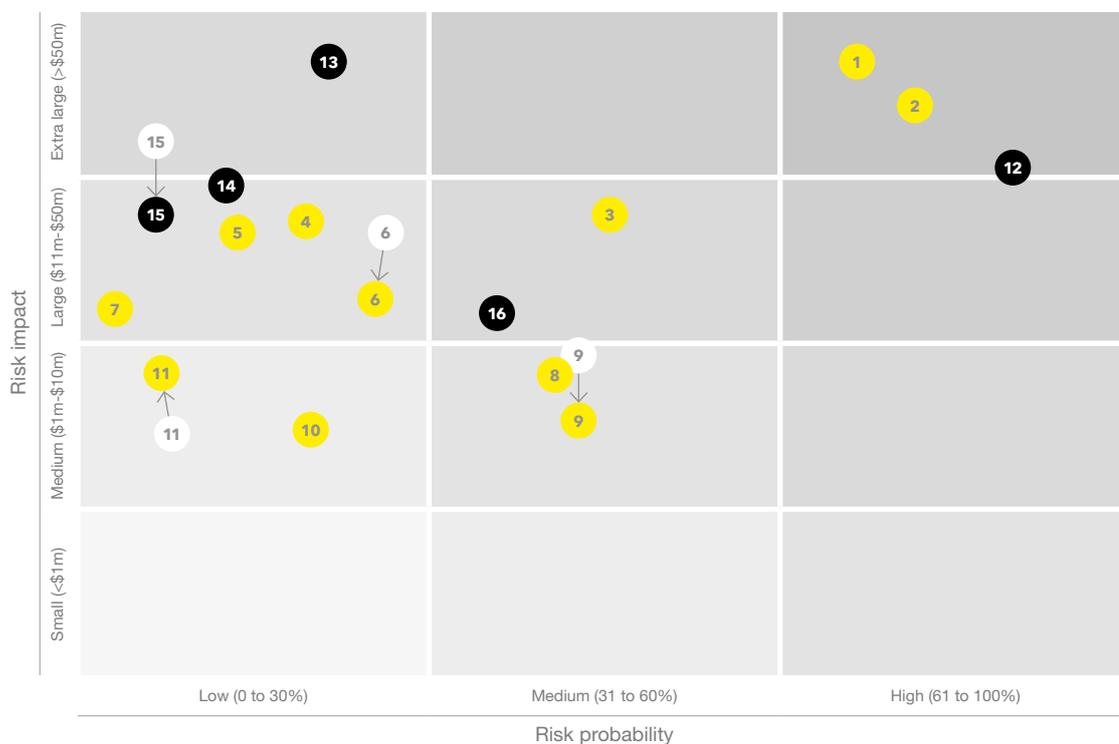


REVIEW OF KEY RISKS

Below we set out a list of the key risks which may have a major impact on SUEK’s operational and financial performance. Within this Report, the risks cited are not exhaustive. There are other inherent risks which are not listed below that may have an adverse impact on SUEK’s performance.



Risk	Ordinal number	Risk	Ordinal number
EXTERNAL RISKS		OPERATIONAL RISKS	
Risk of changes in current legislation	1	Risk of restricted infrastructure availability	12
Regulatory risk	2	Production risk	13
Risk of reduction in coal demand	3	Health and safety risk	14
Cyber risk	4	Environmental risk	15
Risk of emergency situations	5	Human resource risk	16
Risk of reduction in coal prices	6		
Anti-monopoly risk	7	→ Change in 2017 vs 2016	
Inflation risk	8		
Credit risk	9		
Liquidity risk	10		
Foreign exchange and interest rate risks	11		

