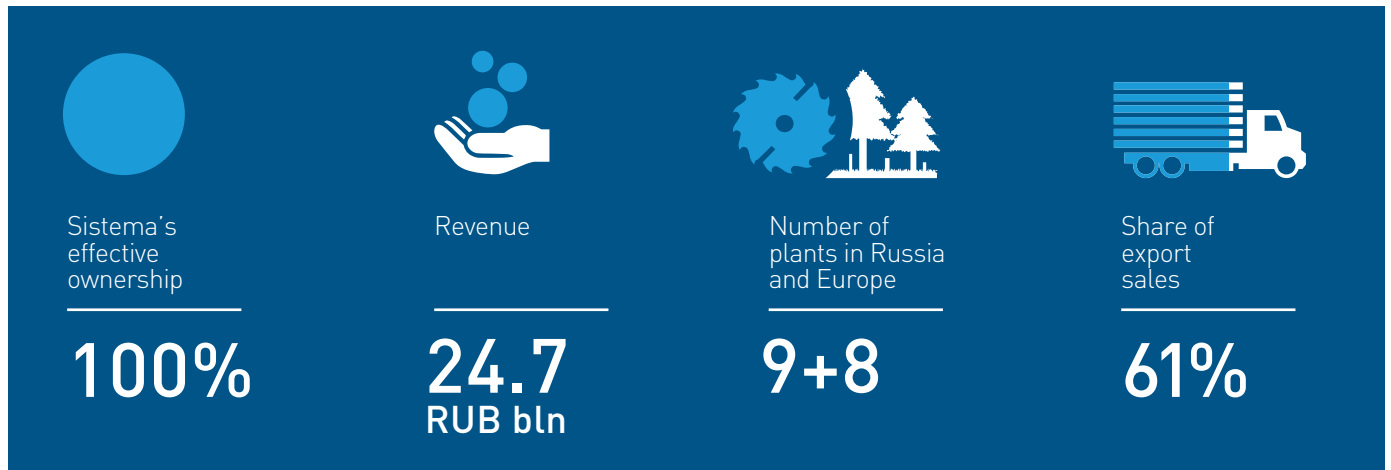
LesInvest Group manufactures pulp and paper products, paper sacks, birch plywood, chipboard, and fibreboard.



Management

President – S.A. Pomelov

Chairman of the Board of Directors – A.M. Uzdenov



Industry*

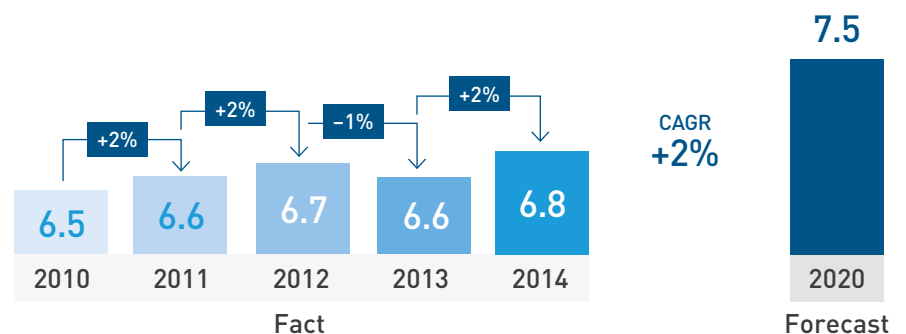
Sack paper

The share of sack paper in the global paper packaging consumption amounts to 3%. The global sack paper market is dominated by unbleached sack paper, accounting for 87%.

Over the next 5 years, the global market for unbleached paper is expected to grow at 2% annually, with consumption growth to be led by Asia, Latin America and the Middle East.

* Source: LesInvest, Vision Hunters, RISI, Enter Vision, BNP Paribas UNECE, Bloomberg, Morgan Stanley, Russian Ministry of Industry and Trade, Rosstat, Federal Customs Service, Pöyry, Federal Forestry Agency, NETLA, Food and Agriculture Organization.

Consumption of unbleached paper, mln tonnes



China producers occupy 41% of the unbleached paper global market, however, this paper is of low quality. Paper quality depends on the availability of coniferous wood feedstock.

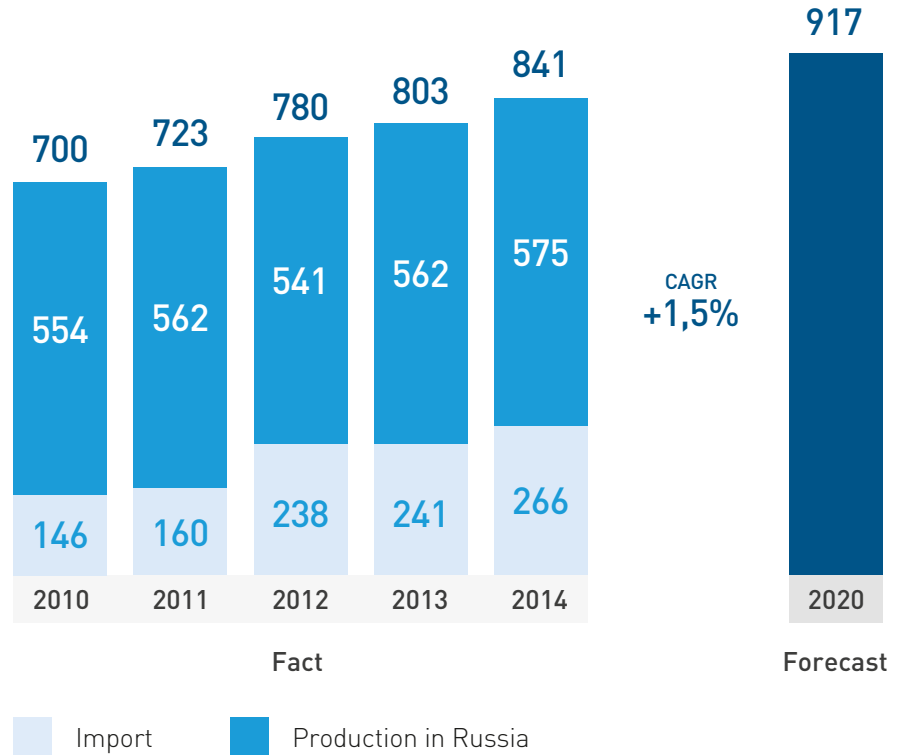
Only 21% of paper produced globally (in Europe, Russia, North America) corresponds to these standards and delivers high profitability.

Paper sacks

In 2014, the consumption of paper sacks in Russia was 841 mln pieces with 32% share of import (the main importers are Ukraine, Poland, Germany). The market is expected to grow by 1.5% annually through 2020 and is local in its nature (with geographic proximity between consumers and producers), which is due to lead time and short hauling distance benefits.

About 86% of consumers are manufacturers of building materials (cement and dry mixtures).

Production of paper sacks in Russia, mln



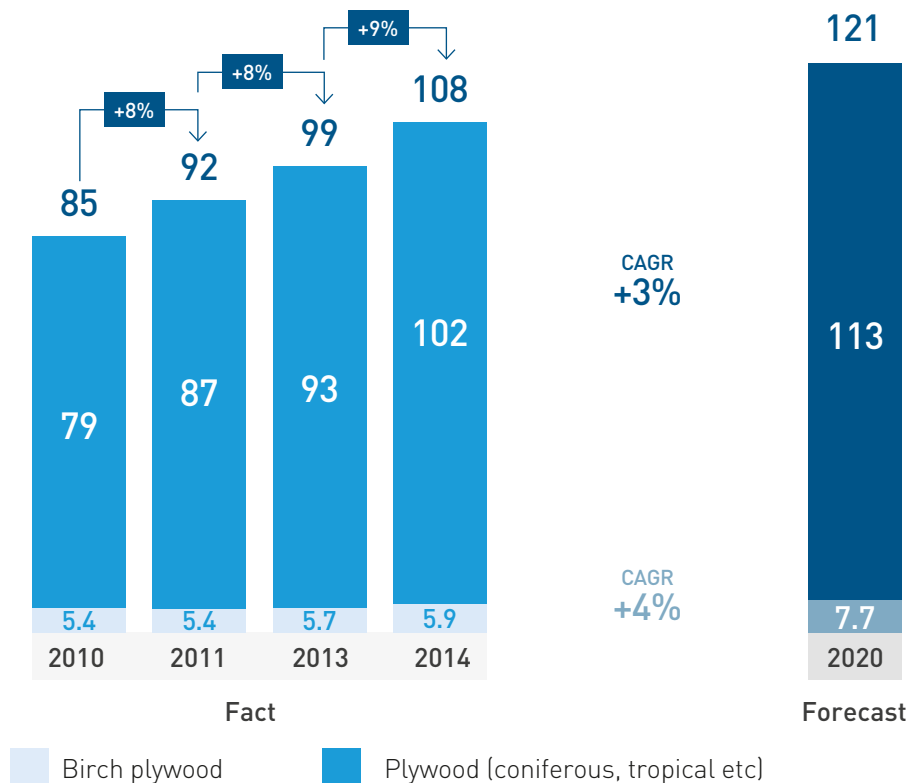
Plywood

The global production of birch plywood is approximately 5.9 mln m³. The largest reserves of feedstock (birchlogs) for plywood production are concentrated in Russia, which accounts for 53% of global market. Birch plywood is a premium segment, growing 4% annually and generating a steady growth in demand and prices.

The largest consumers of birch plywood are Europe (36%), Russia (27%) and Asia (25%). The key growth driver for the birch plywood market is development of shipbuilding, construction and machine building industries, where birch plywood is non-substitutable.

High growth in birch plywood consumption is predicted for both the mature European and North American markets and emerging markets in Asia and the Middle East.

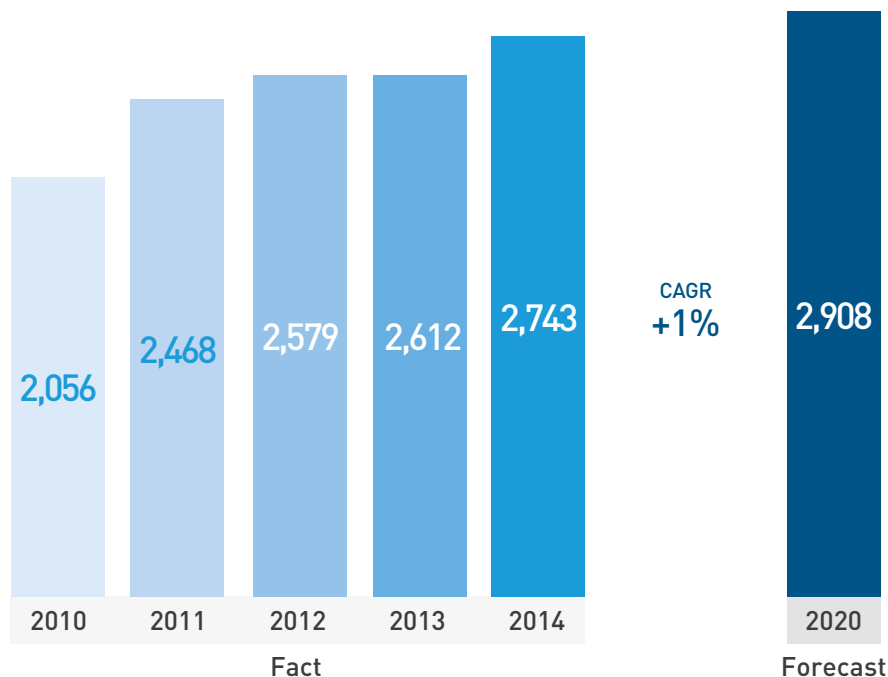
World production of plywood, mln m³



Fibreboard

Consumption of FB (fibreboard), MDF (medium density fibreboard), HDF (high density fibreboard) in Russia totals 3,438,000 m³, with approximately 24% being imported. Production in Russia is 2,743,000 m³ with only 5% being exported. The Russian market is highly fragmented with unmet demand for high-quality boards of 500,000 m³. The share of low-quality board produced by outdated equipment in Russia is still high (21%). The main consumers of wood boards are manufacturers of furniture and doors (57%); the construction industry consumes approximately 39% of the output. Total consumption growth through 2020 is expected at 1% per.

Production of timber products in Russia (fiberboards, MDF, HDF), '000 m³

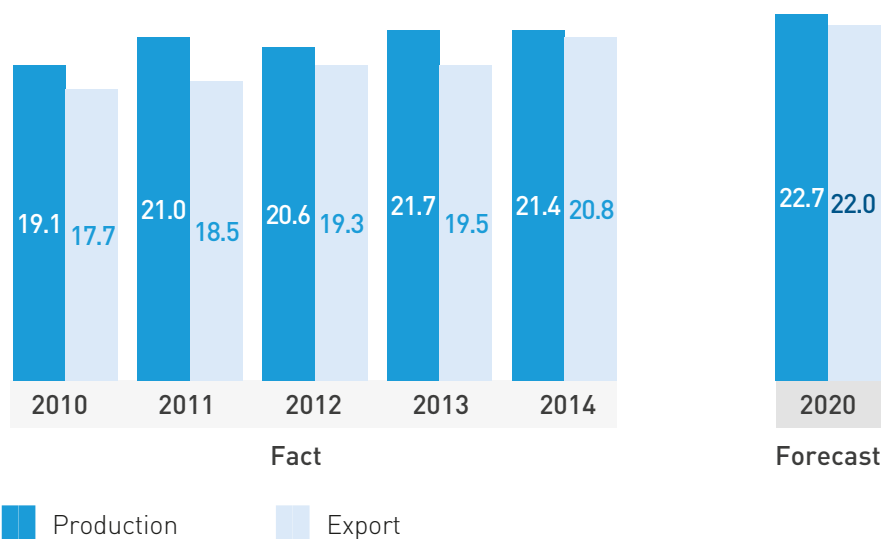


Sawn timber

Out of the 21.4 mln m³ of soft sawn timber produced in Russia, approximately 1 mln m³ per year is consumed within the country and over 90% is exported, mainly to China (32%). The sawn timber market is not saturated with top-5 companies occupying only 10% of the market in Europe and 7% in Russia. The bulk of consumption growth is expected to take place in China, USA, Russia and is estimated at 1.2% per year.

Stagnation in the European market may lead to a drop in sawn timber prices in the short run, while in Asia prices are expected to rise, reflecting growing construction rates and positive GDP growth. The main consumer of sawn timber is the construction industry.

Production and export of sawn timber in Russia, mln m³



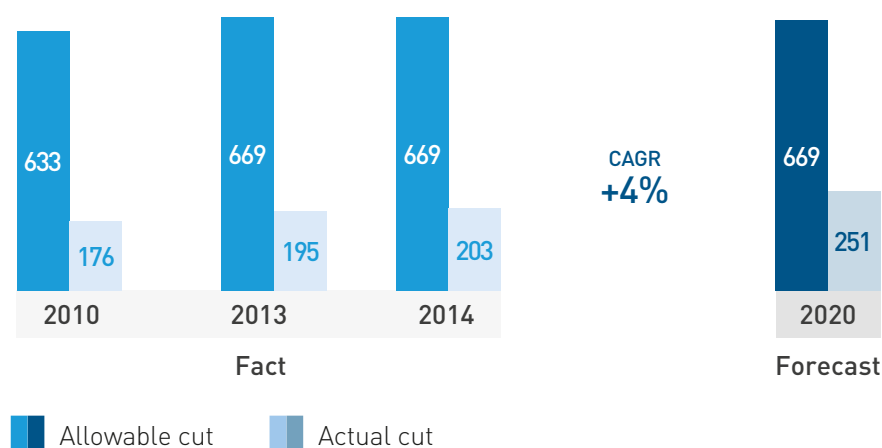
The largest sawn timber producers are located in the Irkutsk and Arkhangelsk regions as well as in the Krasnoyarsk territory.

Forest resources

Worldwide forest resources amount to 527 bln m³; 16% of them are located in Russia with its world's largest coniferous forests of 46.3 bln m³. Russia has a high growth potential with the annual allowable cut of 669 mln m³, which is three times higher than the actual cut.

India and China are among countries that have a deficit of forest resources, while Russia, Brazil and Finland have a potential for growth in wood harvesting.

Allowable and actual cut in Russia, mln m³



Business of LesInvest Group

On September 29, 2014, LesInvest, a subsidiary of Sistema JSFC, completed a transaction to acquire 100% of Segezha Pulp and Paper Mill and 100% of Derevoobrabotka-Proekt.

In 2014, the company conducted negotiations with the key customers and successfully secured contracts for 2015, managing to maintain sta-

ble volumes and win new customers. In 2014, LesInvest focused on the reorganisation of the procurement system, logistics services, which enabled the company to reduce wood harvesting costs and to improve the terms of wood supply contracts. LesInvest Group implemented a new efficient business model, modified the organisational structure and formed a new top

management team, which includes professionals with high expertise in the industry.

In the second half of 2014, on the back of growth in foreign currency sales, which account for 61% of the Group's total revenue, and a weakening rouble, the advantages of LesInvest Group over its key competitors both in Russia and abroad increased substantially.

Segezha Pulp and Paper Mill – sack paper

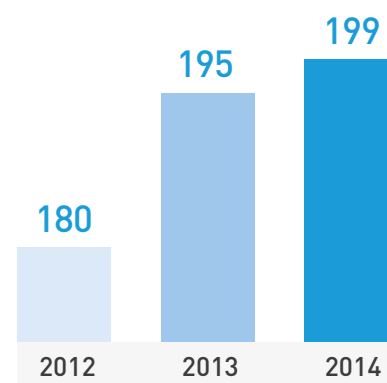
Sack paper accounts for 17% of the Group's total revenue and approximately for 25% of its foreign currency revenue.

Segezha PPM is ranked number four globally and number one in Russia in the production of high-end unbleached sack paper of European quality. Around 45% of produced paper is supplied to the converting plants of the Group producing paper sacks in Russia, Europe and Turkey. Its market share of unbleached paper production in Russia is 70%. The mill is a major

exporter supplying products to Egypt, Indonesia, Pakistan, Mexico, Malaysia, Vietnam. In 2015, Lesinvest costs, which are mostly denominated in local currency, will receive an additional competitive advantage before the importers in the form of more attractive pricing and low transport costs.

In 2015, LesInvest Group plans to implement an investment project for modernisation of Segezha PPM, which is expected to increase the sack paper output by 44% to 366,000 tonnes by 2017.

Segezha Paper Plant. Sack paper export, '000 tonnes



Segezha Packaging – paper sacks

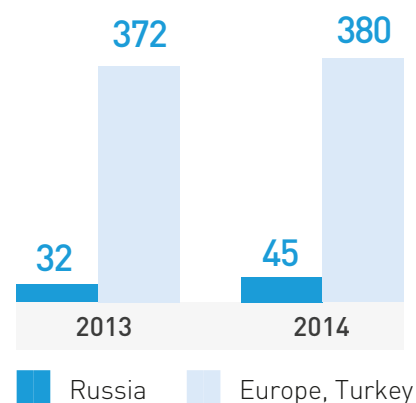
Segezha Packaging is a manufacturer of high-quality sacks, which has one plant in Russia, six plants in Europe (Netherlands, Germany, Denmark, Czech Republic, Romania, Italy) and two plants in Turkey.

Segezha Packaging is ranked number one in Russia and number two in Europe by the production of high-end paper sacks. Own resource base allows to control the cost of production. 11% of sacks produced in Russia are exported to Kazakhstan, Uzbekistan and

Kyrgyzstan. Approximately 49.6% of sacks manufactured at the plants in Europe and Turkey are supplied to Spain, Belgium, France, Hungary, Georgia, USA and Iraq.

In 2015, LesInvest Group started an investment project to increase the conversion capacity for production of paper sacks in Russia. In 2016, supported by import substitution policy, production and sales are expected to grow by 28%. The company also plans to increase maintenance capital expenditures for the plants in Europe and Turkey.

Export of paper sacks, mln



Vyatka Plywood Mill – birch plywood, fibreboard

Vyatka Plywood Mill is the fourth largest producer of birch plywood production Russia. Thanks to its advantageous geographic location (North-West of Privolzhsky Federal District), the company is able to supply products worldwide. The company uses wood feedstock certified by the FSC (Forest Stewardship Council – international organisation which created a system for certification of environmentally and socially responsible forest management). Approximately 56% of the products are exported to Turkey, Germany, Netherlands, France, USA and other countries.

In 2015, LesInvest Group will launch an investment programme to build new production facilities in the Vologda and Kirov regions. By 2020, the company expects to see a threefold increase in production of birch plywood.

Fibreboard

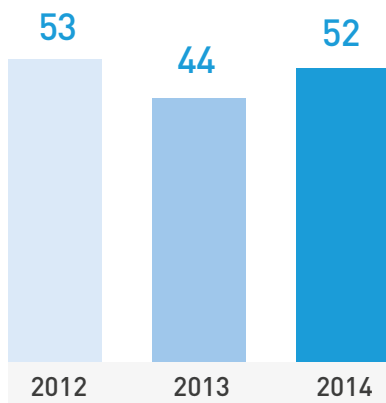
For Vyatka Plywood Mill, fibreboard is a complementary product received in the process of plywood production, enabling the company to efficiently recycle waste. The share of Vyatka Plywood Mill in the Russian fibreboard market is 5%. All products are sold domestically.

Sawn timber

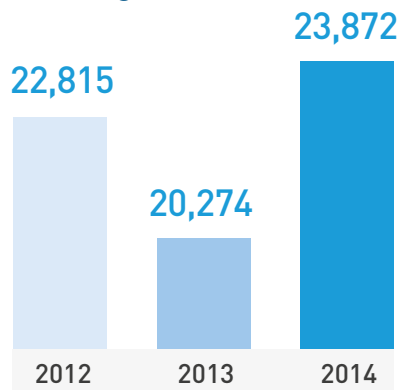
LesInvest Group is a vertically integrated company, which also owns timber sawing facilities making it possible to achieve synergies between the Group's business segments. LesInvest Group holds a 1.4% share of total sawn timber production in Russia and a 3% share in the North-Western Federal District, where major producers are located.

The bulk of the Group's sawn timber is produced by Sokol Woodworking Plant, Segezha Woodworking Plant and Omega Woodworking Plant. The share of export is 95%, products are supplied to the UK, Egypt, France and Belgium.

Export of plywood, '000 m³



Fibreboard production, running m²



In 2015, LesInvest Group plans to construct a new boiler plant at Omega WWP. In-house heat production will enable the company to reduce gas consumption and benefit from cost reduction.

Complete house sets

Sokol WWP is the only company in Russia producing high-quality laminated veneer lumber (LVL) and complete house sets. The plant holds a 15% share of the LVL market in Russia. Sokol WWP is ranked number one in Russia by the production of complete house sets and LVL. The average annual growth rate of this market is expected at around 4.5% through 2020. LVL is an export product which is supplied to Italy, Germany, France, Slovenia and Japan. In 2015, LesInvest Group plans to build a new boiler house at Sokol WWP.

Wood feedstock

Wood feedstock is a major cost item in the cost structure of LesInvest's product portfolio (30% to 60%). Own resource base allows the Group to control the cost of production and guarantees feedstock security. The Group includes 15 wood harvesting companies located in the Republic of Karelia, Kirov, Vologda and Arkhangelsk Regions. The annual allowable cut for LesInvest Group is 4.5 mln m³.

In 2015, LesInvest will continue implementation of the investment project to renew its fleet of lumber trucks, logging and auxiliary equipment. Investments are also planned to build forest roads. These steps will allow it to substantially increase the utilisation of allowable cut.

Key events

- On September 29, 2014, LesInvest LLC, a subsidiary of Sistema JSFC, completed a transaction to acquire 100% of Segezha PPM and 100% of Derevoobrabotka-Proekt.
- In 2014, LesInvest Group implemented the Wood Supply Project to renew logging and auxiliary equipment at key production facilities of the Group.
- The head office of LesInvest Group was relocated from Moscow to Petrozavodsk (Republic of Karelia). This relocation will create additional jobs in Karelia and increase contributions to the Republic's budget.
- In 2014, «Segezha Packaging» (Russia) signed a contract with IKEA to supply paper consumer packaging (bags with handles). In 2015 it is planned to increase the volume of supply by 30%.
- In February 2014, «Sokolsky DOK» won the award of Lesprom Awards-2014 for the project «Residence of Father Christmas» in the Olympic Sochi in the category «Design of wood». The construction of the residence took 110 cubic meters of timber. The palace was built in the coastal area of the park near the Iceberg Ice Palace, which held the Olympic figure skating competitions.
- In 2014, «Sokolsky CBK» in the competition of the Golden Mercury National Prize was awarded a diploma as «The best company-exporter in the production of consumer goods».
- In 2014, Vyatka FC made the first deliveries of birch plywood in Saudi Arabia, UAE and Australia.
- As a result of the 2014 LesInvest won the All-Russian forest industry award Lesprom Awards in the category Business Strategy of the Year. (The award was established in 2002 by the online trading system Lesprom Network and it is the only professional award in the Russian forest industry). The award ceremony was not only an annual meeting place for representatives of the state, forest industry companies and the leading media but also one of the key events in the business community of Russia.

Nº1
in Russia


Nº2
in Europe




by production of high-end paper sacks

Nº4
in the world

Nº1
in Russia




by production of high-quality unbleached sack paper



Nº4
in Russia

by production of birch plywood

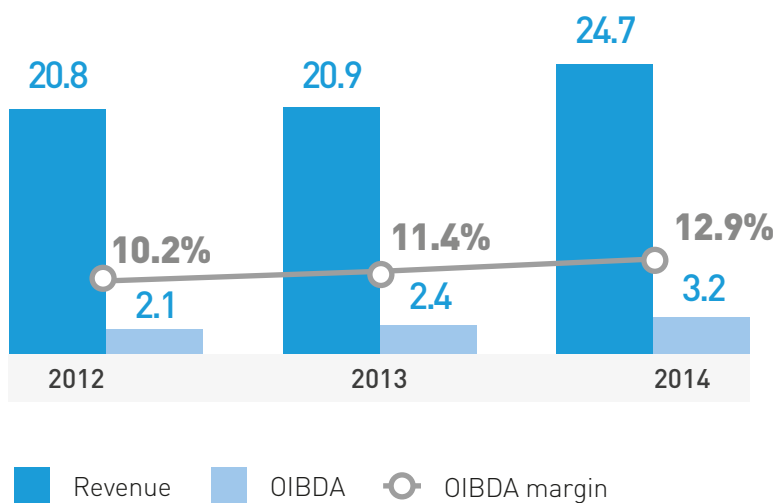


Nº1
in Russia

by LVL production

Financial Results of LesInvest*

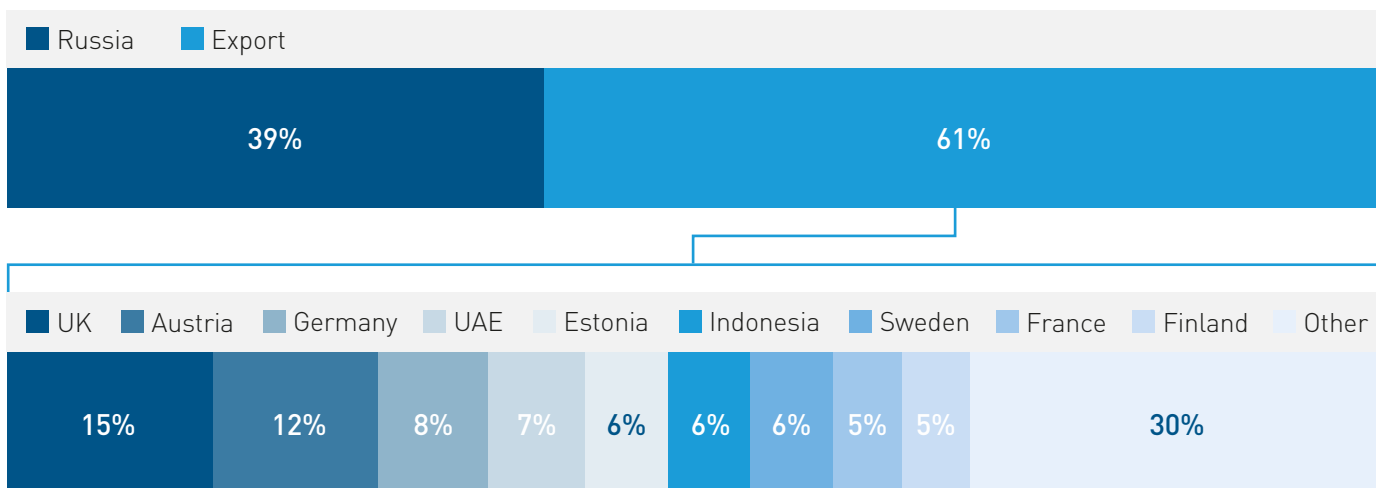
Financial results, RUB bln



Sistema JSFC consolidates the results of LesInvest in Q4 2014. LesInvest's revenue and OIBDA in Q4 2014 brought RUB 7.2 bln and RUB 1.1 bln to the Group, respectively.

In 2014, due to measures aimed at optimizing the business, LesInvest improved the OIBDA margin from 11.4 pct in 2013 up to 12.9 pct in 2014. In general, the growth in revenue was affected by the depreciation of the ruble against the US dollar and euro, given that more than 61 pct of LesInvest's revenue accounts for exports sales. Over 42 pct of all export sales are exports to European countries.

Revenue by geography

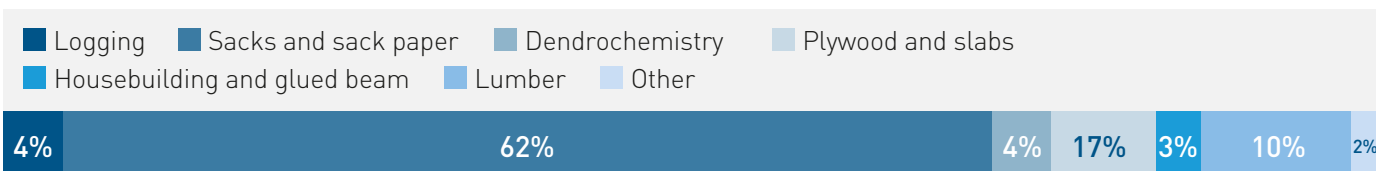


The depreciation of the ruble had a positive impact and improved the LesInvest's competitive advantage in the market. Thus, the

production cost of pouch paper reduced from 510 euro/ton to 394 euro/ton – it is the lowest figure among LesInvest's competitors.

The production cost of birch plywood at the Vyatka Plywood Factory reduced from 280 euro/cu.m to 232 euro/cu.m.

Revenue by segments



* Based on the management reporting data

In 2014, the production segment of pouch paper and paper bags brought the most of the Group's revenue – 65 pct. Operative marketing-control of market prices, elimination of the excessive number of agents in chain sales and increased demand for bleached and unbleached paper in Europe allowed for raising prices in Q3 2014, which in turn resulted in increase in revenue from pouch paper sales by 24 pct. During 2014, due to an increase demand in the market, production of high-tech paper – the highest cost-effective product among all types of paper – was actively developing.

In 2014, the revenue from paper bags has also increased by 14 pct owing to growth of construction materials production and increased demand for this product in the market. The segment profitability rose through the development of manufacture of high-margin products for dry construction mixtures.

The revenue of plywood production segment makes 10 pct in the Group's total revenue, and it increased by 13 pct in 2014. More than 50 pct of this product were exported. The growth of the segment revenue and profitability was also supported by the depreciation of the ruble.

Increase in revenue from fiberboard is due to increase both in sales volume of goods manufactured and accumulated inventories as well as to rise in market prices. Granting the deferral of payment for laminated chip boards made it possible to maintain the sales volumes, as well as to sell the accumulated stock.

The revenue from the Timber segment accounts for 10 pct in the total revenue, and in 2014 it increased by 20.1 pct, which was due to rising market prices and the currency exchange rate.

The logging segment showed an increase by 7 pct in 2014 thanks to review and optimization of current contracts, including through elimination of intermediaries. In addition, high-value assortments were sold and export supplies were increased.

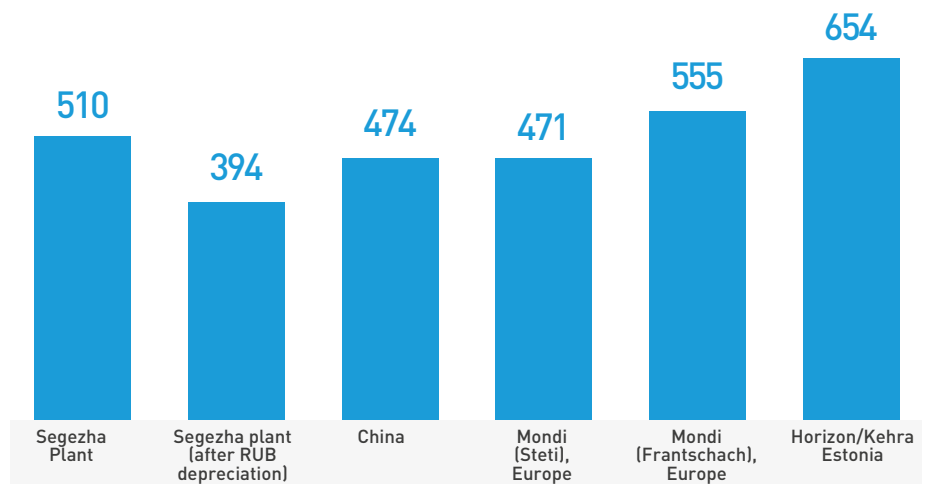
Revenue from housing construction and LVL segment grew by 9 pct

in 2014. Last year, this segment saw an increase in market prices and reduction in rates of commission fees.

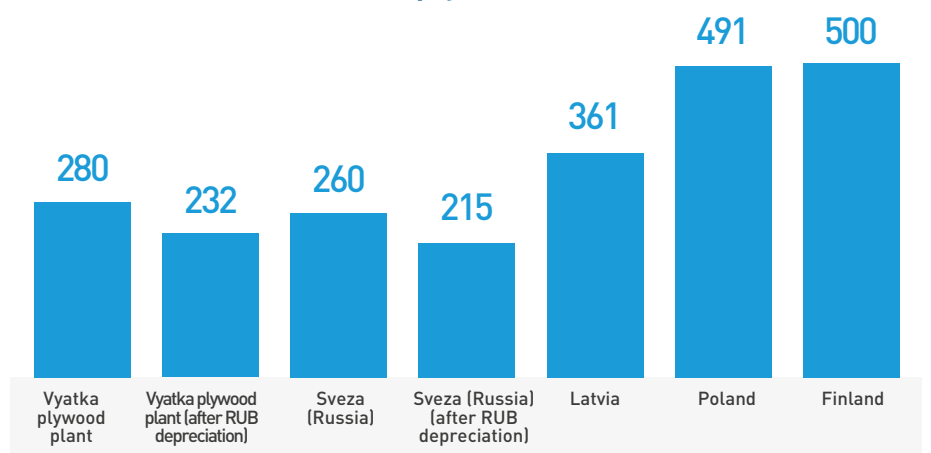
Revenue from wood chemistry segment increased in 2014 by 34 pct mainly due to the grown in demand for some products and, as a result, increase in sales volume.

Production Cost

Production cost for sack paper, EUR/tonnes



Production cost for birch plywood, EUR/m³



Own lumbering helps control the cost of wood raw material, giving additional advantages over

competitors. Production cost of pouch paper and birch veneer is one of the lowest in the global market.

BASHKIRIAN POWER GRID COMPANY

Bashkirian Power Grid Company (BPGC) is a large regional company providing electricity transmission services between central Russia and

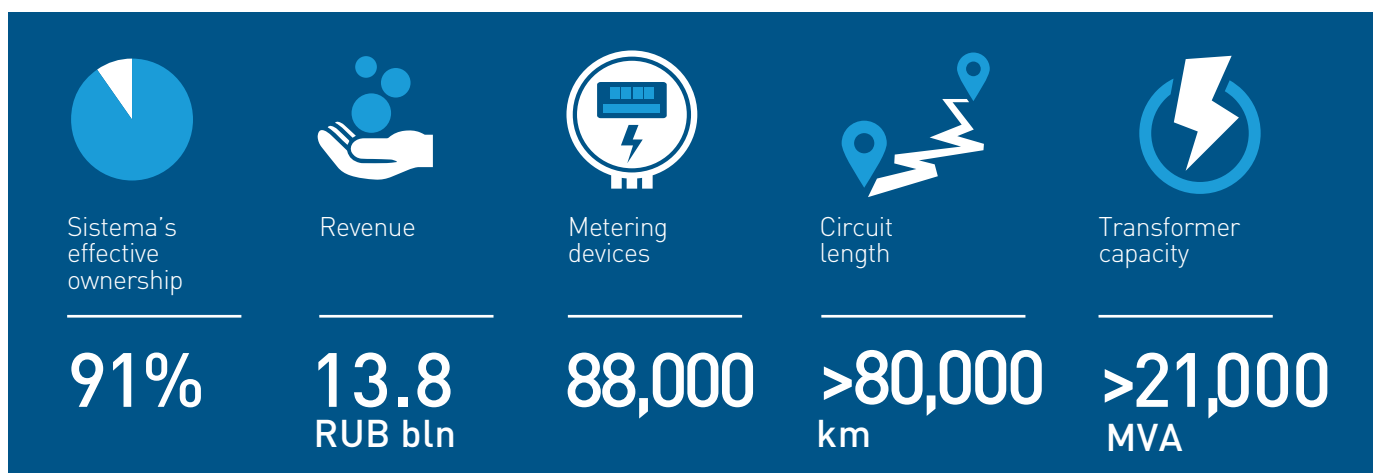
the Urals, and power transmission and distribution services to consumers in the Republic of Bashkortostan.



Management

CEO – A.Y. Makarov

Chairman of the Board of Directors – F.V. Evtushenkov

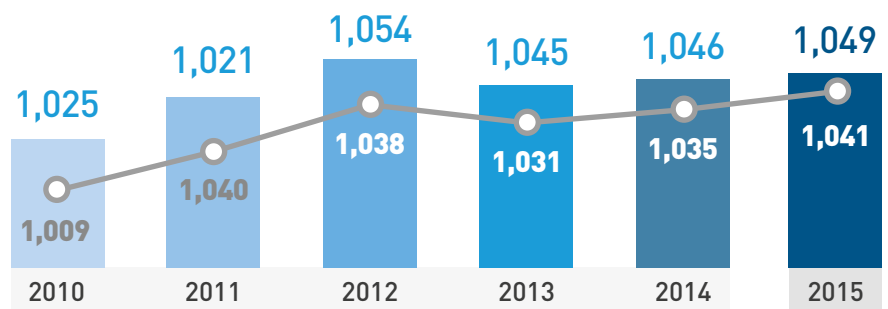


Industry*

One of the main trends in the power utilities industry is a moderate growth rate of demand for electricity, balanced with an increased efficiency of consumption. Electricity consumption in Russia grew by 0.4% in 2014 to 1,035.2 bln kW*h, while power generation increased only by 0.1% to 1,046.3 bln kW*h.

There is a considerable shift in demand - while in rural areas electricity consumption is declining, its consumption in large cities is growing considerably. At the same time, within the cities, a decline in electricity consumption in industrial zones is offset by its growth in areas where construction of office, commercial or residential properties is under-

Electricity production and consumption in Russia, bln kVt*h

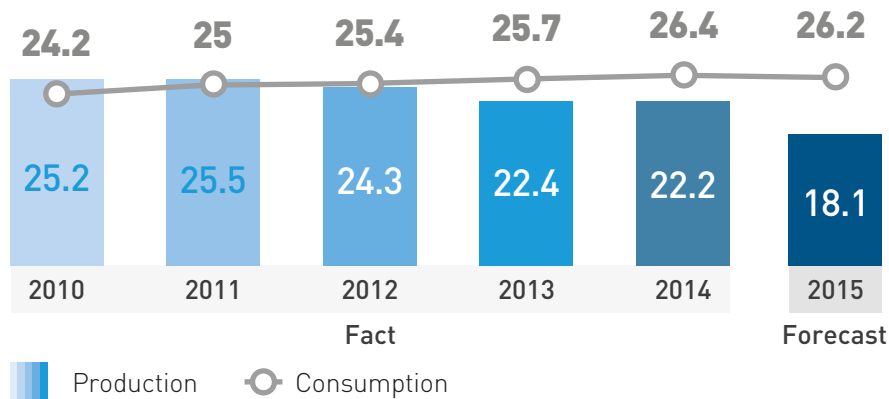


Production Consumption

way. Such changes in the geography of demand for electricity create the need to support underutilised electric grids and invest in power grids on the new sites.

* Source of information: official site of JSC "SO UPS".

Electricity production and consumption in Republic of Bashkortostan, bln kVt*h



As a state-regulated business, the power grid business is affected by frequent changes in legislation. In the autumn of 2013, the Russian Government froze the tariffs of natural monopolies for 2014, which, first of all, was aimed to curb inflation

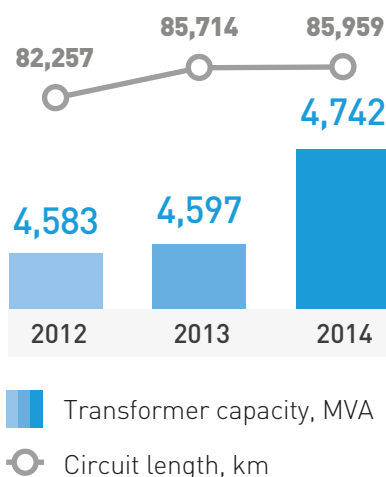
and support companies operating in the construction materials sector, wood processing, metal and mining and chemical industries. In these sectors, the costs of monopoly services account for 11% to 21% of total costs. In 2014, the increase in tariffs

for 2015 was capped at 3.8%. At the same time, according to the regional department of Rosstat, the inflation rate in Bashkortostan in 2014 was 11.2%, which is higher than in the previous five years.

Steady growth in 2014

BPGC is among the ten largest power grid companies in Russia in terms of transmitted power, and holds a leading position relative to other territorial grid companies (TGCs), that are part of Interregional Distribution Grid Company (IDGC), in terms of the total length of transmission lines in operation and the number of substations, transformer substations and distribution points.

Circuit length and transformer capacity



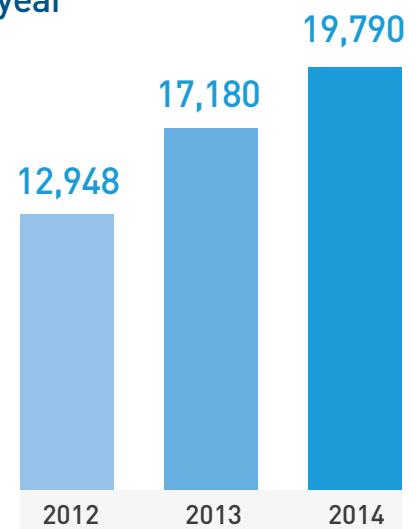
In 2014, BPGC continued installing electricity meters (Automatic System for Commercial Measuring of Power Consumption) as part of the programme aimed at improving the performance of existing power grid assets. During the project implementation, BPGC installed over 88,000 meters, resulting in a substantial reduction of actual power losses. The company also implemented new IT systems to automate project reporting and progress tracking, ensure the efficiency and transparency of business processes.

In 2014, BPGC was also developing non-regulated activities and established BPGC Engineering LLC, which acts as EPC contractor for a number of power grid infrastructure facilities in the Republic of Bashkortostan.

One of the priorities in BPGC's activities is consolidation of power grid assets in the Republic of Bashkortostan to expand the power

grid business. In 2014, the company continued to acquire and lease abandoned and municipal power grids. In particular, comprehensive preparatory work was carried out to privatise power grid assets in Ufa and Kumertau.

Number of new connections per year



BPGC's investment programme in 2014 amounted to RUB 3.3 bln. The company's capital investments in 2014 were directed towards developing the grid infrastructure in the

Republic of Bashkortostan, improving energy efficiency at production facilities and meeting the demand for electric power and capacity in the long- and medium term .

The modernisation programme is designed to create conditions for ensuring reliable power supply to consumers and reducing harmful environmental impacts.

Key events

- In 2014, BPGC's subsidiary, Bashkirenergo LLC, became the first power company in Russia to switch to a 10-year tariff regulation and to determine its rates based on return on invested capital (RAB), while rates of other power companies are set for no more than 5 years. Regulation of tariffs by return on invested capital has a number of advantages for power grid companies, consumers and the country as a whole. These include incentives to reduce costs, solid investments with favourable rates, an opportunity for distribution grid companies to plan development programmes over the long-term, as well as to improve their service quality and offer predictable tariffs. The 10-year regulation period will enable both energy consumers and energy providers to effectively implement long-term business development planning with the aim of enhancing their investment appeal. Investments into the Republic of Bashkortostan's electricity sector will total more than RUB 29 billion for the 10-year period.
- In 2014 the preliminary feasibility study for the comprehensive modernization of the electric grid infrastructure Ufa with elements of Smart Grid was completed. The pilot project (1.5% of the total project) will be implemented in April and May 2015 for the network in which it is in need to provide the maximum level of automation and observability. The main part of the project will be implemented until the end of 2020.

Operational strategy

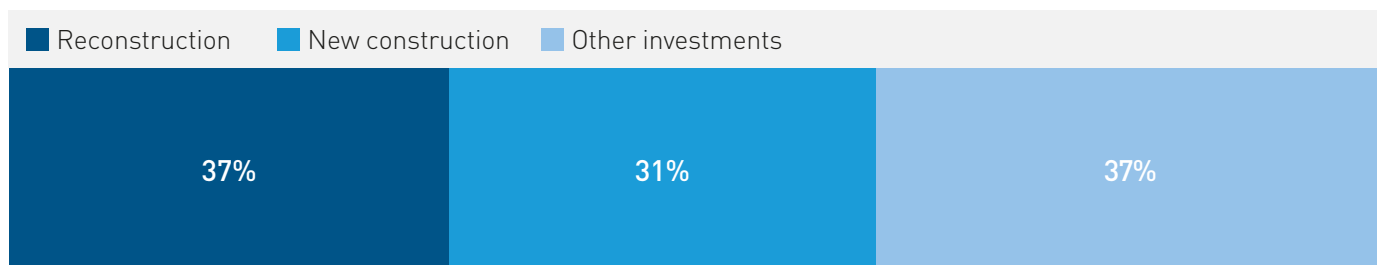
The key objectives of BPGC are to ensure reliable power supply to consumers and improve the operational efficiency of the business.

In 2015, BPGC will proceed with its efficiency improvement programme in order to reduce losses and create

a Data Centre (DC) and a Grid Control Centre (GCC). Key strategic areas include implementation of the long-term equipment upgrade programme, efficient tariff investments, reduction of operational losses. The company also plans to complete the main part of the

Smart Grid project in Ufa and TGC consolidation. As for the company's development in the non-regulated segments, the engineering company plans to replicate the Smart Grid technology in all of BPGC's assets and provide IT and communication services to customers.

Structure of capital expenditures



Financial results of BPGC

RUB millions	2014	2013	Change
Revenue	13,778	13,271	3.8%
OIBDA	5,267	5,651	(6.8%)
Operating income	3,444	3,981	(13.5%)
Net income attributable to Sistema	2,701	2,786	(3.1%)
Capital expenditures	3,262	3,054	6.8%

BPGC's revenue grew by 3.8% year-on-year in 2014, reflecting organic growth in electricity consumption and an increase in technological connections to the power grids. Boiler tariffs for transmission services were frozen in 2014.

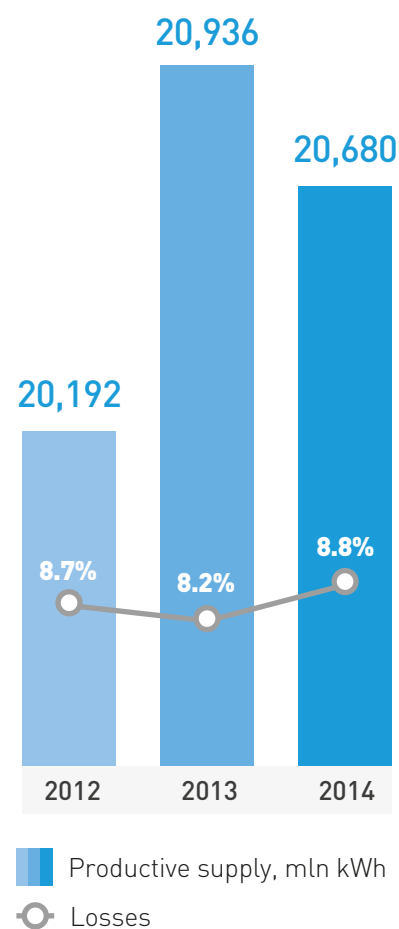
Power consumption in 2014 was up 3.2% year-on-year, largely as a result of acceleration of power connections. BPGC acquired 19,790 new consumers in 2014, 15.2% more than in 2013.