EXTERNAL RISKS

Description of risk and its potential impact	Change over the year	Actions to mitigate the risk
<p>1. Risk of changes in current legislation</p> <p>The company follows Russian statutory regulations and other regulatory acts in the jurisdictions where it produces and sells its products. We also abide by the regulations of the countries and regions from which the Group imports goods and services.</p> <p>In Russia, changes in legislation can relate to tax, customs and foreign exchange regulations, securities market law, anti-monopoly and corporate law, licensing and mineral resources law and judicial practices. They can also arise through the tightening of environmental protection requirements. SUEK's business can be significantly affected by decisions made by Russian governmental agencies to impose tariffs, quotas, trade restrictions, restrictions on the ownership rights of non-residents, subsidies, licensing and anti-monopoly policies, and refinancing rates.</p> <p>In the international market, we operate via our subsidiary SUEK AG, which has representative offices and subsidiaries in Poland, China, Japan, South Korea, Lithuania, Indonesia, Spain, the US, Vietnam and Taiwan. The Group's companies operate in full compliance with the statutory and regulatory requirements of all of these countries and regions.</p> <p>SUEK's companies can also be affected by unfavourable regulatory acts implemented by foreign authorities. Such changes can involve additional controls on export coal and its subsequent sale in certain countries and regions, or the setting of special conditions for importing goods and services to Russia. International sanctions against Russian individuals and legal entities, as well as industry (sectoral) sanctions, can also impose the limitations on certain sectors of the Russian economy. At the moment, existing sanctions do not directly target Russia's coal-mining industry, the Group's companies or their operation. However, a number of economic limitations do currently affect our business and necessitate special control in the selection of counterparties (while closing financial deals, for example). They also affect the availability of financial resources across the Russian market in general, and make it difficult for companies operating in Russia to import certain types of equipment.</p> <hr/> <p>STRATEGIC PRIORITIES S1 S2 S3 MATERIAL MATTERS M1 M6</p>	<p>↑</p>	<p>We constantly monitor proposed projects to amend legislation, as well as Russian legislative and other regulatory requirements. We also review and summarise law enforcement practices, taking into consideration the company's operation. This enables us to quickly adapt our business processes and organisational structure to any changes in the legislative environment, and to operate in full compliance with the current regulatory and legal framework.</p> <p>SUEK's senior managers and experts are actively involved in governmental policy panels for the coal-mining industry, coal markets, transportation, technical supervision, social and labour relations, and financial markets.</p> <p>SUEK constantly monitors (either independently or through external consultants) relevant changes in legislation and law enforcement in other countries where our transactions may fall under local jurisdiction.</p> <p>The company's management also monitors international sanctions and informs SUEK's companies and employees about relevant limitations and what they mean for their activities.</p>
<p>2. Regulatory risk</p> <p>Our production operations are governed by numerous laws and regulations covering natural resource management, mineral exploration and mining, healthcare, and industrial safety. Coal-mining licences obtained by production companies can be suspended, terminated ahead of schedule or left unrenewed upon expiry. These risks are mostly dependent on the decisions made by regulating and supervisory agencies (Rosnedra, Rosprirodnadzor) holding scheduled and ad hoc inspections at the Group's companies. Changes in national environmental and labour regulations may also influence the thermal coal market.</p> <hr/> <p>STRATEGIC PRIORITIES S1 S3 S5 MATERIAL MATTERS M1 M4</p>	<p>→</p>	<p>We make every effort to comply with current legislation, thereby minimising the risk of suspension of operations at our production units. We rigorously monitor any changes in the legislative environment. SUEK's companies have implemented procedures in order to ensure compliance with licence requirements for timely renewal or new applications. If any discrepancies with licence requirements are detected, we strive to complete the instructions from the regulator as quickly as possible. We also seek to adjust our product quality in line with the regulations of the countries where our customers operate.</p>