BPGC's OIBDA in rouble terms declined by 6.8% year-on-year in 2014. This mainly resulted from a rise in operating expenses in 2014 compared to 2013, as well as from the recognition of income from one-off transactions in 2013, including the disposal of fixed assets and accrued penalties for late customer payments.

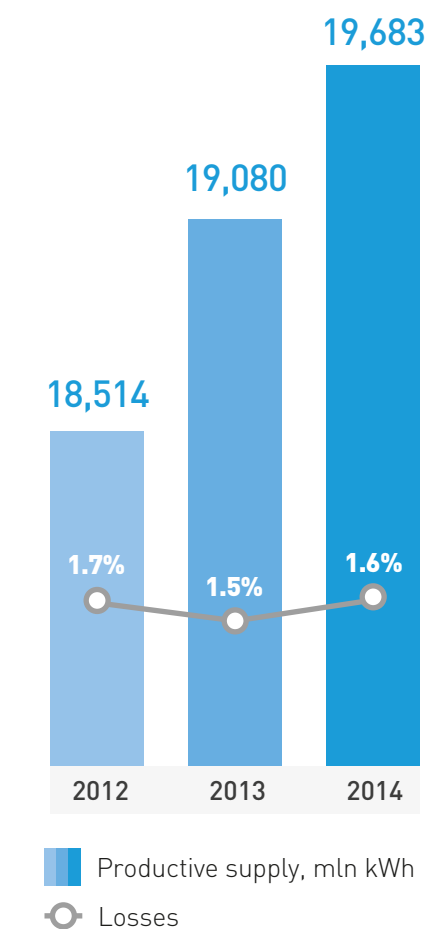
Distribution grid losses increased from 8.27% in 2013 to 8.46% in 2014, as BPGC started to operate electric grid systems previously owned by territorial grid operators (OJSC Rosenergoatom Concern and LLC Teploelektroset) from the second half of 2014, in addition to the grids already in operation.

BPGC is a debt-free company. Its capital expenditures grew by 6.8% to RUB 3.3 billion in 2014.

Distribution grids



Transmission grids



RTI

RTI Group is a major Russian industrial holding, which develops and manufactures high-tech products and infrastructure solutions using proprietary microelectronic technologies. RTI subsidiaries have their own R&D infrastructure and implement projects of unique complexity and scale in the fields

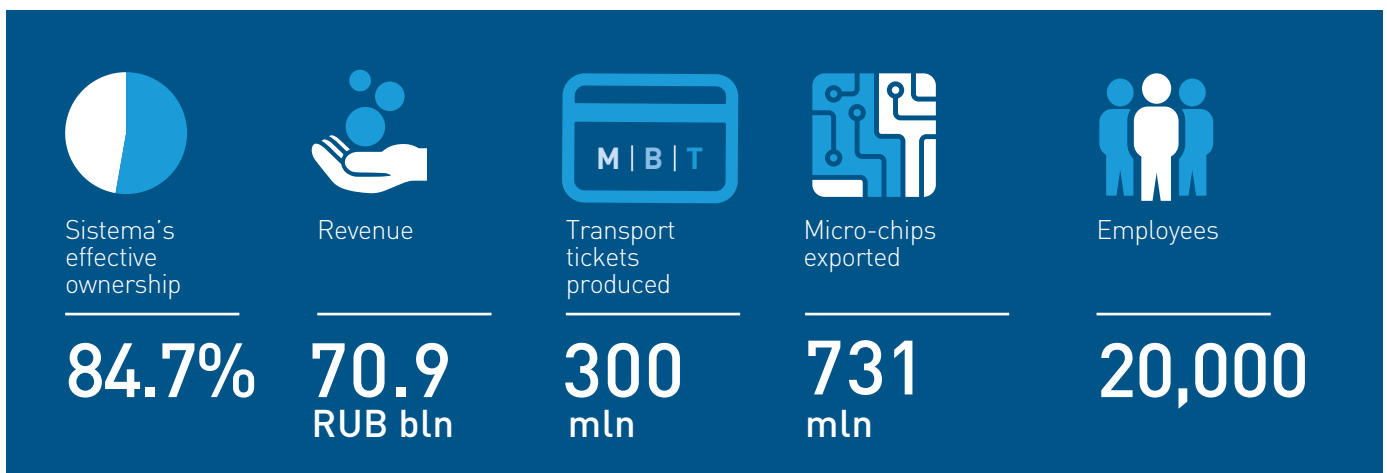
of radio communication and space technology, threat monitoring and control solutions, microelectronics and system integration. RTI was established by Sistema and the Bank of Moscow in February 2011. RTI Group includes RTI Systems Concern, NIIME and Mikron, and NVision Group.



Management

President – S.F. Boev

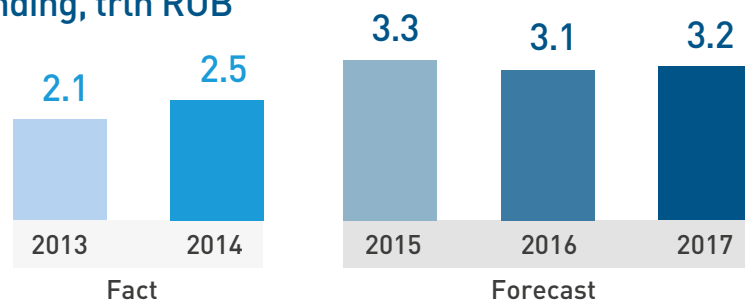
Chairman of the Board of Directors – E.M. Primakov



Industry*

The defence segment is expected to see a considerable growth in demand for high-tech products. In accordance with the approved National Arms Programme through 2020, budgetary defence spending will total about RUB 20 trln. Up to 70% of this amount is expected to be invested in procurement of new defence systems and equipment.

Russia's government defence spending, trln RUB



The Russian microelectronics market in 2014 is estimated at over US\$ 2 bln, which is only 1% of the global market. Mass civil market segments in Russia are dominated by foreign companies. Russian microelectronics companies mainly manufacture products for military and special

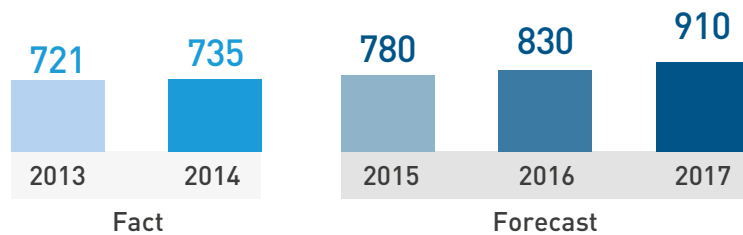
applications, which account for about 40% of the domestic microelectronics market. In the future, the microelectronics industry will be supported by the growing demand for RFID (Radio Frequency Identification) based solutions, including orders from the government. The

main demand drivers are the semiconductor segment and the telecom sector, which, given the import substitution programme, the imposed sanctions and devaluation of the national currency, is likely to boost the demand for Russian microelectronic products.

* Source: the main directions of budgetary policy for 2015 and the planning period of 2016 and 2017, RTI analysis

The Russian market of information and communication technologies in general showed strong growth with the main consumers being the top 20 largest Russian companies. The average annual growth rate in this market is forecast to stand at 10% until 2017, with the segment of integrated security systems being the most attractive one.

Information and Communication technologies market services for government and companies, bln RUB



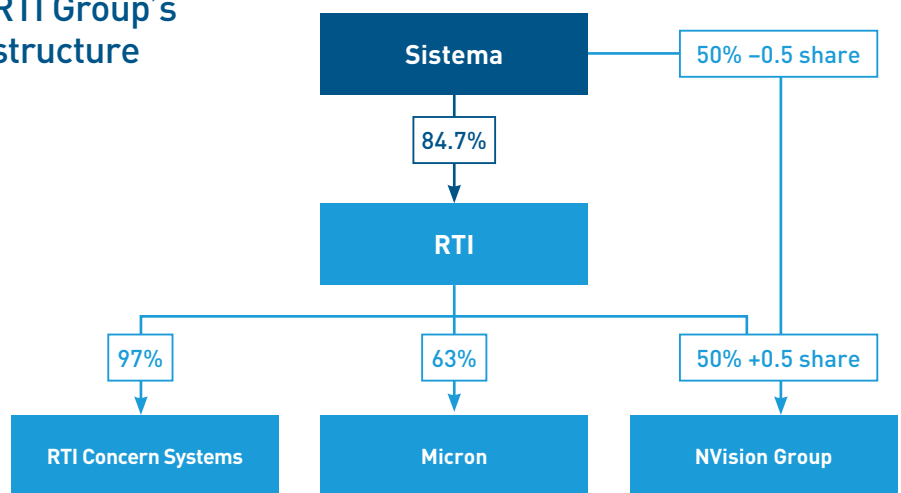
Steady growth in 2014

RTI develops assets in the defence industry, microelectronics and system integration. In 2014, Sistema developed and started implementing a restructuring plan for RTI's high-tech assets to improve its operating efficiency and profitability.

In particular, Sistema completed the transaction to purchase the shares of NVision Group («NVision») and became the sole shareholder of this company. NVision is now headed by a new management team. The system integration segment was severely hit by the economic downturn in Russia in 2014, which also affected the financial results of this business. In 2014, Sistema launched an initiative aimed at streamlining its business and cutting costs. NVision managed to retain its position in its traditional markets and maintained relationships with such anchor customers as MTS, VimpelCom, FGC (UES). Besides, the company increased its customer base by adding such major customers as the Moscow Department of Information Technologies, Transneft, Severstal, Special Economic Zones, regional governments, etc.

RTI's Defence Solutions BU demonstrated the highest growth rates with revenues rising by almost 30% in 2014. This growth was driven by active implementation of contracts

RTI Group's structure



for construction of radar stations. RTI has a big portfolio of national defence orders and the Defence Solutions BU generates the highest profit margin in the Group.

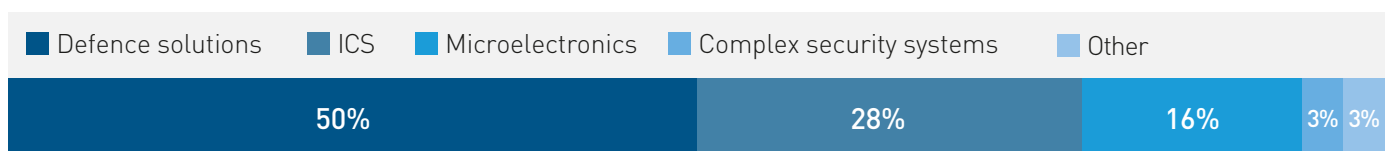
Moreover, RTI develops its own R&D competencies and pays a lot of attention to the development of R&D initiatives. In 2014, RTI started pre-project research and development of proprietary aerospace systems (ASSs), which will enable the company to enter new promising markets. A programme of cooperation between RTI and the Russian Academy of Sciences provides for a broad range of joint

activities in a number of promising areas, including the development of complex robotised energy and transportation systems.

The head company in RTI's Microelectronics Solutions BU is NIIME and Mikron («Mikron»). Mikron is the largest microelectronics manufacturer in Russia, up to 50 mln of its microchips per month are exported to Europe, USA and South-East Asia.

Currently, Mikron is implementing ca. 40 R&D projects aimed at developing nearly 100 new products, some of which are to be launched in the near future.

RTI Group's revenue structure



In February 2014, Mikron completed the development of its proprietary 65 nm chip technology and is now actively carrying out R&D work on the 45 nm technology. Micron Group has set up a complete production chain from chip development to the final product, which allows it to produce the entire range of high-tech products for the mass market: intelligent chip cards – smart cards, transport and other RFID cards (using Radio Frequency Identification technology), SIM cards, chip bank cards, social cards and other identification documents, new products for industrial electronics. The company supplies products to 400 customers in Russia and 100 customers in other countries. Moscow Metro, State Company Transportation Organizer from Saint Petersburg, state transportation companies in Kazan, Magnitogorsk, Tyumen, Nizhny Novgorod are among Mikron Group's customers.


In March 2014, Mikron obtained a licence from Cadence Design Sys-

tems, the world's leader in e-design innovations, for chip design software using 90 nm technology.

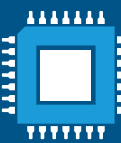
In 2014 Mikron:

- Supplied over 2 mln chips for previous-generation travel passports and 800,000 chips for biometric travel passports;
- Developed 32 types of integrated circuits for industrial and commercial applications;
- Launched production of 51 integrated circuits for various applications;
- Supplied 300 mln transport tickets;
- Exported 713 mln chips.

In 2014, RUSNANO acquired a 25.1% stake in Mikron as a result of conversion of its share in Sitronics-Nano – a joint project between RUSNANO and Mikron to set up the manufacturing of 90 nm microchips.



No. 5 in terms of microchip sales among full cycle manufacturers in Europe



500
types of microchips in production



3,500
customers



60
countries of exports

Key events

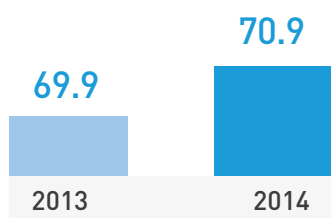
- In February 2014, Mikron became a member of the OSPT (Open Standard for Public Transport) Alliance, which was created in 2010 by the leaders of the payment industry to develop new-generation fare payment systems.
- In May 2014, Mikron became a partner of the Silicon Trust international marketing programme, which comprises more than 20 companies, including the world's microelectronics industry leaders such as Gemalto, Giesecke & Devrient and Infineon Technologies.
- In December, Mikron produced first Elbrus-2CM processors manufactured with 90nm technology. Based on these processors, MCST plans to start production of compact motherboards «Monokub-M».

Financial results of RTI

RUB millions	2014	2013	Change
Revenue	70,892	69,923	1.4%
Adjusted OIBDA	4,564	3,908	16.8%
Adjusted operating income	1,267	839	51.1%
Adjusted net loss attributable to Sistema	(4,416)	(670)	-
Net debt	37,907	29,748	27.4%

In 2014, RTI's rouble revenues increased by 1.4% year-on-year as a result of revenue growth at the Defence Solutions BU and the Microelectronics Solutions BU.

RTI Group's revenue, bln RUB



In 2014, the Defence Solutions BU delivered a 29.0% year-on-year increase in rouble revenue, following the accelerating execution of radar station construction contracts, which

were put on experimental combat duty during the reporting period.

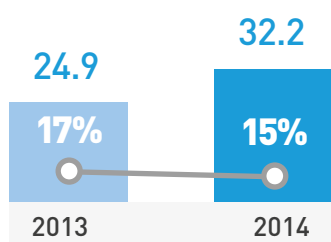
Rouble revenue at the Microelectronics Solutions BU grew by 4.1% year-on-year in 2014, reflecting higher sales of integrated circuits as a result of an increase in demand for home technology in the current economic environment. Thus, in 2014, Mikron produced more than 2.8 million chips for passports, delivered 300 million transport tickets, and exported 713 million chips. The revenue growth in both BUs was, however, offset by decreased revenues at

the Information and Communication Technologies BU.

RTI's adjusted OIBDA in rouble terms increased by 16.8% year-on-year in 2014 and by 23.6% year-on-year in the fourth quarter, following revenue growth. The OIBDA margin of Defence Solutions BU exceeded 15% and the OIBDA margin of Microelectronics Solutions BU increased to 11%. The OIBDA loss of the Information and Communication Technologies BU was reduced from RUB 2.5 billion in 2013 to RUB 0.8 billion in 2014.

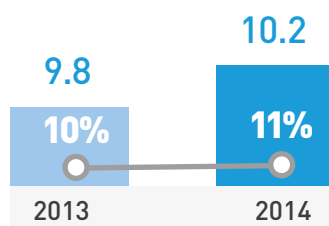
Key segments results

Defense solutions



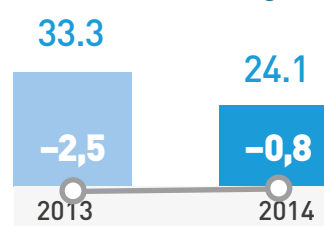
■ Revenue, bln rub
○ Adj OIBDA margin

Microelectronics solutions



■ Revenue, bln rub
○ Adj OIBDA margin

Information and Communication Technologies



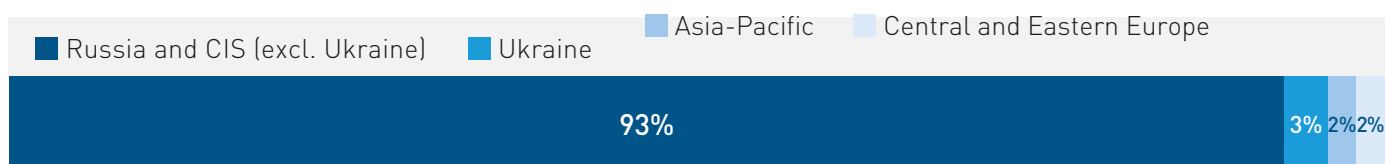
■ Revenue, bln rub
○ Adj OIBDA, bln RUB

Growth of debt in 2014 was mainly due to increased liabilities relating to the loans received under state defence contracts

from large state-owned banks against the guarantees of the Defence Ministry and with full compensation of interest (effec-

tively zero interest rate). The debt related to state defence contracts accounted for 50.1% of the total debt amount.

Sales by geography



Sales by currency



SG-TRANS

SG-trans is a leading railcar operator in Russia, accounting for about 40% of the country's LPG tank car fleet. SG-trans owns a diversified fleet with more than 34,000 rail cars

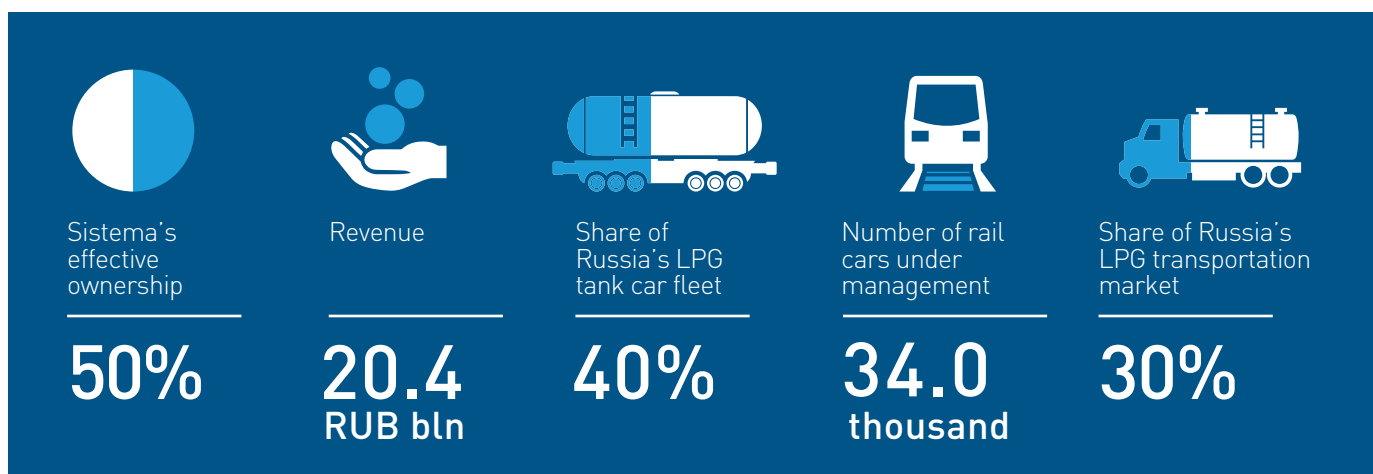
under management in 2014. Sistema has been developing the transportation business in collaboration with its industry partner Unirail since late 2012.



Management

President – A.R. Taicher

Chairman of the Board of Directors – A.M. Uzdenov



Industry*

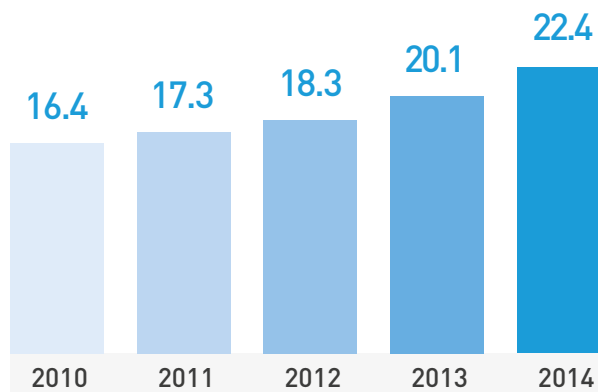
The fall in railway transportation volumes in 2014 was 0.8% compared to a decrease of 2.8% in the previous year. However, the negative trend is expected to continue due to the unfavourable market environment in 2014.

As in 2013, open-car shipments of goods such as building materials, ferrous and non-ferrous metal ore demonstrated the largest decrease. Transportation of fertilizers, grains and timber rose considerably, reflecting increased attractiveness of exports due to the rouble depreciating against the US dollar and favourable export prices. Freight volumes of liquefied gases

(LPG) – one of the main segments of ST-trans – grew by 8% in 2014, while oil cargo volumes rose by 2%

over the year. The share of SG-trans in the LPG transportation market in 2014 was 30%.

LPG gross production in Russia**, mln tonnes



* Source of information: Russian Railways, Cortes, Petromarket **

According to preliminary company data.

Despite the stagnation of transportation in certain segments, there is still a surplus of rail car fleet in the market, mainly attributable to state-owned rail car manufacturers, which is partially offset by a gradual replacement of old fleet by private carriers. The daily leasing rate for open rail cars in December 2014 dropped by approximately 25% year-on-year to RUB 425-450, for oil & petroleum tank cars it fell by 30% to RUB 600 per day, while the rate for LPG tank cars lowered only by 5% to RUB 1,400 per day.

The LPG transportation segment is expected to grow in 2015,

driven by the increasing demand for petrochemical products and launch of new production facilities. However, the growth rate will slow

down as export attractiveness will decrease amid falling prices and reduced investments in the oil and gas sector.

LPG transportation volumes on the Russian Railways network, mln tonnes



Steady growth in 2014

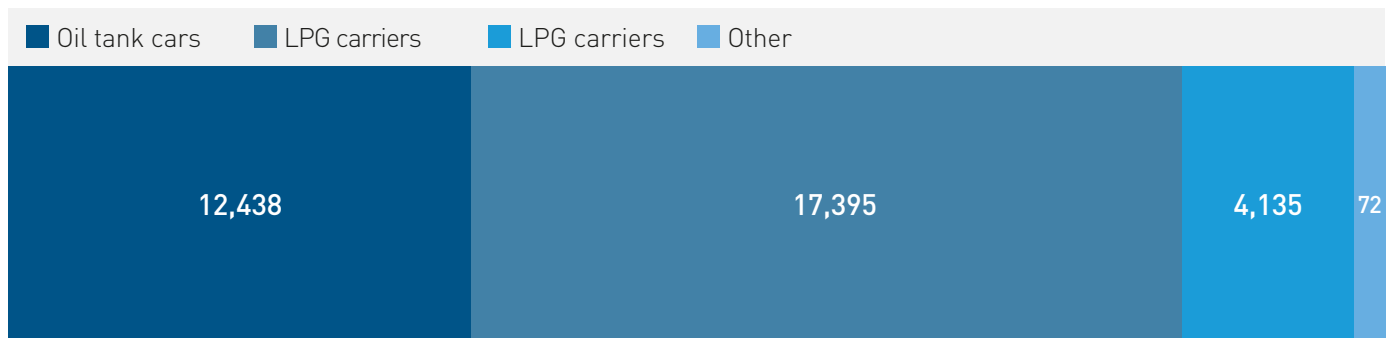
In 2014, company management focused its efforts on streamlining operational processes and optimising the rolling stock to meet customer requirements and to respond to the current market conditions. In particular, the leasing portfolio was streamlined and part of the oil and petroleum fleet was returned

to the leasing companies earlier than planned, which made it possible to reduce cash outflows caused by a drop in leasing rates and to reduce debt.

The company increased its own fleet of LPG tank cars to meet its obligations under long-term con-

tracts. About 60% of the contracts of SG-trans are long-term in nature, securing a strong market position. In 2014, SG-trans customer base exceeded 100 clients, including major oil and gas market players such as SIBUR, Bashneft, SANORS, NOVATEK, Rosneft. In 2014, Tatneft Group became SG-trans' client.

Operated fleet size and composition

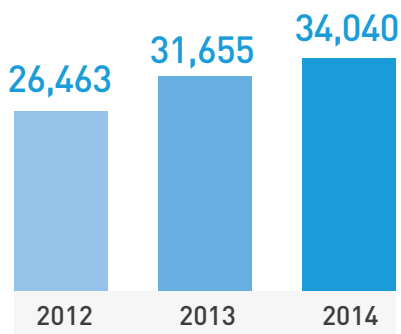


In addition, SG-trans successfully operates in the sector of the loose and bulk cargo, providing services to metal and mining companies. The company chose to take advantage

of low spot rates to rent additional railcars to facilitate volume commitments, as this was more efficient than purchasing railcars in current market conditions. The share of

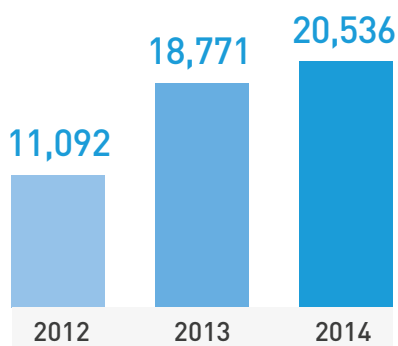
rented rail cars in the total fleet under management increased from 12% at the end 2013 to 24% at the end of 2014.

Growth of rail car fleet managed by SG-Trans



In 2014, the company established a repair management business segment and concluded repair contracts with five companies. In 2014, SG-trans repaired about 4,000 rail cars. As part of an effort to cut costs the company purchases the most expensive components directly from producers.

SG-trans loading volumes, ktonnes



Key events

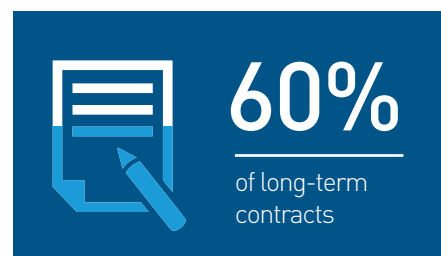
- In January 2014, the consolidation of SG-trans, Financial Alliance and Bashneft-trans was successfully completed.

Operational strategy

In September 2014, Sistema approved an updated development strategy for SG-trans, reflecting the new market environment. The main emphasis will be placed on reducing costs and debt. Oil and liquefied gas transportation will remain the company's target segment. Special attention will be paid to financial discipline and cash management efficiency. In 2015,

management will focus on maintaining and expanding contracts with current customers.

In 2015, SG-trans may purchase new rail cars, provided that favourable opportunities are presented and the demand for such cars is guaranteed. Key investments will be made in the company's own railway infrastructure and IT to reduce operating expenses.



Financial results of SG-trans*

RUB millions	2014	2013	Change
Revenue	20,429	20,119	1.5%
OIBDA	6,253	6,016	3.9%
Net income attributable to Sistema	261	439	(40.5%)
Net debt	21,700	28,010	(22.5%)

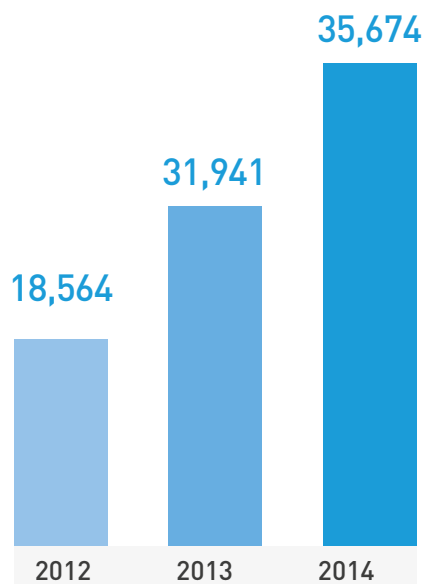
Despite the unfavourable trends in the railway freight industry, SG-trans increased its revenue by 1.5% YoY, which was driven by increased shipping volumes for LPG, crude oil and petroleum products. OIBDA rose by 3.5% YoY as a result of railcar fleet optimisation and improved repair and maintenance management.

Net income fell year-on-year due to a rise in interest expenses. In 2014,

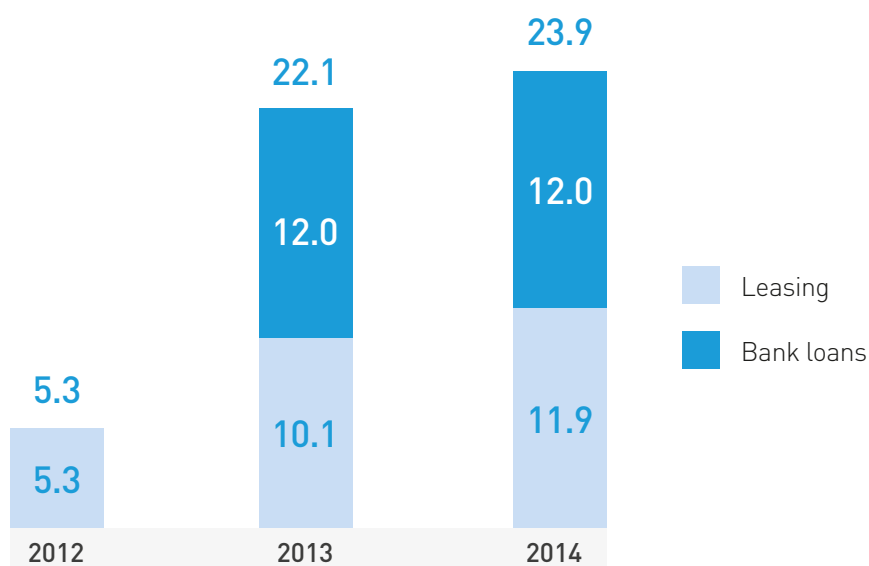
management's efforts were directed towards streamlining operational processes and optimising the rolling stock to meet customer requirements and to respond to the current market conditions. Thus, the leasing portfolio was reduced and some of the oil and petrol rail cars were returned to the leasing companies earlier than planned, which made it possible to reduce cash outflows caused by a drop in leasing rates and to decrease debt.

The railcar fleet under SG-trans' management increased by 7.5% year-on-year to 34 thousand units (including 17.4 thousand of LPG cars). The share of leased cars in the total fleet rose from 12% as of the end of 2013 to 24% as of the end of 2014. Railcars in ownership accounted for 51% of the total fleet.

SG-trans turnover, mln tonnes*km



SG-trans debt profile



* Sistema owns 50% of SG-Trans shares and does not consolidate this company in financial results. Data for 2013 are presented in accordance with US GAAP.

MTS-BANK

MTS Bank is engaged in banking activities in Russia providing a complete range of financial services to individuals and corporate customers. Being a

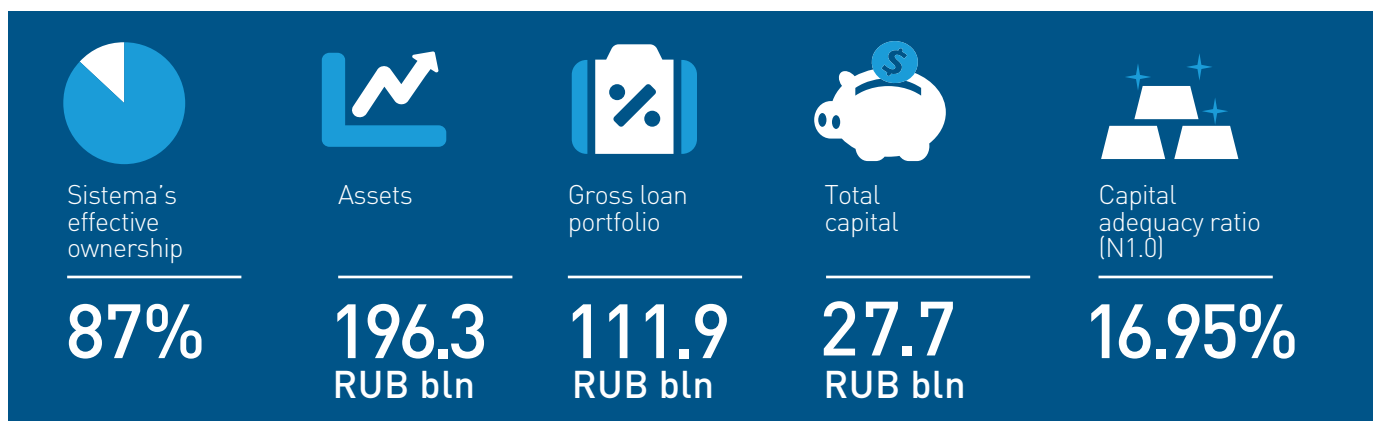
systemically important operator in the payment, lending and savings market, the bank has a strong position among Russia's largest banks.



Management

President – I.V. Filatov (before March 2015 – M.M. Chaikin)

Chairman of the Board of Directors – A.V. Abugov



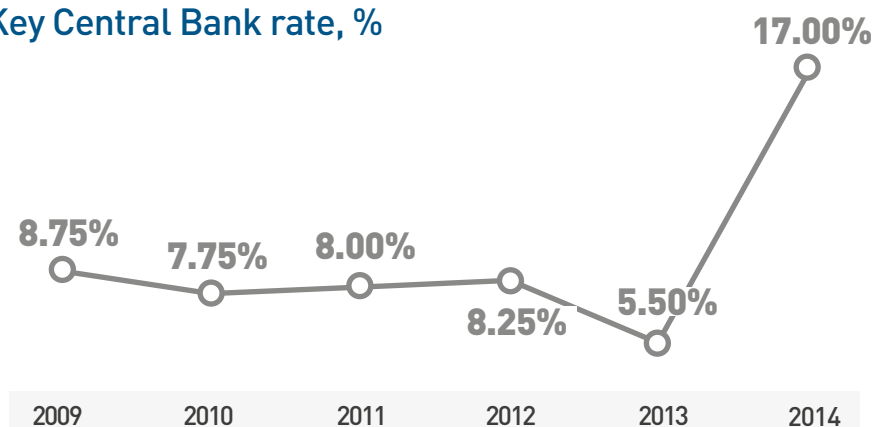
Industry*

Assets of the banking sector, trln RUB



■ Assets, trln RUB ○ Growth rate

Key Central Bank rate, %



The past year was a challenging one for the financial sector. The increase in the CBR's key interest rate from 5.5% p.a. to 17.0% p.a. and a sharp rise in interest rates on other funding sources substantially increased the cost of borrowing. The slowdown in economic growth rates prevented the Russian banks from compensating for this increase by active operations, putting serious pressure on their revenues and capital levels.

According to the year-end results, the consumer lending sector demonstrated slower growth compared to the previous years. In addition to higher interest rates and slower economic growth, consumer lending was affected by tighter regulations introduced by the CBR, a decline in real household income and gloomier consumer sentiment. As a result, retail lending growth rates dropped by half against 2013 and transactional risks increased considerably in all segments by the end of the year.

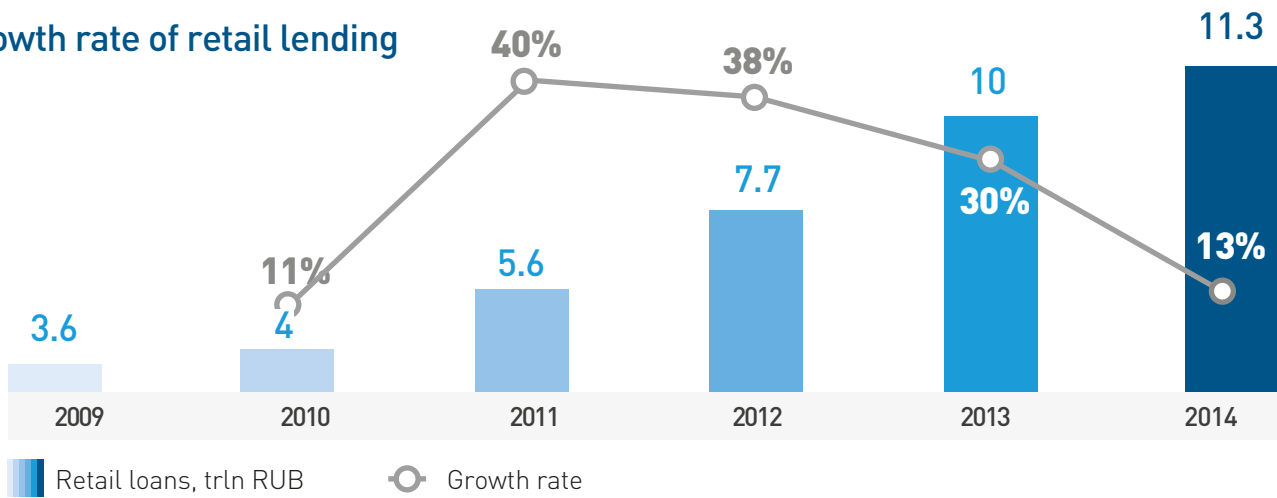
* CBR

The situation in the corporate lending segment is slightly different. The restrictions on foreign fund-

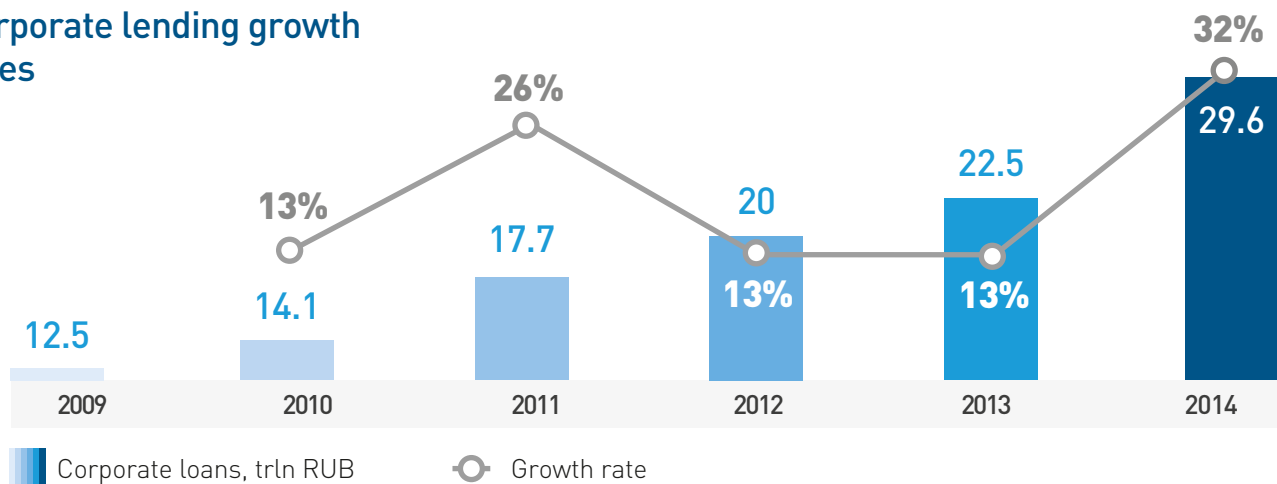
raising forced Russian companies to borrow more actively in the domestic market. According to the year-end

results, corporate lending grew faster than retail for the first time in the last few years.

Growth rate of retail lending



Corporate lending growth rates



Steady growth in 2014

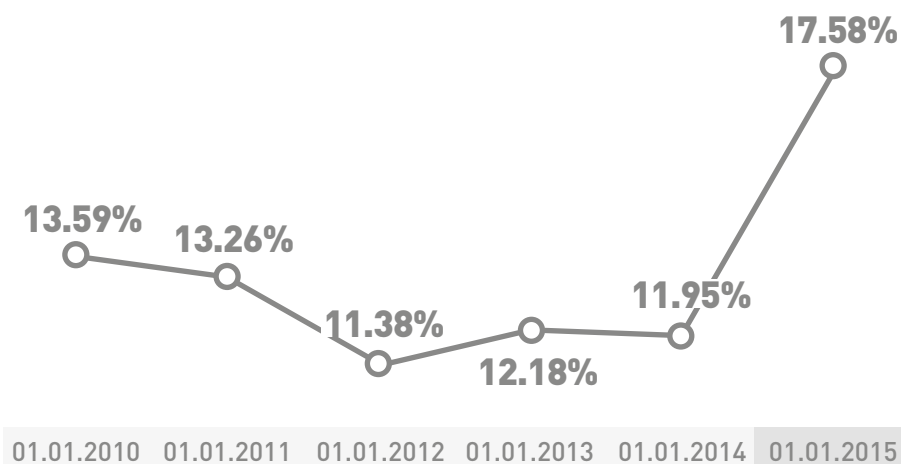
Over the last three years, MTS Bank strengthened its position as a reliable savings institution. Following the expansion of its regional office network, the retail deposit portfolio grew by 23% year-on-year despite the negative market trends.

Number of cards issued by MTS Bank, mln



The retail business imposes very strict requirements on bank capital. Over 2014, MTS Bank increased its capital more than twofold: at the beginning of 2015, the Bank's equity was RUB 27 bln against RUB 12 bln at the beginning of 2012. The largest increase in capital took place in 2014 and during an additional share issue, which was subsequently purchased by MTS and Sistema and generated RUB 13.1 bln for MTS Bank.

Capital adequacy ratio (N1), MTS Bank



In response to the deterioration of the macroeconomic conditions, the Bank adjusted its retail and corporate credit policies to reduce credit risks. In 2014, the Bank pursued a conservative provisioning policy, which will be also continued in 2015. In 2014, the Bank took timely measures to reduce costs and optimise the retail office network.

The CBR granted accreditation to MTS Bank to provide financial services to the companies operating in priority and strategic industries,

which testifies to the bank's reliability.

MTS Bank is included in the list of banks that may receive state funds from the Deposit Insurance Agency for recapitalisation. Through participation in the programme, the Bank will be able to rise over RUB 7 bln for Tier 2 capital on attractive terms for a 3-year period. The main condition of the programme is that the recipient bank should provide loans to sectors that are strategically important for the Russian economy, and grant

mortgage loans and loans to SMBs (small and medium-sized businesses) for an amount at least equal to 1% of the Bank's portfolio on a monthly basis.

In 2014, the Bank started issuing China UnionPay cards. By joining China UnionPay, the Bank substantially minimised the risks associated with the processing of its payments and was able to make attractive propositions to sole traders and private individuals in the Russian Far East, who actively cooperate with suppliers from China.

Key events

- In March 2015, Fitch Ratings confirmed the rating of MTS Bank at B+ with a stable outlook.
- According to the 2014 year-end results, MTS Bank was ranked number eight among plastic card issuers.
- In December 2014, MTS Bank successfully completed an additional share issue, raising RUB 13.1 bln.

Operational strategy



In 2012, MTS Bank completed rebranding and started the implementation of its strategy based on synergies with MTS. The business model restructuring,

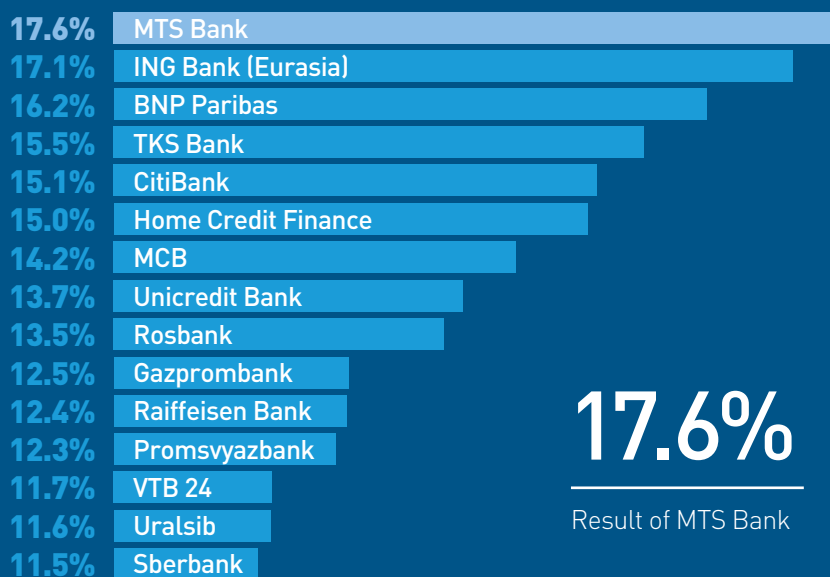
which was started in 2012, resulted in explosive growth in the retail assets portfolio, including the credit card segment. Over the last three years the household loan portfolio increased more than threefold with an annual growth rate of 62%.

MTS Bank's strategy is aimed at development of retail lending and transactional services for individuals segment. However, the Bank does not seek to turn into

a retail monoliner and maintains moderate growth rates in the target corporate segments, having kept its portfolio of corporate borrowers.

The Banks' operational strategy provides for greater cooperation with the mobile operator MTS. MTS Bank already widely uses the operator's retail chain and IT infrastructure. In the future, the Bank and MTS intend to share a common database under the Big Data Project in order to mitigate risks, boost sales and speed up product development.

Capital adequacy ratio (N1) of Russian banks



Financial results of MTS Bank

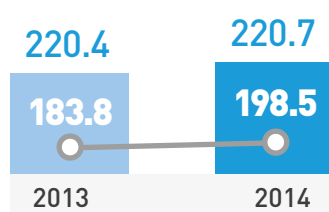
RUB millions	2014	2013	Change
Revenue	26,565	28,763	(7.6%)
Operating (loss)/income	(15,252)	604	-
Net income/(loss) attributable to Sistema	(11,212)	598	-

In 2014, MTS Bank's revenues decreased by 7.6% year-on-year in rouble terms. This was largely due

to lower revenues reported in the fourth quarter amid unfavourable market conditions. Interest income

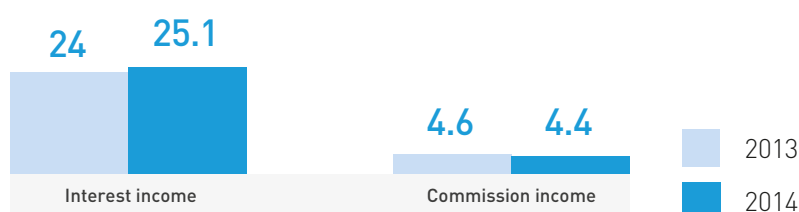
grew by 4.9% in 2014, gross loan portfolio increased by 3.1%.

Assets and loan portfolio, RUB bln



- Assets
- Credit portfolio

Interest and commission income, RUB bln



The bank reported a net loss in the fourth quarter and in 2014 due to increased provisions for the loan portfolio to individuals, which amounted to RUB 73 billion or 39% of total loan portfolio (including

interbank financing). MTS Bank has a conservative provisioning policy and demonstrates high stability ratios. Its provisions/retail loans ratio amounted to 28% compared to 16% in 2013.

* CBR

AGRICULTURE



Sistema's business in the agricultural sector is represented by RZ Agro (50%) and the Group of companies «Step».

RZ Agro Holding («RZ Argo») – is one of the largest producers of grain and oil-bearing crops in the south of Russia with a land bank of 99 thousand ha, jointly controlled by

Sistema JSFC and members of the Louis-Dreyfus family. Currently it comprises six farms grouped into three regional clusters in the Rostov Region and the Stavropol Territory.

GC «Step» unites five farms located in the Krasnodar region, with a land bank to manage – 26.3 thousand hectares.