Description of risk and its potential impact	Change over the year	Actions to mitigate the risk
<p>3. Risk of reduction in coal demand</p> <p>Reduced use of coal by power-generation companies and the emergence of alternative fuels may result in lower demand for coal. This trend could adversely impact the Group's performance.</p> <p>Tighter international environmental standards on coal quality and production conditions could also result in reduced demand for the coal we produce.</p> <p>STRATEGIC PRIORITIES S1 S3 FOR MORE DETAILS, SEE MARKET REVIEW ON PAGES 25-27. </p> <p>MATERIAL MATTERS M1 M2 M5</p>		<p>We wash our coal to improve its quality, enabling us to meet demand for higher-value products from international markets. We constantly monitor the production, sales and market environment within the industry, and prepare coal-demand forecasts based on studies and reports by investment analysts. We diversify our sales to stable and growing markets to make up for declining sales in slowing markets. We also expand our presence in emerging markets and participate in projects to develop new technologies for coal-fired power generation.</p>
<p>4. Cyber risk</p> <p>Today, protection against cyber risks, including cyber attacks, employee errors and data leakage, is very important. Effective management of these risks allows us to minimise and avoid the leakage of confidential information, network security breaches, problem notification costs, system recovery costs, cyberextortions, and protection costs associated with regulatory requirements.</p> <p>STRATEGIC PRIORITY S2 MATERIAL MATTER M6</p>	<p>New</p>	<p>We carefully monitor our compliance with IT security standards. SUEK is developing a system designed to limit access to IT systems while upgrading its IT infrastructure, bringing it into compliance with corporate standards and best practice.</p>
<p>5. Risk of emergency situations</p> <p>Coal mining is inherently dangerous. The risk of accidents and emergency situations at our production facilities is therefore constant and requires due diligence, robust management and mitigation. Preventing fatal accidents and decreasing the number of injuries we experience is one of the company's most important tasks. Damage to or destruction of property due to explosions, fire or failures in equipment operation can result in direct losses. The costs of emergency response and recovery, as well as forced downtime at individual production units, can also negatively impact the Group's financial results.</p> <p>STRATEGIC PRIORITIES S3 S4 MATERIAL MATTERS M1 M3</p>		<p>We continuously monitor hazards at all stages of operation, paying close attention to safe production processes and procedures. All accidents and incidents are thoroughly investigated by experts who serve as members of special panels. Based on the results of their work, we prepare packages of measures to prevent similar accidents from happening in the future.</p>
<p>6. Risk of reduction in coal prices</p> <p>The company's business may be affected by a decline in demand for coal and a reduction in coal prices due to oversupply and growth in demand for other types of fuel. A reduction in global prices for coal and natural gas (the main types of fuel in the power industry) is a key factor which could change the situation for the worse.</p> <p>STRATEGIC PRIORITIES S1 S3 FOR MORE DETAILS, SEE MARKET REVIEW ON PAGES 25-27. </p> <p>MATERIAL MATTER M1</p>	 <p>In 2017, global coal prices increased significantly compared to 2016, mainly due to the pricing and production regulation introduced by Chinese authorities. Its impact may continue into 2018.</p>	<p>We continuously monitor and forecast the price behaviour of commodities in general and coal in particular. We also monitor trade policies relating to long-term contracts. We constantly analyse the correlation between demand trends, coal mine opening and expansion, the closure of existing mines and the postponement of development projects.</p>

Description of risk and its potential impact	Change over the year	Actions to mitigate the risk
<p>7. Anti-monopoly risk</p> <p>SUEK's companies occupy leading positions in the production and sale of thermal coal in a number of Russian regions. Consequently, our operations are subject to the anti-monopoly requirements set out in Russian legislation, including obligations and limitations introduced to protect competition within the thermal coal market.</p> <hr/> <p>STRATEGIC PRIORITIES S1 S3 MATERIAL MATTERS M1 M6</p>		<p>SUEK has implemented procedures ensuring full compliance with the applicable anti-monopoly regulations.</p>
<p>8. Inflation risk</p> <p>Inflation risk relates to rising inflation rates in the countries where SUEK's companies conduct their main operations, as well as to individual business transactions. Rising inflation can result in higher production costs.</p> <hr/> <p>STRATEGIC PRIORITIES S1 S3 MATERIAL MATTER M1</p>		<p>In order to ensure the appropriate level of protection, we hedge inflation risks by using derivatives and investing available cash assets in a stable foreign currency. Most export contracts for coal are concluded in US Dollars, which largely compensates for the effect of inflation in Russia on the Group's EBITDA.</p>
<p>9. Credit risk</p> <p>Increase in overdue receivables under domestic coal supply contracts, and the transition of overdue receivables to problematic or uncollectible accounts, can result in direct losses for the company and restricted access to debt capital markets.</p> <hr/> <p>STRATEGIC PRIORITIES S2 S3 FOR MORE DETAILS, SEE FINANCIAL REVIEW ON PAGES 71-75. </p> <hr/> <p>MATERIAL MATTER M1</p>	 <p>In 2017, Moody's confirmed SUEK's Ba3 rating and improved its outlook to positive.</p>	<p>We focus on liaising with the financial departments of regional governments where we supply coal. The aim here is to improve or establish a mechanism which ensures timely payments by housing and public utility companies, as well as upfront payment clauses in supply contracts. The company may suspend coal deliveries to customers who carry debt, and if necessary re-direct supplies to more financially reliable customers – for example, retail and small-scale wholesale buyers using our own storage network.</p>
<p>10. Liquidity risk</p> <p>Liquidity risk is directly related to cash turnover. It arises if the company cannot fulfil its payment obligations. It is often linked to the effects of inflation, foreign exchange and interest rate risk. The effective management of liquidity risk requires maintaining an adequate level of cash and cash equivalents while ensuring the prompt raising of funds using available lines of credit. Liquidity risk also arises from decreases in coal sales volumes or price, which can result in insufficient revenue being generated to serve the Group's external debt.</p> <hr/> <p>STRATEGIC PRIORITIES S1 S3 MATERIAL MATTER M1</p>		<p>We continuously monitor loan covenants and use a comprehensive forecasting system to ensure we comply with them. At present, the amount of credit lines provided to SUEK fully cover its financing needs.</p>
<p>11. Foreign exchange and interest rate risks</p> <p>Changes in market indicators such as currency exchange and interest rates can have an adverse effect on the Group's financial performance. They can also impact our debt burden and the value of the financial instruments on the company's balance sheet. Currency and interest rate risks need to be managed to mitigate unfavourable fluctuations in these areas.</p> <hr/> <p>STRATEGIC PRIORITIES S1 S3 FOR MORE DETAILS, SEE FINANCIAL REVIEW ON PAGES 71-75 AND FINANCIAL STATEMENT ON PAGE 128. </p> <hr/> <p>MATERIAL MATTER M1</p>	 <p>Global interest rates increased in 2017 due to the Libor rate increase of 0.5-0.75%; another rate increase is forecast for 2018.</p>	<p>SUEK analyses the risks relating to changes in currency exchange and interest rates on a regular basis. We strive to keep these risks within acceptable limits, and to achieve optimal profitability where possible. We also make use of 'natural hedging' as a significant part of the company's revenue, and the majority of our loans are denominated in US Dollars.</p>

OPERATIONAL RISKS

Description of risk and its potential impact	Change over the year	Actions to mitigate the risk
<p>12. Risk of restricted infrastructure availability</p> <p>The risks consist of reduced access to railway and port infrastructure, electricity networks and water facilities. Limited access to infrastructure can result in reduced profit due to higher operational costs, and losses due to downtime at our production units. For SUEK, this risk can increase as a number of our facilities operate in regions where harsh environments can influence power supply and transportation. Availability of infrastructure is also dependent, to a significant degree, on whether our service providers meet their obligations. Refusal to provide services can result in forced suspension of production, which in turn can negatively impact our operational and financial performance. Certain infrastructure is operated by state-owned monopolies. Operation of such facilities is subject to tariff regulation, which can affect the availability and quality of the services in question.</p> <p>STRATEGIC PRIORITIES: S1 S2 MATERIAL MATTERS: M1 M5</p>		<p>SUEK's production and logistics units actively create long-term relations with infrastructure providers. When executing contracts, we pay special attention to the technical conditions and servicing of railway tracks at connecting stations, railway and port-loading facilities, electrical substations, and networks.</p> <p>We also invest heavily in the development of infrastructure that is critical to our business, such as Vanino Bulk Terminal.</p>
<p>13. Production risk</p> <p>In our operations, we face various production risks linked to different factors. These can be either internal (downtime, adverse geology, low coal quality) or external (higher fuel, electricity and equipment requirements and service prices, and the failure of suppliers and contractors to fulfil their obligations). Such factors can affect production targets, which sometimes requires additional expenses, resulting in an increase in our overall production costs.</p> <p>STRATEGIC PRIORITIES: S1 S2 MATERIAL MATTERS: M1 M3 M5</p>		<p>At all of our production units, we have introduced Life of Mine (LoM) deposit development models. Based on geological data and created using XPAC-XERAS software, the LoM models enable each production unit to check its annual budgeted and actual expenses on a regular basis. As part of this process, we pay special attention to operational-efficiency projects associated with reducing the duration of longwall face moves. We also monitor projects designed, among other aims, to improve work rates and increase the availability and deployment of opencast mining equipment. In addition, we employ a monthly reporting procedure based on KPIs, and Enterprise Resource Planning (ERP) systems, allowing management to assess the performance of SUEK and its subsidiaries on a regular basis.</p>
<p>14. Health and safety risk</p> <p>Coal mining is associated with an elevated risk of accidents and emergencies, which can occur due to geological factors, technical conditions and the action or inaction of individuals. Major emergencies can negatively impact SUEK, leading to a possible increase in reputational risk, the discontinuation of business partnerships or claims from the company's lenders for early loan repayments.</p> <p>STRATEGIC PRIORITIES: S3 S4 MATERIAL MATTERS: M1 M3 M4</p> <p>FOR MORE DETAILS, SEE HEALTH AND SAFETY SECTION ON PAGES 76-79. </p>		<p>Every meeting of the Board of Directors and the Nomination and Compensation Committee of the Board starts with a review of health and safety issues. Our Industrial Safety Committee of the Management Board analyses every injury sustained at our sites and proposes actions to prevent similar accidents in the future. As owners of dangerous industrial equipment, all the Group's facilities maintain general liability insurance against possible damage to life, health and the property of third parties. In addition, we insure our employees against permanent or temporary disability.</p> <p>We also provide constant training for company's personnel and regularly monitor the knowledge of our employees in industrial safety and protection.</p>