Management

RZ Agro:

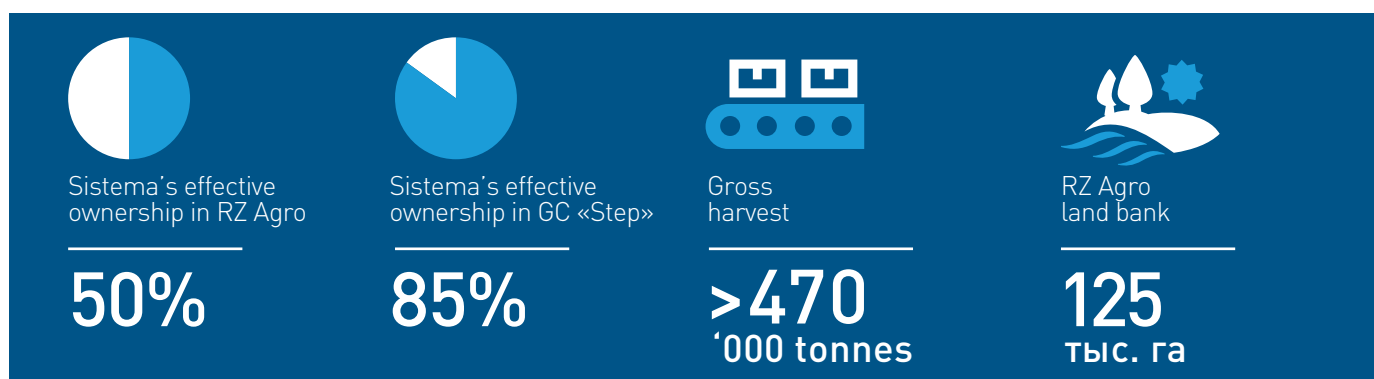
CEO – S. MacFarlane

Chairman of the Board of Directors – T. Schultz

GC «Step»:

CEO – K. Averin

Chairman of the Board of Directors – A. Uzdenov



Industry*

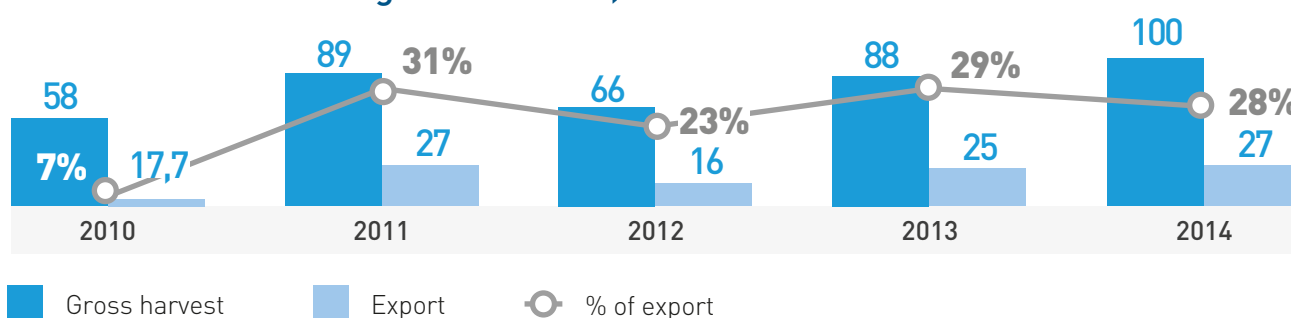
As a result of a steady growth of grain exports over the last few years, Russia, which has 9% of the world's arable land, regained its status as one of the largest global exporters. In 2014, grain exports from Russia totalled 27 mln tonnes, including 20 mln tonnes of wheat, or 12% of global wheat exports. In 2014, owing to favourable weather conditions in

Russia, gross production of main crops – grain, oil-bearing plants, sugar beet, vegetables and fruit – grew considerably.

The 100 mln tonne grain harvest became one of the largest in the last 20 years. Wheat production amounted to 59 mln tonnes, placing Russia among the three largest global

producers (after China and India) with 9% shares. Wheat production in Russia grew by 13%, while the growth in the total worldwide production in 2014 was only 1%.

Gross harvest volume of grain in Russia, mln tonnes



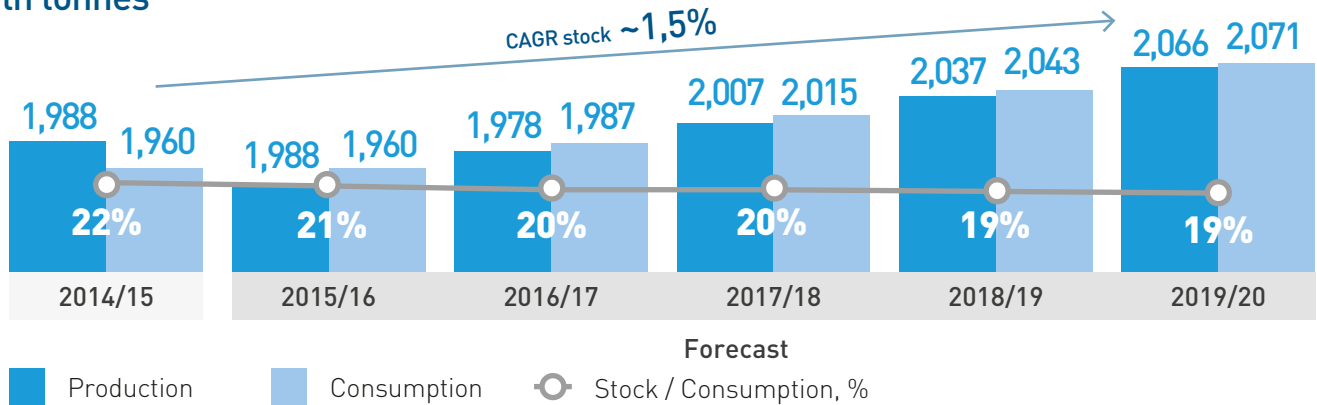
* Source: USDA, International Grains Council.

According to a forecast by the International Grains Council, in 2015-2020 global grain consumption and production will grow at approximately

the same rate – around 1.5% per year, driven by the continuous expansion of the world’s population and rising demand from the food and livestock

breeding industries. Production growth will be primarily driven by an improvement in crop yields.

Wheat production and consumption forecast, mln tonnes



RZ Agro Group operates in the Southern and North Caucasian Federal Districts – Russia’s key grain producing regions, which account for about 70% of winter wheat, over 95%

of winter barley and approximately 35% of oil-bearing crops produced in Russia. In 2014, the grain producers in Rostov Region, where the RZ Agro Group has five farms, harvested

9.5 mln tonnes of grain and grain legumes, almost 3 mln tonnes more than last year. It was a record harvest of the last 24 years.

RZ Agro today

The total land bank under RZ Agro’s management is 99 thousand ha, including 65 thousand ha (66%)

of land in its ownership. Around 91% of RZ Agro land is under cultivation. The Group includes six

farms grouped into three territorial production clusters: Rostov-East, Rostov-South and Stavropol-West.

Land bank by clusters (99,000 ha)

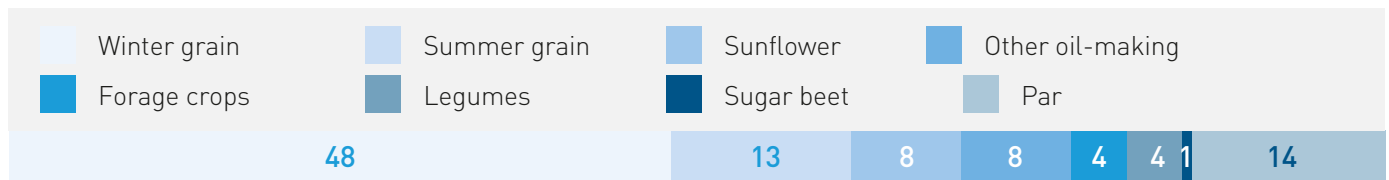


RZ Agro is a highly specialised farm holding. In 2014, crop farming generated 98% of its total income. The main crop types grown are winter wheat, barley, sunflower,

corn, pea, sugar beet. Livestock breeding is represented by First Cavalry Army Stud Farm – a famous horse breeding farm maintaining a nucleus herd and having the largest number of Budyonny horses.

RZ Argo has developed and implemented a long-term crop rotation plan, with minor adjustments made annually depending on the expected profitability of crops and previous harvest.

Structure of cultivated area in 2014



In 2014, special attention was paid to soil condition diagnostics and climate monitoring; soil remediation and land productivity improvement; implementation of technologies that help to adapt production to climatic changes, especially to drought conditions. Starting from the 2013/2014 production year, certain drought-resistant crops such as camelina and sorghum were included in the crop rotation schemes in the Rostov-East cluster.

RZ Agro sells approximately 90% of its products on the international and domestic markets. The remaining 10% is used as seeds and to pay land rent.

Over the last four years, RZ Agro managed to increase its sales 5-fold with the share of direct exports rising from 14% in 2011 to 32% in 2014.

In 2014, RZ Agro carried out direct grain deliveries to Egypt, Georgia, Armenia, Turkey, Iran, Saudi Arabia, South Africa.

RZ Agro actively expands its pool of counterparties by establishing partnership relations with end consumers in the importing countries and on the domestic market. To this end, cooperation is being strengthened with the Russian Export Insurance Agency (EXIAR). Domestic sales (68%) are mainly made to medium-sized exporters and large trading houses and directly to domestic consumers.

Re-equipment of production is one of RZ Agro's priorities. In 2014, 13 new units of modern tillage machinery (cultivators, harrows), 4 sowing machines, 1 tractor, 2 loaders, and other agricultural machinery were purchased. Additionally, investments

were made to install monitoring and security systems, such as fuel consumption monitoring, video surveillance, fencing and automated accounting.

In 2014, a new grain quality laboratory was set up and outfitted with modern equipment at SP Novotroitskoe (part of the Stavropol-West cluster) along with a new electronic weighing scale with a maximum capacity of 80 tonnes. The quality laboratory at Krasnaya Zvezda (Rostov-East cluster) received a new device for express analysis of grain.

The company prepared a five-year production re-equipment programme for 2015-2020. The key objectives are to continue replacing old machinery with modern high-performance units and to upgrade the fleet and equipment.

GC "Step" today

In the second half of 2014, Sistema, via its wholly owned subsidiary Krasnodar-Argo, acquired another agricultural asset - Steppe Group comprising five agricultural

enterprises located in the Krasnodar Territory with a land bank of 26.3 thousand ha under management. In 2014, the average wheat yield at the enterprises was

6.7 tonnes/ha. The high (Class 3) export quality and proximity to export ports enable the enterprises to obtain maximum selling prices for their products.

Operational strategy

Management of agricultural assets is carried out through a cluster approach, whereby self-sufficient clusters of 30,000-50,000 ha of closely located land areas work together to optimise operating and investment costs.

Operational strategy aims to increase crop yields and optimise pro-

duction and management expenses by using modern agricultural technologies and implementing modern cost monitoring systems.

Sistema's management focuses on the development of related activities to enhance business efficiency. Focus areas include:

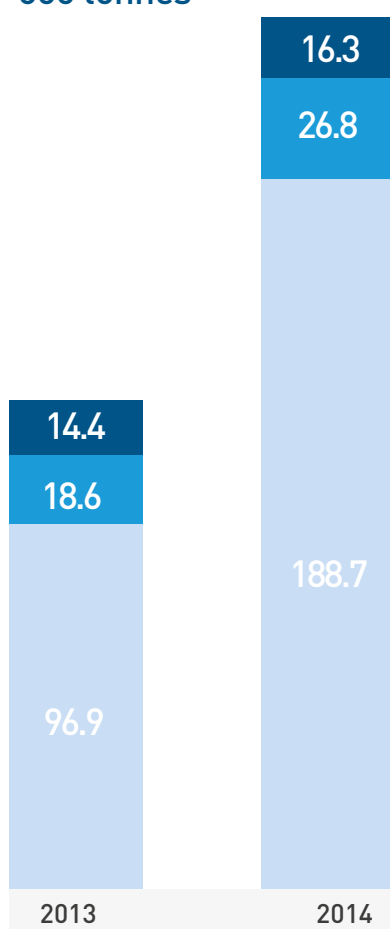
- grain procurement and trading (target procurement programme – up to 500,000 tonnes per year);
- seed production and sale programme;
- harvesting contracting (crop harvesting services in the north regions).

Financial results of RZ Agro

RUB million	2014	2013	Change
Revenue	2 387	895	166.7%
OIBDA	735	(150)	-
Operating income/(loss)	594	(241)	-
Net income/(loss) attributable to Sistema	182	(187)	-

Revenue of RZ Agro increased by 167% YoY driven by a record harvest of 300, 000 tonnes in 2014.

Gross harvest volumes, '000 tonnes



■ Wheat
 ■ Barley
 ■ Sunflower

Crop yield of wheat grew by 50% to 4.5 tonnes/ha, yield of barley increased by 80% to 3.4 tonnes/ha, yield of sunflower also grew by 28% to 2.3 tonnes/ha. The OIBDA margin expanded to 30.8%.

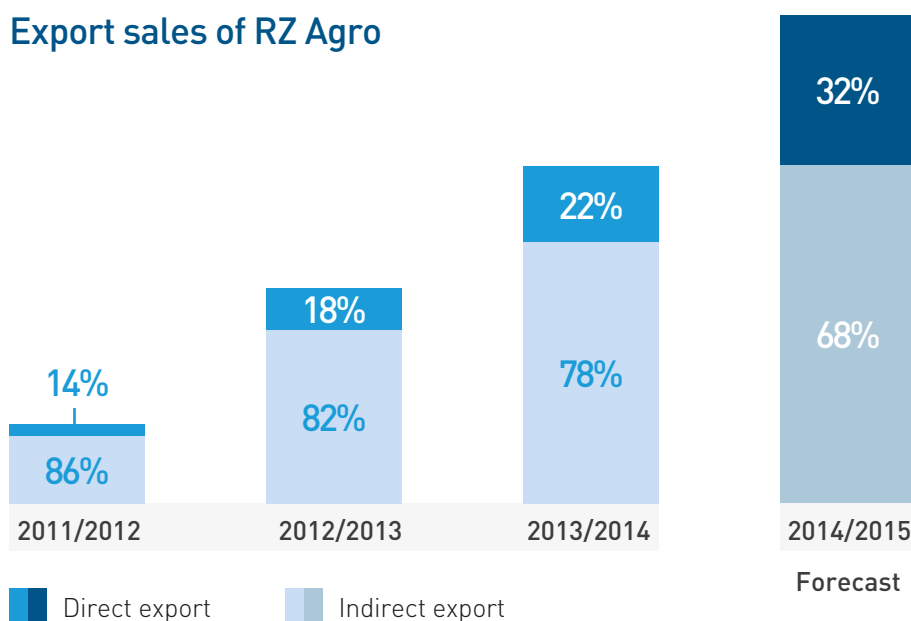
In 2014, RZ Agro developed its own export channels – the share of direct export sales increased to 32% in 2014.

RZ Agro exported wheat to Egypt, Georgia, Armenia, Turkey, Iran and other countries.

Key operating statistics

	2012 (5 clusters)	2013 (5 clusters)	2014 (6 clusters)
Total land bank , ha	89,000	89,000	100,000
Freehold land ratio,%	15%	68%	66%
Cultivated land ratio, %	89%	89%	91%
Production (all crops), kmt	134	141	300
Wheat yield, t/ha	2.8	3.0	4.5

Export sales of RZ Agro



■ Direct export
 ■ Indirect export

TARGIN

Targin is a major Russian oilfield services holding operating in the Republic of Bashkortostan, Nenets Autonomous District, Western and Eastern Siberia. Targin

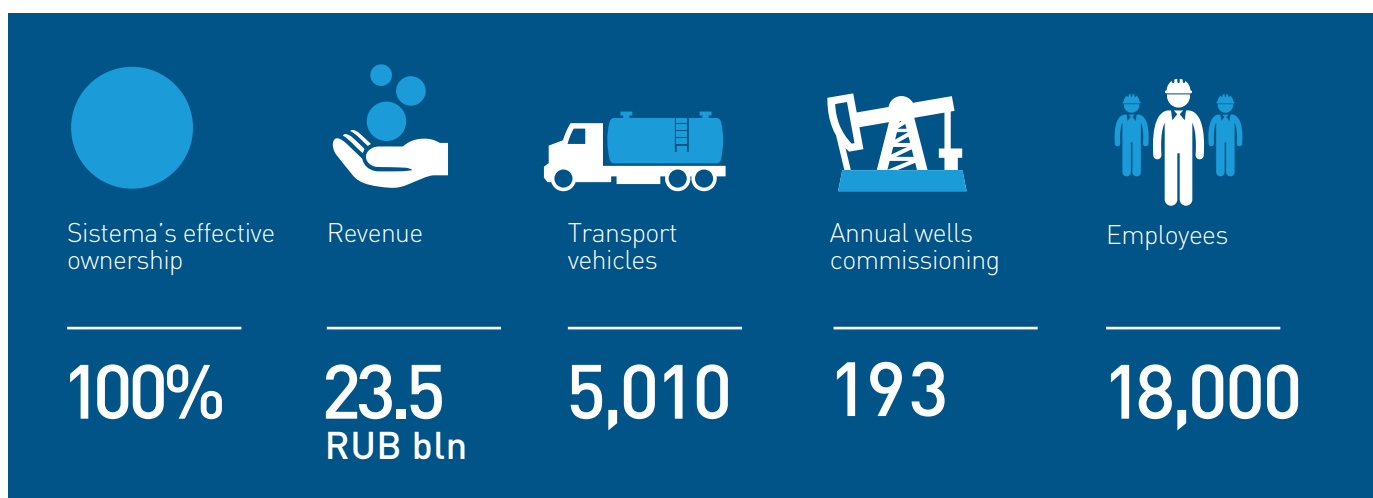
Group consists of a managing company and subsidiaries providing drilling, well repair and workover, mechanical maintenance and transportation services.



Management

President – K.F. Zakirov

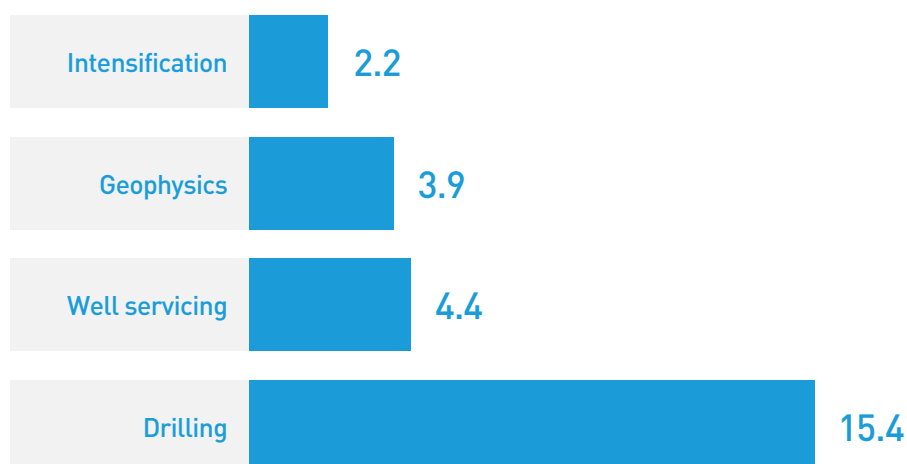
Chairman of the Board of Directors – F.V. Evtushenkov.



Industry*

The global oilfield services market reached US\$ 150 bln in 2014, with Russia capturing about 17% of the market. According to expert forecasts, over the next five years, the market may grow by 33%. The share of foreign companies in the Russian oilfield services market is about 18%, more than half of it is held by Schlumberger, a global oilfield services company. Targin's share of the Russian market is around 2.7%.

Revenue of oil service companies in Russia, US\$ bln



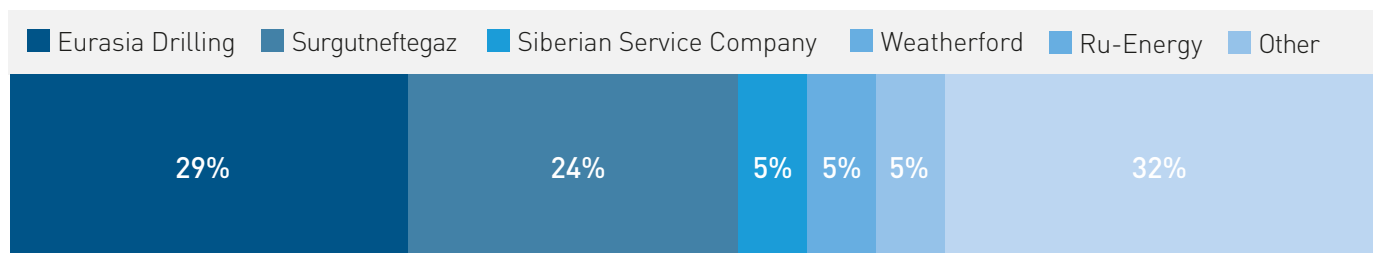
* Sources: RU-Energy, Deloitte, Vedomosti, Kommersant.

Drilling services occupy over half of the Russian oilfield services market. In 2014, Europe, the US and Canada imposed sanctions restricting access to drilling and production technologies in Arctic environment and to offshore and shale projects

for major Russian oil companies. Simultaneously, foreign players started withdrawing from the Russian market, which may slow down the implementation of new projects. These events forced Russian oil companies to start developing their

own oilfield service divisions. The acquisition of Orenburg Drilling Company and Weatherford's drilling operations by Rosneft will considerably increase the market share held by domestic service divisions.

Key players of Russia's drilling market in 2014



2014 was also marked by a trend towards active market consolidation. Closing of the transaction on purchase of Russian drilling industry leader Eurasia Drilling Company (EDC) by a global company Schlumberger will increase the concentration of players in the market in the near future.

Oil well drilling in Russia dropped by 7% in H1 2014 for the first time since the financial crisis of 2008-2009. This drop is also associated with the transition to horizontal drilling with its volumes increasing by 63%. The share of horizontal drilling in Russia grew from 10% to 25% since 2011. Currently, only 20% of oil is extracted by tertiary recovery methods such as hydraulic fracturing and drilling multilateral wells.

The demand for high-tech oilfield services is continuously growing. The competitiveness of independent service companies in the market is determined by the availability of cutting-edge technologies and highly productive multi-functional equipment.

Steady growth in 2014

Sistema acquired Targin at the end of 2013 and carried out work to modernise and restructure the business in 2014. The completed consolidation of the Group companies in accordance with the one segment – one company principle will enable it to reduce costs in future periods.

Implementation of the approved investment programme will improve the company's technological infrastructure to a level in line with best industry practice in just a few years. Capital expenditures totalled RUB 3.7 billion, through which Targin

formed four new workover crews, purchased five mobile drilling rigs (160 tonnes each) and a 320 tonne drilling rig, and upgraded five rigs (250 tonnes each). In addition, it bought more than 290 units of special equipment, over 100 units of process equipment for various purposes and other. Approximately 40% of capital expenditure in 2014 was invested in production development, with about 63% of the total cost spent on the drilling segment. Investment projects are financed with the company's own (32%) and borrowed funds (68%).

Rouble loans were obtained from Russia's largest banks at comfortable terms to finance the investment programme.

In 2015, 60% of investment programme will be directed at production development. The largest projects include acquisition of four drilling rigs, two backfill equipment fleets and two fleets of coiled tubing units with nitrogen pumping equipment, modernisation of one drilling rig and purchase of over 150 specialised equipment units.

Geographical scope



One of the objectives of Targin was to diversify its client base following reorientation of the company from Bashneft's oilfield services division. In 2014, in addition to Bashneft, the company also provided services to Rosneft and its subsidiaries, Gazpromneft, Slavneft-Megionneftegaz, and others. Bashneft accounted for about 77% of the company's revenues in 2014.

In 2014, Targin commenced project in Serbia under a well repair contract. After successful completion of the first stage, the number of crews for the project may be increased. Drilling services are also planned for the future.

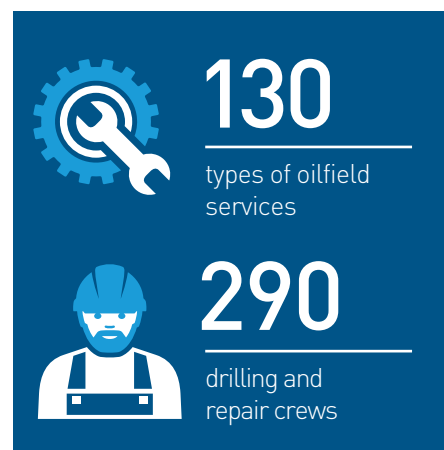
In 2014, Targin started a project to provide integrated services involving the preparation of wells for hydraulic fracturing.

Operational strategy

Targin's strategy focuses on increasing its market share and diversifying its client base by providing a full cycle of high-tech drilling services. The Drilling segment plans to develop well construction services and new service areas in line with the development of Russia's oil and gas industry.

The well repair and workover segment requires implementation of new technologies and services for emergency response and development of enhanced oil recovery and other techniques.

The key objective of the Logistics segment is to maintain the fleet age structure in line with the requirements of the main customers. The key target is the transition from conventional transportation service to transport logistics.



* WRR - Wells repairs and renewals

** FPCP - Flexible pump and compressor pipes

Financial results of Targin

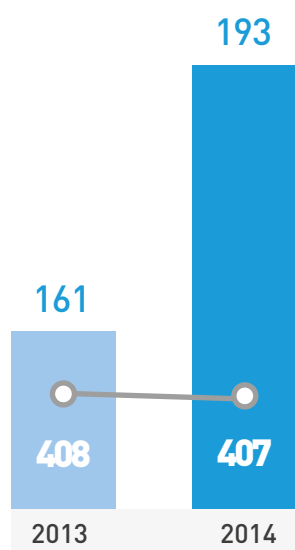
RUB millions	2014	2013	Change
Revenue	23,549	24,435	-3.6%
OIBDA	3,008	1,901	58.3%
Operating income	1,731	1,136	52.3%
Net income attributable to Sistema	1,032	459	124.8%

Sistema acquired Targin in October 2013. During 2014, Targin contributed RUB 23.5 billion and RUB 3.0 billion to

the Group's consolidated revenue and OIBDA, respectively. OIBDA margin grew from 7.8% to 12.8%.

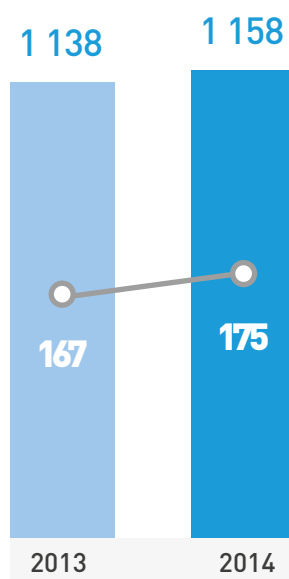
During 2014, Targin's business was restructured and its operating facilities underwent reconstruction. Capital expenditures totalled RUB 3.7 billion, through which Targin formed four new workover crews, purchased five mobile drilling rigs (160 tonnes each) and a 320 tonne drilling rig, and upgraded five rigs (250 tonnes each). In addition, it bought more than 290 units of special equipment, over 100 units of process equipment for various purposes and other. Approximately 40% of capital expenditure in 2014 was invested in production development, with about 63% of the total cost spent on the drilling segment.

Operational results in the Drilling segment

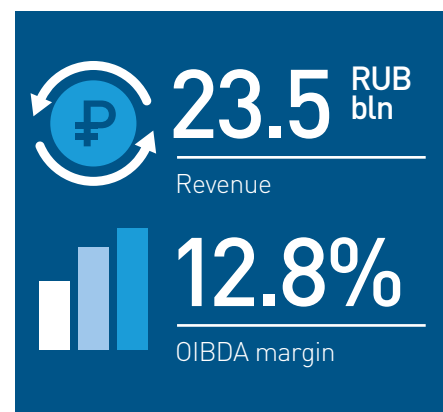


- Drilling volumes, th m
- Commissioned wells

Operational results in the Well Repair and Workover segment



- Workover, khours
- Crews



BINNOPHARM

Binnopharm is a pharmaceutical company that operates one of Russia's largest full-cycle manufacturing facilities, producing biotech drugs in line with the international quality standard GMP (Good Manufacturing Practice). The priority areas of the company's activities include development and commercialisation of drugs for treating socially significant

diseases (oncologic, haematologic, contagious and respiratory diseases).

Binnopharm Group includes Alium Plant - a modern complex for production of infusion solutions - and distribution company Binnopharm Distribution, which sells both Binnopharm's and third-party pharmaceuticals.

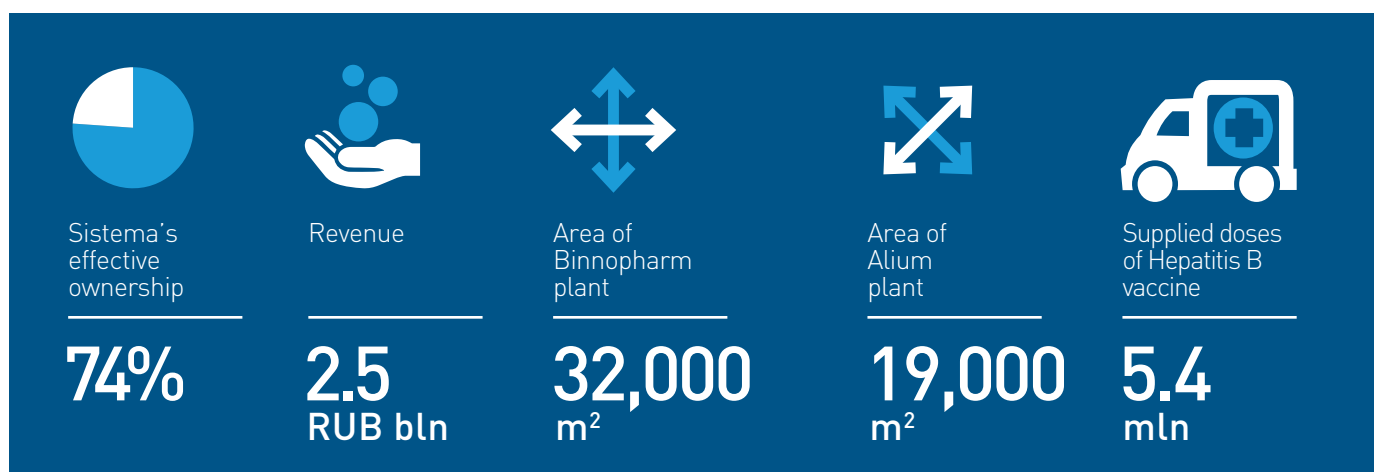


BINNOPHARM
company of JSFC Sistema

Management

CEO – A.N. Chupin

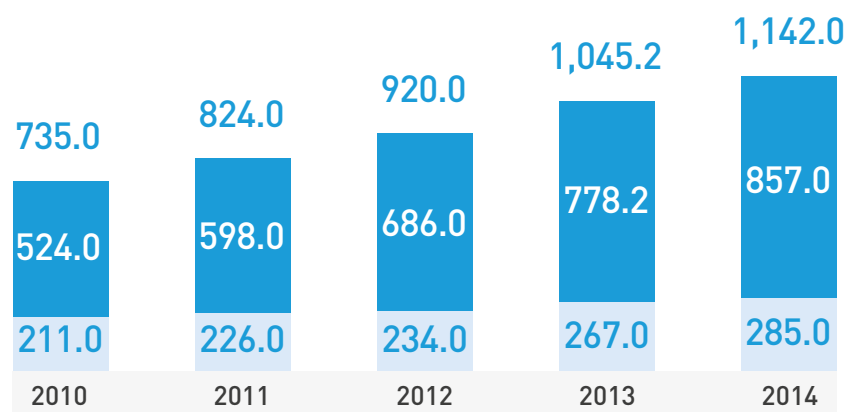
Chairman of the Board of Directors – D.L. Zubov



Industry*

The Russian pharmaceutical market remains one of the fastest growing markets in the world. According to DSM Group, the total market size increased by 9.3% in value terms in 2014 to RUB 1.14 trn, with the commercial segment increasing by 10.8% and hospital segment by 10.0% in monetary terms, while the additional pharmacological support segment contracted by 0.9%.

Volume of Russian pharmaceutical market and share of foreign players, mln RUB



* DCM Group

■ Russian producers ■ Foreign producers

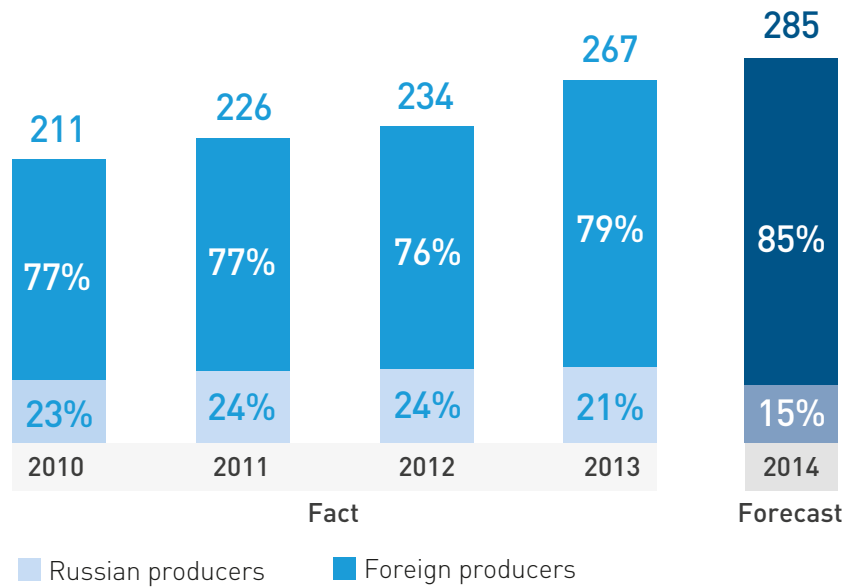
Most of the year-on-year growth in the Russian market came from increases in product selling prices; in physical terms, the market contracted by 3.6%. According to estimates by the Russian Ministry of Health, the market share held by foreign manufacturers in 2014 was over 70% in monetary terms.

The key focus of the import substitution programme is placed on increasing the share of Russian manufacturers in the pharmaceutical industry. The most important event in 2014 in the state control over the industry was a resolution prepared by the Ministry of Industry and Trade, banning the admission of foreign drugs to government tenders in case two or more bids are received from Russian manufacturers.

Another important event in the sector in 2014 was the entry into force of Federal law "On contract system in the area of state procurement" and the government's transition to the Federal Contracting System, which had a short-term effect of reduction in regional purchasing volumes.

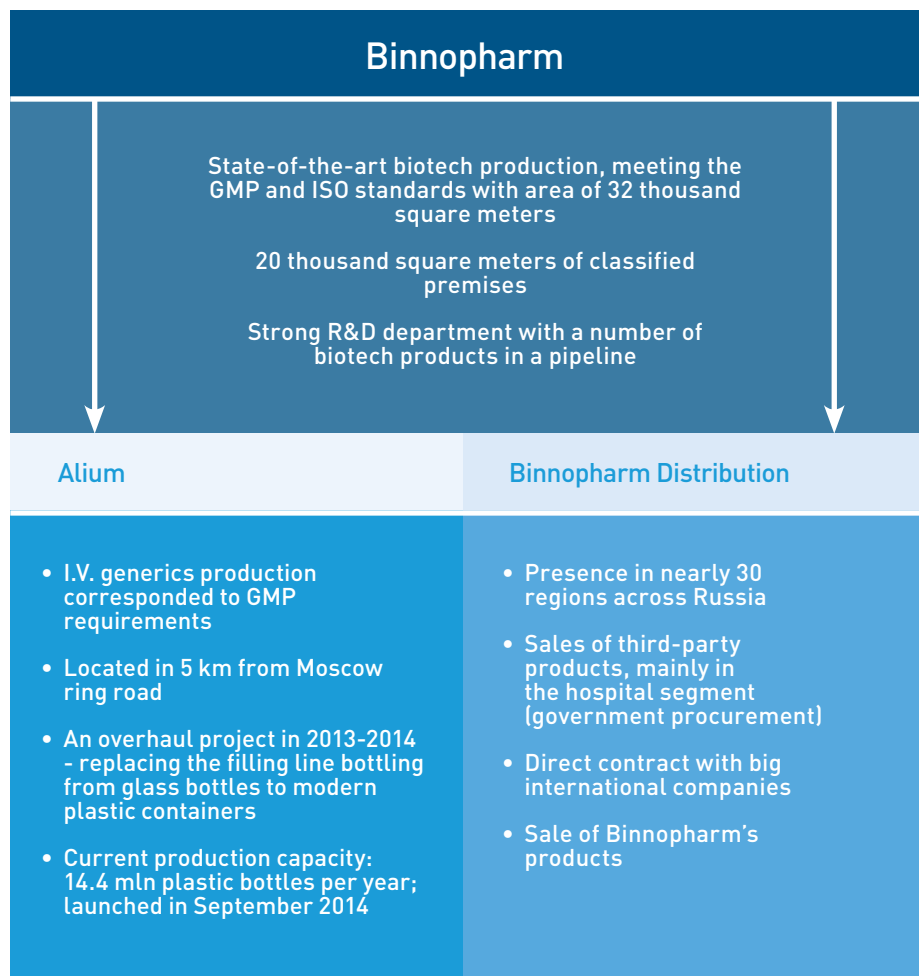
Experts are mostly positive on the outlook for the domestic pharmaceutical market. According to the latest forecasts by DSM Group, market volumes will grow by around 9% in 2015 versus 2014. The growth in the commercial segment is expected at about 10%, and in the state segment at about 6%. Most of that growth will be provided by the Russian pharmaceuticals, facilitated by the import substitution programme.

Volume of state procurements in pharmacy and share of Russian players, bln RUB



Binnopharm's business in 2014

Binnopharm Group

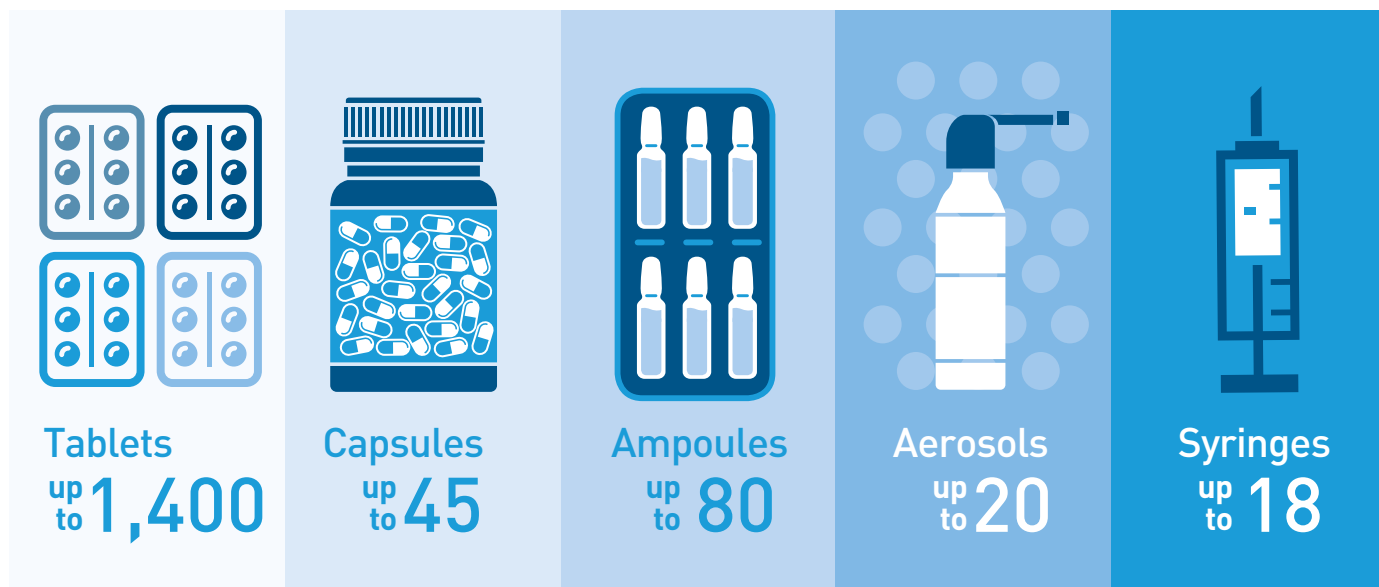


In 2014, Binnopharm's results were affected by the government's transition to the Federal Contracting System. After the relevant law took effect, regional purchases of drugs were virtually frozen, resulting in more than 45% reduction in Binnopharm's distribution revenues in the first half of 2014.

In 2014, Binnopharm continued deliveries of Regevac (a hepatitis B vaccine) under government contracts. The delivery volume in 2014 dropped by 1.8 mln doses from the previous year to 5.4 mln, which also contributed to the decline in the company's revenue.

The expected revenue fall due to structural changes was offset by adequate optimisation measures: selling, administrative and management expenses were reduced by RUB 70 mln, and thus the ratio of these expenses to revenue remained at the level of the previous year.

Binnopharm's annual output capacity, mln pcs



Binnopharm actively cooperates with foreign manufacturers under the existing contract production agreements and plans to enter into new ones (among the company's partners are

ViiV Healthcare and Fresenius Kabi). In early 2015, Binnopharm's facility started repackaging operations for Ketosteril – one of the key products in Fresenius Kabi's Russian portfolio.

In 2014, a new drug, Beklometazon (aerosol for treatment of lung diseases), was registered, the market for this product in Russia is estimated at RUB 500 mln per year.

Key events

- In February 2014, Binnopharm launched a new syringe line for production of pre-filled syringes. The line has an annual capacity of 18 mln of syringes. Registration of Binnopharm's biotech products in the new form is in progress.
- In March 2014, the company signed an agreement with ViiV Healthcare Trading to continue ViiV drug production at Binnopharm's facilities up to the end of 2016.
- In September 2014, Binnopharm launched its upgraded filling line for infusion solutions at the Alium plant. Binnopharm also signed new cooperation agreements with international pharmaceutical companies.
- In December 2014, Alexey Chupin was appointed CEO of Binnopharm.
- In December 2014, Binnopharm's aerosol product line was expanded following the registration of Beklometazol; development and registration of new drugs are underway.

Operational strategy

The key objective of the company's operational strategy is to expand the company's own drug portfolio and efficiently utilise its main production units: biotech production facility, aerosol line, lines for production of solid drug forms and infusion solutions.

Binnopharm will continue producing Regevak B vaccine, erythropoietin β , interferon ingredient. Furthermore, the second and third phases

of clinical research for its own biotech drugs – Interferon $\alpha 2\beta$, Erythropoietin α will be carried out in 2015. Binnopharm actively works on the list of drugs to develop in the medium term, both by the in-house R&D department and through technology transfer by obtaining production licenses for the new drugs.

Utilisation of the lines producing aerosol and solid pharmaceutical

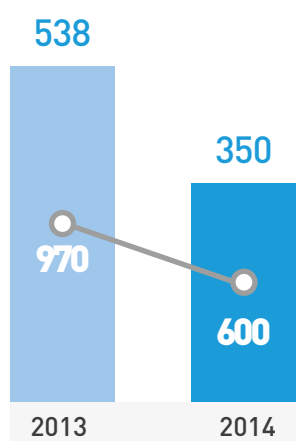
forms will be ensured through implementation of contract production projects with foreign pharmaceutical companies and commencement of Binnopharm's generic drugs production. Alium Plant is currently producing simple infusion solutions – dextroglucose and sodium chloride. In 2015, the plant will start production of amyllum and intravenous generics that do not require clinical trials and may be registered by the end of 2015.

Financial results of Binnopharm

RUB millions	2014	2013	Change
Revenue	2,485	3,321	(25.2%)
OIBDA	322	652	(50.7%)
Operating income	136	425	(68.1%)
Adjusted net income attributable to Sistema	4	285	(98.5%)

Binnopharm's rouble revenue declined by 25.2% year-on-year in 2014 and by 33.1% year-on-year in the fourth quarter. The results were impacted by the entry into force of the Federal law "On the Contract System in the State and Municipal Procurement of Goods, Works and Services" and government's transition to the federal contract system which practically put freeze on regional procurement of medicines and resulted in a temporary decrease of revenues from Binnopharm's distribution business by more than 45% in the first half of 2014. However, government procurement of drugs is generally expected to increase in 2015. Furthermore, Binnopharm will participate in the government's import substitution programmes for drugs as a local manufacturer.

Binnopharm's sales of Regevak



- Sales of Regevak B, mln rub
- Supply of Regevak B, thousands doses

In 2014, Binnopharm's OIBDA decreased following a decline in revenue and gross profit. A drop in revenue was expected due to structural changes, but this was supported by corresponding optimisation measures, which led to Binnopharm's SG&A expenses falling by RUB 70 million in 2014. The SG&A/revenue ratio therefore remained at the same level as in 2013.

REAL ESTATE

This business area is represented by a number of companies, including the following key players: Leader-Invest, Business -Nedvizhi-

most and Mosdachtrest. Sistema's strategy in real estate business is focused on increasing the value of the portfolio under management

with further monetisation through rent income, development and sale.

Management

Leader-Invest:

CEO – E.G. Rubtsov

Chairman of the Board

of Directors – F. V. Evtushenkov

Business-Nedvizhimost:

CEO – I.V. Shabdurasulov

Chairman of the Board

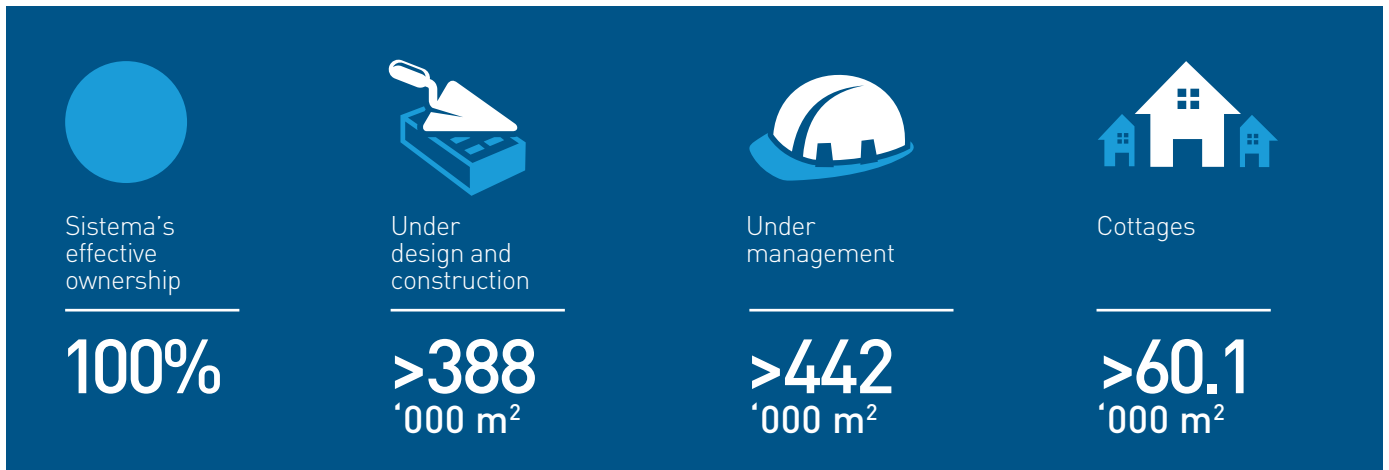
of Directors – L.A. Monosov

Mosdachtrest:

CEO – S.V. Gavrilenko

Chairman of the Board

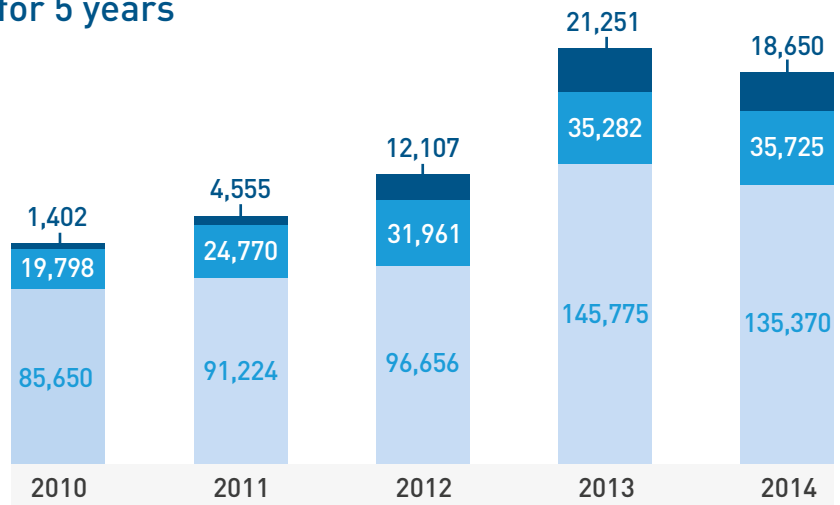
of Directors – S.A. Drozdov



Industry*

In 2014, new residential space commissioned in Moscow increased to 3.2 mln m² from 3.1 mln m² in 2013. Between January and October 2014, 135,370 real estate transactions were made on the market, which is only 7% lower than the record of 2013.