Description of risk and its potential impact	Change over the year	Actions to mitigate the risk
--	----------------------	------------------------------

15. Environmental risk

The environmental risks related to coal mining and washing include air emissions of pollutants and coal dust, contamination of soil and water, and land disturbance by mining activities. These negative impacts can result in claims from regulatory authorities and the suspension of operations, which in turn affect the company's operational and financial performance.

STRATEGIC PRIORITIES

S2 S5

FOR MORE DETAILS, SEE ENVIRONMENTAL SECTION ON PAGES 80-85.



MATERIAL MATTERS

M1 M4



In 2017, numerous meetings were held in Russia, promoting consensus among business and government representatives regarding the approach to creating regulatory acts in the field of environmental legislation. These meetings also addressed the adoption of best available technologies. This balanced approach should ensure that both environmental protection and Russian commercial interests can be pursued equally in the years ahead.

Given the high degree of uncertainty in the development of environmental legislation in Russia, SUEK prefers a proactive approach and in 2017 adopted a new Environmental strategy to ensure that new environmental protection requirements can be met by 2023, minimising risks in this area.

We seek to minimise environmental risks by developing and implementing projects for land rehabilitation, mine methane disposal, and health protection where our production operations are located in the immediate vicinity of inhabited areas. The company takes measures to reduce environmental and ecosystem impacts and pollutant emissions, and to ensure the efficient disposal and recycling of waste. The frequency of these measures is determined by current legislation, as well as by the company's Environmental Policy and environmental protection programme.

We have also increased the scope of our coal washing activities, which allow us to reduce the environmental impact of our products during their transportation and use.

16. Human resource risk

Experienced and highly qualified personnel, in particular mining engineers and mine workers, are the company's most important assets. Failure to recruit and retain qualified personnel can result in missed production targets and increased costs. The socio-demographic situation in Russia increases the risk of a qualitative and quantitative human-resource deficit. Factors complicating recruitment include a decline in birth rates and underdeveloped housing infrastructure in the regions where we operate, plus a shortage of vocational training institutions and low levels of professional skills among graduates.

STRATEGIC PRIORITIES

S2 S4

FOR MORE DETAILS, SEE OUR PEOPLE SECTION ON PAGES 86-89.



MATERIAL MATTERS

M3 M5



SUEK develops a system of employee training and professional development. We also work to improve motivation initiatives and enhance remuneration. In terms of recruitment, we actively search out and support talented vocational college and university students, providing them with employment opportunities at SUEK's facilities.

In addition, we implement projects aimed at delivering social development, including improving housing conditions in the regions where we operate.



Q: In 2017, for the first time in Russia, SUEK introduced a 400-metre longwall. How did you ensure its safety?

A: The main issue with the longwall was ensuring atmospheric safety, which we achieved by improving the gas control scheme at the site. Two parallel surface gas-suction plants were installed along the edges of the mining area which

contributed to stable gas control with a constant volume of extracted methane-air mixture. This scheme allowed us to safely produce 50,000 tonnes per day, and in May 2017 we set the world production record without a single violation of industrial safety rules for coal mines.

VLADIMIR ARTEMIEV,
CHIEF OPERATIONS OFFICER