Deals with real estate in Moscow, for 5 years



■ Purchase and sale ■ Mortgage ■ Share participation agreement

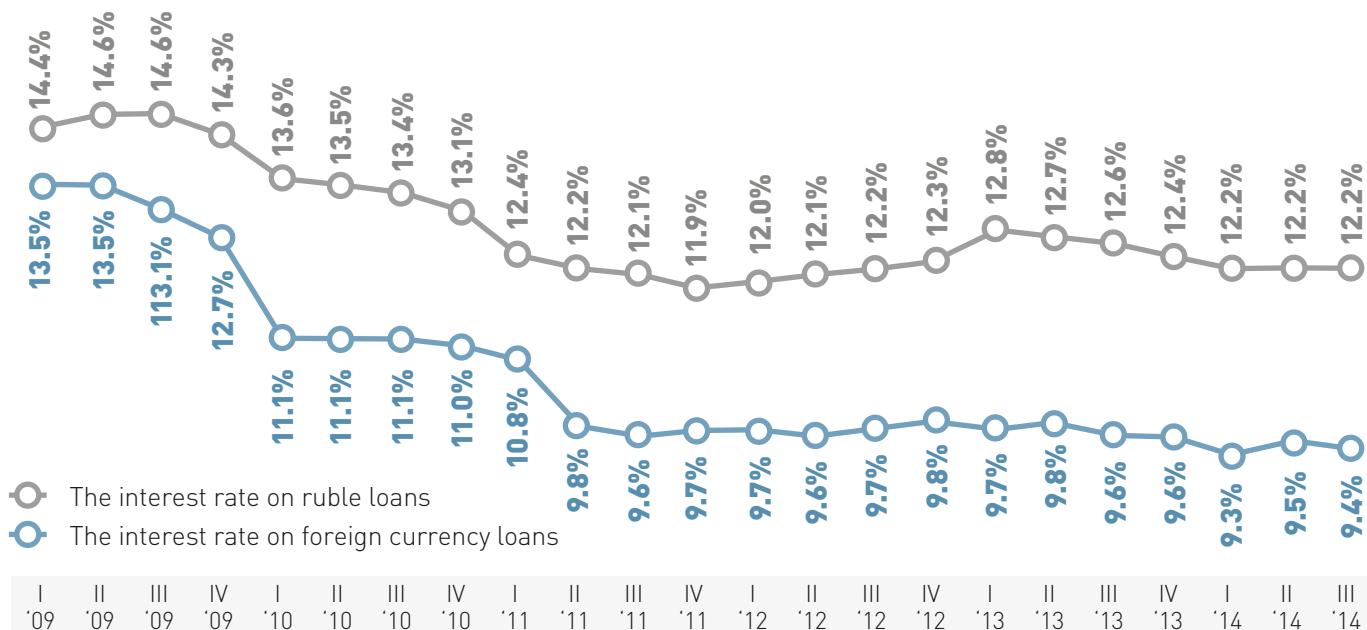
Sources: Rosreestr, AHML, Knight Frank, ILM

Early 2015 saw a decline in purchasing activity due to a rise in mortgage interest rates and toughening of requirements for borrowers. The most badly-hit

segment will be the construction of comfort class housing where the share of mortgage-based transactions is about 60%.

However, the anti-crisis measures taken by the Russian Government to subsidise mortgage interest rates are expected to support the market in the second half of 2015.

Weighted-average mortgage rate for 5 years

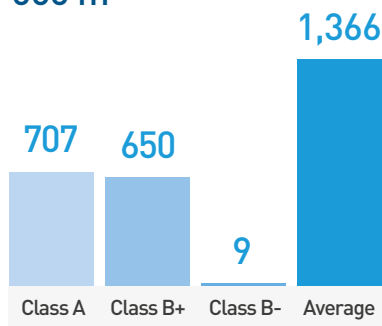


It is most likely that in 2015 the competition among developers will increase and the market will become a buyer's market: the quality of properties offered in the primary market is expected to increase along with active promotion campaign.

The office property market hit a record high in new space delivery (1.4 mln m²), which is almost two times more than in 2013. The vacancy rate grew by 29% for A class space and 17% for B class space amid depressed demand caused by general economic crisis. Dollar-denominated rental rates fell by more than 10%.

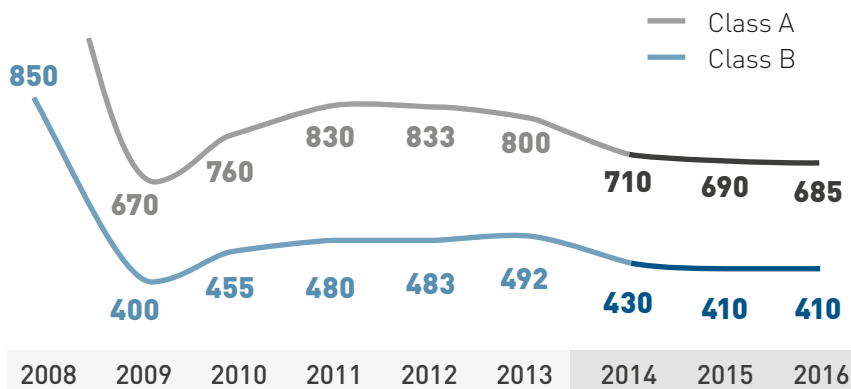
During 2014, 1.29 mln m² of office space was rented or bought out, 15% lower than in 2013. The activity of tenants and investors slowed down by the end of 2014, and in 2015 the demand for office space may continue falling.

Office real estate, commissioned in 2014, '000 m²



High volatility in currency markets in late 2014 resulted in a decline in average rental rates by 10% to 15% depending on the class of properties.

Rent rates



The planned increase in new space delivery in 2014-2016 (almost 3 mln m²) amid slack demand may lead to a further increase in vacancy rate to 30% on average, decline in rental rates by 10% and toughening of competition among the landlords.

According to the 2014 end year results, the demand for rent of premium real estate dropped by 9% year-on-year. The main reasons for the fall in demand for properties of this category are the general economic situation as well as the practice of setting rental rates in foreign currency prevailing in the market.

The Moscow premium rental market in 2015 will depend on two key factors: geopolitical situation and currency exchange rates.

Steady growth in 2014

Sistema's real estate assets are grouped into several distinct areas – real estate management, development, and management of Serebryany Bor real estate – which are represented by Business-Nedvizhimost, Leader-Invest and Mosdachrest, respectively.

Leader-Invest is a development company investing in construction of residential property (comfort, business, premium and deluxe classes in the Central Moscow) and commercial property.

As at the end of 2014, the development project portfolio held by Leader-Invest included 13 real estate objects with a combined area of 388,000 m². Six of these properties with a combined area of 103,000 m² are under construction. In 2014, Leader-Invest continued implementation of the project for the construction of an office building in Nagatino iLand with a total area of 31,000 m². The company successfully completed work on renovation of three buildings (former automatic telephone exchanges) totalling 28,000 m² in area and signed contracts to participate in shared-equity construction of 6,600 m² of apartments worth RUB 1.4 bln in total.

In April 2014, Sistema acquired an additional 49% stake in Business-Nedvizhimost for RUB 3.1 bln, bringing its stake to 100%. Business Nedvizhimost owns 76 real estate sites located across Moscow which cover a total area of approximately 178,000 m² and were used by MGTS as automatic telephone stations (ATS) prior to the implementation of GPON (Gigabit-capable Passive Optical Network) technology.

Business-Nedvizhimost provides professional and management services both for its own commercial real estate and that of its partners, including renting and selling of buildings. Business-Nedvizhimost owns a unique pool of real estate properties: mansions in the centre of Moscow, office and retail properties, business centres located virtually in every district of Moscow, industrial and warehousing properties in Moscow and Moscow Region. The total portfolio of properties under management as at the end of 2014 was over 442,000 m².

In 2014, a detailed operational programme was developed for further commercialisation of the buildings previously occupied by ATS. During 2014, the company partially renovated premises in

six properties located in the centre of Moscow with a total area over 22,000 m², which were cleared from the MGTS equipment.

In 2014, Business-Nedvizhimost completed the sale of a property in Moscow's downtown and entered into a new project together with a co-investor partner for the construction of a residential building with a total area of 13,000 m² and aggregate apartment space of 6,300 m². The project will be completed in the first quarter of 2016.

Mosdachrest is a management company focusing on the rental and maintenance of cottages (Serebryany Bor, Barvikha, Zhavoronki, Trudovaya) and office premises in Moscow. The total cottage area as at the end of 2014 was over 60,100 m².

In 2014, Mosdachrest approved the architectural concept for reconstruction of buildings and performed repair work in Serebryany Bor cottages.



Key events

- In April 2014, Sistema acquired an additional 49% stake in Business-Nedvizhimost for RUB 3.1 bln.
- In early 2015, Business -Nedvizhimost acquired a 51% stake in Rent-Nedvizhimost for RUB 3.8 bln.

Operational strategy

In accordance with the set objectives, in 2015 Leader-Invest plans to put into operation three projects totalling 11,300 m² in area and start construction of four real estate objects with a total area of

41,800 m². Also, there is a plan for Business -Nedvizhimost to transfer 16 properties with a combined area of 179,000 m² to Leader-Invest for development in 2015.

The operational strategy of Mosdachtrest in 2015 will focus on maintaining a steady rental cash flow as well as reconstruction and monetisation of cottages in Serebryany Bor.

SISTEMA SHYAM TELESERVICES

Sistema Shyam TeleServices Ltd. (SSTL) is a CDMA mobile operator

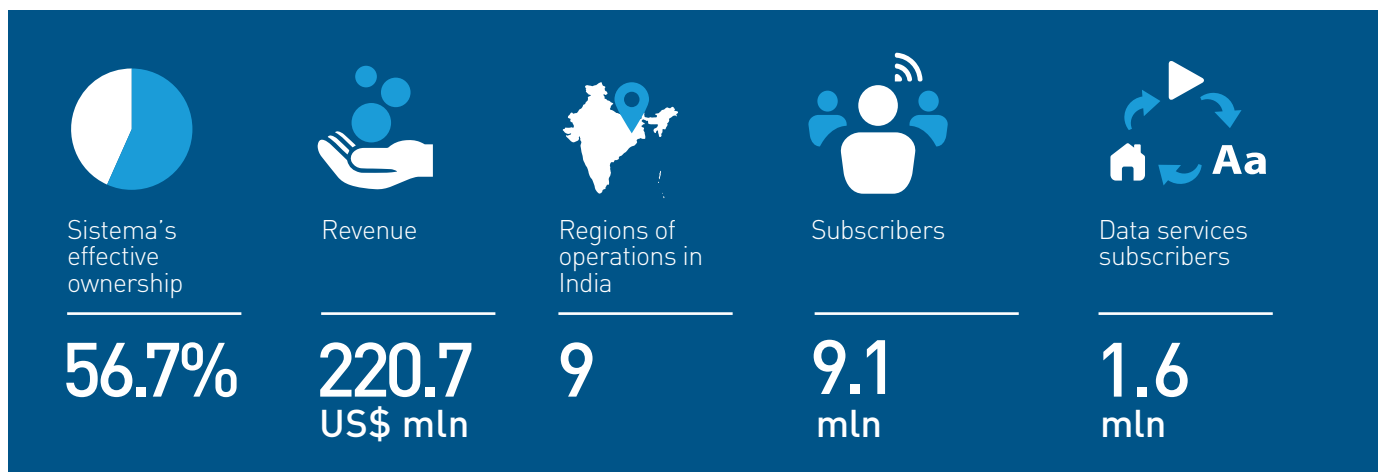
providing telecom services in India under the MTS brand.



Management

CEO – D.V. Shukov

Chairman of the Board of Directors – R. Sommer



Industry*

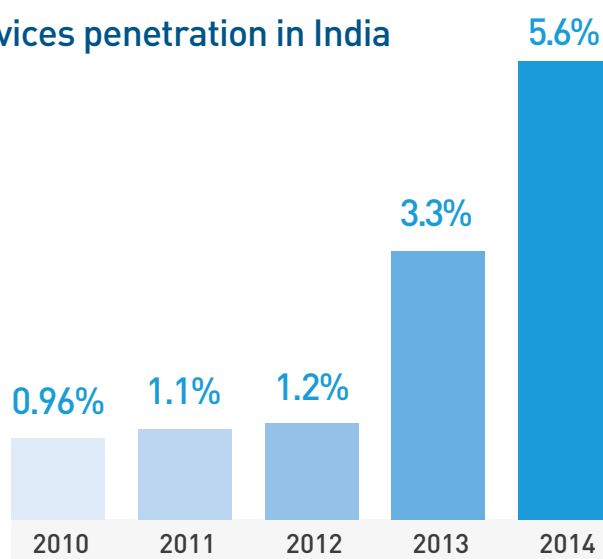
The telecom market in India continued to grow steadily in 2014, with most of its growth coming from GSM subscribers and accelerated development of the data services. As of December 2014, the total subscriber base in the country reached a historical high of 971 mln with the total penetration of 77.6%. The active subscriber base grew by 9.2% over the year.

CDMA subscriber base and market share contracted by 1.1%. Although several companies left the market in 2012-2013, there are still 12 mobile operators in the country, including 8 GSM operators, 3 GSM/CDMA operators and one CDMA operator (SSTL). The top three operators in India (Bharti Airtel, Vodafone and Idea) strengthened their positions in 2014 with a combined market share based on subscriber base exceeding 58%.

Data services segment is the major driver in the industry's development. During 2014, traffic generated by 2G and 3G broadband services grew by 74%, with 3G network traffic

growing by 114%, and 2G network traffic growing by modest 41%. Over the year, the share of 3G services as a percentage of total telecom services rose from 42% to 52%.

Data services penetration in India

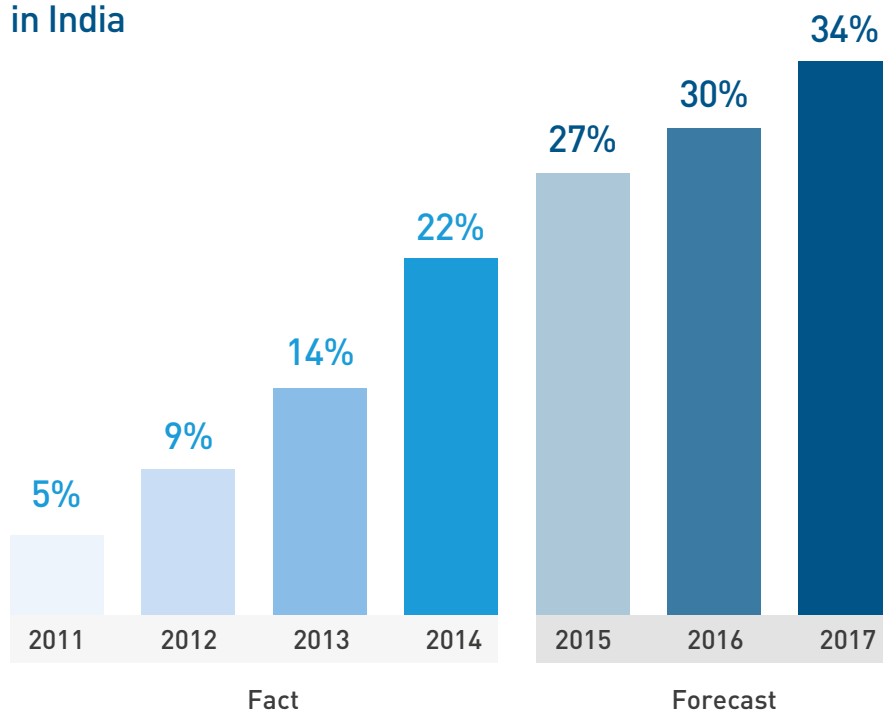


* Source: TRAI, Statista.com

15% each quarter, the current penetration rate is only 22%. The aggressive growth is supported by active promotion of low-priced handsets.

Operators in India are starting to develop and promote 4G (LTE) networks and services in the market. With about 5.5 mln 4G subscriber terminals purchased in the country, only 85 thousand of them are active. The competition in the data services segment should become tougher considering the scheduled launch of LTE by RJIO and growing market activity of 3G operators.

Smartphones penetration in India



The 900 and 1800 MHz licenses of Airtel, Vodafone, Idea Cellular and Reliance Telecom will expire in 2015-2016 in 18 districts. In this connection, the Indian Ministry of Communications held a new auction in March 2015 for a number of frequency bands, including 800 MHz used by SSSL. According to the

auction terms, the starting prices for 800 MHz frequencies were almost twice as high as the price quoted at the last auction in March 2013. SSSL did not participate in the auction.

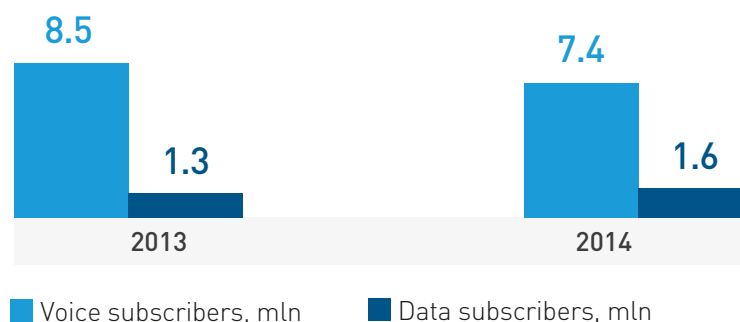
To provide more efficient utilisation of the limited frequency resources

in the country, the Government of India prepared draft regulations on the spectrum sale and spectrum sharing by operators; however, these regulations are not expected to be finalised and approved until the second quarter of 2015 at the earliest.

Steady growth in 2014

In 2014, SSSL's revenue in Indian rupees grew by 10% from 2013, with a 33.6% increase in the revenue from data transmission services - of company's key area of development. The share of data revenue in total sales grew from 27% to 47%.

SSSL subscriber base



In March 2014, SSTL introduced one of the cheapest rate plans in India for data services, presented its own Internet movie theatre called MTS Movies, where the subscribers can watch movies free of charge, and conducted an active marketing campaign, with the MTS Internet Baby video watched by 25 mln of

viewers, marking a new record in viewing on Youtube in India.

SSTL was able to rapidly develop its data services by introducing measures to streamline and improve sales efficiency. This included implementing a pilot project to launch SSTL's distribution

sales model in Gurgaon and New Delhi, a pilot project in Kerala providing distributors with loans to purchase voice devices and data transmission equipment, and a model for sharing revenue with distributors in Delhi.

Key events

- In July 2014, SSTL started selling a new innovative device (Mblaze PowerWifi) – a mobile Wi-Fi router with high-capacity storage battery and smartphone recharging function.
- In October 2014, SSTL launched a new advertising campaign GB Festival and started promotion of a new line of data rate plans, thus strengthening its position as a price leader.
- In 2014, for the third year in a row, the MTS brand was included in the list of Brand Equity 50 Most Trusted Service Brands in India. The brand was also recognised as the most innovative brand in the telecom sector in India and ranked among the top three most recognizable brands of mobile Internet providers.

Operational strategy

The key strategic objective of SSTL in 2015 is to achieve OIBDA breakeven. SSTL will focus on

growth in the data segment, active monetisation of voice services and optimisation of company costs.



Financial results of SSTL

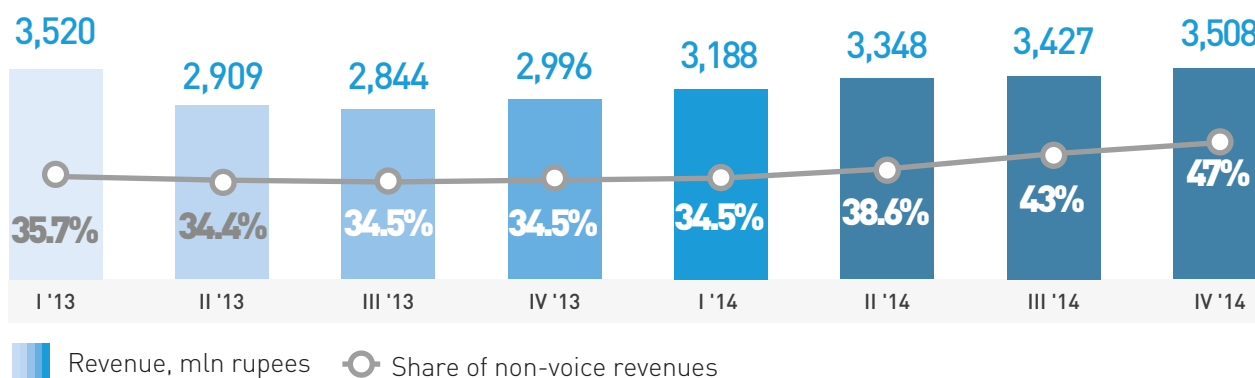
US\$ millions	2014	2013	Change
Revenue	220.7	209.4	5,4%
Adjusted OIBDA	(81.5)	(146.5)	-
Adjusted operating loss	(141.8)	(210.2)	-
Adjusted loss attributable to Sistema	(129.7)	(225.1)	-
Net debt	544.0	568.6	(4.3%)

SSTL's revenues increased by 5.4% year-on-year in 2014, mainly as a result of development of its data segment. Non-voice revenues from both data and

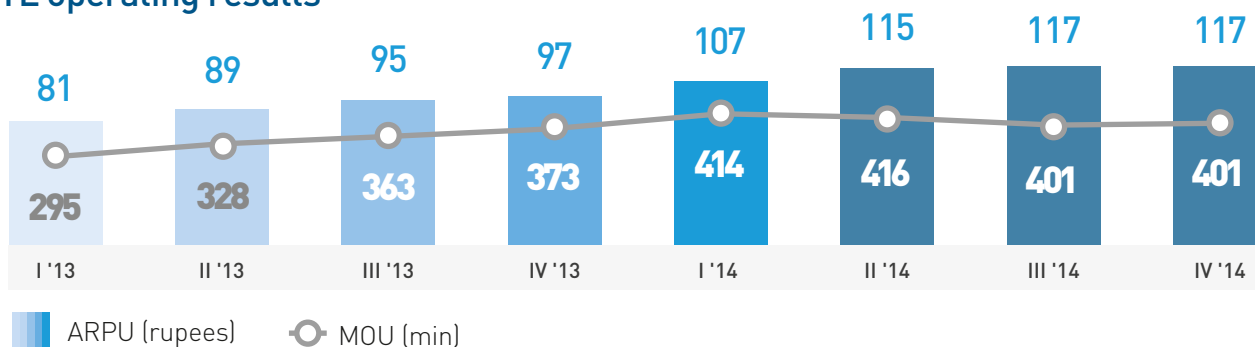
VAS accounted for 46.9% of the operator's total revenue in the fourth quarter of 2014, compared to 34.5% in the corresponding period of 2013.

In 2014, SSTL significantly narrowed its year-on-year adjusted OIBDA loss by 44.3% through its cost optimisation programme despite the active marketing campaign it conducted in the fourth quarter of 2014.

SSTL results in local currency



SSTL operating results



As of December 31, 2014, SSTL's wireless (voice and data) subscriber base totalled 9.0 million. The data subscrib-

er base grew by 23.0% year-on-year in 2014 to 1.6 million. In the fourth quarter, subscribers' MOU increased

by 6% year-on-year to 396 minutes. Blended mobile ARPU in rupees grew by 26% year-on-year to INR 122.

SISTEMA MASS MEDIA

Sistema Mass Media (SMM) is one of Russia's leading media holdings that manages media assets in pay TV, advertising, digital content distribution and VAS services for

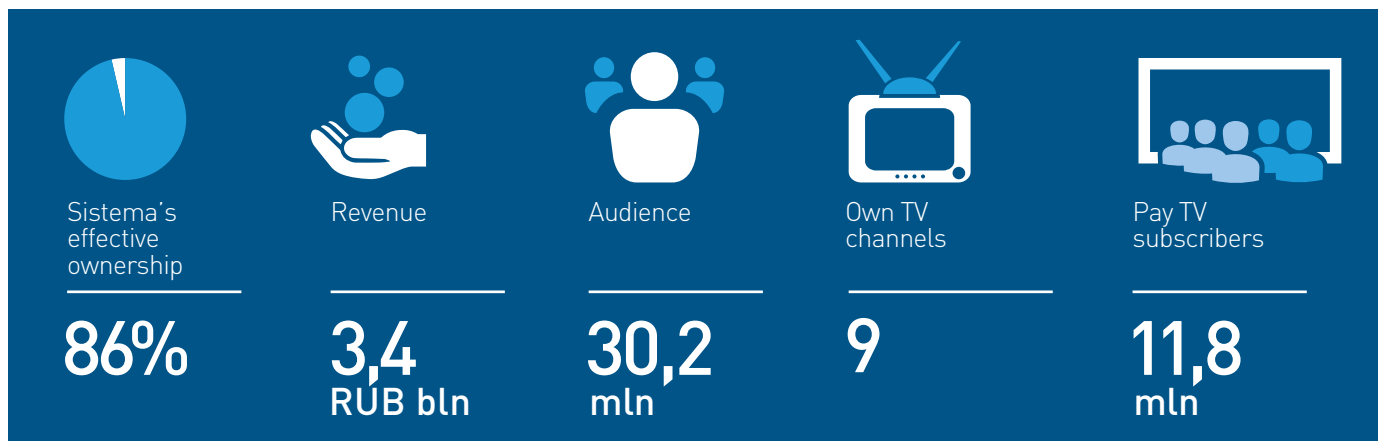
telecom operators. SMM owns and manages STREAM TV Company JSC («Stream TV»), RA Maxima JSC («Maxima»), TsTC LLC («TsTV»), and Stream LLC («Stream»).



Management

President – G.Sh. Khasianova

Chairman of the Board of Directors – A.V. Abugov



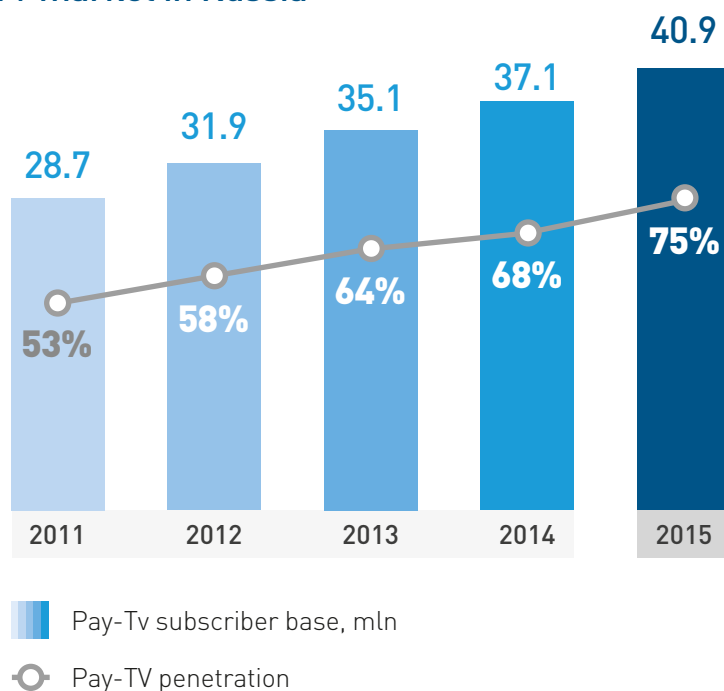
Industry*

Russia's multimedia market in 2014 was affected by the overall slowdown in economic growth rates and changes in the geopolitical situation.

In the segment of TV content production, changes in the geopolitical situation caused a decline in sales of Russian content in Ukraine and, as a result, a fall in profitability of Russian producers. The negative effect was partially offset by the growth of the Russian pay TV market. Due to the rapid growth of digital technologies, the market experienced considerable changes in terms of subscriber base structure, with the share of cable TV subscribers dropping from 52% to 49%.

* Association of Russian Communication Agencies, ZenithOptimedia, company data.

Pay-TV market in Russia



In 2014, the federal Law «On Mass Media» was amended to include provisions which capped the stake that can be held by foreign companies in any Russian media at 20%. The law affects the following three groups of market players: representative offices of foreign publishing holdings in Russia, Russian versions

of foreign TV channels broadcast via cable networks and public media holdings with foreign participation.

Advertising on non-terrestrial channels has been banned with effect from January 1, 2015; however, in February 2015, commercial channels with a foreign content not

exceeding 25% regained this right.

The most promising segments in the industry under the current conditions are still represented by digital media and Internet advertising using new audience targeting and analysis tools and technologies.

Steady growth in 2014

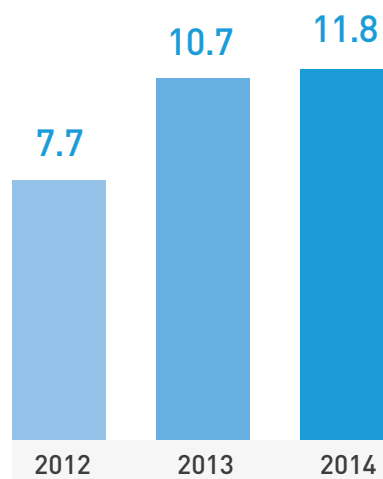
In 2014 work to optimise Sistema's media assets and improve their efficiency continued, allowing SMM to generate a net profit despite the general deterioration of the situation in the industry.

Stream TV channels maintain their leadership position in the market in terms of average annual reach in the majority of niche groups. The company has been actively expanding its subscriber base in the Russian and CIS markets: in 2014, its subscriber base grew by 10.3% to 11.8 mln.

In 2014, Stream LLC, which provides a universal multimedia entertainment service, actively developed in cooperation with MTS the following services launched in 2013: GOOD'OK (RBT – replacing the usual ringback tone sound with music), MTS-Info (information services for MTS subscribers), MTS Puls (application with entertainment content for mobile phones). The GOOD'OK service was also launched for subscribers of MTS Ukraine and MTS Belarus in 2014. Primary sales of RBT service to MTS Russia subscribers grew by 31% over the year.

In 2014, Stream LLC launched a new area – mobile advertising and distribution of A2P messages with information and service content based on its own proprietary solution. The successful implementation of the strategy ensured considerable growth of revenue and OIBDA. The revenue grew by approximately 60% to RUB 1.3 bln, while OIBDA reached RUB 330 mln, with the increase in OIBDA margin from 7% in 2013 to 26% in 2014.

TC Stream subscriber base, mln



Key events

- In March 2014, Gyulnara Khasianova was appointed SMM President.
- In April 2014, ORK signed a contract to launch a full-cycle film production project under the order of Rossiya Channel.
- In October 2014, Okhota i Kybalka (Hunting and Fishing) TV channel owned by TVC Stream won in the «Best Lifestyle Channel» category at the Golden Ray Awards.
- In December 2014, SMM took control over Stream LLC.

Operational strategy

SMM's strategy aims to further improve efficiency and profitability in traditional areas and launch new business areas in digital media and online advertising.

In the situation of changes in market conditions, Stream TV will focus on retaining current positions and increasing distribution in the CIS markets. The company plans to launch and promote an international version of the Hunting and Fishing Channel and special versions of channels for foreign markets.

Stream's development strategy envisages further development of value-added services (VAS) for MTS and development of mobile advertising services (A2P) in partnership with MTS.

Financial results

RUB millions	2014	2013	Change
Revenue	3,366	3,498	(3.8%)
OIBDA	977	1,454	(32.8%)
Operating profit	308	199	54.7%
Net income attributable to Sistema	95	15	554.0%
Net debt	292	204	43.1%

Revenue of SMM in rubles fell by 3.8% for the full 2014 and by 28.1% year on year in the fourth quarter. OIBDA in rubles decreased in 2014 by 32.8% compared to the previous

year and by 65.0% year on year in the fourth quarter of 2014. Decrease in revenues and OIBDA was due to a general deterioration of the situation in the industry (reducing

advertising budgets led to a fall in demand for TV series) as well as the loss of the market of Ukraine for the re-sale and distribution of television series.



CORPORATE GOVERNANCE SYSTEM

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Corporate Governance Principles

Maintaining the system of corporate governance and transparency at the level of the world's best practices is one of the crucial elements of the strategy of Sistema as an investment company. High quality of corporate governance and informational transparency enable the company to attract partners and investors and increase return on equity by taking more efficient managerial decisions. The Corporation's corporate governance system is based on the following core principles:

- transparency and clarity of all processes for investors and partners;
- a transparent dividend policy;
- an active and professional Board of Directors;
- investment decisions made in compliance with the established procedures;
- the attention of the Board of Directors to all transactions with related parties;
- an active role of the Board of Directors in the strategic planning process;
- development of corporate governance in portfolio companies.

Sistema is guided by these principles in all of its activities, including strategic and financial management, HR and social policy,

reporting, control and audit, risk management.

Sistema's principles and procedures of corporate governance are set forth in its Charter and a number of publicly available internal regulations. Together these documents define the structure and competence of the Corporation's governance and control bodies. The Corporate Governance and Ethics Code sets forth additional commitments of Sistema in the area of transparency, social responsibility, and ethical business principles.

Sistema makes every effort to bring its corporate governance practices in line with the recommendations specified by the Bank of Russia in the Corporate Governance Code [Letter of the Bank of Russia No. 06-52/2463* dated April 10, 2014] and the guidelines set out in the UK Corporate Governance Code.** The consistency of Sistema's corporate governance practices with the standards set out in the Corporate Governance Code and the UK Corporate Governance Code is analyzed in Annexes 9.7 and 9.8 to this report. Where corporate governance practices at Sistema deviate from the recommendations set forth in the above documents, the Corporation clarifies how the balance of interests is otherwise maintained in accordance with the applicable standards of corporate governance.

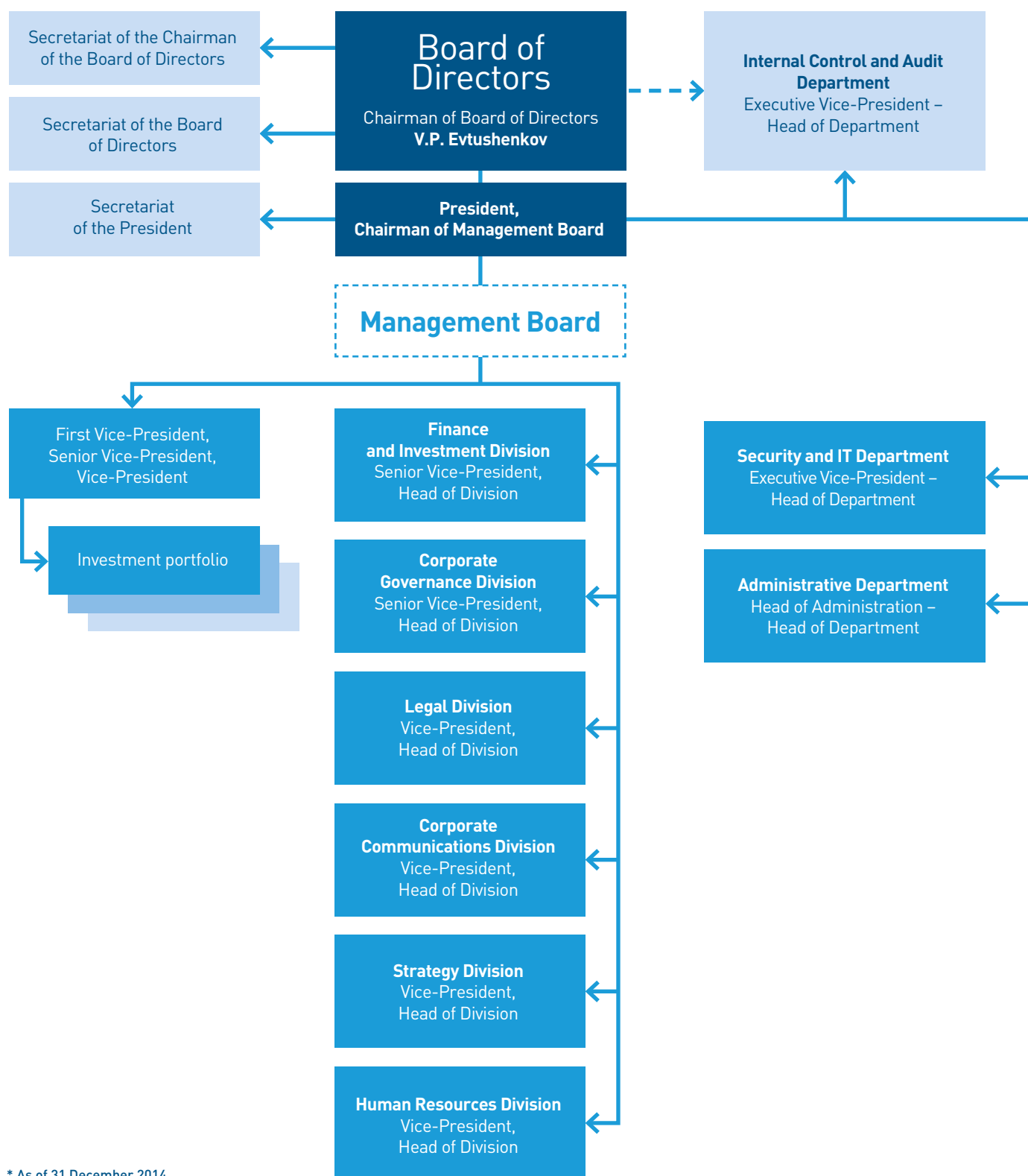
The Corporation's main governance bodies are: the General Meeting of shareholders, the Board of Directors, the President and the Management Board. The Board of Directors and the President have committees that conduct a more in-depth analysis of the proposed solutions in specific areas and develop recommendations for the governance bodies of Sistema.

The existing organizational structure of the Corporation that was adopted in December 2013, including the adjustments and amendments made later, reflects Sistema's operation in accordance with investment company model.

* The text of the Corporate Conduct Code is available at the following address: http://www.cbr.ru/sbrfr_new/files/legislation/letters/2014/inf_apr_1014.pdf

** The text of the UK Corporate Governance Code is available at the following address: <http://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/UK-Corporate-Governance-Code-September-2012.aspx>

Corporate Governance Structure of Sistema JSFC*



* As of 31 December 2014.

GENERAL MEETING OF SHAREHOLDERS

Principles of operation

The General Meeting of shareholders is the supreme governance body of Sistema. Its operation is governed by the laws of the Russian Federation on joint-stock companies, as well as the provisions of the Corporation's Charter and bylaws. The General Meeting procedure aims to make sure that the rights of the sharehold-

ers are respected and all applicable legal requirements, as well as best international practices in corporate governance, are observed.

Information and materials for the meeting are made available to the shareholders in Russian and in English and are published on Sistema's

official website (www.sistema.ru; www.sistema.com). Along with the notice of the forthcoming meeting, shareholders get voting ballots. The venues of Sistema's General Meetings of shareholders are always located in the vicinity of the Corporation's headquarters.

Observance of shareholders' rights

Sistema aims to ensure maximum protection of the shareholders' right to participate in running the Corporation and receiving profit. The fundamental rights of a shareholder in this respect are the rights to participate in the work of the General Meeting of shareholders and to vote on the items on the agenda, and also the right to receive dividends.

To secure the right of the shareholders to take part in the work of the general meeting, a notice of Sistema's General Meetings of shareholders, as well as voting ballots, are circulated to all the shareholders at least 30 days before the meeting, and all materials covering the agenda items are published on the Company's website in Russian and in English (www.sistema.ru; www.sistema.com). The ballot may be filled out by the shareholder in advance and mailed to Sistema to the address specified in the ballot. In this case the vote of the shareholder will be taken into account when counting the voting results.

Depository receipt holders may vote on the agenda items of shareholder meetings by proxy through Deutsche Bank AG, which is used as the depository bank for Sistema's GDR programme:

*Global Equity Services,
Trust and Securities Services,
Email: adr@db.com*

The votes of GDR holders, information about whom has been disclosed to the depository, are collected by Deutsche Bank AG via clearing systems and are included in the general voting ballot of the depository, with all votes cast for the proposed draft resolution, against it, and abstentions specified.

Each shareholder can also attend General Meetings of shareholders in person or through a representative and vote on the agenda items directly at the Meeting.

An important guarantee of the shareholder's right to participate in running the Corporation is the right to access documents that the Company is obliged to retain in line with the provisions of the Federal Law On Joint-Stock Companies. To exercise this right, a shareholder should send a written request to the Corporate Secretary of Sistema asking for access to the documents that the shareholder wishes to see. When a shareholder is granted access to confidential documents, such a shareholder makes a written non-disclosure obligation

thus providing a guarantee for the protection of the rights of all the shareholders of the Corporation.

Holders of material blocks of shares are entitled to make proposals on the agenda of the General Meeting of shareholders and nominate candidates to the Corporation's governance and control bodies*. Proposals on the agenda of the Annual General Meeting of shareholders of Sistema are accepted in writing within 100 days after the end of the financial year**. Candidates nominated to the governance and control bodies of the Corporation are preliminarily interviewed by the Nomination, Remuneration and Corporate Governance Committee of the Board of Directors of Sistema.

*** Holders of 10 and more % of the Company's voting shares also have the right to request an Extraordinary General Meeting of shareholders to be conducted.**

**** If an Extraordinary General Meeting of shareholders is conducted with its agenda containing an item on the election of the Board of Directors, holders of sufficient blocks of shares have the right to nominate candidates to the Board of Directors. Proposals to this effect must be received by the Company no later than 30 days before the date of such a meeting.**

For the purposes of observance of the shareholders' rights to the Company's profit the Corporation announces the amount of dividends recommended by the Board of

Directors in advance along with the date on which the shareholder register is to be made for the purposes of the payment. Therefore, the shareholders always have the

opportunity to dispose of their shares taking into account the expected dividend payments.

Dividend policy

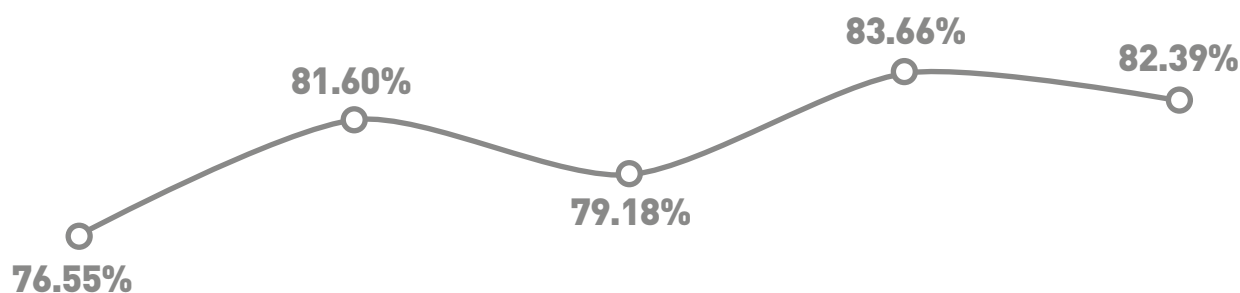
To determine the recommended amount of dividends payable, the Corporation's Board of Directors abides by the dividend policy approved in October 2011. In compliance with this policy, the amount of dividends payable shall

be at least 10% of the group's net income generated during the previous financial year as per reports prepared in compliance with international accounting standards and at least 10% of the net cash income generated

by the Corporation's investment transactions over the same period (special dividend). This approach allows the Corporation to pay predictable amounts of dividends.

General Meetings held in 2014 and their results

Quorum at General Meetings of Shareholders for three years



EGM dated
14/06/2012

AGM dated
30/06/2012

EGM dated
01/11/2012

AGM dated
29/06/2013

AGM dated
28/06/2014

The Annual General Meeting of the shareholders of Sistema was held on 28 June 2014. The AGM (1) approved the Company's annual report and annual financial statements, including the profit and losses account for 2013, (2) determined the amount, procedure, forms and timelines of dividend payments on the company's shares, (3) elected members of the Board of Directors, (4) elected members of the Auditing Commission, (5) and approved the auditors of the Corporation.

As resolved by the Annual General Meeting of shareholders and recommended by the Corporation's Board of Directors, RUB 19, 879m were allocated to pay dividends, which equalled RUB 2.06 per one ordinary share of Sistema. The amount of dividends was determined in compliance with the current dividend policy. Dividends increased by 115% compared with the amount paid in 2013.*

The Annual General Meeting of shareholders approved CJSC Deloitte and Touche CIS as Sistema's auditor for 2014 to perform the audit according to the Russian Accounting Standards and the US GAAP. The auditor was selected following an open tender organized by the Audit, Finance and Risk Committee of the Board of Directors of Sistema.

In 2014, Sistema did not convene any Extraordinary General Meetings.

* In 2013, RUB 9,264m were allocated for dividends, equalling RUB 0.96 per one share of Sistema JSFC.

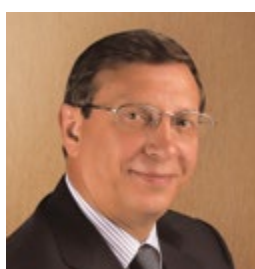
BOARD OF DIRECTORS

The Board of Directors of Sistema is responsible for strategic management of the Corporation and plays the key role in organising an effective system of corporate governance: it determines the strategy, works out strategic and financial development plans, sets the principles for investing,

appraises executive performance and assesses risks, approves principles for corporate governance procedures, approves transactions and controls the work of the Corporation in general. The terms of reference of the Board of Directors are set out in the Charter of Sistema.

The Board of Directors of Sistema effective as of 31 December 2014 was elected at the Annual General Meeting of the Company's Shareholders on 28 June 2014, and its membership remained unchanged compared to the previous year. The Board of Directors of Sistema has 13 members. Independent members of the Board of Directors form a majority.

Members of the Board of Directors of Sistema elected on June 28, 2014



Vladimir Evtushenkov

Chairman of the Board of Directors



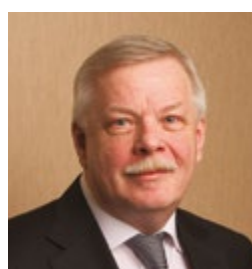
Alexander Goncharuk

Deputy Chairman of the Board of Directors
Non-executive member



David Yakobachvili

Deputy Chairman of the Board of Directors
Independent Director



Sergey Boev

Non-executive member



Brian Dickie

Independent Director



Dmitry Zubov

Non-executive member



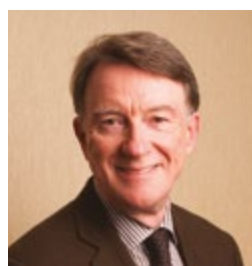
Robert Kocharyan

Independent Director



Jeannot Krecké

Independent Director



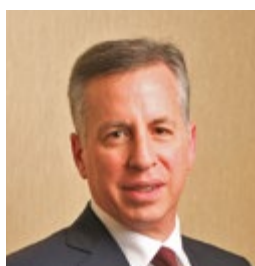
Peter Mandelson

Independent Director



Munnings Roger

Independent Director



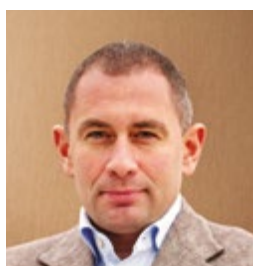
Mark Holtzman

Independent Director



Serge Tchuruk

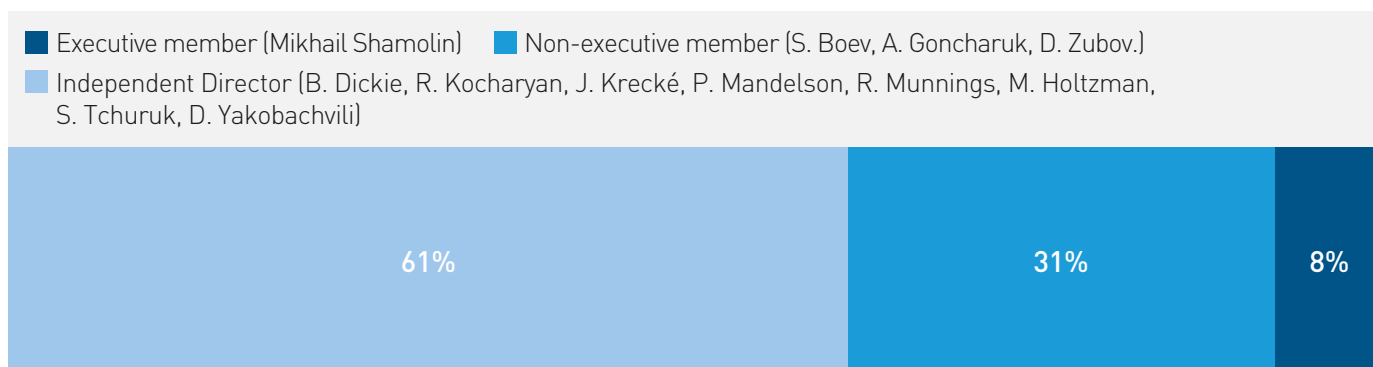
Independent Director



Mikhail Shamolin

Executive member,
President and CEO

Composition of Board of Directors



Meetings of the Board of Directors

approved work plan for the year. The work plan of the Board of Directors is developed proceeding from the logics of the strategic planning and reporting cycle of Sistema. Reports on and discussions of additional matters (such as transactions) are included in agendas of scheduled Board meetings

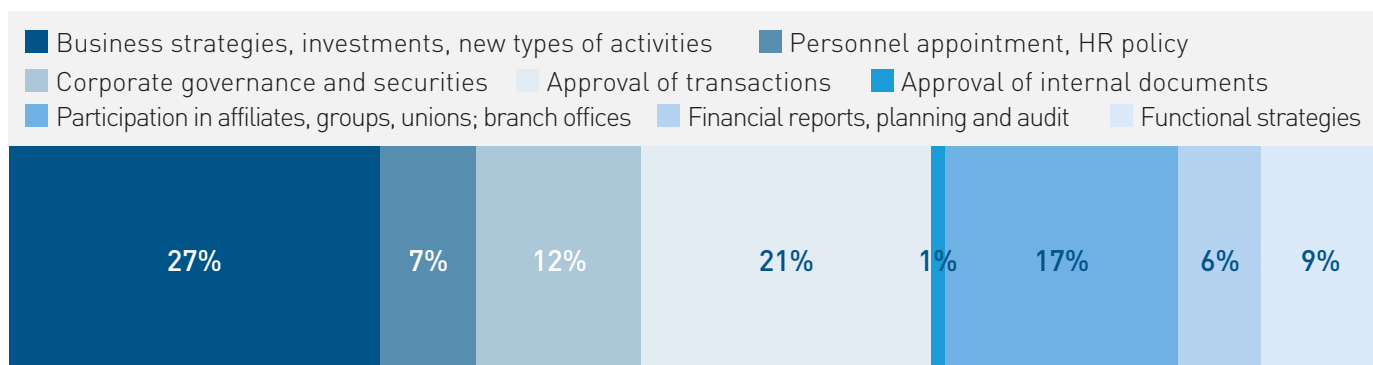
on a routine basis. Additional sessions are organized whenever an urgent matter needs to be considered.

Forming the work plan of the Board of Directors and including additional items into the plan falls within the remit of the Board Chairman.

In 2014 the Board of Directors held 10 meetings: eight scheduled regular Board meetings, and two extraordinary meetings, one of which was held in the form of absentee voting. The Board of Directors reviewed a total of 100 agenda items in 2014:

	2014	2013
Number of in-person meetings	9	8
Number of letter ballots	1	1
Number of items in accordance with the BoD work plan	39	43
Number of items reviewed at Board meetings	100	105

Subjects reviewed by the Board of Directors in 2014



In 2014 the agenda of the Board of Directors was mainly related to business strategy, approval of transactions (including shareholdings in portfolio companies) and corporate

governance. The Board of Directors' focus on these areas proceeds from the nature of the Corporation's operation as an investment company, when particular attention should

be given to strategy and corporate governance of portfolio companies, portfolio strategy, analysis of new investment opportunities and transactions.

Preparation for the meetings and quorum of the Board of Directors

The procedure of preparation for the meetings of the Board of Directors is aimed at ensuring an efficient use of the time and experience of the Board members in order to enable them to take important decisions on the Corporation's strategic development. Materials on the agenda are provided to the Board of Directors of Sistema 10 days before meetings, which gives them

the possibility to comfortably form their own position for the voting. The majority of main agenda items must be previewed at the meetings of Committees of the Board of Directors of the Corporation.

Members of the Sistema Board of Directors meet with the speakers and the management at a business dinner the evening before the

meeting, so that they can discuss the items on the agenda of the Board and inquire about the voting positions of the parties in an informal environment.

Sessions of the Board of Directors normally take place with high attendance of the Board members. The average quorum of meetings in 2014 was 91.5%.

Participation of the Sistema Board members in meetings of the Board of Directors and its committees in 2014*

	Board of Directors	Strategy Committee	Audit, Finance and Risk Committee	Nomination, Remuneration and Corporate Governance Committee	Ethics and Control Committee	Investor Relations and Dividend Policy Committee
Participation in meetings						
V. Evtushenkov	9/10**	8/11				
S. Boev	9/10	6/11	10/13		4/7	
A. Goncharuk	7/10	4/11		5/8	3/7	
B. Dickie	10/10	0/3		3/3	7/7	
D. Zubov	10/10			8/8		
R. Kocharyan	10/10	5/8		8/8	6/7	
J. Krecké	10/10			8/8		7/7
P. Mandelson	8/10		11/13			5/7
R. Munnings	10/10		13/13	8/8	7/7	7/7
M. Holtzman	7/10		12/13			5/7
S. Tchuruk	9/10	1/3	2/5		6/7	
M. Shamolin	10/10	10/11		5/5		1/7
D. Iakobachvili	10/10	6/8	13/13			7/7

* The membership of the Board of Directors is given as of 31 December 2014.

** The first number denotes the number of meetings attended by the Board member, the second number stands for the total number of meetings the member could potentially participate in.

Committees of the Board of Directors

Nomination, Remuneration and Corporate Governance Committee

R. Kocharyan
Committee Chairman,

A. Goncharuk
B. Dickie, D. Zubov,

J. Krecké,
R. Munnings.



The main tasks

- preliminary consideration of the candidates:
 - to the board of directors;
 - to the top management positions in the Corporation and portfolio companies;
- to the boards of directors of portfolio companies;
- to the position of corporate secretary of the Corporation;
- the policy of motivation and compensation for the Corporation employees;
- management's performance evaluation and determination of parameters of awarding bonuses to employees;
- systems of corporate governance of the Corporation and portfolio companies, protection of rights and interests of shareholders.

Meetings and issues considered in 2014

8 meetings, considered 26 issues



Audit, Finance and Risk Committee

R. Munnings
Committee Chairman,

S. Boev, P. Mandelson,
M. Holtzman,

S. Tchuruk,
D. Iakobachvili

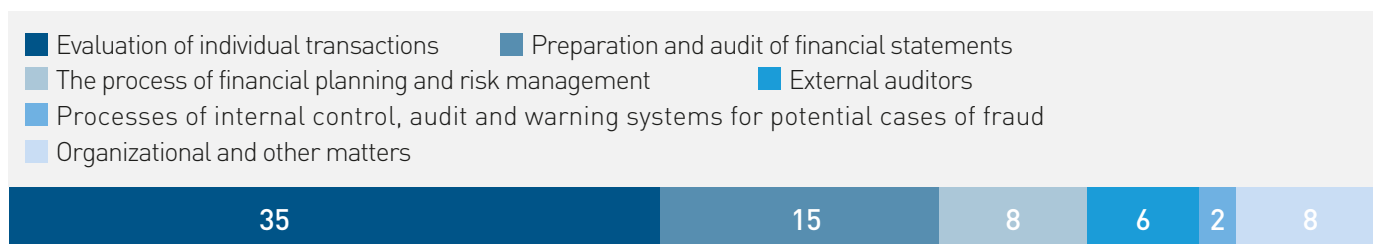


The main tasks

- Preparation and audit of the financial statements of the Corporation, control of these processes;
- interaction with the external auditors of the Corporation;
- assessment of the risk management system and compliance with applicable legal requirements in the area of financial reporting, auditing and planning;
- budget process and financial modeling;
- internal audit;
- warning system on potential cases of fraud;
- preliminary assessment of large transactions and transactions with interested parties.

Meetings and issues considered in 2014

13 meetings, considered 74 issues

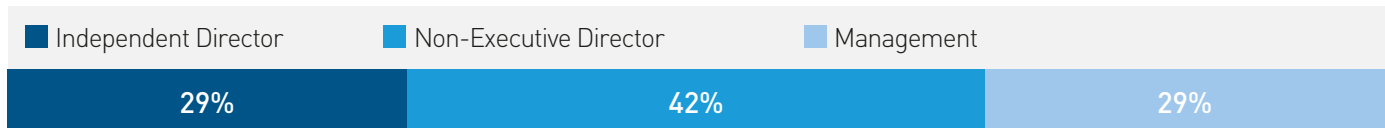


Strategy Committee

V. Evtushenkov
Committee Chairman,

S. Boev, A. Goncharuk,
R. Kocharyan, M. Shamolin,

D. Iakobachvili,
M. Hecker



The main tasks

- strategy development for portfolio companies;
- strategic planning methodology review;
- preliminary approval of the strategy and the strategic objectives of the Corporation;
- reviewing mergers and acquisitions and major investment projects;
- all mergers and acquisitions in the Group with monetary value of more than US\$ 100 million;
- all projects of the Group associated with entering new markets;
- all projects of the Group with substantial Government participation.

Meetings and issues considered in 2014

11 meetings, considered 12 issues, all questions on the development strategy of the portfolio companies.

Ethics and Control Committee

A. Goncharuk
Committee Chairman,

S. Boev, B. Dickie,
R. Kocharyan,

R. Munnings,
S. Tchuruk

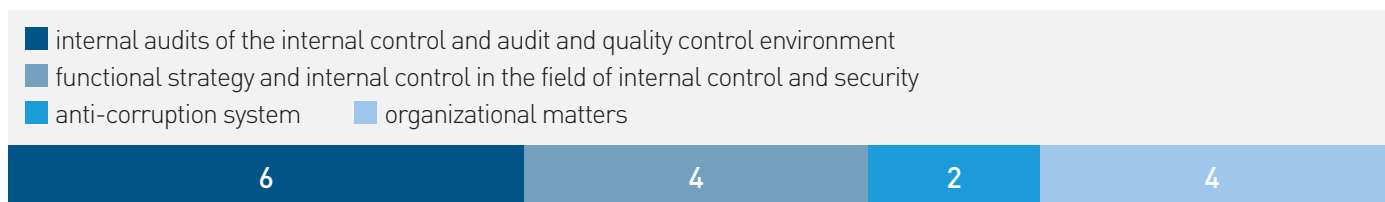


The main tasks

- internal control and audit (together with the Audit, Finance and Risk Committee);
- function of corporate security;
- monitoring of compliance with the Code of Ethics;
- anti-corruption system in the Corporation and Group companies.

Meetings and issues considered in 2014

7 meetings, considered 16 issues.



Investor Relations and Dividend Policy Committee

D. Iakobachvili
Committee Chairman,

J. Krecké, P. Mandelson,
R. Munnings,

M. Holtzman,
M. Shamolin



The main tasks

- maintaining effective relationships with the financial community and public authorities as well as increasing the investment attractiveness of Sistema securities;
- the dividend policy of Sistema, including the formation of recommendations to the Board of Directors in respect of the amount of dividends payable;
- protect the rights and interests of the shareholders.

PRESIDENT AND THE MANAGEMENT BOARD



Mikhail Shamolin

President of Sistema,
Chairman of the Management Board

- Mikhail was born in 1970 in Moscow.
- In 1992, he graduated from the Moscow Automobile and Road Technical Institute.
- In 1993, graduated from the Russian Presidential Academy of Public Administration.

Sistema's Management Board determines the methods of implementing the development strategy of the Corporation, works out development plans, sets investment procedures and controls their observance, appraises the performance of the personnel, and pre-considers items submitted to the Corporation's Board of Directors.

- In 1996-1997, he completed an Executive Programme in Finance and Management at the University of Pennsylvania's Wharton School of Business.
- In 1998-2004, he worked at the international consulting company McKinsey&Co.
- In 2004-2005, he held the position of the Managing Director for the Ferroalloys Division at Interpipe Corp (Ukraine).
- In 2004-2005, he held the position of the Managing Director for the Ferroalloys Division at Interpipe Corp (Ukraine).
- In 2005-2011, he was Vice President for Sales and Customer Service, then Vice President, Head of MTS Russia and President of MTS.
- Appointed President of Sistema on 10 March 2011. On 15 March 2014, the Board of Directors reappointed Mr Shamolin President and Chairman of the Management Board of Sistema for a three-year term.

In 2014, the Management Board of the Company held 24 meetings and considered 33 agenda items in the following key areas:

1. Preliminary review of matters to be submitted to the Board of Directors, including:
 - the Corporation's investment policy and priority investment areas;
 - development strategy and value creation for key portfolio assets of Sistema;
 - internal control and audit;
 - HR policy;
 - corporate social responsibility.

The President of Sistema is a permanent chief executive officer whose main function is executive management and settlement of relevant matters outside the remit of the General Meeting of shareholders, Board of Directors and Management Board for the purposes of ensuring profit of the Corporation, as well as observance of its shareholders' rights and legitimate interests. The President reports to the Board of Directors and the General Meeting of the Corporation's shareholders.

From 10 March 2011, Sistema's President is Mikhail Shamolin. On 15 March 2014, the Board of Directors took the decision to extend his appointment as the Corporation's President for three years.

2. Preparation of forecasts of and reports on the execution of quarterly, semi-annual, and annual budgets.
3. Strategic planning at the Corporation and S/As, including the establishment of top-down indicators of the strategic planning cycle.
4. Debt and borrowings management.
5. Risk management and preparation of risk maps.
6. Monitoring and management of investment projects.

Members of Sistema's Management Board



Mikhail Shamolin

Chairman of the Management Board, President and CEO



Anton Abugov

First Vice-President, Investment portfolio manager



Christopher Alan Baxter

Senior Vice-President, Investment portfolio manager



Elena Vitshak

Vice-President, Head of HR Department



Sergey Drozdov

Senior Vice-President, Head of the Corporate governance division



Felix Evtushenkov

First Vice-President, Investment portfolio manager



Leonid Monosov

Vice-President, Investment portfolio manager



Oleg Mubarakshin

Vice-President, Head of the Legal functional division



Vsevolod Rozanov

Senior Vice-President, Chief Financial Officer



Andrei Terebenin

Senior Vice-President, Investment portfolio manager



Ali Uzdеноv

Senior Vice-President, Investment portfolio manager



Michael Hecker

Vice-President, Head of Strategy

After the end of the reporting period, in February 2015, Nikolay Vasilkov became member of the Management

Board, after being appointed Vice President, Head of Strategy Function. Michael Hecker was at the same

time relieved of the responsibilities of a Management Board member.

Changes in the top management in 2014

A number of changes in the top management of the Company took place in 2014:

A. Buyanov	25 June 2014	was relieved of his duties as First Vice President.
A. Terebenin	22 May 2014	was appointed Senior Vice President and relieved of his duties as Vice President, Head of the Corporate Communications Function.
A. Chupin	07 May 2014	was relieved of his duties as Vice President.
D. Khidasheli	30 September 2014	was relieved of his duties as Vice President.
M. Hecker	12 February 2014	was appointed Vice President, Head of Strategy Function.
A. Shlyakhturov	10 September 2014	was transferred from the position of Executive Vice President, Head of the Security and IT Department to the position of the Advisor to the Chairman of the Board of Directors.
V. Shukshin	10 September 2014	was appointed Executive Vice President, Head of the Security and IT Department.

INTERNAL CONTROL AND AUDIT

The process of internal control is implemented at all levels of the Corporation's management, including the Board of Directors, Board Committees, the Corporation's management and the Internal Control and Audit Department.

Internal audit at the Corporation and Sistema Group companies is the scope of responsibility of the Internal Control and Audit Department that functionally reports to the Board of Directors and administratively to the President. Head of the Department is appointed and dismissed by the President following a resolution passed by the Corporation's Board of Directors after preliminary approval of the Board's Ethics and Control Committee. Head of the Department is a certified internal auditor and has more than 15 years of experience in the field.

The main tasks of the Internal Control and Audit Department are:

- helping shareholders and the management improve the internal control system by performing regular audits of efficiency of the Corporation's internal control, risk management, and corporate governance systems;
- contributing to the achievement of the Corporation's strategic goals in the most efficient ways possible;
- supplying the management and the shareholders of the Corporation with objective information on existing internal risks and their probability;
- enhancing the awareness of the Corporation's management about the performance of Sistema Group companies;
- controlling the achievement of the goals of the shareholders of the Corporation and Sistema Group companies.

To perform its key tasks, the Internal Control and Audit Department carries out the following functions:

- performing independent audits of individual operations, processes, and units;
- assessing the efficiency of the internal control system;
- assessing the efficiency of the risk management system;
- assessing the corporate governance system, preventing violation of law and the Corporation's regulations, ensuring observance of professional and ethical standards, and preparing recommendations for improvement thereof;
- developing recommendations to remedy deficiencies identified and monitoring remediation thereof;
- examining and evaluating documents provided with regard to specific investment projects for compliance with current regulations; performing scheduled and unscheduled monitoring of performance against project targets;
- ensuring uninterrupted functioning of the whistleblowing programme;
- administering investigations, including internal ones;
- monitoring compliance with the Corporation's internal regulations;
- monitoring execution of assignments issued by the Management Board and the President of the Corporation;
- monitoring and investigating instances potentially qualifying as disciplinary violation and/or violation of execution discipline and/or conflict in the Corporation or Sistema Group companies.

The Internal Control and Audit Department has all the resources and authority required to perform the above functions.

The Internal Control and Audit Department closely interacts with the Corporation's external auditors, coordinates work and offers consultations in the course of preparing the Department's annual audit plan with regard to assessment of the efficiency of internal control over financial accounts, and also during discussion and assessment of identified risks.

In 2014, the Internal Control and Audit Department conducted 65 scheduled and unscheduled audits to assess the efficiency of internal control and risk management systems. Audits performed by the Internal Control and Audit Department did not uncover any weaknesses or risks that could affect the sustainability of the Corporation's business as a whole.

Reports on results of activities performed by the Internal Control and Audit Department in H1 2014 and FY2014 were submitted to the Audit, Finance and Risk Committee and to the Ethics and Control Committee of Sistema's Board of Directors*. The Department's report for FY2014 was reviewed by Sistema's Board of Directors.

In December 2014, in accordance with requirements of the Listing Rules of the Moscow Exchange, the Corporation's Board of Directors approved the Policy on internal audit at Sistema, which defines the goals, objectives and powers of the Internal Control and Audit Department.

* Joint meetings of the Committees.

After the end of the reporting period, in February 2015, the Board of Directors approved the Policy on the internal control system. This top level documents sets forth the key principles of organisation of internal control as an ongoing and integrated process, which involves all divisions and governance bodies of the

Corporation. Notably, the Policy on the internal control system defines:

- the goals and objectives of the internal control system;
- principles of functioning of the internal control system;
- the structure of the internal control system and the list of its entities;

- division of responsibilities and powers between entities of the internal control system (management, the Internal Control and Audit Department, the Board of Directors and Board Committees).

External Audit

In compliance with the decision of the Board's Audit and Finance Committee, the following procedures have been developed at the Corporation for selecting external consultants for the purposes of audit of the financial and accounting reports of Sistema. The Audit and Finance Committee

performs annual assessment of the quality of audit services. If the quality of services provided by the current auditor is deemed insufficient, the Audit Committee arranges a tender for selection of a new auditor. If the quality of services provided by the current auditor is deemed sufficient, nego-

tiations will be held with the auditor about the price of auditing services for the next period. However, to ensure impartiality and objectivity of the auditor, the Audit and Finance Committee of Sistema has decided that a tender for auditing services shall be held at least once in every five years.

DEVELOPMENT OF THE CORPORATE GOVERNANCE SYSTEM IN 2014

In 2014, 13 members were elected to the Corporation's Board of Directors, out of whom eight meet the independence criteria of the Moscow Exchange and the Russian Corporate Governance Code. The following independent directors were elected to the Board:

- David Iakobachvili;
- Brian Dickie;
- Robert Kocharyan;
- Jeannot Krecké;
- Peter Mandelson;
- Roger Munnings;
- Marc Holtzman;
- Serge Tchuruk.

All independent directors have extensive practical work experience and solid reputation in the international professional community, which means that their judgment in the capacity of Board members will not be influenced by the management or individual shareholders. One of the Board members has vast experience in the audit of financial statements.

Independent directors make up the majority of the Board, which ensures the required level of objectivity and independence from the influence of the Corporation's executive bodies in the course of decision-making by the Board.

In June 2014, the Corporation's ordinary shares were included in the first (top) quotation list of the

Moscow Stock Exchange, thus confirming their status as the first class securities in the Russian market, attesting to the high assessment of Sistema's corporate governance standards and granting access to a broader range of investors.

In view of the above, the Corporation assumed additional commitments to maintain the corporate governance system at the high level and bring some of its components in compliance with the new requirements of the Listing Rules of the Moscow Exchange. In December 2014, the Board of Directors approved new versions of the terms of reference of some Board Committees and the Corporate Secretary and adopted a new Policy on internal audit. The

introduced amendments formalised the functions of Board Committees and the Corporate Secretary that are directly specified in the Listing Rules and introduced provisions on the procedure of appointment of head of the Internal Control and Audit Department. The Corporation also plans to amend the Terms of

Reference of the General Meeting of Shareholders and the Terms of Reference of the Board of Directors in the near term.

In June 2014, Sistema's Annual General Meeting of shareholders approved payment of dividends in the amount of RUB 19,879m,

i.e. RUB 2.06 per ordinary share, which corresponds to a dividend yield of ca. 5.22% per annum. The sum of dividends was determined in compliance with the current dividend policy, which was applied for the second successive year.

Remuneration

Remuneration and compensations payable to members of Sistema's Board of Directors are calculated on the basis of the Policy on remuneration and compensations payable to members of the Board of Directors of the Corporation, approved by the resolution of the General Meeting of shareholders of Sistema on 30 June 2006 (Minutes No.1-06) as amended by the resolution of the General Meeting of the shareholders of Sistema on 16 February 2009 (Minutes No.1-09). The Policy provides for the payment of the following to the Board members:

- fixed amounts for participation in meetings of the Board of Directors and its Committees, including reimbursement of expenses related to participation in meetings of the Board of Directors;
- fixed amounts for acting in the capacity of the Chairman or a Deputy Chairman of the Board of Directors, and for chairing Board Committees;
- based on the performance during a year, members of the Board of Directors get additional performance-related remuneration in the form of a fixed amount, half of which is payable in shares (US\$ 250,000 - 325,000);
- also, if the capitalisation of the Corporation has grown over the year, members of the Board of Directors get additional remuneration amounting to 0.1% of the incremental capitalisation.

The Policy on remuneration and compensations payable to members of the Board of Directors of the Corporation also envisages standard liability insurance for Board members.

The Corporation does not provide loans to Board members.

The short-term (up to 1 year) incentive scheme for the top managers of Sistema in 2014 consisted of the following elements:

- a fixed monthly salary determined in line with the internal system of job categories (grades);
- bonuses paid for project implementation and generating cash income. Remuneration is paid based on workers' individual performance and positive cash flow generated by projects of Investment Portfolios and Functions and Departments of Sistema. Payments may amount to up to 20% of cash income exceeding the target.

In 2014, the three-year long-term incentive programme for Sistema's top management (2012-2014) was completed. Its members were allocated the last shares due for distribution for the last period of the programme.

The long-term incentive system for top management of Sistema was extended for another three-year period (2015-2017). The programme is aimed at increasing Sistema's shareholder value and creating additional incentives for maintaining long-term

employment and corporate relations between the Corporation and its management;

No extra compensation above the level stipulated by labour laws of the Russian Federation is paid to the President or other senior executives in case of termination of employment.

Sistema does not pay remuneration to members of executive bodies for serving on the Management Board.

The Corporation does not grant loans to senior executives.

Top executives of the Corporation were paid a total of RUB 2,746,764,517 in fixed salary and bonuses for the calendar year 2014. Payments to top executives under the long-term incentive programme in the form of the Corporation's shares totalled RUB 1,659,419,767 in 2014, including RUB 1,559,140,150 for years 2013 and 2012.

Remuneration paid to the members of Sistema's Board of Directors in 2014 totalled RUB 334,447,900. Board members also received reimbursement of their expenses incurred in connection with their duties amounting to RUB 3,608,900.

RISKS

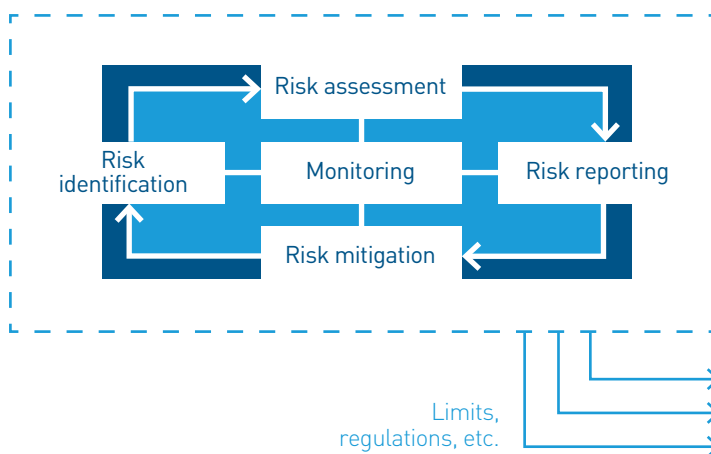
The key risk factors related to Sistema

The Corporation may face a variety of risks in the course of its business operations. The main risks that the Corporation may encounter are the consequences of the processes and factors that Sistema has little or no influence on. Hence, efficient assessment and management of risks remain an important component of the strategy of Sistema.

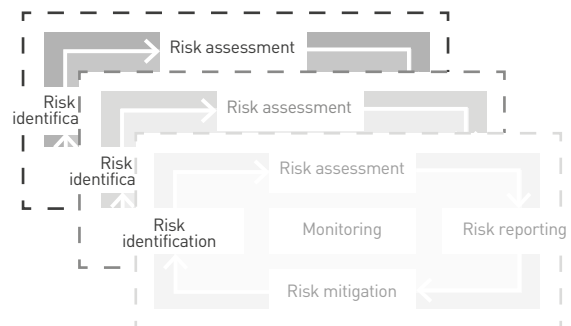
The risk management system of Sistema is based on a two-level approach to risk management, namely, detection of risks in subsidiaries and affiliates and in the Corporation and their integration for assessing their influence on the Group in general. The main objective is to provide a reasonable guarantee that the strategic goals

will be achieved and to ensure that the level of risk will be kept within the limits that are acceptable for the shareholders and the management of the Corporation. The integrated risk management system (ERM) operating at Sistema was built in compliance with international standards, recommendations and best practices in risk management.

Corporation



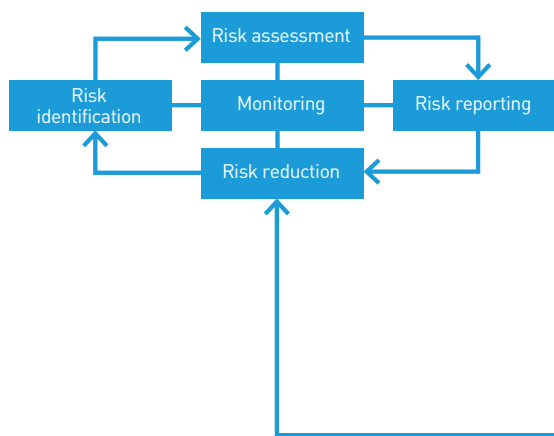
At subsidiaries level



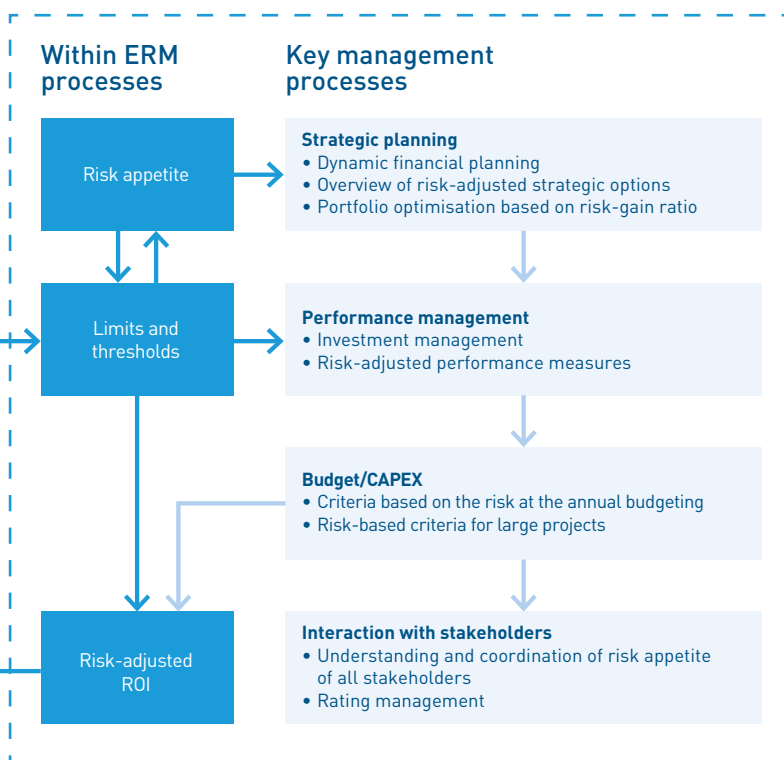
The integrated risk management system (ERM) implemented in the Corporation envisages the presence of the following components and procedures:

- identification of risks at all levels of the management (from the top to the line management), which includes finding the risk owner and making a risk passport;
- primary assessment of the materiality of identified risks and their analysis (VaR methodology);
- ranging of risks by management levels;
- assessment of the aggregate influence of material risks on the Company's key financial indicators (Monte Carlo modelling);
- development of plans to mitigate identified risks at all management levels;
- regular risk monitoring and control;
- preparation of reports on the company's risks.

Risk management process



Link with the decision-making process



As part of quarterly ERM procedures the risk managers of Sistema Group compile risk registers for subsidiaries and a consolidated risk register for the Group, prioritise risks and aggregate them into portfolios, develop a risk map and analyse its key trends, conduct an analysis of the impact that material risks have on the financial results of specific subsidiaries and Sistema Group as a whole, using simulation and financial modelling methods.

In order to deal with the risks included in the risk register of Sistema Group the company developed risk management (mitigation) and response plans for specific subsidiaries, which may be extended, adjusted and then approved by the risk committees of the respective companies.

Quarterly monitoring of the Corporation's risks is performed at the level of the Management Board and the Risk Sub-Committee operating under the umbrella of the Finance and Investment Committee of Sistema by reviewing the effects of the mitigation and response measures taken and by reassessing the already identified and/or new risks, as well as by evaluating their potential impact on the financial results of the Corporation and Sistema Group as a whole.

The top management of Sistema presents a regular risk management report to the Audit, Finance and Risk Committee of the Board of Directors of Sistema. Sistema's Board of Directors review risk management reports on a biannual basis.

The Group's risk management system keeps developing and improving. Various risk mitigation

mechanisms are being widely applied (including insurance), financial risk control and response procedures are being improved. At the Corporation level particular attention is given to the risks of investment projects starting from the stage of project origination up to the stage of completion. The risk management systems of subsidiaries are currently at different stages of development depending on the time of their introduction. These systems are being gradually improved in accordance with the plans approved earlier. As new assets are added to Sistema's portfolio, individual plans are developed in order to implement risk management systems depending on the specific needs of such assets. The risk management processes of subsidiaries are monitored by the Corporation via Sistema's representation in collective governance and executive bodies of S/As.

External risks

The risks related to changes in the political and economic situation in Russia are material to Sistema because most of the Corporation's

business is conducted in the Russian Federation. Moreover, many of the Corporation's subsidiaries operate in the emerging markets, including

Armenia, the Republic of Belarus, Ukraine, Uzbekistan, Turkmenistan and India, which are also characterized by the risks listed below.

Economic risks

- The business of Sistema is inextricably linked with the state of the global economy and financial markets and heavily depends on the Russian economy in particular, which in its turn relies on the export of oil, gas and other commodities. Further weakening of the rouble against the US dollar and Euro amid a slump in the oil prices, imposed sanctions and increased capital flight from Russia may result in a rise in costs and a drop in revenues or impede the achievement of financial targets and repayment of debt by the Group's subsidiaries.
- Capital flight from Russia and the downgrading of the sovereign credit rating by international rating agencies, as well as restrictions introduced for foreign companies in Russia as a result of sanctions, may have a negative impact on the joint ventures (partnerships) and new investment projects of the Group's companies. Growing inflation may result in higher expenses and, therefore, put pressure on profit margins and also affect the domestic demand for products of Sistema Group's companies.
- If in the medium term sanctions are maintained and the access of Russian banks and businesses to foreign debt remains restricted, this may significantly increase the current liquidity deficit in the market and result in further interest rate rises.
- An unfavourable macroeconomic environment in many countries of Sistema's operations may make it necessary to reevaluate goodwill for some of the assets.
- Foreign currency control and restrictions on capital repatriation may adversely affect the business of Sistema Group and reduce the value of Sistema's investment in Russia.

Political and social risks

- The influence of geopolitical risks has significantly intensified as protectionism and economic sanctions are increasingly being used as a tool for achieving geopolitical goals.
- The risks of inter-state conflicts have significantly risen compared with the beginning of 2014, both in terms of their probability and the effect that they may produce on various areas.

Legal risks and uncertainty

The risks related to weaknesses in the Russian regulatory framework include, to various degrees, the following.

- Possible discrepancies, ambiguity and anomalies in: (1) federal laws; (2) orders, directives and regulations issued by the Russian President, Government and federal ministers; (3) and regional and local laws, rules and requirements.
- Relative unpredictability of legislative and administrative decisions and court rulings and a lack of means that could make the understanding of such legislative decisions and court rulings easier.
- There is no clarity about the influence of the Federal Law «On Strategic Foreign Investment» and the new Customs Treaty of Russia, Belarus and Kazakhstan on Sistema's business and its foreign shareholders. Russia's accession to the World Trade Organisation may result in certain legislative and other changes in the markets of Sistema's operations.
- The shareholder responsibilities provided for by the corporate laws of the Russian Federation may result in Sistema being held financially liable for its subsidiaries.

- If minority shareholders of Sistema's subsidiaries contest past or future related-party transactions or other transactions or vote against related-party transactions or other transactions in the future, this will limit Sistema's operational capacity.
- If the Russian Federal Anti-monopoly Service (FAS) concludes that Sistema or one of its material subsidiaries has acquired or founded a new company in violation of the anti-monopoly law or has otherwise violated competition laws, this may result in administrative sanctions.
- Failure to formally comply with certain requirements of the Russian law may result in Sistema or one of its subsidiaries incorporated in Russia being forced to carry out liquidation, their ownership structure may be called into question and early debt repayment claims may be made.

Taxation system of the Russian Federation

- The Russian law on transfer pricing may make it necessary to introduce adjustments to the price setting system of Sistema Group's companies and result in additional tax obligations with regard to controlled transactions.
- On 1 January 2015 new rules were introduced relating to the taxation of undistributed profits of controlled foreign companies, the concept of a beneficiary owner, tax residence of legal entities and indirect sale of properties in Russia.

As a result of the need to apply new taxation rules the Group's companies may face new tax liabilities arising due to the uncertainty around interpretation of the tax law and the lack of previous law enforcement practice.

Risks related to the operations of Sistema

There is no certainty that the business strategy will be successfully implemented.

- The key components of the business strategy include development of a balanced and diversified asset portfolio in sectors and regions where Sistema has competitive advantages, and also proactive management of the investment portfolio and involvement of leading international and Russian partners. Despite having a well-formulated strategy, Sistema cannot guarantee achievement of the established goals, efficient management of the portfolio companies or taking up of new investment opportunities.
- The success of Sistema's strategy depends on numerous factors, including obtaining of the necessary permits from the authorities, sufficient demand

from consumers, successful development of technologies, efficient management of spending, timely completion of development and introduction of new products and services by the Group's companies, successful differentiation of the companies' offers from their rivals and perception of the goods by the market.

The company may face difficulties in generating profits from acquisitions, integration, disposal or restructuring of assets.

- Sistema grows its business via new acquisitions, sale and restructuring of assets. The process of taking investment opportunities in the market entails certain risks, including the risks

of not finding relevant targets or their not being available for acquisition, a risk of insufficient or inadequate due diligence of the target company's operations and/or financial situation, risks of the assets being overvalued and overpaid for and, consequently, of occurrence of financial risks exceeding expectations and discovery of financial liabilities not found earlier.

- Acquisition of additional businesses may also put additional pressure on the Corporation's cash flows, especially if the acquisition is paid for in cash. Besides, if an acquisition deal is not closed or closed with delays, it may negatively affect Sistema's achievement of its strategic growth goals and have a substantial negative impact on the current business, operational results, financial situation and prospects.

- Moreover, Sistema may encounter problems of integrating assets into the existing structure, their optimal management or necessary restructuring. These risks include inability to efficiently assimilate and integrate operating assets and personnel of the acquired company into the business, inability to establish and integrate all the necessary control systems and mechanisms, including with regard to facilities and agreements related to logistics and distribution, conflicts between majority and minority shareholders, hostility and/or unwillingness to cooperate on the part of the acquired asset's management, potential loss of customers of the acquired asset.
- Potential disposals of assets carry certain risks related to potential inability to execute the transaction or undervaluation of the sold asset, liabilities arising from the sale of asset, failure to meet deadlines for transaction closure or loss of synergy between existing assets. Besides, execution of such transactions, including restructuring, merger of businesses or financial resources depends on a combination of necessary conditions, including corporate and government consents. There is no certainty that such deals will be completed on the announced terms or closed at all.

Sistema's ability to maintain its competitiveness and implement its business strategy in many respects depends on the management and key employees.

- The top management team is the key to implementing Sistema's strategy. Moreover, further success of the investment portfolios and their ability to efficiently implement a common strategy, including plans of growth and increase of scale, will to a large degree depend on the efforts of individual management teams working with the specific assets.

Sistema's ability to service its debt largely depends on the cash flows from its subsidiaries.

Sistema's financial performance largely depends on the ability of its subsidiaries to generate cash flows needed to service its financial liabilities, including repayment of debt and interest and any other borrowing in the future. From time to time, the Group companies' abilities to make such payouts may be limited as a result of regulatory, tax or other restrictions. Disposal of one of the Group's core assets reduces the Group's materiality and the amount of expected dividend flow from subsidiaries, which along with tightening of bank funding may have a negative impact on servicing current liabilities and hinder access to debt financing in the future.

The success of Sistema in many respects depends on the success of its core asset, MTS.

Sistema's financial performance in many respects depends on the success of its core asset, MTS. If MTS fails to generate the necessary income, it may impinge on Sistema's ability to service its debt liabilities and secure growth and business expansion through restructuring and acquisition of assets. Consequently, the risks and events that may have a material detrimental effect on MTS, its operating results, financial standing and prospects may, in turn, have a material detrimental effect on Sistema, its operating results, financial standing or prospects.

In the event of problems with fund raising or financing, Sistema's operations would be curtailed accordingly.

Future financial receipts and cash flows from Sistema's subsidiaries and affiliates may not be sufficient to cover the planned expenses in the event of contingencies, such as:

- absence of external sources of financing;
- changes in the terms of existing agreements on financing;
- emergence of new business opportunities or investment in existing businesses, in case of sizable investments;
- a slower than planned growth of revenue;
- deterioration of the economic situation in the countries of Sistema's operations.

Covenants might limit the ability to raise debt financing, carry out investment programmes or participate in various businesses.

Sistema's bank loan agreements and agreements of some of its S/As on bank loans and debt securities contain certain restrictive covenants. These covenants put restrictions on attraction of additional debt financing, encumbrance of property with pledges, sale of assets and transactions with affiliates. Such covenants may result in restriction of Sistema's operations, including financing of capital expenses, or limit the possibilities for timely repayment of debt or payments on liabilities. If operations of subsidiaries are restricted, their revenue may decline, which, in turn, may limit Sistema's opportunities for using such revenue to service the debt or finance its subsidiaries. Moreover, mergers and restructuring of subsidiaries, in certain circumstances, disposal of assets may lead to breach of restricting covenants under such subsidiaries' loan agreements, which may bring about acceleration of such loans or reclassification of long-term loans into short-term loans.

Licences and permits required for Sistema Group companies' business may be deemed invalid, revoked, rescinded or not prolonged, or contain encumbrances that restrict Sistema's operations.

Operations of Sistema Group companies are regulated by various government bodies and agencies as pertains to obtaining and renewing licences, approvals and permits and also the need to constantly abide by existing legislation, regulations and standards. Regulating authorities to a large extent rely on their own judgment when interpreting and implementing requirements of applicable laws, regulations and standards, issuing and extending licences, approvals, sanctions and permits and monitoring compliance with licence requirements. There is no guarantee that existing licences and permits, including those issued to the Group's companies, will be extended, new licences and permits will be issued or that the companies will be able to comply with the terms of corresponding licences. There is no guarantee either that any of the existing or future licences or permits will not be suspended or revoked on some or other grounds. Any of these circumstances can have material negative consequences for the business of Sistema.

If ambiguity of privatisation laws is used to challenge Sistema's property rights to its privatised subsidiaries, and the company is unable to defend its position, there is a risk of losing its share in such assets or subsidiaries.

- Sistema's portfolio contains several privatised assets. Since the Russian laws on privatisation are rather ambiguous, inconsistent and conflicting with other laws, for example, there are conflicts

between federal and local laws, the privatisation of many companies could be challenged, including the possibility of discriminatory challenges.

- If the legitimacy of privatisation of a company is contested, and Sistema is unable to defend its stand in the dispute, there is a risk of losing a stake in such company or its assets, which may have a material adverse effect on the business, financial situation, performance or development prospects of the Corporation..

The business of Sistema is regulated by the anti-corruption laws under the jurisdictions in which it operates, including the anti-corruption laws of the Russian Federation and the Foreign Corrupt Practices Act of the USA, and may be regulated by the UK Bribery Act 2010, and violations of applicable laws may lead to penalties and reputational risks.

- Any investigation into potential violations of the FCPA, the UK Bribery Act or other anti-corruption laws of the US, the UK or other jurisdictions may affect the reputation, business, financial situation and performance of Sistema.

All segments where Sistema operates are open to competition on the part of other companies.

- Operations in the segments of telecommunications, high technology, banking, retail, media, tourism, private healthcare services and pharmaceuticals are exposed to the influence of economic and other factors. Each segment exhibits strong competition between

companies in Russia and other countries, including but not limited to competition in terms of price, product and service quality. Inability of Sistema Group companies to compete efficiently may have a material negative impact on the business, performance, financial situation and prospects.

Sistema depends on the ability to maintain its brand quality and reputation.

- Developing and maintaining brand awareness for the Group companies is a crucial component of shaping the public opinion about their existing and future products and services. Sistema believes that the importance of company brand is growing steadily at the highly competitive markets. Successful development and improvement of brand awareness to a large extent depends on the efficiency of marketing operations and the companies' ability to provide useful and quality products and services at competitive prices. The efforts to develop the brand may be incommensurate with actual revenues which may be insufficient to cover expenses on such activities.

EVENTS RELATED TO THE DECONSOLIDATION OF BASHNEFT

The civil proceedings brought against Sistema and Sistema-Invest

On September 24, 2014, a civil claim was filed with the Arbitrazh (Commercial) Court of the City of Moscow ("Arbitrazh Court") by the First Deputy General Prosecutor of Russia seeking to return shares of JSOC "Bashneft" (Bashneft) held by Sistema and its wholly owned subsidiary Sistema-Invest ("Bashneft Shares") to the Russian Federation (the "Civil Claim"). The Civil Claim asserted that the privatization of Bashneft was unlawful as Bashneft was originally the property of the Russian Federation and, as a result, the authorities of the Republic of Bashkortostan were not legally entitled to privatize Bashneft without obtaining the requisite consents from the Russian Federal authorities.

On November 7, 2014, the Arbitrazh Court issued a written decision, ruling in favour of the Civil Claim.

On November 12, 2014, Sistema's Board of Directors considered and decided not to appeal the decision of the Arbitrazh Court, but rather focus on filing claims for the recovery of damages from the counterparties and/or their legal successors (LLC Ural-Invest) which sold the Bashneft Shares to Sistema and Sistema-Invest.

In December 2014, Bashneft Shares were transferred to the Russian Federation.

In December 2014, Sistema as a good faith buyer filed a claim with the Arbitrazh Court for the recovery of damages from LLC Ural-Invest ("Ural-Invest"), suffered by Sistema as a result of loss of the Bashneft Shares.

In February 2015, the Arbitrazh Court ruled in favour of Sistema's claim for the recovery of RUB 70.7 billion damage from Ural-Invest.

In March 2015, Sistema and Ural-Invest signed a settlement agreement. In accordance with the terms of the settlement agreement, all the property owned by Ural-Invest, i.e. cash assets of approximately RUB 46.5 billion, will be transferred to Sistema.

Given the social importance of the projects of the URAL charitable fund ("Fund"), which is affiliated with Ural-Invest, and in accordance with the terms of the settlement agreement Sistema will invest RUB 4.6 billion of the funds receivable from Ural-Invest to the Fund's socially important charitable projects.

On March 30, the Arbitrazh Court approved the settlement agreement signed by Sistema and Ural-Invest.

Criminal proceedings relating to the privatization of Bashneft

In April 2014, a criminal investigation was commenced in respect of Mr. Ural Rakhimov (the son of Mr. Murtaza Rakhimov, who was the President of the Republic of Bashkortostan during the period when the BashTEK companies were privatized) and Mr. Levon Airapetyan. These persons have been accused of misappropriating Bashneft via an illegal privatization process and have also been accused of legalization with respect to Bashneft.

On September 16, 2014, the majority shareholder and Chairman of the Board of Directors of Sistema, Mr. Vladimir Evtushenkov was charged with legalization of assets that were wrongfully acquired by other persons, and placed under house arrest.

In December 2014, Mr. Vladimir Evtushenkov was released from house arrest and is now participating as normal in business of Sistema Group, as the Chairman of Sistema's Board of Directors.

SUSTAINABLE DEVELOPMENT

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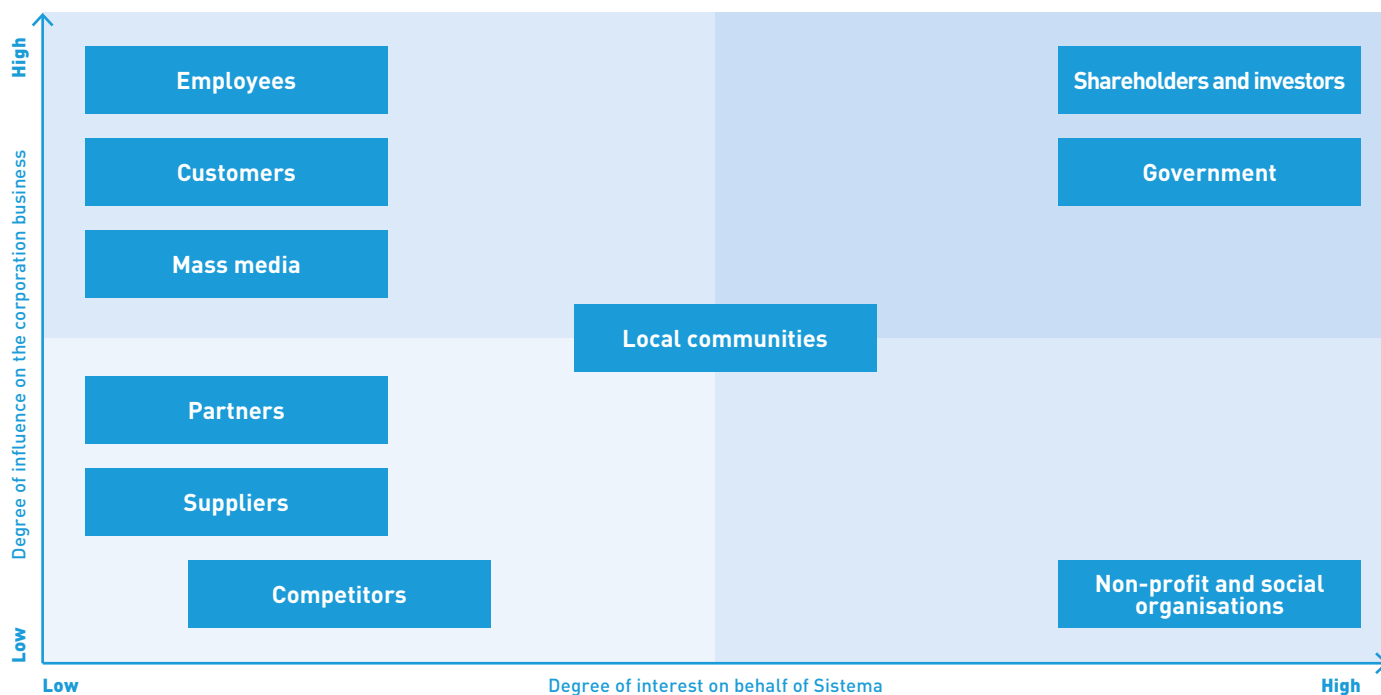
Responsible investor

Sistema has substantial influence on the development of many sectors of the Russian economy and society in general. The Corporation abides by the Principles for Responsible Investment developed by an international investor group under

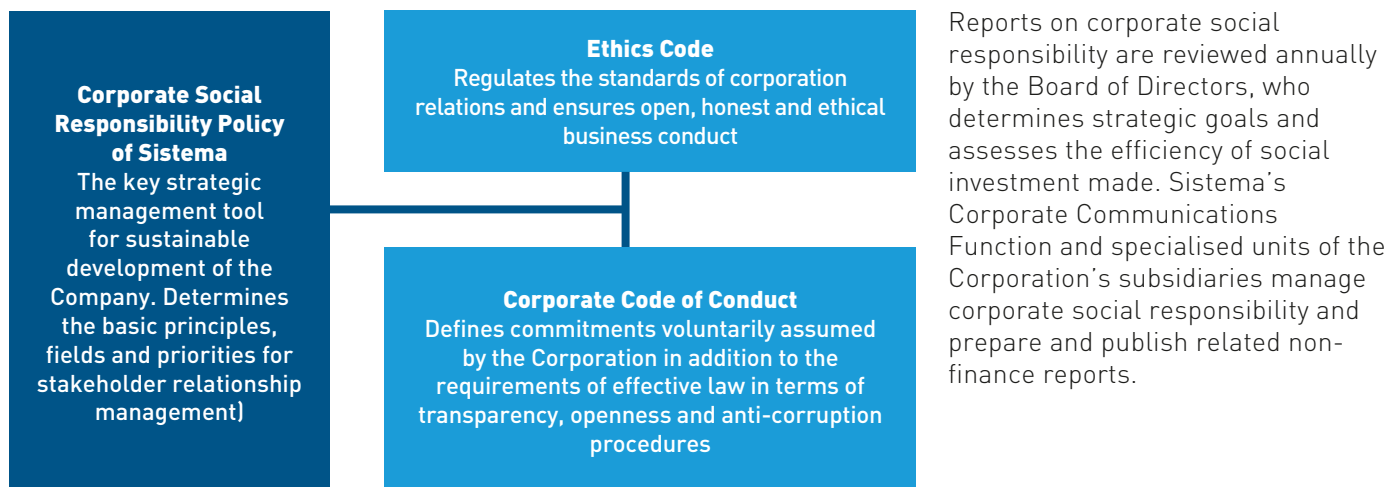
the UNO's aegis in response to growing concerns involved in the interplay of environmental and social issues as well as issues of corporate governance and investment practices. The Company measures up its business goals

against the background of social interests and gives consideration to environmental, social, and corporate governance (ESG) factors underpinning the development of market sectors and regions its portfolio companies operate in.

Matrix of Interested Parties



Sistema's core documents governing sustainable development



Social investment

An important component of Sistema's corporate social responsibility is charity promoted in line with the social investment concept, i.e., a purposeful long-term social policy linking strategic interests of the corporation and its shareholders with society's needs. The basic principles of charity efforts as well as areas to be addressed are outlined in the Policy Sistema's Charity Work. The key body in charge of the Corporation's charity and social projects is Sistema Charitable Foundation (Sistema CF), who accumulates funds allocated from profits of subsidiaries for general corporate programmes. The Foundation works in the following key focus areas:

- science;
- education;

- awareness;
- culture and art;
- preservation of religious and historical heritage;
- healthcare and social security;
- fitness and sports.

On top of that, subsidiaries pursue their own CSR and charity projects. In the last three years (2012, 2013, and 2014), Sistema Group's total spending on charity and social responsibility exceeded RUB 5.3 bln.

The Corporation seeks to consistently deepen integration of its CSR projects and improve their efficiency through combined effort of all companies of the Sistema Group. These companies increasingly use projects designed to develop business and

address social needs at the same time. 2014 was the year when the Corporation reached a whole new level of synergies in corporate social responsibility: its subsidiaries and affiliates took active part in joint projects promoting high technologies, human development, and education of the youth, as well as volunteer campaigns, the cornerstones of Sistema's social policy.



>4,5 RUB mln

total amount of expenses on charity and social responsibility projects for three years

Education, science, innovation

Sistema's broadest-scale project in education and science is Lift to the Future, a nationwide young talent development programme launched in 2011 with the support of the Russian Ministry of Education and Science, the Agency for

Strategic Initiatives (ASI), and more than 500 partner organisations. The programme uses a special procedure for talent screening and development and intends to provide students with early career guidance and inspire scientific and techno-

logical creativity. The ASI's supervisory board (chaired by the Russian president V.Putin) recommended the project for replication in various regions of Russia (administrations of 19 regions of Russia signed related cooperation agreements).










2014 became the year of establishment of four talent high schools for science and research in the Moscow, Smolensk, and Vladimir regions and Bashkortostan. School and university students submitted 370 innovation projects in Environment & Natural Resources, Power Engineering, Information

Technologies, Telecommunications, Transport Technologies, Healthcare & Pharmaceuticals, Microelectronics, etc., to be reviewed by expert contest judges. Master classes, lectures, contests, and conferences for school and university students involved representatives of most companies of the Sistema

Group. The Corporation also offered a career guidance programme for participants of Lift to the Future, children of employees of S/As, and students of sponsored child welfare centres and schools by organising tours to MTS, MTS Bank, MGTS, Detsky Mir, Mikron, Stream, and BPGC.

Lift to the Future

 <p>19 regions of Russia</p>	 <p>>30 ths</p> <p>participants of innovation project contests</p>	 <p>64 winners</p> <p>admitted for traineeship in European hi-tech enterprises</p>
 <p>>150 ths</p> <p>project participants</p>	 <p>95 contests</p> <p>held among school and college students since the beginning of the Programme</p>	 <p>270 academic mentors</p> <p>provided with grants to organise projects for school students in various regions of Russia</p>
 <p>500 holders</p> <p>of the Programme scholarship</p>		

In December 2014 Sistema and its subsidiaries MTS and SSTL held a first-ever Russian-Indian Youth Innovation Summit in New Delhi dedicated to latest technologies and prospects of international cooperation in telecom innovations. The summit was supported by the Russian Embassy in India. MTS hosts Telecom Idea, a contest of new 'smart' IT solutions helping city environments become more comfortable, eco-friendly, and accessible for all social groups. After four years in Russia, in 2014 the contest was extended to India for the first time.

>400 colleges and startups

participating in the contest since its start

>600 projects

submitted by young scientists for potential use in business; some of them successfully implemented

The summit also involved an interactive culture and technology exhibition From Russia with Progress dedicated to outstanding Russian inventions.

TOCHAMAC

1968 THE BEST AVAILABLE MACHINE FOR CONTROLLED NUCLEAR FUSION

Physicists in many countries tried to tackle the problem, aiming to create the world's first fusion reactor. One method showing promise was to reproduce nuclear fusions similar to those observed on the Sun.

To get power today, we mostly burn oil, gas, and coal. However, the planet's oil and gas reserves are limited, and with ever-growing power consumption, they may be almost exhausted within 30-50 years. Besides, oil and gas are not just fuels, they are valuable feedstocks used to produce a variety of chemicals, proteins, and other useful substances. What kind of progress should power engineering now aim for? Within the universe, there is colossal energy released from the interior of the Sun and stars in nuclear fusions. Using such power on planet Earth might seem nothing more than fantasy at first. It would require temperatures of millions and millions of degrees. Physicists in many countries tried to tackle the problem, aiming to create the world's first fusion reactor. One method showing promise was to reproduce nuclear fusions similar to those observed on the Sun. The first tochamac was developed and demonstrated in 1968 by a group of physicists lead by Lev Artsimovich, fellow of the Soviet Academy of Sciences. The name of the device is an acronym of the Russian full name translated as "TOroidal Chamber with MAgnetic Colls". The tochamac is still perceived as the best available machine for controlled nuclear fusion, and it is hoped it will provide mankind with inexhaustible energy.

MTS and MGTS are partners of the New Technology School project originated by the IT Department of Moscow and designed to broaden the use of information and communication technologies (ICT) in education.


VivaCell-MTS supported Armenian schools in setting up Creativity Labs, modern classrooms equipped with interactive blackboards, latest computers and movable furniture specially designed for individual and group use.

Sistema takes active part in the development of national innovation

infrastructure. The Corporation is among the shareholders of Technopark Sarov (co-run with Rosatom and RUSNANO) designed for innovation projects to be carried out at the VNIIEF Russian Federal Nuclear Centre for the benefit of Russian economy.

In October 2013 Sistema CF first provided support to Valdai International Discussion Club, a convention in Sochi bringing together more than 800 representatives of the global academic community, including professors from major universities of nearly 50 countries.

Technopark Sarov




1.5

RUB

bln

in aggregate revenue of the Technopark's companies as of the end of 2014



54

resident
companies

at Technopark Sarov (with over 600 employees)

Culture

Sistema pursues several sizeable initiatives in culture and arts aiming to preserve and promote national cultural and historical legacy. Sistema CF supports numerous theatre, music, and art projects, as well as leading performance teams and museums.

Its charity recipients include over 20 institutions and foundations active in the field of culture, including the Nikolay Petrov Foundation, the Benois Centre, the Valery Gergiev Foundation, the Foundation for Support of Church Construction in Moscow, the Valaam Convent & Nature Reserve, and the Field of Prokhorovka Museum of Armoured Vehicles.



The largest recipient of the Corporation's long-term social investments is the Russian Museum, Sistema's partner since 2003. Support of the Sistema CF allows the museum to carry out large-scale exhibition, editorial, art restoration, and educational projects. In particular, the museum is currently building an extensive interregional and international network of 'virtual branches' to make the vast collection of Russian arts accessible to the mainstream audience. The number of new museum branches doubled in 2013-2014. In 2014 the museum opened 28 information and education centres based in libraries, museums, and learning institutions in St Petersburg, Angarsk, Arkhangelsk, Volsk, Izhevsk, Ishim, Kaluga, Kostomuksha, Kondopoga, Petrozavodsk, Pikalyovo, Saransk, Sortaval, Yuzhno-Sakhalinsk, and locations in Turkey and Finland.



The West wing of St Michael's Castle (the Engineers' Castle) in St Petersburg now hosts an «e-museum», a state-of-the-art multi media centre providing access to the Russian Museum's rich art collection via latest technologies. Sistema helps the museum to constantly upgrade the centre's hard- and software to maintain its high-tech status. The various projects performed by the Russian Museum in 2014 with support from Sistema include new multi media programmes, books on Russian arts, and the VIIth international Imperial Garden of Russia festival.

Russian Museum

A new cooperation agreement between Sistema and the Russian Museum on financing of various museum's projects was signed. It is termed until 2023 and contemplates financing in amount of

 **300** RUB mln

The Russian Museum currently operates

158 «virtual branches»



(119 – in Russia, 37 – abroad, 2 – in the Antarctica)



4,000 visitors

of the multi media centre in 2011-2014



4,700 participants

of video conference calls



127 events

organised in the multi media theatre



600 images

exhibited in the multi media centre's gallery

Since 2009 Sistema has been sponsoring the annual May Festival of Children's Films organising free charity shows of Russia's best motion pictures and cartoons for children. The programme is designed to develop modern learning methods and provide leisure experience to children from orphanages and social boarding schools, disabled children, and families with foster children.

Another project that made great progress in 2014 is Mobile Library, an innovative social learning project originated by MTS and involving the installation of «virtual» bookshelves in libraries and other broad access institutions allowing users to download masterpieces of the Russian and foreign literature, including those from school curricula, on mobile devices using QR codes. MTS pursues the Mobile Library project in over 30 regions of Russia, as well as Ukraine and Belarus.

>400 mobile libraries

opened in just 8 regions of Central Russia in 2014

>10 ths books

of a combined volume that would take almost 300 years to read have been downloaded by mobile library users

Environment

The Corporation's environmental efforts are focused on:



- implementation of energy-saving principles;
- safe waste reclamation;
- protection of the atmosphere;
- protection of water and land resources;
- environmental education of the younger generation.

Sistema and its subsidiaries are actively involved in environmental efforts in regions where they operate, working to gradually

reduce their environmental impact, improve the ecology and enhance environmental consciousness. The Corporation rigorously abides by

environment protection principles and complies with all relevant laws and regulations.

The amount of resources used*

Resource type	Used for 2014	
Thermal energy	2,738.12 Gcal	3,422,652.91 RUB
Electrical energy	3,491 thous. kWh	13,266,014.45 RUB
Water	16,470 m ³	438,275.64 RUB

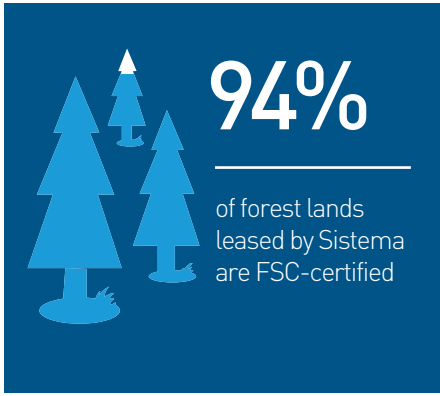
Sistema participated in financing of the Republic of Bashkiria's water programme. The programme embraced 20 districts and 8 cities of Bashkiria and envisaged reconstruction and major repairs of existing and construction of new water intakes, conduits and water supply systems, drilling of wells and installation of water towers, mainly in remote rural areas where they are often the only source of drinking water.

Companies whose activities are directly related to natural resources management or have an impact on public health pay special attention to environmental safety. Notably, Targin has introduced an HSE (health, safety and environment) system that enables it to work safely at a customer's facilities and helps to preserve the environment. In 2014 the system was first certified by ISO 9001, ISO 14001, and OHSAS - 18001.

LesInvest Group, the biggest forest user in the European part of Russia, is certified to FSC**, which, among other things, envisages forest restoration and close cooperation with environmental organisations and local communities.

* Data for 2014 according to the Corporate Center

** FSC (Forest Stewardship Council) is an independent international organisation who has created a certification system for environmentally and socially responsible forest management.



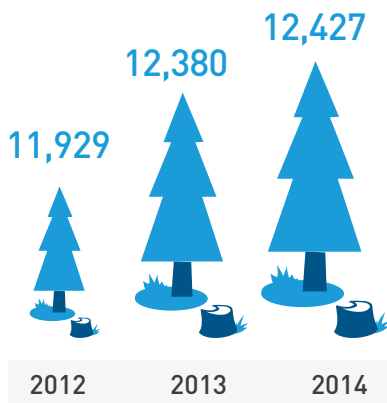
In 2014, the pilot project for safe disposal of batteries and electronic waste was launched at 300 sales outlets in Moscow and the Moscow region.

The project was then carried out in 10 Russian cities.

>3,000
Sistema Group employees

took part in the corporate Saturday clean-up

Reforestation, ha



The amount of the Group's reforestation work is growing year after year: In 2014, the area where planting and combined reforestation work took place grew by 4.2% vs 2012.

Medsi Group strictly complies with Russian sanitary regulations on hospital waste handling. Medsi clinics take regular steps to prevent hospital-acquired infections and ensure epidemiological safety of their patients and employees. Bacteriological tests show a definite improvement in the epidemic safety of Medsi clinics in recent years.

MTS' retail outlets now serve as drop-off stations for used batteries to be disposed as per high environmental safety standards. The campaign runs under the title Discard It Right and fits into a broader Eco Office

programme promoting environment conservation principles since 2012.

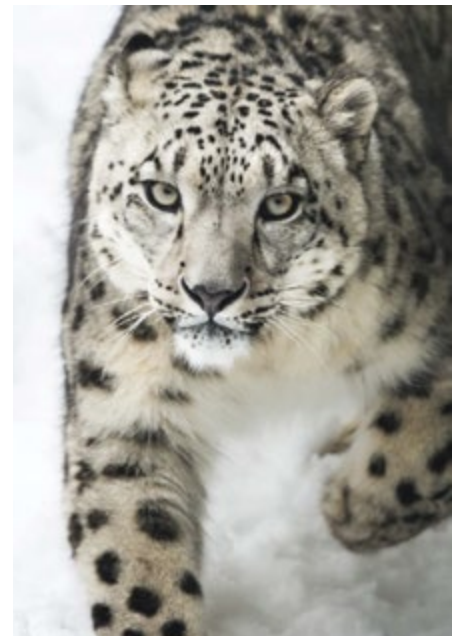
In 2014 MTS organised its first national open eco lesson Mobile Technology for Ecology as part of the Green Schools programme supported by the inter-regional public organisation EKA Green Movement of Russia. During the lesson, teachers and volunteers at more than 1,000 Russian schools talked about the role of modern technologies in environment protection.

In Armenia, VivaCell-MTS together with the Foundation for the Preservation of Wildlife and Cultural Assets (FPWC) launched a number of innovative projects seeking to develop alternative energy sources and introduce environment-friendly solutions in rural areas.

The Corporation is also involved in preservation of biological diversity, notably, by supporting the Eurasian Center for Leopard Studies and Preservation and particularly one of its key projects, the Leopard Land national park. Thus, in 2014 it sponsored biochemical works in the park and the development of technology infrastructure, fire control, and an electronic database of the Amur leopard population. Sistema also contributed to a leopard-themed education campaign targeting local communities, including school students of the Khasansky municipality (Primorye).

It has already become a good tradition for Sistema employees to volunteer to clean up public areas in cities and natural sites by organising spring Saturday clean-ups in Moscow and other regions.

Since 2010, Sistema has been supporting projects of the Russian Geographic Society. In 2014 it supported the Society's first nationwide festival involving all of its 85 regional divisions at the Central House of Artists in Moscow. The week-long festival attracted about 60,000 visitors, including many children and teenagers who also participated in the event's rich educational programme.



Society

In 2014, the Sistema Charitable Foundation began shaping a corporate volunteer movement as a tool of non-financial charity. Volunteers from Sistema supported tens of cultural, social, educational and sports projects in various regions where the Group operates. MTS has launched a corporate volun-

teer theater, whose actors stage educating performances for the employees' children and inmates of orphanages. Detsky Mir joined this project in 2014. BPGC arranged an educational show on electrical safety staged by the Bashkirian State Puppet Theater in Belebei, Kumer-tau, Neftekamsk and Ufa.

In just 2014, the number of volunteers at the Sistema Group grew by almost 2.5 times, from 3,300 to 8,000. Employees of all Sistema Group companies took part in New Year charity campaigns, with over 2,000 employees acting as volunteers.

The Wishing Tree	Charity Performances	Theater Season
		
<p>In 2014, 200 volunteers bought New Year gifts for children at orphanages and helped to organise holiday parties for them.</p>	<p>Every December, the Sistema Charitable Foundation organises charity performances for disadvantaged children.</p>	<p>Sistema employees bought tickets for Town Musicians of Bremen, a musical.</p>
<p>New Year celebrations were attended by children from the Moscow region, Vladimir, Torzhok, Emmaus, Tula, Ryazan, Noginsk and Udomlya.</p>	<p>Children from 17 orphanages and from poor families from Moscow, the Moscow region and the Tver region attended the charity performances.</p>	<p>The project reached out to over 300 children from orphanages, children from large families and disabled children from the Moscow and Tver regions.</p>

In summer 2014, the Sistema Charitable Foundation sponsored the purchase and delivery of a large relief consignment for refugees from Ukraine. Employees of all group companies joined the Foundation's initiative, contributing over 200 cu m of humanitarian

aid, including living essentials and vaccines.

The Group's companies work hard to implement social and educating programmes for the benefit of their customers. MTS pursues Children and the Internet, a programme de-

signed to promote rules of useful and safe use of the world wide web among younger schoolchildren, their parents and teachers, as well as Internet for All, a programme teaching older people to use the Internet and adapt in the information-oriented society.



The project has been implemented in most cities of Russia and Belarus, its total audience exceeding

300,000

people

Responsibility towards employees

Sistema is one of Russia's biggest and most attractive employers, employing over 150,000 people in Russia (0.4% of the workforce) and other countries it operates in. The Corporation uses the best HR management practices and fully complies with labour legislation of countries it works in, offering its employees competitive remuneration and social benefits (health and life insurance, sports events, etc.).

For social aid to employees, employees' children and retirees in 2014 Company allocated



220 RUB mln

Following the Corporation's transition to the investment company model, the Board of Directors approved a new incentive system designed to ensure profitability of investment and monetisation of created value for each individual project and for the Corporation in general. The incentive programme is geared towards value creation and/or implementation of projects, as well as financial self-sufficiency of project teams. The new incentive mechanism provides the best way to align the interests of Sistema's management and shareholders. The incentive system for the senior management first launched in 2010 is based on changes in the price of Sistema shares and total shareholder return (TSR). The programme's participants may receive additional bonuses linked to increase of the Corporation's capitalisation in the form of ordinary shares.

MTS and MGTS support the Children Online help line, has by now received over 10,000 calls and processed over 2,500 e-mails regarding safe use of the Internet by minors.

In September 2014, BPGC signed an agreement with the Bashkirian Education Ministry on joint implementation of initiatives to prevent children's electrical injuries as part of the Safe Childhood project. Bashkirenergo's employees gave electric safety lessons at 221 schools of the republic.

In November 2014, Medsi launched a unique project under the slogan Be Healthy with Medsi promoting a healthy lifestyle among corporate customers and partners of the company. Within this programme, Medsi's best doctors and fitness instructors offer lectures and consultations on such issues as handling chronic fatigue and stress, pregnancy and work, children's health, etc.

Healthcare, support of the disabled and promotion of sports are among priorities of Sistema's social policy. Renovation of a rehabilitation center for children with cerebral palsy at the Martha and Mary Convent of Mercy began in 2014. Since 2008, the Sistema Charitable Foundation has provided a total of RUB 100m for the Convent's restoration. This unique project supported by the Moscow City Government and the Russian Orthodox Church will help to improve the quality of life of families with disabled children that are in need of continuous care.

For several years, SSTL has been involved in an initiative to end polio in India, working hard to increase general awareness about polio vaccination through promotional text messages and other channels of communication. In the past three years, subscribers of MTS India received 20m texts reminding them to get their shots. As a result of this large-scale programme, on 27 March 2014 the World Health Organisation certified India polio-free, and UNICEF is now considering this model for use in Africa.

Sistema encourages the development of Russian sports by supporting the country's Olympic and Paralympic teams, as well as sports schools and clubs for children and the young. In November 2014, Sistema and the Russian Paralympic Committee organised treatment and rehabilitation of athletes in the Republic of Altay, at the unique Altay Resort belonging to the Intourist Hotel Group. The Sistema Charitable Foundation also supported the Moscow Olympro team of the Vozrozhdenie club, which participated in the 12th International Football Tournament for Amputees that took place in Sochi. Sistema sponsored the establishment of a family camp for the disabled in Yevpatoria (Crimea), where children underwent a unique course of rehabilitation through exercise. Sistema's subsidiaries are also actively involved in promotion of sports at regional and national levels.

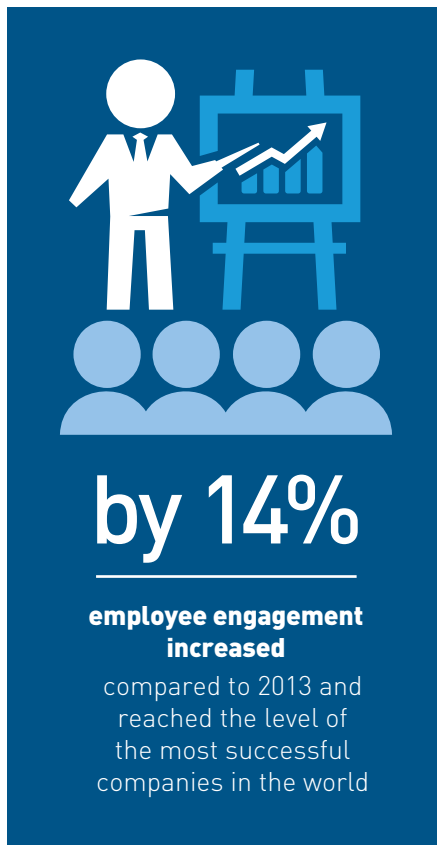
The Corporation has a system of internal career lifts. In 2014, Sistema launched the Talent Bank project that is designed to search for, develop and rotate top managers of subsidiaries that have high potential and high motivation for growth. In 2014, over 100 senior managers from the Group's companies underwent remote and in-person assessment. Based on its results, 53 managers were selected to start a development programme in 2015.

Yet another HR initiative that was launched in 2014 is the School of In-House Coaches. The project seeks to create a pool of efficient corporate coaches to develop key business skills and competencies of medium and junior management using the best expertise in the sphere.

Important tools of non-financial motivation and employee engagement promotion are corporate volunteering and sports movements. The central sports event of the year was the 12th Summer Games, which united over 3,000 employees from 60 companies of Sistema Group from different regions of Russia, the CIS and India.

Sistema conducts annual engagement surveys to give its employees an opportunity to share their thoughts on the most important issues and give feedback, to find out the company's strengths and areas that need improvement and development and to determine priorities when planning HR events for the next year. The Corporation sets itself ambitious goals and looks up to the most successful international companies. In 2014, about 28,000 employees took part

in the survey. The measures taken by Sistema improved employee engagement by 14% compared to 2013, reaching the level of the world's most successful companies. Almost all areas and parameters of the survey demonstrated a positive trend.



Sistema's Board Chairman ranks among the top 10 business leaders of Russia according to Kommersant and the Russian Managers' Association. Sistema's president was ranked 1st among CEOs of diversified holding companies in Russia's Top 1000 Best Managers 2014. Yet another six of the company's top managers were named best in their respective professional categories (finance and investment, corporate governance, HR, GR, PR, IT).

Sistema and MTS traditionally win leading positions in Russian employer ratings. In 2014:



Sistema confirmed its previously won A.hr grade («High level of employer appeal») in Expert RA's employer rating



Sistema won the special nomination award Best Corporate Mass Media System in the Best Corporate Media 2014 competition



MTS won the #1 position in HeadHunter's annual Employers of Russia rating for a second consecutive year, and was also included in HeadHunter's list of top Russian employers of the young

SISTEMA JSFC AND SUBSIDIARIES

Consolidated Financial Statements

As of December 31, 2014 and 2013
and for the Years Then Ended

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Shareholders of Sistema Joint Stock Financial Corporation

We have audited the accompanying consolidated financial statements of Sistema Joint Stock Financial

Corporation and its subsidiaries, which comprise the consolidated statements of financial position as of December 31, 2014 and 2013, and the related consolidated statements of operations and comprehensive income, cash flows and changes

in shareholders' equity for the years then ended, and the related notes to the consolidated financial statements and appendix thereto.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally

accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation

of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with the Russian Federal Auditing Standards and auditing standards generally accepted in the United States of America. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in

the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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 entity's internal control. Accordingly, we express no such opinion.

An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sistema Joint Stock Financial Corporation and its subsidiaries as of December 31, 2014 and 2013, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

April 2, 2015

Moscow, Russian Federation

Raikhman M.V., Partner

(Certificate no. 01-001195 dated January 14, 2013)

The Entity: Sistema Joint Stock Financial Corporation
Certificate of state registration № 025.866, issued by the Moscow Registration Chamber on 16.07.1993.

Certificate of registration in the Unified State Register № 1027700003891 of 11.11.2002, issued by Moscow Inspectorate of the Russian Ministry of Taxation № 46.
Address: Building 1, 13 Mokhovaya street, Moscow, 125009, Russia.

Independent Auditors: ZAO Deloitte & Touche CIS
Certificate of state registration № 018.482, issued by the Moscow Registration Chamber on 30.10.1992.
Certificate of registration in the Unified State Register № 1027700425444 of 13.11.2002, issued by Moscow Interdistrict Inspectorate of the Russian Ministry of Taxation № 39.

Certificate of membership in "NP "Audit Chamber of Russia" (auditors' SRO) of 20.05.2009 № 3026, ORNZ 10201017407.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION AS OF DECEMBER 31, 2014 AND 2013

(Amounts in thousands of U.S. dollars, except share and per share amounts)

	Notes	<u>2014</u>	<u>2013</u>
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents		\$ 1,288,722	\$ 1,537,492
Short-term investments	8	479,341	1,562,547
Assets from banking activities, current portion (including cash and cash equivalents of \$843,715 and \$1,132,368)	7	2,180,196	3,898,740
Accounts receivable	9	1,163,092	1,630,593
VAT receivable		236,438	335,289
Inventories and spare parts	11	1,244,509	1,131,302
Deferred tax assets	21	245,571	330,388
Other current assets	10	832,060	1,084,547
Current assets of Bashneft	2	-	3,054,728
Total current assets		<u>7,669,929</u>	<u>14,565,626</u>
NON-CURRENT ASSETS:			
Property, plant and equipment	12	7,191,394	11,151,341
Advance payments for non-current assets		84,560	162,978
Goodwill	13	817,537	1,327,779
Other intangible assets	14	1,721,389	2,162,700
Investments in affiliates	16	356,018	365,266
Assets from banking activities, net of current portion	7	1,374,367	2,554,229
Debt issuance costs		42,267	78,348
Deferred tax assets	21	392,866	297,419
Long-term investments	17	316,625	249,071
Other non-current assets		703,525	714,458
Non-current assets of Bashneft	2	-	9,619,779
Total non-current assets		<u>13,000,548</u>	<u>28,683,368</u>
TOTAL ASSETS		<u>\$ 20,670,477</u>	<u>\$ 43,248,994</u>

См. Примечания к консолидированной финансовой отчетности и приложение к ним.

	Notes	2014	2013
LIABILITIES AND EQUITY			
CURRENT LIABILITIES:			
Accounts payable		\$ 1,584,251	\$ 1,943,133
Liabilities from banking activities, current portion	18	2,180,491	3,864,415
Taxes payable		290,635	490,564
Deferred tax liabilities	21	64,947	114,192
Subscriber prepayments, current portion		390,736	620,281
Accrued expenses and other current liabilities	19	1,315,656	1,567,890
Short-term loans payable		129,938	40,836
Current portion of long-term debt	20	1,598,770	2,102,911
Current liabilities of Bashneft	2	-	2,663,432
Total current liabilities		<u>7,555,424</u>	<u>13,407,654</u>
LONG-TERM LIABILITIES:			
Long-term debt, net of current portion	20	6,534,055	8,375,161
Subscriber prepayments, net of current portion		59,064	101,240
Liabilities from banking activities, net of current portion	18	167,860	772,525
Deferred tax liabilities	21	787,631	902,591
Asset retirement obligations	28	53,715	83,809
Postretirement benefits obligations		45,344	53,943
Property, plant and equipment contributions		41,358	74,174
Other long-term liabilities		475,713	443,032
Non-current liabilities of Bashneft	2	-	3,734,024
Total long-term liabilities		<u>8,164,740</u>	<u>14,540,499</u>
TOTAL LIABILITIES		<u>15,720,164</u>	<u>27,948,153</u>
Commitments and contingencies	30	-	-
Redeemable noncontrolling interests	29	792,766	805,130
SHAREHOLDERS' EQUITY:			
Share capital (9,650,000,000 shares issued; 9,435,902,596 and 9,274,755,045 shares outstanding with par value of 0.09 Russian Rubles, respectively)	24	30,057	30,057
Treasury stock (214,097,404 and 375,244,955 shares with par value of 0.09 Russian Rubles, respectively)		(246,351)	(426,715)
Additional paid-in capital		2,604,913	2,616,608
Retained earnings		4,210,623	8,993,469
Accumulated other comprehensive loss	24	(3,743,402)	(906,718)
Total shareholders' equity		<u>2,855,840</u>	<u>10,306,701</u>
Non-redeemable noncontrolling interests		<u>1,301,707</u>	<u>4,189,010</u>
TOTAL EQUITY		<u>4,157,547</u>	<u>14,495,711</u>
TOTAL LIABILITIES AND EQUITY		<u>\$ 20,670,477</u>	<u>\$ 43,248,994</u>

See notes to the consolidated financial statements and appendix thereto.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amounts in thousands of U.S. dollars, except share and per share amounts)

	Notes	2014	2013
Sales		\$ 15,886,775	\$ 17,623,153
Revenue from banking activities		698,182	878,832
TOTAL REVENUES		16,584,957	18,501,985
Cost of sales, exclusive of depreciation and amortization shown separately below		(7,460,524)	(7,907,148)
Cost related to banking activities, exclusive of depreciation and amortization shown separately below		(760,084)	(523,960)
Selling, general and administrative expenses		(3,431,075)	(3,896,207)
Depreciation and amortization		(2,292,118)	(2,633,548)
Taxes other than income tax		(193,122)	(239,814)
Equity in results of affiliates		73,124	29,866
Impairment of goodwill	15	-	(258,048)
Impairment of other assets	15	(864,629)	(804,545)
Gain on disposal of investment in RussNeft	4	-	1,200,000
Gain from reentry into Uzbekistan	6	181,305	-
Gain on Bitel case resolution	30	-	371,100
Other operating expenses		(99,385)	(273,109)
OPERATING INCOME		1,738,449	3,566,572
Interest income		212,774	182,447
Interest expense		(811,346)	(960,136)
Change in fair value of derivative instruments		-	30,199
Foreign currency transaction loss		(548,596)	(298,264)
Income before income tax		591,281	2,520,818
Income tax expense	21	(453,417)	(842,107)
Net income excluding Bashneft		\$ 137,864	\$ 1,678,711
Income of Bashneft operations, net of tax effect of \$427,716 and \$455,637	2	1,517,054	1,540,489
Loss on deconsolidation of Bashneft, net of tax effect of nil	2	(4,969,011)	-
NET (LOSS) / INCOME		(3,314,093)	3,219,200
Noncontrolling interests		(773,539)	(961,672)
NET (LOSS) / INCOME ATTRIBUTABLE TO SISTEMA JSFC		(4,087,632)	2,257,528
Including:			
From continuing operations		(278,161)	1,102,161
From Bashneft operations and its deconsolidation		(3,809,471)	1,155,367
OTHER COMPREHENSIVE (LOSS)/INCOME, NET OF TAX			
Currency translation loss		\$ (3,886,388)	\$ (885,770)
Unrealized (loss)/gain on available-for-sale securities		(52,099)	32,200
Unrealized gain on derivatives		72,899	45,499
Unrecognized actuarial gain		172	5,310
Other comprehensive (loss)/income, net of tax		(3,865,416)	(802,761)
TOTAL COMPREHENSIVE (LOSS)/INCOME		\$ (7,179,509)	\$ 2,416,439

См. Примечания к консолидированной финансовой отчетности и приложение к ним.

	Notes	<u>2014</u>	<u>2013</u>
Including:			
Attributable to noncontrolling interests		(255,193)	738,912
Attributable to Sistema JSFC		(6,924,316)	1,677,527
Weighted average number of common shares outstanding – basic and diluted		9,350,539,484	9,239,817,019
Earnings per share, basic and diluted, U.S. cent			
(Loss)/earnings per share from continuing operations		(2.98)	11.93
(Loss)/earnings per share from Bashneft operations and its deconsolidation		(40.74)	12.50
Total (loss)/earnings per share attributable to Sistema JSFC shareholders		(43.72)	24.43

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amounts in thousands of U.S. dollars)

	<u>2014</u>	<u>2013</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) / income	\$ (3,314,093)	\$ 3,219,200
Income of Bashneft operations	(1,517,054)	(1,540,489)
Loss on deconsolidation of Bashneft	4,969,011	-
Net income excluding Bashneft	137,864	1,678,711
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation and amortization	2,292,118	2,633,548
Equity in results of affiliates	(73,124)	(29,866)
Deferred income tax expense	36,338	140,292
Foreign currency transaction loss	548,596	298,264
Gain from disposal of investment in RussNeft	-	(1,200,000)
Gain on Bitel case resolution, net of cash received of \$125,000	-	(246,100)
Gain on reentry into Uzbekistan	(181,305)	-
Gain on disposal of property, plant and equipment	(26,731)	(7,226)
Gain on disposal of subsidiaries	(139,082)	-
Amortization of connection fees	(23,019)	(60,309)
Allowance for loan losses	260,417	212,081
Dividends received from affiliates	70,369	65,247
Non-cash compensation to employees	79,430	54,158
Impairment of goodwill	-	258,048
Impairment of other assets	864,629	804,545
Other non-cash items	19,937	(15,057)

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013 (CONTINUED)

(Amounts in thousands of U.S. dollars)

	<u>2014</u>	<u>2013</u>
Changes in operating assets and liabilities, net of effects from purchases of businesses:		
Trading securities	267,153	(406,687)
Accounts receivable	(44,241)	(240,586)
VAT receivable	(17,192)	(174,951)
Inventories and spare parts	(490,362)	(171,320)
Other current assets	(114,574)	(93,381)
Accounts payable	560,603	533,948
Subscriber prepayments	(11,593)	110,112
Taxes payable	(5,394)	109,503
Accrued expenses and other current liabilities	281,592	(54,127)
Net cash from operating activities excluding Bashneft	<u>4,292,429</u>	<u>4,198,847</u>
Net cash from operating activities of Bashneft	<u>2,755,291</u>	<u>2,629,988</u>
Net cash provided by operating activities	7,047,720	6,828,835
CASH FLOWS FROM INVESTING ACTIVITIES:		
Payments for purchases of property, plant and equipment	(2,362,652)	(2,455,276)
Proceeds from sale of property, plant and equipment	80,332	39,592
Payments for purchases of intangible assets	(539,930)	(539,117)
Payments for businesses, net of cash acquired	(392,409)	(34,664)
Proceeds from sale of subsidiaries, net of cash disposed	150,000	561,402
Purchase of investments in affiliated companies	(201,582)	(63,753)
Payments for purchases of long-term investments	(836,916)	(105,000)
Proceeds from sale of long-term investments	511,227	1,286,292
Payments for purchases of short-term investments	(1,327,702)	(1,337,304)
Proceeds from sale of short-term investments	1,622,718	1,047,317
Payments for purchases of other non-current assets	-	(44,879)
Increase in restricted cash	-	(15,819)
Net decrease/(increase) in loans to customers of the banking segment	664,089	(70,458)
Net cash used in investing activities excluding Bashneft	<u>(2,632,825)</u>	<u>(1,731,667)</u>
Net cash used in investing activities of Bashneft (net of cash disposed of \$961,733)	<u>(3,256,540)</u>	<u>(1,158,995)</u>
Net cash used in investing activities	\$ <u>(5,889,365)</u>	\$ <u>(2,890,662)</u>

См. Примечания к консолидированной финансовой отчетности и приложение к ним.

	<u>2014</u>	<u>2013</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from/(principal payments on) short-term borrowings, net	\$ 185,838	\$ (231,036)
Net decrease in deposits from customers of the banking segment	(701,620)	(177,105)
Proceeds from long-term borrowings	2,850,171	1,900,322
Principal payments on long-term borrowings	(2,274,350)	(2,539,405)
Acquisition of noncontrolling interests in existing subsidiaries	(67,432)	(299,184)
Dividends paid	(1,198,028)	(1,225,440)
Proceeds from capital transactions with shares of existing subsidiaries	41,141	69,002
Net cash used in financing activities excluding Bashneft	(1,164,280)	(2,502,846)
Net cash provided by/(used in) financing activities of Bashneft	885,338	(580,164)
Net cash used in financing activities	<u>(278,942)</u>	<u>(3,083,010)</u>
Effect of foreign currency translation on cash and cash equivalents	<u>(1,938,436)</u>	<u>(293,247)</u>
Net (decrease)/increase in cash and cash equivalents	(1,059,023)	561,916
Cash and cash equivalents at the beginning of the year, including Bashneft (включая денежные средства и их эквиваленты АНК «Башнефть»)	3,191,460	2,629,544
Less: cash and cash equivalents of Bashneft at the end of the year	2,132,437	3,191,460
Cash and cash equivalents at the end of the year	-	(521,600)
Cash and cash equivalents at the end of the year	\$ <u>2,132,437</u>	\$ <u>2,669,860</u>
Comprising:		
Non-banking activities	1,288,722	1,537,492
Banking activities	843,715	1,132,368
CASH PAID DURING THE YEAR FOR:		
Interest, net of amounts capitalized	\$ (876,692)	\$ (1,160,300)
Income taxes	(377,298)	(735,797)
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Acquisition of intangible assets	-	670,300
Equipment and licenses acquired under capital leases	203,904	223,628
Amounts owed for capital expenditures	401,206	124,826
Payables related to business acquisitions	<u>1,760</u>	<u>345</u>

See notes to the consolidated financial statements and appendix thereto.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amounts in thousands of U.S. dollars, except share amounts)

	Share capital		Treasury stock		Additional paid-in capital
	Shares	Amount	Shares	Amount	
Balances at January 1, 2013	9,650,000,000	30,057	(440,425,038)	(501,109)	2,859,491
Net income/(loss)	-	-	-	-	-
Other comprehensive (loss)/income	-	-	-	-	-
Settlements under long-term motivation program	-	-	65,180,083	74,394	(13,262)
Accrued compensation cost	-	-	-	-	54,158
Business combinations, disposals and capital transactions of subsidiaries	-	-	-	-	(283,779)
Change in fair and redemption value of noncontrolling interests	-	-	-	-	-
Dividends declared by Sistema JSFC	-	-	-	-	-
Dividends declared by subsidiaries	-	-	-	-	-
Balances at December 31, 2013	9,650,000,000	30,057	(375,244,955)	(426,715)	2,616,608
Net (loss)/income	-	-	-	-	-
Other comprehensive (loss)/income	-	-	-	-	-
Settlements under long-term motivation program	-	-	122,129,298	132,811	(141,239)
Accrued compensation cost	-	-	-	-	79,430
Business combinations, disposals and capital transactions of subsidiaries	-	-	39,018,253	47,553	50,114
Change in fair and redemption value of noncontrolling interests	-	-	-	-	-
Dividends declared by Sistema JSFC	-	-	-	-	-
Dividends declared by subsidiaries	-	-	-	-	-
Deconsolidation of Bashneft	-	-	-	-	-
Balances at December 31, 2014	9,650,000,000	30,057	(214,097,404)	(246,351)	2,604,913

See notes to the consolidated financial statements and appendix thereto.

Retained earnings	Accumulated other comprehensive Loss	Shareholders' equity	Non-redeemable non-controlling interests	Total equity	Redeemable non-controlling interests
7,110,467	(326,717)	9,172,189	4,109,505	13,281,694	731,661
2,257,528	-	2,257,528	1,021,588	3,279,116	(59,916)
-	(580,001)	(580,001)	(229,192)	(809,193)	6,432
-	-	61,132	-	61,132	-
-	-	54,158	-	54,158	-
-	-	(283,779)	237,429	(46,350)	27,547
(99,406)	-	(99,406)	-	(99,406)	99,406
(275,120)	-	(275,120)	-	(275,120)	-
-	-	-	(950,320)	(950,320)	-
8,993,469	(906,718)	10,306,701	4,189,010	14,495,711	805,130
(4,087,632)	-	(4,087,632)	852,476	(3,235,156)	(78,937)
-	(5,128,557)	(5,128,557)	(974,348)	(6,102,905)	(54,384)
-	-	(8,428)	-	(8,428)	-
-	-	79,430	-	79,430	-
-	-	97,667	(491,574)	(393,907)	-
(120,957)	-	(120,957)	-	(120,957)	120,957
(574,257)	-	(574,257)	-	(574,257)	-
-	-	-	(889,068)	(889,068)	-
-	2,291,873	2,291,873	(1,384,789)	907,084	-
4,210,623	(3,743,402)	2,855,840	1,301,707	4,157,547	792,766

See notes to the consolidated financial statements and appendix thereto.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2014 AND 2013

(Amounts in thousands of U.S. dollars, unless otherwise stated)

1. BASIS OF PREPARATION

Sistema Joint Stock Financial Corporation (the "Company", together with its subsidiaries, the "Group") invests in, and manages a range of companies which operate in the telecommunications, oil and energy, high technology, banking, timber, real estate and other sectors. The Company

and the majority of its consolidated subsidiaries are incorporated in the Russian Federation ("RF").

The controlling shareholder of the Company is Vladimir P. Evtushenkov. Minority holdings are held by certain top executives and directors of the

Company. The rest of the shares are listed on the London Stock Exchange in the form of Global Depositary Receipts ("GDRs") and on the Moscow Exchange.

Below are the Group's significant entities and their principal activities as of December 31, 2014:

Significant entities	Short name	Principal activity	Beneficial ownership as of December 31,	
			2014 года	2013 года
Sistema Joint Stock Financial Corporation	Sistema	Investing and financing		
Mobile TeleSystems	MTS	Telecommunications	53%	53%
SistemaShyamTeleServices Limited	SSTL	Telecommunications	57%	57%
MTS Bank	MTS Bank	Banking	87%	87%
RTI	RTI	Technology	85%	85%
Detsky mir-Center	Detsky mir	Retail trading	99%	100%
Medsi	Medsi	Healthcare services	75%	75%
Targin	Targin	Oilfield services	100%	100%
Bashkirian Power Grid Company (Note 5)	BPGC	Energy transmission	91% ⁽¹⁾	79%(1)
LesInvest (Note 3)	LesInvest	Timber	100%	-
Leader-Invest	Leader-Invest	Real estate	100%	100%

Voting interests as of December 31, 2014 and 2013 – 93%.

The accompanying consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The Group's entities maintain accounting records in the local currencies of the countries of their domicile in accordance with the requirements of respective accounting and tax legislation. The accompanying financial statements differ from the financial statements prepared for statutory purposes in that they reflect certain adjustments,

appropriate to present the financial position, results of operations and cash flows in accordance with U.S. GAAP, which are not recorded in the accounting books of the Group's entities.

In determining and applying accounting policies, judgement is often required in respect of items where the choice of specific policy, accounting estimate or assumption could materially affect the reported results of operations or financial position of the Group.

Management considers that certain accounting estimates and assumptions relating to business combinations and disposals, property, plant and equipment, intangible assets and goodwill, provisions and contingent liabilities and impairment are the Group's critical accounting estimates

A discussion of these estimates together with the summary of the Group's significant accounting policies is provided in appendix A1 to the notes to these consolidated financial statements.

2. DECONSOLIDATION OF BASHNEFT

In September 2014, a civil claim was filed with the Moscow Court of Arbitration by the Prosecutor General's Office of the Russian Federation seeking the transfer to the Russian Federation of all shares in Bashneft held by the Group. The civil claim asserted that the transfer of Bashneft from the property of the Russian Federation into the property of Bashkortostan in 1992-1993 had been unlawful, as no requisite consent had been obtained from the federal authorities, and therefore all subsequent transactions with Bashneft shares should be considered null and

void. In November 2014, the court ruled in favour of the plaintiff and ordered the transfer of the Bashneft shares held by the Group to the Russian Federation. The transfer of the shares took place in December 2014.

The Group deconsolidated Bashneft in December 2014 and recognized a loss upon loss of control, measured as the difference between the carrying amount of noncontrolling interests in the former subsidiary (including accumulated other comprehensive income attributable to the noncontrolling interests) at the date

Bashneft was deconsolidated and the carrying amount of its assets and liabilities. The Group also removed the amount previously accumulated in the translation adjustment component of equity and attributable to Bashneft and reported it as part of the loss on transfer of Bashneft shares to the Russian Federation.

The loss on deconsolidation of Bashneft recognized in the consolidated statement of operations and comprehensive income for the year ended December 31, 2014 is measured as follows:

Net assets as at deconsolidation date	\$	4,061,927
Noncontrolling interests		(1,384,789)
Accumulated currency translation adjustment		<u>2,291,873</u>
		-
Loss on deconsolidation of Bashneft	\$	<u>4,969,011</u>
Noncontrolling interests		-
Loss on deconsolidation of Bashneft	\$	<u>4,969,011</u>
Tax effect		-
Loss on deconsolidation of Bashneft, net of tax		<u><u>4,969,011</u></u>

Bashneft results were separately presented in the consolidated statements of operations and comprehensive income for the years ended December 31, 2014 and 2013 as follows:

	<u>2014</u>	<u>2013</u>
Revenues	\$ 16,224,383	\$ 17,783,111
Income from Bashneft, before income taxes	1,944,770	1,996,126
Income tax expense	(427,716)	(455,637)
Income from Bashneft, net of tax effect	<u>1,517,054</u>	<u>1,540,489</u>

Additionally, the assets and liabilities pertaining to Bashneft have been presented separately within the consolidated statement of financial position as of December 31, 2013 as follows:

Cash and cash equivalents	\$	625,417
Accounts receivable		593,016
Inventories and spare parts		716,847
Other current assets		2,659,069
Intragroup balances		(1,539,621)
Current assets of Bashneft	\$	3,054,728
Property, plant and equipment		8,794,360
Other non-current assets		941,695
Intragroup balances		(116,276)
Non-current assets of Bashneft	\$	9,619,779
Accounts payable		(1,351,326)
Debt, current portion		(367,147)
Other current liabilities		(1,096,320)
Intragroup balances		151,361
Current liabilities of Bashneft	\$	(2,663,432)
Debt, long-term portion		(2,419,639)
Other long-term liabilities		(1,344,437)
Intragroup balances		30,052
Long-term liabilities of Bashneft	\$	(3,734,024)

The Group retains no continuing involvement with Bashneft after it has been deconsolidated, other than routine transactions in the normal course of business.

In December 2014, the Group filed a claim with the Moscow Court of Arbitration for the recovery of RUB 70.7 billion losses from Ural-Invest, a legal successor of the

seller of the Bashneft shares to the Group. In February 2015, the court upheld the Group's claim. In March 2015, the Group and Ural-Invest signed a settlement agreement. In accordance with its terms, all assets owned by Ural-Invest of RUB 46.5 billion, will be transferred to the Group, which will invest RUB 4.6 billion of this amount into the projects of Ural charitable fund. In

March 2015 the Moscow Court of Arbitration approved the settlement agreement between the Group and Ural-Invest. The transfer of assets did not occur as of the date of the issuance of the consolidated financial statements and therefore the Group did not recognize the gain in the consolidated statement of operations and comprehensive income.

3. BUSINESS COMBINATIONS

Business combinations in 2014

LesInvest – In September 2014, LesInvest, a wholly owned subsidiary of the Group, acquired 100% of the share capital of OJSC Segezha Pulp and Paper Mill and LLC Derevoobrabotka-Proekt (together

with their subsidiaries – “LesInvest Group”), a leading manufacturer of sack paper and paper sacks and exporter of timber products and ply wood, for a total cash consideration of \$287 million. The Group sees high growth potential for the LesInvest Group business, to be unlocked by

improving operating efficiency and upgrading production facilities. The following table summarizes consideration paid and the amounts of the assets acquired and liabilities assumed that were recognized at the acquisition date:

Property, plant and equipment	\$	110,917
Inventories		109,876
Deferred tax assets		76,047
Other assets		117,367
Accounts payable and other liabilities		(127,000)
Cash consideration paid	\$	<u>287,207</u>

The purchase price allocation of LesInvest Group was not finalized as of the date of these consolidated financial statements, as the Group

had not completed the valuation of individual assets and liabilities of LesInvest Group. The Group’s consolidated financial statements

reflect the allocation of the purchase price based on a preliminary fair value assessment of the assets acquired and liabilities assumed.

Other acquisitions

The information on other business combinations which took place in 2014 is summarized below:

Acquiree	Principal activity	Date of acquisition	Interest acquired	Acquiring segment	Purchase price
SMARTS-Ivanovo	Mobile operator	December	100%	MTS	7,480
SMARTS-Ufa	Mobile operator	December	100%	MTS	7,040
Penza-GSM	Mobile operator	December	100%	MTS	34,121
Step Group	Grain production	December	85%	Corporate	63,965
Total					\$ <u>112,606</u>

The following table summarizes the amounts of the assets acquired and liabilities assumed relating to such acquisitions at the acquisition date:

Current assets	\$	25,935
Property, plant and equipment		78,467
Rights to use radio frequencies		25,759
Goodwill		29,247
Other non-current assets		5,061
Current liabilities		(32,722)
Non-current liabilities		(9,546)
Noncontrolling interests		(9,595)
Purchase price	\$	112,606

The purchase price allocations of SMARTS-Ivanovo, SMARTS-Ufa and Penza-GSM were not finalized as of the date of these financial statements as the Group had not completed the valuation of the individual assets of each entity. The Group's consolidated financial statements reflect the allocation of the purchase price

based on a preliminary fair value assessment of the assets acquired and liabilities assumed. The excess of the consideration paid over the value of net assets in the amount of \$29 million was preliminarily allocated to goodwill which was attributable to the MTS segment. Goodwill is mainly attributable to the expected synergies

from combining the operations of MTS and acquired companies.

In December 2014, Krasnodar Agro, a wholly owned subsidiary of the Group, acquired 85% of the voting shares of the five grain producers in Krasnodar region (Step Group).

Pro forma results of operations (unaudited)

The following pro forma financial data for the years ended December 31, 2014 and 2013 give effect to the

acquisition of LesInvest Group as if it had occurred as of January 1, 2013:

	2014	2013
Revenues	\$ 17,130,212	\$ 19,199,485
Net income	(3,346,547)	3,052,629

The pro forma information is based on various assumptions and estimates. The pro forma information is neither necessarily indicative of the operating results that would have occurred if the Group acquisitions had been consummated as of January 1, 2013, nor is it necessarily indicative of future operating results. The pro forma information does not

give effect to any potential revenue enhancements or cost synergies or other operating efficiencies that could result from the acquisitions. The actual results of operations of these companies are included into the consolidated financial statements of the Group only from the respective dates of acquisition.

The following amounts of revenue and earnings of LesInvest Group since the acquisition date in September 2014 are included into the consolidated statement of operations and comprehensive income for the year ended December 31, 2014:

	2014
Net revenues	\$ 151,227
Net income	14,178

The results of operations of other acquired businesses have not been included because the effects of these

business combinations, individually and in aggregate, were not material to the Group's consolidated results

of operations.

Business combinations in 2013

SITRONICS-Nano – In May 2013, the Group acquired an additional 12.3% ownership interest in SITRONICS-Nano, previously an affiliate, from RUSNANO for cash consideration of RUB 2 billion (\$61.1 million at the acquisition date) increasing its voting interest to 62.1%. Simultaneously, the Group and RUSNANO amended existing call and put option agreements. Under the amended agreements, the Group had a call

option to acquire RUSNANO's shares in Sitronics-Nano for RUB 6.1 billion plus 7.63% p.a. at any time till November 1, 2017. RUSNANO had a put option to sell its remaining shares in SITRONICS-Nano for RUB 8.1 billion not earlier than October 31, 2016 and not later than November 1, 2017. This acquisition allowed the Group to secure its rights for use of 180 and 90 nanometre equipment that has been leased from SITRONICS-Nano.

As a result of the transactions, the Group obtained control over SITRONICS-Nano and accounted for this business combination by applying the acquisition method. The following table summarizes the consideration paid for SITRONICS-Nano and the assets acquired and liabilities assumed recognized at the acquisition date, as well as the fair value of the noncontrolling interests in the investee:

Current assets	\$	73,231
Net investment in the lease		518,916
Current liabilities		(76,700)
Non-current liabilities		(18,829)
Noncontrolling interests		(187,164)
		309,454
Fair value of previously held interest		(248,309)
Cash consideration	\$	61,145

As part of this business combination, the Group recognised a revaluation gain resulting from the remeasurement of its previously held interest. The difference in the amount of \$22.4 million between the fair value of previously held interest and the carrying value of the Group's investment has been recorded

within other operating expenses, net in the consolidated statement of operations and comprehensive income. The fair value of previously held interest and the noncontrolling interests in SITRONICS-Nano were estimated based on the amount of consideration in the transaction described above.

In May 2014, following the issuance of additional shares in Mikron, a subsidiary of RTI, such put and call option agreements between the Group and ROSNANO were amended (Note 5).

4. DISPOSALS

Disposals in 2014

NIIDAR-Nedvizhimost – In 2014, the Group sold its 100% interest in NIIDAR-Nedvizhimost, a subsidiary of RTI which managed rental property, for a total cash consideration of \$150.0 million. As a result of this transaction, the Group recognized gain on disposal of subsidiaries of \$139.1 million, included in other operating expenses in the consolidated statement of operations and comprehensive income.

Disposals in 2013

SG-trans – During 2013, the Group completed a reorganisation of its transportation assets. As a result of the reorganization, SG-trans,

which was acquired in 2012 was split into two legal entities: SG-trading which comprised the non-core non-transportation assets and SG-trans which retained all the core transport assets. In April 2013 the Group sold a 70% stake in SG-trans to Financial Alliance, an affiliate of the Group, for cash consideration of RUB 12 billion (\$380.2 million at the disposal date), thereby reducing its direct ownership in SG-trans from 100% to 30%.

Upon disposal, the Group deconsolidated SG-trans and accounted for its remaining interest using the equity method. As a result of the transaction, the Group recognized a gain of \$4.0 million in the consolidated statement of operations and comprehensive income.

In July 2013, the Group further sold additional 15% of SG-trans to Unirail, a shareholder of Financial Alliance, for a cash consideration of RUB 2.5 billion (\$76.4 million) with no gain or loss recognized as a result of this transaction.

RussNeft – In July 2013, the Group sold its 49% stake in RussNeft, the Group's affiliate, for cash consideration of \$1,200 million. Prior to the disposal, the Group has been accounting for this investment using the equity method. As of the disposal date, the carrying value of the Group's investment in RussNeft was nil. Accordingly, the Group recognized a \$1,200 million gain on this disposal being the difference between the consideration received and the carrying value of investment disposed.

5. CAPITAL TRANSACTIONS OF SUBSIDIARIES

Transactions in 2014

MTS Bank – In December 2014, the Group participated in additional share issue of MTS Bank for \$309.0 million. The transaction resulted in no change in noncontrolling interests and additional paid-in capital.

Mikron – In May 2014, Mikron issued additional shares representing 25.1% of its share capital in exchange for 37.7% interest in SITRONICS-Nano, owned by OJSC RUSNANO. Upon completion of the transaction, the Group's effective ownership in Mikron decreased to 53.0%. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests and an increase of additional paid-in capital by \$44.1 million. Simultaneously, the Group and RUSNANO substituted their existing put and call option agreements on RUSNANO's share in SITRONICS-Nano for new put and call option agreements on its 25.1% share in Mikron. The terms of the option agreements remained unchanged.

Business-Nedvizhimost – In April 2014, MTS sold a 49% stake in Business-Nedvizhimost, a company which owns and manages a real estate portfolio in Moscow, to the Company for \$91.8 million. This transfer of ownership interest within the Group resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by \$47.4 million.

NVision – In January 2014, the Group acquired an additional 38.75% stake in NVision from minority shareholders for \$82.5 million, \$37.5 million of which was paid in cash and \$45.0 million in the Company's treasury shares. Upon completion of this transaction, the Group's ownership in NVision was 88.75%. The transaction was accounted for directly in equity and resulted in an increase of noncontrolling interests by \$42.0 million and a decrease of additional paid-in capital by \$121.8 million. In December 2014, the Group acquired the remaining 11.25% stake in NVision for approximately \$10.0 million. The transaction was

accounted for directly in equity and resulted in a decrease of noncontrolling interests by \$13.8 million and a decrease of additional paid-in capital by \$24.0 million.

Transactions in 2013

Business-Nedvizhimost – In December 2013, MTS sold a 51% stake in Business-Nedvizhimost to the Company for RUB 3.2 billion (\$98.5 million as of the transaction date). This transfer of ownership interest within the Group resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by \$42.7 million.

RTI – In December 2013, RTI issued 4,687,500,000 common shares with par value of 1 Russian ruble which were acquired by existing shareholders, the Company and the Bank of Moscow, for cash consideration of RUB 6.0 billion (\$183.9 million as of the purchase date) in proportion to their existing ownership interests. The Bank of Moscow received a put

option to sell its 703,125,000 shares acquired upon their issuance to the Group at a price of \$27.5 million plus 8.25% p.a. not earlier than December 26, 2016 and not later than December 26, 2018. As a result of this put option, the Group classified the underlying noncontrolling interests as redeemable.

Targin – In September 2013, the Company acquired a 100% stake in Bashneft Services Assets, (renamed to Targin in July 2014) from Bashneft for RUB 4.1 billion (\$126.8 million as at transaction date). This transfer of ownership interest within the Group resulted in a decrease of noncontrolling interests and an increase of additional paid-in capital by \$24.4 million.

MTS – In September-December 2013, the Group acquired 0.6% of MTS ordinary shares on the open market for \$120.0 million. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests by \$23.0 million and a decrease of additional paid-in capital by \$97.0 million.

Detsky mir – In September 2013, Detsky mir purchased 25%+1 of its own shares from Sberbank for cash consideration of \$140.0 million. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests by \$5.4 million and a decrease of additional paid-in capital by \$134.6 million. The Group took a long-term loan from Sberbank to fund the purchase. Simultaneously the Group has pledged these shares to Sberbank as security against the loan.

SITRONICS-N – In September 2013, the Group undertook restructuring of certain RTI assets. Upon completion of a series of transactions, SITRONICS, a subsidiary of RTI, spun off two companies, SITRONICS-N and RTI Microelectronics, with allocation of all its major assets and liabilities to these companies. To complete the restructuring process a 100% stake in SITRONICS was sold to SITRONICS-N

for 1 RUB. In October 2013, the Company acquired a 100% stake in SITRONICS-N from RTI for RUB 1.0 billion (\$31.0 million as at transaction date). This transaction resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by \$11.0 million.

Mikron – In August 2013, Mikron issued 691,962 ordinary shares which were purchased by the RF for cash consideration of RUB 465 million (\$14.1 million). This transaction was accounted for directly in equity and resulted in an increase of noncontrolling interests by \$5.2 million and an increase of additional paid-in capital by \$8.9 million.

MTS Bank – In April 2013, MTS acquired a 25.0945% stake in MTS Bank through the purchase of its additional share issuance for RUB 5 billion (\$123 million). Upon completion of the transaction, the Group's effective ownership in MTS Bank decreased from 99% to 87%. This transfer of ownership interest within the Group resulted in an increase of noncontrolling interests and a decrease of additional paid-in capital by \$105 million.

Capital transactions of Bashneft and its subsidiaries

UPC – In September 2014, the Group terminated a contract for the acquisition of a 98% stake in UPC from Bashneft. As a consequence of this transaction, Bashneft obtained control over UPC. This resulted in the Group's ownership in UPC decreasing from 99.0% to 78.0% and the Group's ownership in Ufaorgsintez decreasing from 86.5% to 78.7%. These transactions resulted in an increase of noncontrolling interests in the amount of \$4.8 million and a decrease of additional paid-in capital by \$20.9 million.

Bashneft-Polyus – On 23 May 2014, in accordance with an order from the Federal Agency for Subsoil Use

(“Rosnedra”) the Trebs and Titov oilfield license was transferred from Bashneft to its subsidiary Bashneft-Polyus. This transaction resulted in an increase in noncontrolling interests in the amount of \$113.0 million with a corresponding decrease in the Group's constructive obligation to OJSC LUKOIL in the amount of \$139.1 million and an increase in additional paid-in capital by \$26.1 million.

Sistema-Invest – In May 2014, the reorganization of CJSC Sistema-Invest (“Sistema-Invest”) was completed. 38,139,925 ordinary shares of Bashneft previously held by CJSC Bashneft-Invest, wholly-owned subsidiary of Bashneft created through a spinoff from Sistema-Invest, and 8,885,866 preferred shares bought back from the shareholders were cancelled. The transactions were accounted for directly in equity and resulted in a decrease of noncontrolling interests by \$694.6 million and an increase of additional paid-in capital by \$199.4 million. The Group's ownership in Bashneft increased from 75.0% to 78.8% and in BPGC – from 79.3% to 91.0%.

Ufaorgsintez – In March 2014, pursuant to the terms of a voluntary tender offer originally announced in December 2013, Ufaorgsintez completed the acquisition of its ordinary shares for a total consideration of \$26.5 million. As a result, the Group's ownership in Ufaorgsintez increased from 76.8% to 86.5%. The transaction was accounted for directly in equity and resulted in a decrease of noncontrolling interests by \$49.5 million and an increase of additional paid-in capital by \$22.5 million.

UPC – In September 2013, the Company acquired a 98% stake in United Petrochemical Company (“UPC”) from Bashneft for RUB 6.2 billion (\$192.0 million as at transaction date), which resulted in a decrease of noncontrolling interests and an increase of additional paid-in capital by \$41.4 million.

6. BREENTRY INTO UZBEKISTAN

Following unsuccessful tenders on sale of Uzdunrobita equipment, the representatives of the Republic of Uzbekistan and MTS commenced negotiations in relation to the return of MTS to the market. In July 2014, MTS signed a settlement agreement with the Republic of Uzbekistan eliminating all mutual claims ("Settlement Agreement"). International arbitration proceedings between MTS and the Republic of Uzbekistan in the International Center for Settlement of Investment Disputes, Member of the World Bank Group (ICSID), were discontinued following the submission of a joint application by the both parties.

The government authorities provided certain guarantees to MTS in relation to the protection of any future investment in the Republic of Uzbekistan to encourage the return of MTS to the market.

Also, the Republic of Uzbekistan established a legal entity, Universal

Mobile Systems LLC ("UMS"), with such entity having no legal connection to the previously liquidated entity, Uzdunrobita. UMS was granted 2G, 3G and LTE licenses and received frequencies, numbering capacity and other permits required for the launch of operations.

In September 2014, a 50.01% ownership interest in UMS was transferred to the Group by a state-owned enterprise established and managed by the State committee for communications, development of information systems and telecommunications technologies of the Republic of Uzbekistan, which retained the remaining 49.99% in UMS. The Group concluded that, upon receiving the 50.01% ownership interest, the Group obtained control over UMS and consolidated the entity. The Group estimated the fair value of the entity's assets and liabilities, as well as the noncontrolling interests in UMS as of the date of the transfer,

and recognized a gain from reentry into Uzbekistan pursuant to the Settlement Agreement in the amount of \$181 million.

The Group has determined that the Settlement Agreement primarily addressed two separate elements – the elimination of all mutual claims and guarantees granted to MTS in connection with its reentry into the Republic of Uzbekistan. The Group concluded that the aforementioned consideration of \$181 million related to, in its entirety, a financial incentive to encourage the reentry into the Republic of Uzbekistan and as such, recognition in continuing operations was appropriate. No element was allocated to the non-satisfaction and elimination of mutual claims as this was deemed to have minimal value.

The following table summarizes the amounts of the assets and liabilities recognized at the date of obtaining control, as well as the fair value of the noncontrolling interests at that date:

Property, plant and equipment	\$	119,211
Intangible assets		132,333
Other non-current assets		31,610
Noncontrolling interests		(101,849)
Gain from reentry into Uzbekistan	\$	181,305

7. ASSETS FROM BANKING ACTIVITIES

Assets from banking activities, net of an allowance for loan losses, as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Cash and cash equivalents	\$ 843,715	\$ 1,132,368
Loans to customers	2,597,696	4,842,982
Investments in securities (trading)	368,567	551,513
Loans to banks	131,919	161,229
Investments in securities (available-for-sale)	87,652	154,356
Other investments	85,956	127,096
Less: allowance for loan losses	(560,942)	(516,575)
Assets from banking activities, net	3,554,563	6,452,969
Less: amounts maturing after one year	(1,374,367)	(2,554,229)
Assets from banking activities, current portion	\$ 2,180,196	\$ 3,898,740

Major categories of loans to customers as of December 31, 2014 and 2013 comprise the following:

	2014	2013
Corporate customers	\$ 1,294,744	\$ 2,739,345
Individuals	1,302,952	2,103,637
Total	\$ 2,597,696	\$ 4,842,982

As of December 31, 2014, 79.7% and 0.6% of the balance of loans to corporate customers and individuals, respectively, were evaluated individually for impairment (2013: 80.0% and 0.5%).

The following table presents the effective average interest rates by category of loans as of December 31, 2014 and 2013:

	2014			2013		
	RUB	USD	Other	RUB	USD	Other
Loans to customers						
- corporate customers	10.5%	8.8%	9.2%	10.8%	7.0%	9.8%
- individuals	19.0%	4.4%	6.5%	23.4%	8.3%	4.2%
Loans to banks	7.9%	0.01%	0.01%	4.5%	0.1%	0.1%

The movement in the allowance for loan losses in 2014 and 2013 was as follows:

	2014	2013
Allowance for loan losses, beginning of the year	\$ 516,575	\$ 329,803
Additions charged to operating results less recovery of allowance	423,121	248,032
Amounts written off against the allowance	(162,705)	(37,185)
Currency translation adjustment	(216,049)	(24,075)
Allowance for loan losses, end of the year	\$ 560,942	\$ 516,575

8. SHORT-TERM INVESTMENTS

Short-term investments as of December 31, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Bank deposits with original maturities exceeding three months	\$ 202,644	\$ 647,077
Trading securities	97,550	499,437
Available-for-sale securities	74,149	354,838
Promissory notes and loans	104,998	61,195
Total	\$ 479,341	\$ 1,562,547

Promissory notes and loans to third parties are primarily denominated in USD and bear interest rates varying from 4.0% to 6.0% as of December 31, 2014.

The effective interest rates on bank deposits with original maturities exceeding three months as of December 31, 2014 are between 1.0% and 5.3% (December 31, 2013: 4.2% and 14.0%).

9. ACCOUNTS RECEIVABLE

Accounts receivable, net of provision for doubtful accounts, as of December 31, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Trade receivables	\$ 1,246,580	\$ 1,808,403
Less: provision for doubtful accounts	(83,488)	(177,810)
Total	\$ 1,163,092	\$ 1,630,593

Write-off of trade receivables against provision for doubtful accounts in 2014 and 2013 amounted to \$134.7 million and \$96.5 million respectively.

10. OTHER CURRENT ASSETS

Other current assets as of December 31, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Prepaid expenses and other receivables	\$ 564,594	\$ 763,791
Tax advances and overpayments	121,360	136,164
Advances paid to third parties	242,184	246,727
	928,138	1,146,682
Less: provision for doubtful accounts	(96,078)	(62,135)
Total	\$ 832,060	\$ 1,084,547

11. INVENTORIES AND SPARE PARTS

Inventories and spare parts as of December 31, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Finished goods and goods for resale	\$ 405,243	\$ 593,500
Raw materials and spare parts	232,248	377,292
Work-in-progress	89,506	151,434
Costs and estimated earnings in excess of billings on uncompleted contracts	531,052	116,984
	1,258,049	1,239,210
Less: long-term portion	(13,540)	(107,908)
Total	\$ 1,244,509	\$ 1,131,302

12. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, net of accumulated depreciation, as of December 31, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Switches, transmission devices, network and base station equipment	\$ 9,066,682	\$ 14,083,007
Buildings and leasehold improvements	1,392,585	2,166,179
Power and utilities	496,303	760,686
Other plant, machinery and equipment	1,495,420	2,620,291
Construction in progress and equipment for installation	897,260	1,576,285
Land	148,238	160,973
	13,496,488	21,367,421
Less: accumulated depreciation	(6,305,094)	(10,216,080)
Total	\$ 7,191,394	\$ 11,151,341

Depreciation expense for the years ended December 31, 2014 and 2013 amounted to \$1,778.6 million and \$2,089 million respectively. Impairments of property, plant and equipment for the years ended December 31, 2014 and 2013 amounted to \$290.4 million and \$285.9 million respectively (Note 15).

13. GOODWILL

The carrying amounts of goodwill attributable to each reportable segment are as follows:

	<u>MTS</u>	<u>SSTL</u>	<u>RTI</u>	<u>MTS Bank</u>	<u>Other</u>	<u>Total</u>
Balance as of January 1, 2013						
Gross amount of goodwill	1,441,836	339,059	278,449	67,919	95,636	2,222,899
Accumulated impairment loss	(48,261)	(339,059)	-	(67,919)	-	(455,239)
	\$ 1,393,575	\$ -	\$ 278,449	\$ -	\$ 95,636	\$ 1,767,660
Impairment (Note 15)	-	-	(258,048)	-	-	(258,048)
Disposals	(722)	-	-	-	(67,816)	(68,538)
Currency translation adjustment	(93,958)	-	(17,210)	-	(2,127)	(113,295)
Balance as of December 31, 2013						
Gross amount of goodwill	1,343,717	300,047	254,291	63,068	25,693	1,986,816
Accumulated impairment loss	(44,822)	(300,047)	(251,100)	(63,068)	-	(659,037)
	\$ 1,298,895	\$ -	\$ 3,191	\$ -	\$ 25,693	\$ 1,327,779
Business combinations (Note 3)	29,247	-	-	-	-	29,247
Currency translation adjustment	(524,502)	-	(1,335)	-	(13,652)	(539,489)
Balance as of December 31, 2014						
Gross amount of goodwill	829,716	293,424	147,937	36,691	12,041	1,319,809
Accumulated impairment loss	(26,076)	(293,424)	(146,081)	(36,691)	-	(502,272)
	\$ 803,640	\$ -	\$ 1,856	\$ -	\$ 12,041	\$ 817,537

14. OTHER INTANGIBLE ASSETS

Intangible assets other than goodwill as of December 31, 2014 and 2013 consisted of the following:

	2014			2013		
	Gross carrying value	Accumulated amortization	Net carrying value	Gross carrying value	Accumulated amortization	Net carrying value
Amortized intangible assets:						
Billing and telecommunication software	\$ 974,142	(603,303)	370,839	1,053,559	(580,156)	473,403
Operating licenses	704,536	(214,352)	490,184	768,488	(157,778)	610,710
Radio frequencies	203,419	(101,034)	102,385	301,042	(149,954)	151,088
Acquired customer base and customer relationships	225,495	(136,714)	88,781	468,497	(247,643)	220,854
Software and other	855,003	(376,890)	478,113	973,084	(481,941)	491,143
	2,962,595	(1,432,293)	1,530,302	3,564,670	(1,617,472)	1,947,198
Unamortized intangible assets:						
Trademarks	184,811	-	184,811	206,135	-	206,135
Numbering capacity with indefinite contractual life	6,276	-	6,276	9,367	-	9,367
Total	\$ 3,153,682	(1,432,293)	1,721,389	3,780,172	(1,617,472)	2,162,700

Impairments of intangible assets other than goodwill for the years ended December 31, 2014 and 2013 amounted to \$nil and \$298.2 million respectively (Note 15).

Amortization expense recorded on other intangible assets for the years ended December 31, 2014 and 2013 amounted to \$513.5 million and \$544.6 million, respectively. The estimated amortization expense for the five years ending December 31, 2019 and thereafter is as follows:

Year ending December 31,	
2015	\$ 367,272
2016	306,060
2017	214,242
2018	122,424
2019	61,212
Thereafter	459,092
	\$ 1,530,302

Actual amortization expense to be reported in future periods could differ from these estimates as a result of new intangible assets acquisitions, changes in useful lives and other relevant factors.

15. IMPAIRMENT OF OTHER ASSETS

Impairment of other assets recognized by the Group in the years ended December 31, 2014 and 2013 comprised the following:

	<u>2014</u>	<u>2013</u>
Impairment of long-lived assets in India	\$ 290,438	\$ -
Impairment of 180 and 90 nm equipment and intangible assets	-	357,906
Impairment of system integration intangible assets	-	125,747
Impairment of other long-lived assets	175,386	106,753
Impairment of available-for-sale securities	135,000	-
Provision for cash and deposits in Delta Bank (Ukraine)	92,517	-
Provision for doubtful accounts	103,625	134,392
Inventory obsolescence	30,442	46,504
Other	37,221	33,243
Total impairments of other assets	\$ 864,629	\$ 804,545

Impairment of 180 and 90 nm equipment and intangibles assets –

As of December 31, 2013 the Group carried out a review of the recoverable amount of long-lived assets used in the production of microchips. As a result of this impairment review, an impairment charge of \$357.9 million was recognized in the consolidated statement of operations and comprehensive income for the year ended December 31, 2013, which was allocated to the RTI segment.

As of December 31, 2014, the Group identified indicators that the carrying amounts of 180 and 90 nm equipment with a total carrying value of \$108.4 million may not be recoverable. These indicators included lower than expected revenue and profitability levels. The Group carried out review that supported the carrying value of the equipment and indicated that no additional impairment is required.

The estimated fair value of such long-lived assets was determined based on unobservable inputs (“Level 3” of the hierarchy established by U.S. GAAP guidance). When calculating the future cash flows used in the assessment of the fair value of long-lived assets, the Group considered historical and projected revenue and operating

costs, market conditions, asset ages, asset utilization and other relevant information. The key assumptions used in the fair value calculations included pre-tax discount rate of 25.0%-56.3% depending on the business line (2013: 21.5%-43.8%), compound annual growth rate during the projected twelve-year period of 21.8% (2013: 11.7%), growth rate after that period of 2.3% (2013: 2.3%).

Impairment of system integration intangible assets – During the year ended December 31, 2013, the Group identified indicators that the carrying amounts of long-lived assets attributable to NVision, a subsidiary of RTI, may not be recoverable. These indicators included lower than expected revenue and profitability levels and downward revisions to management’s forecasts for the NVision business.

Subsequent to its acquisition by the Group in 2012, NVision experienced a significant decrease in purchases made by its key customers and, as a result, revenue forecasts were substantially reduced as compared to those existing at the acquisition date. Based on the revised forecasts, the Group determined that the carrying value of the NVision asset group exceeded its undiscounted cash flows. The Group then compared the fair value of the asset group to its

carrying value and determined the impairment loss. The impairment loss was allocated to the carrying values of the long-lived assets, but not below their individual fair values. The Group estimated the fair value of the assets primarily using an income approach based on unobservable inputs (“Level 3” of the hierarchy established by U.S. GAAP guidance), with the key assumptions including a discount rate of 16.5% and 3-7% of revenue royalty payments for the trademark. The decline in the fair value of the NVision reporting unit and its intangible assets, as well as fair value changes for other assets and liabilities in the two-step goodwill impairment test, resulted in an implied fair value of goodwill being substantially below its carrying value.

As a result of the impairment review, for certain intangible assets with a carrying value of \$129.1 million the Group concluded that the fair value amounted to \$3.3 million and recorded an impairment charge of \$125.7 million in the consolidated statement of operations and comprehensive income for the year ended December 31, 2013. The Group also recorded an impairment charge on goodwill of \$258.0 million based on its implied fair value. The relevant impairment charges were allocated to the RTI segment.

Provision for cash and deposits in Delta Bank (Ukraine) – As of December 31, 2014, MTS Ukraine, a subsidiary of MTS, held \$90.2 million in current accounts and deposits in Delta Bank, the fourth largest

bank in Ukraine. In December 2014, Delta Bank delayed customer payments and put limits on cash withdrawals. In March 2015, the National Bank of Ukraine adopted a resolution declaring Delta Bank to

be insolvent. The Group treated Delta Bank's insolvency as a recognized subsequent event and provided against the full amount of deposited funds (\$90.2 million) and related interest (\$2.3 million).

16. INVESTMENTS IN AFFILIATES

Investments in affiliates as of December 31, 2014 and 2013 consisted of the following:

	2014		2013	
	Voting power	Carrying value	Voting power	Carrying value
MTS Belarus	49.0%	\$ 107,237	49.0%	\$ 165,174
OZON	21.6%	91,080		-
SG-trans (2013: SG-trans and Financial Alliance, Note 4)	50.0%	83,555	50.0%	133,551
Concept Group	40.0%	18,913		-
Other		55,233		66 541
Total		\$ 356,018		\$ 365,266

Investment in OZON – In April 2014, the Group acquired a 21.6% of ownership interest in OZON Holdings Limited (“OZON”), a leading Russian e-commerce company, through an additional share issuance for \$150.0 million. The Group has the right to nominate two out of eight representatives to the board of directors. Management concluded that, upon completion of the acquisition, the Group gained significant influence over OZON and therefore adopted equity method of accounting for this investment. The Group also obtained a call option for an additional 4.6% stake in OZON exercisable through August 2015. The difference between the equity investment carrying amount of \$91 million and underlying equity in net assets as of December 31, 2014 of \$26.0 million represents equity-

method goodwill, mainly attributable to the expected synergies from commercial arrangements and co-branding programs.

Investment in Concept Group – In October 2014, the Group acquired a 40% of ownership interest in Rangelcroft Ltd, a holding company of Concept Group, one of Russia's leading fashion clothing retailers, for \$26.0 million, and obtained a call option to acquire another 14.2% of its share capital exercisable till October 2017. In accordance with the shareholders agreement, the Group has the right to nominate three out of nine representatives to the board of directors and, if the call option is exercised, up to five of the nine representatives. A number of key operating decisions for Concept Group, including an approval of an

operating budget, require seven out of nine votes; such operating decisions represent participating rights of the shareholders. As a consequence of this, the Group has concluded that it does not have control over the investee and has therefore adopted the equity method of accounting for this investment.

Merger of SG-trans and Finance Alliance – In January 2014, SG-trans and Finance Alliance merged into a single legal entity named SG-trans. The Group retained 50% beneficial interest in the newly established entity.

The financial position and results of operations of significant affiliates as of and for the year ended December 31, 2014 were as follows:

The financial position and results of operations of significant affiliates as of and for the year ended December 31, 2014 were as follows:

	(unaudited)			
	MTS Belarus	OZON	SG-trans	Concept Group
Total assets	\$ 303,315	192,860	641,193	91,607
Total liabilities	(94,102)	(71,403)	(453,119)	(65,646)
Net income/(loss)	194,317	(77,690)	12,059	5,792

The financial position and results of operations of significant Group affiliates as of and for the year ended December 31, 2013 were as follows:

	(unaudited)	
	MTS Belarus	Financial Alliance(1)
Total assets	\$ 379,050	1,480,703
Total liabilities	(96,580)	(1,185,979)
Net income/(loss)	145,975	13,435

⁽¹⁾Including SG-trans amounts.

17. LONG-TERM INVESTMENTS

Long-term investments as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Bank deposits	\$ 242,006	\$ 90,727
Loans and notes	51,400	129,638
Other	23,219	28,706
Total	\$ 316,625	\$ 249,071

The effective interest rates on long-term investments as of December 31, 2014 were between 6.2% and 6.3% for EUR denominated investments (2013: 6.0% – 8.6%).

18. LIABILITIES FROM BANKING ACTIVITIES

Liabilities from banking activities as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
Term deposits	\$ 1,567,548	\$ 2,561,569
Deposits repayable on demand	537,365	1,859,832
Promissory notes issued and other liabilities	243,438	215,539
	2,348,351	4,636,940
Less: amounts maturing within one year	(2,180,491)	(3,864,415)
Total liabilities from banking activities, net of current portion	\$ 167,860	\$ 772,525

As of December 31, 2014 the fair value of liabilities from banking activities amounted to \$2,270 million; as of December 31, 2013 – approximated their carrying value.

The following table presents the effective average interest rates by categories of bank deposits and notes issued as of December 31, 2014 and 2013:

	2014			2013		
	RUB	USD	Other	RUB	USD	Other
Term deposits:						
- corporate customers	14.5%	3.0%	2.9%	7.4%	1.8%	2.1%
- individuals	10.0%	3.7%	3.4%	9.7%	3.7%	2.3%
Promissory notes issued	8.0%	-	-	7.3%	-	-
Deposits repayable on demand:						
- corporate customers	0.5%	-	-	4.9%	-	-
- individuals	0.5%	0.1%	0.2%	0.6%	0.07%	0.1%

19. ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities as of December 31, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Customers' advances	\$ 546,793	\$ 350,896
Accrued payroll	267,971	430,946
Accruals for services	210,924	328,050
Accrued interest on loans	51,805	74,621
Financial instruments at fair value	47,086	13,199
Dividends payable	1,369	6,729
Other	189,708	363,449
Total	\$ 1,315,656	\$ 1,567,890

20. LONG-TERM DEBT

Long-term debt as of December 31, 2014 and 2013 consisted of the following:

	<u>2014</u>	<u>2013</u>
Loans from banks and financial institutions	\$ 5,049,820	\$ 5,447,071
Notes and corporate bonds	2,781,512	4,888,603
Capital leases	239,401	80,506
Loans from related parties	37	64
Vendor financing	16,662	31,871
Other borrowings	45,393	29,957
	8,132,825	10,478,072
Less: amounts maturing within one year	(1,598,770)	(2,102,911)
Total	\$ 6,534,055	\$ 8,375,161

The schedule of repayments of long-term debt for the next five years and thereafter is as follows:

Year ended December 31		
2015	\$	1,598,770
2016		1,185,257
2017		1,469,871
2018		1,022,949
2019		1,148,236
Thereafter		1,707,742
Total	\$	8,132,825

Loans from banks and financial institutions – Loans from banks and financial institutions as of December 31, 2014 and 2013 consisted of the following:

	Maturity	Interest rate (as at December 31, 2014)		2014	2013
USD-DENOMINATED:					
Calyon, ING Bank, Nordea Bank, Raiffeisen Zentralbank Österreich	2015-2020	LIBOR+1.15% (1.51%)	\$	673,698	798,440
China Development Bank	2015-2018	LIBOR+1.5% (1.86%)		179,421	187,497
Bank of China	2015-2021	LIBOR+1.5%-3.5% (1.86%-3.86%)		170,552	170,615
Skandinaviska Enskilda Banken	2015-2017	LIBOR+0.23%-1.8% (0.59%-2.16%)		91,987	129,494
Bank of Moscow	2015	LIBOR+7.5% (7.76%)		82,552	82,552
HSBC Bank and ING BHF Bank				-	12,022
Other				14,230	27,223
				1,212,440	1,407,843
EUR-DENOMINATED:					
Credit Agricole Corporate Bank, BNP Paribas	2015-2018	EURIBOR+1.65% (1.82%)		33,649	47,574
Bank of Moscow	2015-2017	EURIBOR+5.0% (5.15%)		27,333	-
LBBW	2015-2017	EURIBOR+1.52% (1.69%)		16,995	25,630
Bank of China				-	74,403
Other				12,187	14,398
				90,164	162,005
RUB-DENOMINATED:					
Sberbank	2015-2021	8.45%-15.0%		3,007,244	2,922,817
Gazprombank	2015-2018	9.0%-10.6%		253,170	294,439
Raiffeisenbank	2015-2016	Mosprime+1.45%-5.25% (23.42%-29.02%), 9.45%		149,568	71,891
Bank of Moscow	2015-2018	CBR+3.0% (11.25%); Mosprime+4.5%-8.85% (28.27%-31.02%);		128,993	256,258
VTB	2015-2018	9.0%-22.75%		86,461	77,571
Unicredit	2016	Mosprime+5.2% (12.17%); 10.1-10.4%		37,179	73,248
Alfa-Bank	2015	9.75%-14.18%		27,143	92,486
Credit bank of Moscow	2016	19.0%		8,888	30,554
Other				30,928	53,560
				3,729,574	3,872,824
Other currencies				17,642	4,399
Total			\$	5,049,820	5,447,071

The fair value of loans from banks and financial institutions, including the current portion, is estimated using discounted cash flows and market-based expectations for interest rates, credit risk and the

contractual terms of the debt instruments ("Level 2" of the hierarchy established by the U.S. GAAP guidance). As of December 31, 2014 the fair value of loans from banks and financial institutions,

including the current portion, amounted to \$4,730 million; as of December 31, 2013 – approximates their carrying value.

Notes and corporate bonds – Notes and corporate bonds as of December 31, 2014 and 2013 consisted of the following:

	Currency	Interest rate	2014		2013
			Fair value	Carrying value	Carrying value
MTS International 2020	USD	8.625%	\$ 601,019	\$ 623,140	\$ 747,634
MTS International 2023	USD	5.00%	369,641	478,500	500,000
Sistema International 2019	USD	6.95%	338,193	464,979	487,854
MTS OJSC Notes due 2020	RUB	8.15%	253,296	266,627	458,306
SSTL 2019	INR	15.75%	202,111	202,111	206,795
MTS OJSC Notes due 2023	RUB	8.25%	133,313	177,751	305,538
MTS OJSC Notes due 2017	RUB	8.70%	151,181	171,894	294,191
Sistema JSFC Bonds due 2016	RUB	8.75%	113,840	145,949	329,790
MTS OJSC Notes due 2015	RUB	7.75%	131,364	134,045	230,567
Sistema JSFC Bonds due 2016	RUB	7.65%	60,376	65,271	406,985
MTS OJSC Notes due 2016	RUB	8.75%	29,851	31,780	54,627
DM-Center Bonds due 2015	RUB	8.50%	16,238	16,418	35,137
MTS OJSC Notes due 2018	RUB	12.00%	2,298	2,419	117,442
MTS OJSC Notes due 2014	RUB	-	-	-	416,098
Sistema JSFC Bonds due 2014	RUB	-	-	-	296,544
Other			531	628	1,095
Total			\$ 2,403,252	\$ 2,781,512	\$ 4,888,603

All Group RUB-denominated notes and corporate bonds are traded on Moscow Exchange.

USD-denominated notes issued by MTS International due 2020 and 2023 and Sistema International due 2019 are traded on the Irish Stock Exchange. The fair values of notes and corporate bonds are based on the market quotes as of December 31, 2014 at the exchanges which they are traded on.

In certain instances the Group has an unconditional obligation to repurchase notes at par value if

claimed by the noteholders, where a subsequent sequential coupon is announced. The notes therefore can be defined as callable obligations under the FASB authoritative guidance on debt, as the holders have the unilateral right to demand repurchase of the notes at par value upon announcement of new coupons. The FASB authoritative guidance on debt requires callable obligations to be disclosed as maturing in the reporting period when the demand for repurchase could be submitted disregarding the expectations of the Group about the intentions of the noteholders.

The Group discloses such notes in the aggregated maturities schedule in the reporting periods when the noteholders have the unilateral right to demand repurchase. The dates of the announcement for each particular note issue are as follows:

MTS OJSC Notes due 2018	December 2015
MTS OJSC Notes due 2020	November 2015
MTS OJSC Notes due 2023	March 2018

Available credit facilities – As of December 31, 2014, the Group’s total available unused credit facilities amounted to \$1,344.2 million and related to the following credit lines:

	Maturity	Interest rate	Available till	Available amount
Sberbank	2015 – 2018	9.3%-18%	2015 – 2018	766,013
CitiBank Europe	2024	LIBOR 6M+0.9%;	2015	300,009
Gazprombank	2016 – 2021	9.75%-25%	2016 – 2021	198,291
ING BankEurasia	2015	Mosprime/LIBOR/ EURIBOR + 1.50%	2015	44,438
Other				35,468
Total			\$	1,344,219

Covenants – Loans and notes payable by the Group are subject to various restrictive covenants, including, but not limited to compliance with certain financial ratios, limitations on dispositions of assets and transactions within the Group and retention of principal telecom licenses. The adverse court’s ruling in respect of the Bashneft shares owned

by the Group and their further disposition (Note.2) gave certain lenders the right to call the debt under several loan agreements. The lenders waived their rights to demand early repayment with regard to these covenant violations prior to the issuance date of these consolidated financial statements, and the Group retained noncurrent classification for this long-term

debt in its consolidated statement of financial position as of December 31, 2014. As of December 31, 2014, the Group also had \$138.5 million of its RUB-denominated long-term debt which was presented within current liabilities in the consolidated statement of financial position because of non-compliance with certain financial ratios by its subsidiaries.

21. INCOME TAX

The Group’s income tax expense for the years ended December 31, 2014 and 2013 was as follows:

	2014	2013
Current provision	\$ 417,079	\$ 619,643
Deferred income tax expense	36,338	222,464
Total	\$ 453,417	\$ 842,107

Income tax expense calculated by applying the Russian statutory income tax rate of 20% to income from continuing operations before income tax differs from income tax expense recognized in the consolidated statements of operations and comprehensive income as a consequence of the following adjustments:

	2014	2013
	\$ 118,256	\$ 504,164
Adjustments due to:		
Equity in earnings of subsidiaries	147,678	144,647
Other non-deductible expenses	98,094	129,330
Change in valuation allowance	165,819	148,909
Settlements with tax authorities	11,553	(9,108)
Effect of rates different from standard	(43,477)	(44,044)
Currency exchange and translation differences	(5,685)	(10,828)
Non-taxable income	(21,491)	-
Other	(17,330)	(20,963)
Income tax expense	\$ 453,417	\$ 842,107

The tax effects of temporary differences that give rise to the deferred tax assets and liabilities are presented below:

	<u>2014</u>	<u>2013</u>
Deferred tax assets:		
Tax losses carried forward	\$ 1,088,645	\$ 855,851
Accrued expenses and accounts payable	165,569	248,061
Property, plant and equipment	243,112	152,210
Intangible assets	143,917	182,846
Other	111,686	209,147
	1,752,929	1,648,115
Less: valuation allowance	(1,194,858)	(996,221)
Total deferred tax assets	558,071	651,894
Deferred tax liabilities:		
Property, plant and equipment	(348,206)	(534,109)
Intangible assets	(219,907)	(218,014)
Undistributed earnings of subsidiaries and affiliates	(124,444)	(208,995)
Other	(79,655)	(79,751)
	(772,212)	(1,040,869)
Total deferred tax liabilities	\$ (772,212)	\$ (1,040,869)
Net deferred tax assets, current portion	\$ 245,571	\$ 330,388
Net deferred tax assets, long-term portion	392,866	297,419
Net deferred tax liabilities, current portion	(64,947)	(114,192)
Net deferred tax liabilities, long-term portion	(787,631)	(902,591)

The Group has the following balances for income tax losses carried forward as of December 31, 2014 and 2013:

Jurisdiction	Period for carry-forward	<u>2014</u>	<u>2013</u>
India	2015-2020	\$ 521,547	\$ 483,680
Russia	2015-2024	442,370	246,870
Luxembourg	не ограничен	124,728	125,301
Total		\$ 1,088,645	\$ 855,851

Management has established valuation allowances against certain deferred tax assets, which are less likely than not to be realized in future periods. In evaluating the Group's ability to realize its deferred tax assets, the Company considers all available positive and negative evidence, including operating results, ongoing tax planning, and forecasts of future taxable income on a jurisdiction by jurisdiction basis. The valuation allowance as of December 31, 2014 and 2013 relates to the following deferred tax assets:

	<u>2014</u>	<u>2013</u>
Tax losses carried forward	\$ 850,118	\$ 689,731
Sale of investment in Svyazinvest	51,103	65,996
Impairment of long-lived assets in SSTL	128,286	70,194
Other	165,351	170,300
Total	\$ 1,194,858	\$ 996,221

22. HEDGING ACTIVITIES

The Group regularly enters into variable-to-fixed interest rate swap agreements to manage exposure to changes in variable interest rates related to its debt obligations. The instruments qualify for cash flow hedge accounting under U.S. GAAP. Each interest rate swap matches the exact maturity dates of the underlying debt allowing for highly-effective hedges. Interest rate swap contracts outstanding as of December 31, 2014 mature in 2015, 2018 and 2020

In addition to the above, the Group has also entered into several

cross-currency interest rate swap agreements. These contracts hedged the risk of both interest rate and currency fluctuations and assumed periodic exchanges of both principal and interest payments from RUB-denominated amounts to USD- and Euro- denominated amounts to be exchanged at a specified rate. The rate was determined by the market spot rate upon issuance. Cross-currency interest rate swap contracts mature in 2019-2020. The Group entered into cross-currency interest rate swap agreements designated to manage the exposure of changes in

variable interest rate and currency exchange rate for 21.7% of its USD- and Euro- denominated bank loans and Eurobonds outstanding as of December 31, 2014.

The following table presents the fair value of the Group's derivative instruments designated as hedges in the consolidated statements of financial position December 31, 2014 and 2013.

	Location	2014	2013
ASSETS			
Cross-currency interest rate swaps	Other non-current assets	\$ 389,915	\$ 55,760
Interest rate swaps	Other non-current assets	142	367
Total		390,057	56,127
LIABILITIES			
Interest rate swaps	Accrued expenses and other current liabilities	(47,086)	(13,199)
Total		\$ (47,086)	\$ (13,199)

The following table presents the effect of the Group's derivative instruments designated as hedges (i.e. gain/(loss) recognized) in the consolidated statements of operations and comprehensive income for the years ended December 31, 2014 and 2013. The amounts presented include the ineffective portion of derivative instruments and the amounts reclassified into earnings from accumulated other comprehensive income.

	Location	2014	2013
Interest rate swaps, including ineffective portion of 4,503 and (879)	Interest income / (expense)	\$ 6,012	\$ (5,778)
Cross-currency interest rate swaps, including ineffective portion of (60,252) and nil	Foreign currency transaction loss / (gain)	397,901	(24,397)
Total		\$ 403,913	\$ (30,175)

The following table presents the effect of the Group's agreements designated as hedges in accumulated other comprehensive income for the years ended December 31, 2014 and 2013 (net of tax).

	<u>2014</u>	<u>2013</u>
Accumulated gain, beginning of the year	\$ 46,210	\$ 807
Fair value adjustments	376,582	21,697
Reclassified into earnings	<u>(303,683)</u>	<u>23,706</u>
Accumulated gain	\$ <u>119,109</u>	\$ <u>46,210</u>

As of December 31, 2014, the outstanding hedging instruments were highly effective. \$18.0 million of accumulated gain is expected to be reclassified into net income during the next twelve months.

Cash inflows and outflows related to hedging instruments were included in cash flows from operating and financing activities in the consolidated statements of cash flows for the years ended December 31, 2014 and 2013.

23. FAIR VALUE MEASUREMENTS

The following fair value hierarchy table presents information regarding the Group's assets and liabilities measured at fair value on a recurring basis as of December 31, 2014 and 2013:

	Fair value measurements using			Total fair value
	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	
DECEMBER 31, 2014				
Assets at fair value:				
Trading securities	\$ 466,117	\$ -	\$ -	466,117
Available-for-sale securities	158,370	-	3,431	161,801
Derivative instruments	-	390,057	-	390,057
Total assets	624,487	390,057	3,431	1,017,975
Liabilities at fair value:				
Derivative instruments	(12,128)	(59,933)	-	(72,061)
Contingent consideration	-	-	(1,760)	(1,760)
Redeemable noncontrolling interests	-	-	(56,734)	(56,734)
Total liabilities	\$ (12,128)	\$ (59,933)	\$ (58,494)	(130,555)
DECEMBER 31, 2013				
Assets at fair value:				
Trading securities	\$ 1,050,950	\$ -	\$ -	1,050,950
Available-for-sale securities	248,534	253,255	7,405	509,194
Derivative instruments	1,575	56,127	-	57,702
Total assets	1,301,059	309,382	7,405	1,617,846
Liabilities at fair value:				
Derivative instruments	-	(12,863)	-	(12,863)
Contingent consideration	-	-	(336)	(336)
Redeemable noncontrolling interests	-	-	(89,583)	(89,583)
Total liabilities	\$ -	\$ (12,863)	\$ (89,919)	(102,782)

24. SHARE CAPITAL

As of December 31, 2014 and 2013, the Company had 9,650,000,000 voting common shares with a par value of RUB 0.09 issued, of which 9,435,902,596 and 9,274,755,045 shares were outstanding, respectively.

Dividends declared by the Company in the years ended December 31, 2014 and 2013 are as follows:

	2014	2013
Dividends declared (including dividends on treasury shares of \$16,842 and \$8,080 respectively)	591,099	283,200

Accumulated other comprehensive loss – The following table represents components of accumulated other comprehensive loss balance, net of taxes, as of December 31, 2014 and 2013:

	2014	2013
Accumulated currency translation loss	\$ (5,402,999)	\$ (1,516,611)
Unrealized (loss)/gain on available-for-sale securities	(14,499)	37,600
Unrealized gain on derivatives	119,109	46,210
Unrecognized actuarial gain	9,553	9,381
Total accumulated other comprehensive loss	\$ (5,288,836)	\$ (1,423,420)
Less: amounts of accumulated other comprehensive loss attributable to noncontrolling interests	1,545,434	516,702
Total accumulated other comprehensive loss attributable to Sistema JSFC	\$ (3,743,402)	\$ (906,718)

25. SEGMENT INFORMATION

As a diversified holding company, the Company invests in a range of companies which meet its investment and return criteria. The Chief Operating Decision Maker is the Company's Management Board. Information reported to the Company's Management Board for the purpose of resource allocation and the assessment of segment performance is focused on each individual investment holding. The

Group's reportable segments are MTS, SSTL, MTS Bank, RTI and Corporate. The Other category includes other operating segments including Targin, BPGC, LesInvest, Sistema Mass-media, Detsky mir, Intourist, Medsi, Binnopharm, Sitronics-N, Leader-Invest and SG-trans, none of which meets the quantitative thresholds for determining reportable segments.

See Note 1 for a description of the activities of each operating segment of the Group. The accounting policies of the reportable segments are the same as the Group's accounting policies described in appendix A1 to the notes to the financial statements. Segment profit represents the operating income/(loss).

Financial information by reportable segment is presented below:

For the year ended December 31, 2014	MTS	RTI	MTS Bank	SSTL	Corporate	Total reportable segments	Other	Total
Net sales to external customers ^(a)	10,837,126	1,528,287	698,182	220,717	49,967	13,334,279	3,250,678	16,584,957
Intersegment sales	28,521	316,820	17,263	-	25,391	387,995	37,242	425,237
Equity in results of affiliates ^(b)	(37,940)	-	-	-	-	(37,940)	(24,477)	(62,417)
Чистый процентный доход / (расход) ^(b)			(377,575)	-	-	(377,575)		(377,575)
Depreciation and amortization	1,934,339	85,796	17,735	60,374	14,274	2,112,518	179,600	2,292,118
Operating income/(loss)	2,765,484	172,070	(396,963)	(431,828)	(546,842)	1,561,921	286,744	1,848,665
Interest income	120,926	42,160	-	7,477	106,825	277,388	50,609	327,997
Interest expense	435,117	143,175	-	90,277	135,031	803,600	73,809	877,409
Income tax expense/ (benefit)	533,856	33,831	(61,779)	-	(127,264)	378,644	74,773	453,417
Investments in affiliate	152,262	36	-	-	100,448	252,746	95,815	348,561
Segment assets	11,014,182	2,125,279	3,882,609	485,465	1,949,713	19,457,248	3,201,538	22,658,786
Indebtedness ^(d)	5,191,423	841,307	-	568,170	1,223,056	7,823,956	438,807	8,262,763
Capital expenditures ^(e)	2,314,951	105,052	27,592	43,296	28,099	2,518,990	383,592	2,902,582

For the year ended December 31, 2013	MTS	RTI	MTS Bank	SSTL	Corporate	Total reportable segments	Other	Total
Net sales to external customers ^(a)	12,488,877	1,685,546	878,832	209,432	46,237	15,308,924	3,193,061	18,501,985
Intersegment sales	21,884	509,963	24,301	-	36,742	592,890	18,115	611,005
Equity in results of affiliates ^(b)	77,615	(1,696)	-	-	-	75,919	(40,165)	35,754
Net interest revenue/ (expense) ^(c)	-	-	40,678	-	-	40,678	-	40,678
Depreciation and amortization	2,244,014	96,374	19,152	63,666	14,378	2,437,584	195,964	2,633,548
Operating income/(loss)	3,662,740	(776,878)	18,954	(210,185)	834,945	3,529,576	84,721	3,614,297
Interest income	87,704	45,045	-	9,522	116,328	258,599	45,791	304,390
Interest expense	486,636	138,020	-	121,513	159,215	905,384	129,802	1,035,186
Income tax expense/ (benefit)	720,893	(80,025)	(2,645)	-	140,376	778,599	63,508	842,107
Investments in affiliates	153,168	-	-	-	45,210	198,378	166,886	365,264
Segment assets	15,218,084	2,530,299	6,919,610	847,342	3,572,805	29,088,140	3,250,757	32,338,897
Indebtedness ^(d)	6,682,047	1,228,635	-	596,641	1,574,531	10,081,854	437,054	10,518,908
Capital expenditures ^(e)	2,561,310	95,009	21,379	45,765	73,224	2,796,687	197,706	2,994,393

^(a) Interest income and expense of MTS Bank are presented as revenues from financial services and cost of financial services, correspondingly, in the Group's consolidated financial statements.

^(b) Equity in results of affiliates of MTS segment for the year, 2014 includes \$135 million of its share of the earnings of MTS Bank and Stream, which is further eliminated on consolidation (2013: \$5 million).

^(c) Represents the net interest result of the Group's banking activities. In reviewing the performance of MTS Bank, the chief operating decision maker reviews the net interest result, rather than the gross interest amounts.

^(d) Represents the sum of short-term and long-term debt.

^(e) Represents purchases of property, plant and equipment and intangible assets.

The following table summarizes dividends to Corporate, declared in 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Bashneft	\$ 818,456	\$ 1,162,041
MTS	744,460	635,369
Other	89,903	49,084

The reconciliation of segment operating income to the consolidated income from continuing operations before income tax expense and a reconciliation of segment assets to the consolidated assets are as follows:

	<u>2014</u>	<u>2013</u>
Operating income – reportable segments	\$ 1,561,921	\$ 3,529,576
Operating income – other	286,744	84,721
	<u>1,848,665</u>	<u>3,614,297</u>
Intersegment eliminations	(110,216)	(47,725)
Operating income	\$ 1,738,449	\$ 3,566,572
Interest income	212,774	182,447
Change in fair value of derivative financial instruments	-	30,199
Interest expense	(811,346)	(960,136)
Foreign currency transaction loss	(548,596)	(298,264)
Income from continuing operations before income tax	\$ 591,281	\$ 2,520,818

	<u>2014</u>	<u>2013</u>
Total assets – reportable segments	\$ 19,457,248	\$ 29,088,140
Total assets – Bashneft	-	12,674,507
Total assets – other	3,201,538	3,250,757
	<u>22,658,786</u>	<u>45,013,404</u>
Intersegment eliminations	(1,988,309)	(1,764,410)
Total assets	\$ 20,670,477	\$ 43,248,994

For the years ended December 31, 2014 and 2013, the Group did not have revenues from transactions with a single external customer amounting to 10% or more of the Group's consolidated revenues. For the years ended December 31, 2014 and 2013 the Group's revenues outside of the RF were as follows:

	<u>2014</u>	<u>2013</u>
Ukraine	\$ 818,456	\$ 1,162,041
India	272,863	253,196
Armenia	186,120	156,883
Central and Eastern Europe	107,372	40,997
Other	154,753	210,661
Total	\$ 1,534,816	\$ 1,944,147

As of December 31, 2014 and 2013, the Group's long-lived assets located outside of the RF were as follows:

	2014	2013
Ukraine	\$ 332,987	\$ 755,373
India	320,604	710,225
Armenia	288,308	354,840
Central and Eastern Europe	68,369	34,953
Other	87,870	111,887
Total	\$ 1,098,138	\$ 1,967,278

26. RELATED PARTY TRANSACTIONS

The Group sells goods and provides services to and purchases goods and services from its related parties on normal commercial terms. During the years ended December 31, 2014 and 2013, the Group entered into transactions with related parties as follows:

	2014	2013
Sales	\$ 17,220	\$ 14,921
Revenue from banking activities	34	51
Cost related to banking activities	(48,385)	(30,370)
Cost of sales	(45,595)	(1,188)
Selling, general and administrative expenses	(515)	(12,110)

As of December 31, 2014 and 2013, the related party balances were as follows:

	2014	2013
Assets:		
Short-term investments	\$ 5,212	\$ 9,840
Accounts receivable, net	5,469	1,362
Other current assets	27,083	4,907
Long-term investments	36,174	17,402
Liabilities:		
Accounts payable	(4,134)	(890)
Liabilities from banking activities	(541,556)	(526,056)
Accrued expenses and other current liabilities	(3,411)	(646)
Long-term debt	\$ (37)	\$ (64)

27. SHARE-BASED COMPENSATION

The Company and several of its subsidiaries operate share-based compensation plans in order to compensate their employees. This is done through either “equity” plans, in which employees may exercise their options for shares, or “phantom” plans, which generally allow employees to receive cash compensation which varies depending on the share price that the options are linked to.

All such plans, including those of MTS, are immaterial to the Group and consequently have not been

disclosed here. A discussion has been included below of the plans operated at the Company level.

Sistema JSFC share-based long-term motivation program – In 2014 and 2013 the Company’s Board of Directors established two-year motivational programs for senior and mid-level management. Participants of the programs upon fulfillment of certain performance conditions and subject to continuing employment with the Group will be granted ordinary shares in the Company. As a result, the Group recognized an

expense of \$79.4 million and \$54.2 million in the consolidated statement of operations and comprehensive income for the years ended December 31, 2014 and 2013, respectively. The fair value of awards granted was measured based on the fair value of the Company’s ordinary shares.

28. ASSET RETIREMENT OBLIGATIONS

As of December 31, 2014 and 2013, the estimated present value of the Group’s asset retirement obligations and change in liabilities were as follows:

	2014	2013
Balance, beginning of the year	\$ 83,809	\$ 90,986
Liabilities incurred in the current period	1,900	9,257
Property dispositions	(1,067)	-
Accretion expense	6,559	2,963
Revisions in estimated cash flows	677	(13,840)
Currency translation adjustment	(38,163)	(5,557)
Balance, end of the year	\$ 53,715	\$ 83,809
Current portion	-	-
Long-term portion	53,715	83,809
Balance, end of the year	\$ 53,715	\$ 83,809

The Group’s asset retirement obligations relate primarily to the cost of removing telecommunication equipment from sites. Revisions in estimated cash flows are attributable to changes in economic assumptions, such as inflation rates.

The Group recorded the long-term portion of asset retirement obligations as a separate line item in the consolidated statements of financial position, the current portion – as a component of accrued expenses and other current liabilities.

29. REDEEMABLE NONCONTROLLING INTERESTS

Redeemable noncontrolling interests as of December 31, 2014 and 2013 consisted of the following:

	2014	2013
SSTL	\$ 720,000	\$ 688,000
K-Telecom, MTS subsidiary in Armenia	56,734	89,583
RTI (Note 5)	16,032	27,547
Total	\$ 792,766	\$ 805,130

The Group is a party to a put option agreement to acquire the RF's 17.14% interest in SSTL during one year beginning March 2016 at the higher of

\$777 million or its market value at that date determined by an independent appraiser. The Group accounted for the redeemable noncontrolling

interests in SSTL at the redemption value and presented this as temporary equity in its consolidated statements of financial position.

30. COMMITMENTS AND CONTINGENCIES

Operating leases – The Group leases land, buildings and office space mainly from municipal organizations through contracts which expire in various years through 2068.

Rental expense under operating leases amounting to \$641.0 million and \$678.5 million for the years

ended December 31, 2014 and 2013, respectively, is included in selling, general and administrative expenses. Rental expense under operating leases amounting to \$204.6 million and \$238.1 million for the years ended December 31, 2014 and 2013 respectively, is included in cost of sales.

Future minimum rental payments under operating leases in effect as of December 31, 2014, are as follows:

Year ended December 31		
2015	\$	282,393
2016		204,009
2017		202,489
2018		204,662
2019		199,758
Thereafter		303,487
Total	\$	1,396,798

Capital commitments – As of December 31, 2014, the Group had executed purchase agreements of approximately \$840.0 million to acquire property, plant and equipment and intangible assets.

Guarantees – As of December 31, 2014, MTS Bank and its subsidiaries guaranteed loans for several companies, including related parties, which totaled \$217.2 million. These guarantees would require payment by the Group only in the event of default on payment by the respective debtor.

As of December 31, 2014, no event of default has occurred under any of the guarantees issued by the Group.

Commitments on loans and unused credit lines – As of December 31, 2014, MTS Bank and its subsidiaries had \$126.9 million of commitments on loans and unused credit lines available to its customers.

Taxation – Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include VAT, corporate income tax, a number of turnover-based taxes, and payroll (social) taxes. Laws related to these taxes have not been in force for significant periods, in contrast to more developed market economies; therefore, the government's implementation of these regulations is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established. Tax declarations, together with other legal compliance areas (for example, customs and currency control matters), are subject to review and investigation by a number of authorities, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia that are more significant than those typically found in countries with more developed tax systems.

Generally, according to Russian tax legislation, tax declarations remain open and subject to inspection for a period of three years following the tax year. As of December 31,

2014, tax declarations of certain companies of the Group in Russia for the preceding three fiscal years were open for further review.

The Group purchases supplemental software from foreign suppliers of telecommunications equipment in the ordinary course of business. The Group's management believes that customs duties are calculated in compliance with applicable legislation. However there is a risk that the customs authorities may take a different view and impose additional customs duties.

Pricing of revenue and expenses between each of the Group's subsidiaries and various discounts and bonuses to the Group's subscribers in the course of performing its marketing activities may be subject to transfer pricing rules. The Group's management believes that taxes payable are calculated in compliance with the applicable tax regulations relating to transfer pricing. However there is a risk that the tax authorities may take a different view and impose additional tax liabilities. As of December 31, 2014 and 2013, no provision was recorded in the consolidated financial statements in respect of such additional claims.

In November 2014, the Russian legislation was amended to introduce the concept of "controlled foreign companies" and the new tax regime for such entities. It is expected that the adoption of the new rules will generally lead to an increase in the administrative and, in certain cases, tax burden for the Russian entities that have subsidiary structures incorporated outside the Russian Federation. The management does not believe the law can materially impact the Group's tax obligations as of December 31, 2014.

Management believes that it has adequately provided for tax and customs liabilities in the accompanying consolidated financial statements. As of December 31, 2014 and 2013, the provision accrued amounted to \$53.3 million and \$69.6 million, respectively. In addition, the

accrual for unrecognized income tax benefits, potential penalties and interest recorded in accordance with the authoritative guidance on income taxes totaled \$6.1 million and \$18.8 million as of December 31, 2014 and 2013, respectively. However, the risk remains that the relevant authorities could take differing positions with regard to interpretive issues and the effect could be significant.

With regard to matters where practice concerning payment of taxes is unclear, management estimated possible tax exposure to be \$21 million and \$nil as of December 31, 2014 and 2013, respectively.

Operating environment – Starting from March 2014, sanctions have been imposed in several tranches by the U.S. and the E.U. on certain Russian officials, businessmen and companies. Following the decline in oil prices in 2014 and early 2015, Russia, which is the main market of the Group's operations, has experienced significant economic instability, characterized by the substantial depreciation of the Russian rouble, growth of interest rates caused by the decision of the Central Bank of the Russian Federation to significantly increase its key interest rate, a forecasted decline in gross domestic product and a significant decline in the value of shares traded on the Russian stock exchanges. International credit agencies downgraded Russia's long-term foreign currency sovereign rating with a negative outlook. Neither the Company, nor any of its subsidiaries are subject to the current sanctions, and the Group does not appear on the U.S. or E.U. lists of sanctioned parties. However, there is significant uncertainty regarding the extent or timing of any potential further economic or trade sanctions. Any continuing economic and political instability could have a negative impact on the Group's operating results.

Although the Group's reporting currency is the U.S. dollar, it generates most of its revenues in Russian roubles, which is also the functional currency of its principal

operating subsidiaries. Therefore, the Group's reported results of operations are significantly impacted by the fluctuations in the exchange rate between the U.S. dollar and the Russian rouble, which depreciated against the U.S. dollar by 42% in 2014, and was on average 17% lower than the average value of the Russian rouble compared to the U.S. dollar during 2013. Also, given that most of the Group's revenues are generated in Russian roubles, the Group faces exchange rate risk relating to payments that the Group must make in currencies other than the Russian rouble.

During 2014, a deterioration in the political environment in Ukraine, the second largest market of the Group's operations, has led to general instability, economic deterioration and armed conflict in the eastern portion of Ukraine. The deterioration has further exacerbated the country's already weak macroeconomic trends, which have led to reduced credit ratings, significant depreciation of its national currency and increased inflation. In 2014, the Ukrainian Parliament adopted a law allowing for the imposition of sanctions against countries, persons and companies deemed by the Ukrainian government to threaten Ukrainian national interests, national security, sovereignty or the territorial integrity of Ukraine. The National Bank of Ukraine passed a decree prohibiting Ukrainian companies from paying dividends to foreign investors. These circumstances, combined with continued political and economic instability in Ukraine, could result in a negative impact on our business, including the Group's financial position and results of operations. For example, such risks apply to the Group's funds deposited in Ukrainian banks, the liquidity of which is negatively affected by the economic downturn. As of December 31, 2014, the Group held \$376.9 million in current accounts and deposits in Ukrainian banks, including \$90.2 million in Delta Bank (Note 15) (fully provided as of December 31, 2014) and \$25.1 million in Kyivska Rus Bank (Note 31).

LTE license – In July 2012, the Federal Service for Supervision in the Area of Communications, Information Technologies and Mass Media allocated MTS the necessary license and frequencies to provide LTE telecommunication services in Russia. Under the terms and conditions of the LTE license, the Group is obligated to fully deploy LTE networks within seven years, commencing from January 1, 2013 and deliver LTE services in each population center with over 50,000 inhabitants in Russia by 2019. Also, the Group is obligated to invest at least 15 billion rubles (\$266.6 million using December 31, 2014 exchange rate) annually toward the LTE roll-out until the network is fully deployed. Management believes that as of December 31, 2014 the Group is in compliance with these conditions.

Bitel – In June 2013, an agreement was reached between Altimo, Altimo Holdings, MTS and its subsidiary MTS Finance, Nomihold and other associated parties to settle all disputes that have arisen from the Group's investment in Bitel made in 2005. The agreement covered matters involving a number of parties and legal proceedings, including those in the Isle of Man, London, Luxembourg and other jurisdictions. Pursuant to the agreement, all proceedings between the parties and their associated parties were discontinued and waived, and MTS received a total payment of \$150 million. All parties made the necessary submissions to the respective courts and tribunals to document the settlement, which, among other actions, fully discharged any and all outstanding obligations under the award previously rendered by the London Court of International Arbitration (LCIA) against MTS Finance in 2011, as well as settled the tripartite LCIA arbitration between MTS, MTS Finance and Nomihold and a tort action filed by Nomihold against MTS in the English Courts.

Upon concluding the settlement agreement, the Group released a provision of \$221 million, comprising \$170 million set by the LCIA plus

\$51 million in damages, interest and other costs, that had been previously provided for in relation to the dispute with Nomihold. The Group also recognized a gain of \$150 million with respect to the settlement payment in the consolidated statement of operations and comprehensive income for the year ended December 31, 2013.

Restriction on transactions with the shares of BPGC and Ufaorgsintez

In 2014, in the course of a litigation, which the Group is not a party to, the court imposed restrictions on transactions with the shares of BPGC and Ufaorgsintez, owned by the Group. The restrictions do not limit the Group's voting rights, rights to receive dividends or any other shareholders rights.

Investigations into former operations in Uzbekistan – In March 2014, the Group received requests for the provision of information from the United States Securities and Exchange Commission and the United States Department of Justice relating to an investigation of the Group's former subsidiary in Uzbekistan. The Group cannot predict the outcome of the investigations, including any fines or penalties that may be imposed, and such fines or penalties could be significant.

Other – In the ordinary course of business, the Group is a party to various legal proceedings, and subject to claims, certain of which relate to the developing markets and evolving fiscal and regulatory environments in which the Group operates. In the opinion of management, the Group's liability, if any, in all pending litigation, other legal proceedings or other matters will not have a material effect upon the financial condition, results of operations or liquidity of the Group. Management estimates the range of reasonably possible losses, if any, in all pending litigations or other legal proceedings being up to \$28.0 million.

31. SUBSEQUENT EVENTS

For the purpose of the accompanying consolidated financial statements, subsequent events have been evaluated through April 2, 2015.

Acquisition of 3G license in

Ukraine – In February 2015, MTS-Ukraine won a tender to acquire a nationwide license for the provision of 3G telecommunications services. The license with the cost of UAH 2,715 million (\$156.9 million at the acquisition date) has been granted for 15 years. In accordance with the

terms of the license MTS-Ukraine is required to launch provision of 3G services in all of the regional centers across Ukraine within 18 months upon allocation of the license.

Bond placement – In February 2015, the Company completed the placement of Series BO-01 unconvertible interest-bearing RUB-denominated bonds for the total amount of RUB 10 billion (\$160.3 million at the date of the placement) at the coupon rate of 17% per annum.

Insolvency of Kyivska Rus Bank –

In March 2015, the National Bank of Ukraine adopted a resolution declaring Kyivska Rus Bank (Ukraine) to be insolvent. As of December 31, 2014, the Group held \$25.1 million in deposits in the bank. Management determined that insolvency of the bank did not provide evidence related to conditions existing as of December 31, 2014, and therefore considered to be a nonrecognized subsequent event.

A1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation –

The consolidated financial statements include the accounts of the Company, as well as entities where the Company has operating and financial control, most often through the direct or indirect ownership of a majority voting interest. Those ventures where the Group exercises significant influence but does not have operating and financial control are accounted for using the equity method. Investments in which the Group does not have the ability to exercise significant influence over operating and financial policies are accounted for under the cost method and included in long-term investments in the consolidated statements of financial position. The consolidated financial statements also include accounts of variable interest entities (“VIEs”) in which the Group is deemed to be the primary beneficiary. An entity is generally a VIE if it meets any of the following criteria: (i) the entity has insufficient equity to finance its activities without additional subordinated financial support from other parties, (ii) the equity investors cannot make significant decisions about the entity’s operations or (iii) the voting rights of some investors are not proportional to their obligations to absorb the expected losses of the entity or receive the expected returns of the entity and substantially all of the entity’s activities involve or are conducted on behalf of the investor with disproportionately few voting rights.

All significant intercompany transactions, balances and unrealized gains and losses on transactions have been eliminated.

Use of estimates – The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses of the reporting period. Actual results could differ from those estimates.

Significant estimates for the Group include the allowances for doubtful accounts, customer loans and deferred tax assets, the valuation of goodwill and other long-lived assets, asset retirement obligations, unrecognized income tax benefits, redeemable noncontrolling interests, derivative instruments, share-based compensation, assets acquired and liabilities assumed in business combinations, the recoverability of investments, and the estimates of oil and gas reserves.

Concentration of business risk –

The Group’s principal business activities are in the RF, Ukraine and India. Laws and regulations affecting businesses operating in these countries are subject to rapid changes, which could impact the Group’s assets and

operations.

Foreign currency – Management has determined that the functional currencies of most of the Group’s operating subsidiaries are the currencies of the countries of their domicile.

In preparing the financial statements of the entities within the Group, transactions in currencies other than the entities’ functional currency are recognized at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing at that date. Non-monetary items carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not restated.

The Group has selected USD as its reporting currency. The Group’s assets and liabilities are translated into USD at exchange rates prevailing on the reporting period end date. Revenues, expenses, gains and losses are translated into USD at average exchange rates prevailing during the reporting period. Equity is translated at the applicable historical rates. The

resulting translation gain or loss is recorded as a separate component of other comprehensive income.

On the disposal of a subsidiary whose financial statements are prepared in a currency other than the reporting currency of the Group, all of the accumulated currency translation adjustments in respect of that operation attributable to the Group are reclassified to profit or loss.

As of December 31, 2014, the official exchange rate of the Russian Ruble, the functional currency of most of the Group's subsidiaries, determined by the Central Bank of the RF was RUB 56.26 for 1 USD (RUB 32.73 for 1 USD as of December 31, 2013).

Revenue recognition – Generally, revenues are recognized when all of the following conditions have been met: (i) there is persuasive evidence of an arrangement; (ii) delivery has occurred; (iii) the fee is fixed and determinable; and (iv) collectability of the fee is reasonably assured. Revenue amounts are presented net of value-added taxes.

Revenues under arrangements specific to the respective reportable segments of the Group are recognized as follows:

MTS

Revenues derived from wireless, local telephone, long distance, data and video services are recognized when services are provided. This is based upon either usage (minutes of traffic processed, volume of data transmitted) or period of time (monthly subscription fees).

Content revenue is presented net of related costs when MTS acts as an agent of the content providers while the gross revenue and related costs are recorded when MTS is a primary obligor in the arrangement.

Upfront fees received for connection

of new subscribers, installation and activation of wireless, wireline and data transmission services ("connection fees") are deferred and recognized over the estimated average subscriber life, as follows:

Mobile subscribers	1 - 12.5 years†
Residential wireline voice phone subscribers	15 years
Residential subscribers of broadband internet service	1 year
Other fixed line subscribers	3-5 years†

MTS calculates an average life of mobile subscribers for each region in which it operates and amortizes connection fees based on the average life specific to that region.

Incentives provided to customers are usually offered on signing a new contract or as part of a promotional offering. Incentives representing the reduction of the selling price of the service (free minutes and discounts) are recorded in the period to which they relate, when the respective revenue is recognized, as a reduction to both accounts receivable and revenue. However, if the sales incentive is a free product or service delivered at the time of sale, the cost of the free product or service is classified as an expense. In particular, the Group sells handsets at prices below cost to contract subscribers. Such subsidies are recognized in the cost of sales.

RTI

Revenues from the long-term contracts are recognized using the percentage-of-completion method of accounting, measured by the percent of contract costs incurred to-date to estimated total contract costs. The completed-contract method is used for a single contract or a group of contracts for which reasonably dependable estimates cannot be made or for which inherent hazards make estimates doubtful. Provisions for estimated losses on construction contracts in progress are made in their entirety in the period in which such losses are determined.

A total expected loss on a contract is recognized immediately in profit or loss.

Contract expenses are recognized as incurred unless they create an asset related to future contract activity.

The sales of software products and system integration services are generally multiple-element arrangements, involving the provision of related services, including customization, implementation and integration services, as well as ongoing support and maintenance provided to customers.

A multiple-element arrangement is separated into more than one unit of accounting if all of the following criteria are met: (a) the delivered items have value to the customer on a standalone basis; and (b) the arrangement includes a general right of return relative to the delivered items, delivery or performance of the undelivered items is considered probable and substantially in the control of the Group.

If evidence of the fair value of the undelivered elements of the arrangement does not exist,

all revenue from the arrangement is deferred until such time that evidence of fair value does exist, or until all elements of the arrangement are delivered. Fees allocated to post-contract support are recognized as revenue on a pro rata basis over the support period. Fees allocated to other services are recognized as revenue as services are performed.

In cases where extended payment terms exist, license and related customization fees are recognized when payments are due, unless a history of collection, without providing concessions, has been established under comparable arrangements.

When sale agreements provide price protection to the dealer, the revenue is deferred until the dealer sells the merchandise to a third party due

to the frequent sales price reductions and rapid technology obsolescence.

Where certain products of this segment are sold with a product return right, a reserve is established. In addition other post-contract support obligations are accrued at the time of sale.

MTS Bank

Revenues from interest bearing assets are recognized on an accrual basis using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Regulated services – Regulated tariff services provided by the Group primarily consist of local fixed-line telephone services and services rendered to other operators, such as traffic charges, connection fees and line rental services, provided by MTS in certain regions of RF, and energy transmission services provided by BPGC. Changes in the rate structure for such services are subject to the Federal Tariff Service approval. Revenues from regulated tariff services represented approximately 5.5% and 6.0% of the consolidated revenues for the years ended December 31, 2014 and 2013, respectively.

Cash and cash equivalents – Cash equivalents include demand deposits and other highly liquid investments with an original maturity of three months or less. Within the cash and cash equivalents balance are cash

equivalents of \$777.2 million and \$1,211.8 million as of December 31, 2014 and 2013, respectively, which primarily comprise term deposits with banks and bank promissory notes with original maturities of three months or less.

Restricted cash – Restricted cash includes cash and cash equivalents restricted by agreements with third parties for special purposes.

Financial instruments – The Group's financial instruments include cash and cash equivalents, short-term investments, accounts receivable, derivative financial instruments, financial assets and liabilities from banking activities, accounts payable and short-term and long-term debt.

Hedging activities – The Group uses derivative instruments, including swap, forward and option contracts to manage foreign currency and interest rate risk exposures.

The Group designates derivatives as either fair value hedges or cash flow hedges in case the required criteria are met. Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the consolidated statement of operations and comprehensive income together with any changes in the fair value of the hedged asset or liability that is attributed to the hedged risk.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognized in accumulated other comprehensive loss. Gains and losses associated with the related hedged items are recognized in the consolidated statements of operations and comprehensive income, depending on their nature. The gain or loss relating to the ineffective portion is recognized immediately in the consolidated statement of operations and comprehensive income. For derivatives that do not meet the conditions for hedge accounting, gains and losses from changes in the fair value are included in the consolidated statement of operations and comprehensive income (Note 22).

Assets and liabilities related to multiple derivative contracts with one counterparty are not offset by the Group.

The Group does not use financial instruments for trading or speculative purposes.

Fair value of financial instruments – The fair value of certain financial instruments approximates their carrying value due to the short-term nature of these amounts, namely cash and cash equivalents, short-term investments, accounts receivable and accounts payable, short-term debt and assets and liabilities from banking activities which are included in current assets and liabilities.

Fair value measurements – The Group reviews its fair value hierarchy classifications quarterly. Changes in significant observable valuation inputs identified during these reviews may trigger reclassification of fair value hierarchy levels of financial assets and liabilities. During the years ended December 31, 2014 and 2013 no reclassifications occurred.

A three-level valuation hierarchy has been established under U.S. GAAP for disclosure of fair value measurements. The valuation hierarchy is based on the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 – inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets;
- Level 2 – inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument;
- Level 3 – one or more inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Accounts receivable – Accounts receivable are stated at their net realizable value after deducting a provision for doubtful accounts. Such provision reflects either specific cases of delinquencies or defaults or estimates based on evidence of collectability.

Assets from banking activities – Assets from banking activities comprise assets (cash and cash equivalents, loans, investments and other) involved in operations of MTS Bank. Impairment losses on loans to customers and banks are included in the allowance for loan losses. The allowance for loan losses represents management's best estimate of probable credit losses inherent in the lending portfolios as of the reporting period end. Loans that are not individually reviewed are evaluated as a group using reserve factor percentages based on historic loss experience and qualitative factors. Loans deemed to be uncollectible are charged against the allowance for loan losses. Correspondingly, recoveries of amounts previously charged as uncollectible are credited to the allowance for loan losses. A provision for loan losses is charged to the consolidated statement of operations and comprehensive income based on management's evaluation of the estimated losses, after giving consideration to the net chargeoffs which have been incurred in the Group's loan portfolio.

The Group performs detailed reviews of its lending portfolios on a periodic and systematic basis to identify inherent risks and to assess the overall collectability of those portfolios. The allowance on certain homogeneous loan portfolios, which generally consist of consumer and mortgage loans, is based on an evaluation of aggregated portfolios of homogeneous loans, generally by loan type.

Depreciation for property, plant and equipment is computed under the straight-line method utilizing estimated useful lives of the assets as follows:

Buildings	20-50 years
Leasehold improvements	Lesser of the estimated useful life or the term of the lease
Switches and transmission devices	7-31 years
Network and base station equipment	4-12 years
Power and utilities	3-47 years
Other plant, machinery and equipment	3-25 years

Loss forecast models are utilized for portfolios of homogeneous loans which consider a variety of factors including, but not limited to, historical loss experience, anticipated defaults or foreclosures based on portfolio trends, delinquencies and credit scores, and estimated loss factors by loan type. The remaining loan portfolios are reviewed on an individual loan basis.

Loans subject to individual reviews are analyzed and segregated by risk according to the Group's internal risk rating scale. These risk classifications, in conjunction with an analysis of historical loss experience, current economic conditions and performance trends within specific portfolio segments, and any other pertinent information result in the estimation allowances for loan losses. An allowance for loan losses is established for individually impaired loans. A loan is considered impaired when, based on current information and events, it is probable that the Group will be unable to collect all amounts due, including principal and interest, according to the contractual terms of the agreement. Individually impaired loans are measured based on the present value of payments expected to be received, or for loans that are solely dependent on the collateral for repayment, the estimated fair value of the collateral. If the recorded investment in impaired loans exceeds the measure of estimated fair value, an allowance is established as a component of the allowance for loan losses.

Inventories and spare parts – Inventories comprise raw materials, work-in-progress, finished goods and goods for resale. Inventory and spare parts are stated at the lower of cost or market value. Inventory is accounted for using either first-in, first-out or the weighted-average cost method.

The cost of raw materials includes the cost of purchase, customs duties, transportation and handling costs. Work-in-progress and finished goods are stated at production cost which includes direct production expenses and manufacturing overheads. Costs and estimated earnings in excess of billings on uncompleted contracts include the accumulated costs of projects contracted with third parties, net of related progress billings. The Group periodically assesses its inventories and spare parts for obsolete or slow-moving stock.

Value-added taxes – Value-added taxes ("VAT") related to sales are payable to the tax authorities on an accrual basis based on invoices issued to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales. VAT related to purchase transactions that will be reclaimed against future sales are recorded as VAT receivable in the accompanying financial statements.

Property, plant and equipment – Property, plant and equipment are stated at historical cost. Cost includes major expenditures for improvements and replacements, which extend useful lives of the assets or increase their revenue generating capacity. Repairs and maintenance, including preventative maintenance, are charged to the consolidated statement of operations and comprehensive income as incurred.

The cost of major overhauls and replacements, which extend useful lives of the assets or increase their revenue generating capacity, are capitalized to the cost of the assets.

Whilst there are certain assets within the Group that have useful lives longer than those presented above, these assets are quantitatively insignificant in comparison to the overall Group balance for each category. As such, the Group has taken the approach of reporting the useful economic lives which most faithfully represent the majority of assets, in order to provide a more reasonable range that more closely relates to the Group norm. Assets held under capital leases are initially recognized as assets of the Group at their fair value at the inception of a lease or, if lower, at the present value of minimum lease payments. The discount rate used in determining the present value of the minimum lease payments is the Group's incremental borrowing rate, unless (1) it is practicable to determine the implicit rate computed by the lessor; and (2) the implicit rate is less than the Group's incremental borrowing rate. If both of those conditions are met, the interest rate implicit in the lease is used.

Items of property, plant and equipment that are retired or otherwise disposed of are eliminated from the consolidated statement of financial position along with the corresponding accumulated depreciation. Any gain or loss resulting from such retirement or disposal is included in the determination of net income.

Construction in progress and equipment for installation are not depreciated until an asset is placed into service.

Asset retirement obligations –

The Group calculates asset retirement obligations and an associated asset retirement cost when the Group has a legal or constructive obligation in connection with the retirement of tangible long-lived assets.

Business combinations – Acquisitions of businesses from third parties are accounted for using the acquisition method, with assets and liabilities of an acquired entities being measured at their fair values as at the date of acquisition. Noncontrolling interests are measured at fair value.

Goodwill – Goodwill is determined as the excess of the consideration transferred plus the fair value of any noncontrolling interests in the acquiree at the acquisition date over the fair values of the identifiable net assets acquired. The excess of the fair values of the identifiable net assets acquired over the cost of the business combination plus the fair value of any noncontrolling interests in the acquiree at the acquisition date is credited to income ("negative goodwill").

Goodwill is not amortized to operations, but instead is reviewed for impairment at least annually.

At first step, the Group assesses qualitative factors to determine whether it is more likely than not that goodwill is impaired as a basis for determining whether it is necessary to perform the quantitative impairment test. Goodwill is then reviewed for impairment by comparing the carrying value of each reporting unit's net assets (including allocated goodwill) to the fair value of the reporting unit. If the reporting unit's carrying amount is greater than its fair value, the next step is performed whereby the implied fair value that relates to the reporting unit's goodwill is compared to the carrying value of the reporting unit's goodwill. The Group recognizes a goodwill impairment charge for the amount by which the carrying value of goodwill exceeds the fair value.

Other intangible assets – Other intangible assets include billing and telecommunication software and other software, operating licenses, acquired customer bases and customer relationships, radio frequencies, trademarks and telephone numbering capacity.

All finite-life intangible assets are amortized using the straight-line method utilizing estimated useful lives of the assets as follows:

Billing and telecommunication software	1-20 years
Operating licenses	3-20 years
Acquired customer base	1-8 years
Acquired radio frequencies	2-15 years
Software and other	1-10 years

Trademarks and numbering capacity with indefinite contractual life are not amortized, but are reviewed, at least annually, for impairment.

If the fair value of the intangible asset is less than its carrying value, an impairment loss is recognized in an amount equal to the difference. The Group also evaluates the remaining useful life of its intangible assets that are not subject to amortization on an annual basis to determine whether events and circumstances continue to support an indefinite useful life. If an intangible asset that is not being amortized is subsequently determined to have a finite useful life, that asset is tested for impairment.

Investments – The Group's share in the net assets and net income of certain entities, where the Group has the ability to exercise significant influence over their operating and financial policies ("affiliates") is included in the consolidated financial statements using the equity method of accounting. The Group's share in the net income of affiliates is included within operating income, given that the Group has day-to-day involvement in the business activities and they are considered to be integral to the Group's business. Other-than-temporary decreases in the value of investments in affiliates are recognized in net income.

All other equity investments, which consist of investments for which the Group does not have the ability to exercise significant influence, are accounted for under the cost method or at fair value. Investments in private companies are carried at cost, less provisions for other-than-temporary impairment in value. For public companies that have readily determinable fair values, the Group classifies its equity investments as available-for-sale or trading. For available-for-sale securities, the Group records these investments at their fair values with unrealized holding gains and losses included in the consolidated statement of operations and comprehensive income/(loss), net of any related tax effect. For trading securities, the Group records the investment at fair value. Unrealized holding gains

and losses for trading securities are included in earnings.

The Group purchases promissory notes for investing purposes. These notes are carried at cost and the discount against the nominal value is accrued over the period to maturity. A provision is made, based on management assessment, for notes that are considered uncollectible. The notes are classified as held-to-maturity.

Investments which are expected to be realized within twelve months after the statement of financial position date are classified as short-term investments. Other investments are classified as long-term investments.

Debt issuance costs – Debt issuance costs are recorded as an asset and amortized using the effective interest method over the terms of the related loans.

Impairment of long-lived assets other than goodwill and indefinite lived intangible assets – The Group periodically evaluates the recoverability of the carrying amount of its long-lived assets. Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, the Group compares the undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, the Group records impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets (Note 15).

Liabilities from banking activities –

Liabilities from banking activities include deposits from banks and customers, promissory notes issued and other liabilities that arise out of operations of MTS Bank.

Property, plant and equipment

contributions – Telecommunication equipment and transmission devices, installed at newly constructed properties in Moscow, have been historically transferred to OJSC Moscow City Telephone Network (hereinafter,

“MGTS”), a fixed line operator and subsidiary of the Group, by the Moscow City Government free of charge. These assets are capitalized by the Group at their market value at the date of transfer. Simultaneously, deferred revenue is recorded in the same amount and is amortized as a reduction of the depreciation charge in the consolidated statement of operations and comprehensive income over the contributed assets’ life.

Income taxes – Income taxes of the Group’s Russian entities have been computed in accordance with RF laws. The corporate income tax rate in the RF is 20%. The income tax rate on dividends paid within Russia is 9% or 0% subject to meeting certain conditions. The foreign subsidiaries of the Group are paying income taxes in their respective jurisdictions.

Deferred tax assets and liabilities are recognized for differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the tax bases of assets and liabilities that will result in future taxable or deductible amounts. The deferred tax assets and liabilities are measured using the enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. In making such determination, the Group considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies and recent financial operations.

Uncertain tax positions are recognized in the consolidated financial statements for positions which are not considered more likely than not of being sustained based on the technical merits upon examination by the tax authorities. The measurement of the tax benefit recognized in the consolidated financial statements is based upon the largest amount of tax benefit that, in management’s judgment, is greater than

50% likely of being realized based on a cumulative probability assessment of the possible outcomes.

The Group recognizes interest and penalties relating to unrecognized tax benefits within income taxes.

Treasury stock – If the Group reacquires the Company’s own equity instruments, those instruments

(“treasury shares”) are recognized as a deduction of equity at cost, being the consideration paid to reacquire the shares. No gain or loss is recognized in profit or loss on the purchase, sale, issue or cancellation of the Company’s own equity instruments. Such treasury shares may be acquired and held by the Company or by other subsidiaries of the Group.

Share-based compensation – The Group calculates and records the fair value of equity instruments, such as stock options or restricted stock, awarded to employees for services received and recognizes such amounts in the consolidated statement of operations and comprehensive income. The fair value of the equity instruments is measured on the date they are granted and is recognized over the period during which the employees are required to provide services in exchange for the equity instruments (Note 27). Share-based compensation expense includes the estimated effects of forfeitures. Such estimates are adjusted over the requisite service period to the extent actual forfeitures differ, or are expected to differ from such estimates. Changes in estimated forfeitures are recognized in the period of change and also impact the amount of expense to be recognized in future periods.

For share-based compensation that include a component that will be settled in cash, and a component that is settled in equity, the Group accounts for the awards separately, based on their substance. For the component that is settled in cash, the awards generally are accounted for as liabilities with compensation cost recognized over the service (vesting) period of the award based on the fair value of the award remeasured at each reporting

period. For the component that is settled in equity, compensation cost is measured based on the fair value of the award on the date of grant and the compensation cost is recognized over the service (vesting) period of the award.

Retirement and postretirement

benefits – Subsidiaries of the Group contribute to local state pension funds and social funds, on behalf of their employees.

In Russia all social contributions paid during the year ended December 31, 2014 are represented by payments to governmental social funds, including the Pension Fund of the Russian Federation, the Social Security Fund of the Russian Federation and the Medical Insurance Fund of the Russian Federation.

In the Ukraine, subsidiaries of the Group are required to contribute a specified percentage of each employee's payroll up to a fixed limit into a pension fund, an unemployment fund and a social security fund. The contributions are expensed as incurred.

In addition to the above, MGTS have defined benefit plans to provide their employees certain benefits upon and after retirement. The net period cost of the Group's defined benefit plans is measured on an actuarial basis using the projected unit credit method and several actuarial assumptions. The recognition of expense for defined benefit plans is significantly impacted by estimates made by management such as discount rates used to value certain liabilities, expected return on assets, mortality rates, future rates of compensation increase and other related assumptions. Gains and losses occur when actual experience differs from actuarial assumptions. If such gains or losses exceed ten percent of the greater of plan assets or plan liabilities the Company amortizes those gains or losses over the average remaining service period of the employees.

The Group records in the statement of financial position the funded status of its pension plans based on the projected benefit obligation.

Borrowing costs – Borrowing costs are recognized as an expense in the period in which they are incurred. Borrowing costs for assets that require a period of time to get them ready for their intended use are capitalized and amortized over the related assets' estimated useful lives.

Advertising costs – Advertising costs are expensed as incurred. Advertising costs for the year ended December 31, 2014 and 2013 were \$266.0 million and \$328.7 million, respectively, and were reflected as a component of selling, general and administrative expenses in the accompanying consolidated statements of operations and comprehensive income.

Redeemable noncontrolling

interests – From time to time, in order to optimize the structure of business acquisitions and to defer payment of the purchase price the Group enters into put and call option agreements to acquire noncontrolling interests in the existing subsidiaries. As these put and call option agreements are not freestanding, the underlying shares of such put and call option agreements are classified as redeemable securities and are accounted for at either redemption value or the fair value of redeemable noncontrolling interests as of the reporting date. The fair value of redeemable noncontrolling interests is assessed based on discounted future cash flows of the acquired entity ("Level 3" significant unobservable inputs of the hierarchy established by U.S. GAAP guidance). Any changes in redemption value of redeemable noncontrolling interests are accounted for in the Group's retained earnings. Redeemable noncontrolling interests are presented as temporary equity in the consolidated statement of financial position.

Earnings per share – Basic earnings per share ("EPS") is based on net income attributable to the Group divided by the weighted average number of shares outstanding during the year.

Diluted EPS is based on net income attributable to the Group adjusted in certain circumstances, divided by the weighted average number of shares

outstanding during the year, adjusted for the dilutive effect of all potential shares that were outstanding during the year. Such potentially dilutive shares are excluded when the effect would be to increase diluted earnings per share or reduce the diluted loss per share.

Distributions to shareholders

– Distributable retained earnings of the Group are based on amounts extracted from the standalone statutory accounts of the Company (based on the Russian accounting standards) and may significantly differ from consolidated amounts calculated on the basis of U.S. GAAP.

Reclassifications and revisions

– Certain comparative information presented in the consolidated financial statements for the year ended December 31, 2013 has been revised in order to achieve comparability with the presentation used in the consolidated financial statements for the year ended December 31, 2014. Such reclassifications and revisions were not significant to the Group financial statements, except for presentation of the loss on deconsolidation of Bashneft (Note 2).

Recently adopted accounting pronouncements

– Effective January 1, 2014, the Group adopted Accounting Standards Update ("ASU") 2013-05, Parent's Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity, ASU 2013-07, Liquidation Basis of Accounting and ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. The adoption of these amendments did not have a material impact on the Group's consolidated balance sheet or results of operations.

Transition to International Financial Reporting Standards

– To conform with the Russian legislation, the Group will prepare its consolidated financial statements for the year ended December 31, 2015 in accordance with International Financial Reporting Standards ("IFRS").

CONTACTS

Investor Relations Department

+7 495 730-66-00
+7 495 692-22-88

Press Center

+7 495 730-71-88

Inquiry Desk

+7 495 737-01-01

Address

13, Mokhovaya Str.,
Moscow 125009

DISCLAIMER

Certain statements in this report may contain assumptions or forecasts in respect to forthcoming events within Sistema. The words “expect”, “estimate”, “intend”, “will”, “could” and similar expressions identify forward-looking statements. We wish to caution you that these statements are only predictions and that actual events or results may differ materially. We do not intend to update these statements to reflect events and circumstances occurring after the above-mentioned

date or to reflect the occurrence of unanticipated events. Many factors could cause Sistema’s actual results to differ materially from those contained in our projections or forward-looking statements, including, among others, deteriorating economic and credit conditions, our competitive environment, risks associated with operating in Russia, rapid technological and market change in our industries, as well as many other risks specifically related to Sistema and its operations.

JSFC Sistema
13, Mokhovaya Str., Moscow 125009
Tel. +7 (495) 692 2288
ir@sistema.ru

www.sistema.com

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