

PetroNeft Resources plc
Final Results
for the year ended 31 December 2016

PetroNeft Resources plc

Final Results

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Forward Looking Statements

This report contains forward-looking statements. These statements relate to the Group's future prospects, developments and business strategies. Forward-looking statements are identified by their use of terms and phrases such as 'believe', 'could', 'envisage', 'potential', 'estimate', 'expect', 'may', 'will' or the negative of those, variations or comparable expressions, including references to assumptions.

The forward-looking statements in this report are based on current expectations and are subject to risks and uncertainties that could cause actual results to differ materially from those expressed or implied by those statements. These forward-looking statements speak only as at the date of these financial statements.

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Chairman's Statement

2016 was an active year for our Company, particularly at Licence 61 where, with our partner Oil India, we drilled wells at Arbuzovskoye and Sibkrayevskoye. The work programme saw a mix of results, as described below. 2016 also saw continuing challenges for the industry as a whole with further significant weakness in the oil price internationally.

Operations

The existing production wells at Lineynoye and Arbuzovskoye generally performed reasonably well during 2016 but continued their expected natural decline. The main development programme in 2016 brought the southern part of the Arbuzovskoye oil field into production. Thanks to the considerable experience gained in drilling horizontal wells in 2015 we achieved excellent results at South Arbuzovskoye where the two horizontal and two vertical wells all achieved initial production rate greater than forecast.

In August 2016 we announced the results of a delineation well at Sibkrayevskoye. The S-374 well was a long (10 km) step out from previous wells to a different structural high. Unfortunately it failed to encounter commercial oil and the well was plugged and abandoned.

2017 work programme

Following the S-374 result, and in view of the low oil prices expected in the near term, it was decided to defer the first development pad at the Sibkrayevskoye oil field until we could drill a further appraisal well just 2 km from existing wells. We will drill this delineation well (S-375) at Sibkrayevskoye in 2017 with a view to commencing development of Sibkrayevskoye in 2018. Oil India have indicated their willingness to provide the funding for these two projects by way of a shareholder loan to the joint venture company.

Reserves

The table below contains the details of the Ryder Scott report as at 1 January 2016 as adjusted for 2016 production. The report, which is available on www.petroneft.com, demonstrates the large potential of the Sibkrayevskoye oil field which we expect to start developing in 2018.

Ryder Scott Estimated Reserves in Oil Fields (net to PetroNeft)

Oil Field Name	Proved	Proved & Probable	Proved, Probable & Possible
Licence 61	1P mmbo	2P mmbo	3P mmbo
Lineynoye	7.0	12.8	15.9
Tungolskoye	0.3	2.9	3.6
Kondrashevskoye	0.7	1.3	1.6
Arbuzovskoye	1.7	4.2	5.4
Sibkrayevskoye	5.8	29.4	52.8
North Varyakhskoye	0.2	0.4	0.5
	15.7	51.0	79.8
Licence 67			
Ledovoye	1.5	14.0	17.4
Total net to PetroNeft	17.2	65.0	97.2

- Licence 61 as at 31 December 2016 (Ryder Scott report as at 1 January 2016, adjusted for 2016 production).
- Reserves reflect just PetroNeft's 50% share of reserves for each licence.
- All oil in discovered fields is in the Upper Jurassic section.
- Reserves were determined in accordance with the Society of Petroleum Engineers ("SPE") Petroleum Resources Management System ("PRMS") rules.

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Chairman's Statement (*continued*)

Engagement with Natlata

Following extensive engagement with our largest shareholder, Natlata Partners Limited ("Natlata"), during 2015 and in connection with their requisitioned EGM, in April 2016 we announced that we reached an agreement on a new Board composition and structure. This involved the appointment Maxim Korobov as non-executive Director and Anthony Sacca and David Sturt as independent non-executive Directors. David Sanders, Gerry Fagan and Paul Dowling left the Board. Mr. Dowling remains CFO of the Company. The agreement includes a commitment from Natlata that it will support the newly constituted Board for a period of two years and I am pleased to report that the new Board has worked well together in the period since April 2016.

I would like to thank David Sanders, who was a founder of the Company, and Gerry Fagan for their many years of service to the Company.

Review of PetroNeft loss for the year

The loss after taxation for the year was US\$5,427,660 (2015: US\$8,474,383). The loss included a foreign exchange gain on intra-group loans of US\$77,458 (2015: loss of US\$284,449) and the share of joint venture's net loss in WorldAce Investments of US\$5,721,232 (2015: US\$8,765,055).

As discussed in previous Annual Reports, the effect of the Licence 61 Farmout was that PetroNeft became a 50% owner of WorldAce Investments Limited which is the 100% owner of Stimul-T the Russian entity that owns Licence 61 and all of the associated infrastructure. Prior to the farmout the WorldAce Group was consolidated 100% in the financial statements of PetroNeft. Once the farmout was completed the consolidation method changed to the equity method which means that just the 50% share of the profit or loss of the WorldAce Group is included in the Income Statement of PetroNeft and 50% of the share of net assets of WorldAce Group is included in the Balance Sheet of PetroNeft rather than showing the proportional share of revenue, expenditure and individual classes of assets and liabilities.

PetroNeft Key Financial Metrics	2016	2015
	US\$'000	US\$'000
Continuing operations		
Revenue	2,280	2,398
Cost of sales	(2,038)	(2,371)
Gross profit	242	27
Administrative expenses	(2,155)	(1,380)
Exchange profit/(loss) on intra-Group loans	77	(284)
Operating loss	(1,836)	(1,637)
Share of joint venture's net loss – WorldAce Investments Limited	(5,721)	(8,765)
Share of joint venture's net loss – Russian BD Holdings B.V.	(288)	(315)
Finance revenue	3,248	3,042
Loss for the year for continuing operations before taxation	(4,597)	(7,675)
Income tax expense	(830)	(799)
Loss for the year	(5,427)	(8,474)

Revenue

Revenue in 2016 and 2015 includes income as operator of both licences and the revenue of PetroNeft's wholly owned subsidiary, Granite Construction in respect of construction services provided in relation to both joint ventures.

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Chairman's Statement (*continued*)

Income of PetroNeft Group as Operator of Licence 61 and Licence 67

In the joint venture agreements related to both Licence 61 and Licence 67, PetroNeft is designated as the operator of each Licence. This means that PetroNeft employees and management are responsible for the day to day running of both Licences. Major strategic and financial decisions relating to the Licences require unanimous approval by both shareholders in the respective joint venture agreements.

As PetroNeft management and employees are responsible for day to day matters in both Licences, PetroNeft is entitled to recover a portion of its expenses from the joint ventures. The costs associated with this revenue are included in cost of sales.

In 2016 PetroNeft Group charged a total of US\$1.46 million (2015: US\$1.64 million) to the joint ventures in respect of management services. PetroNeft also owns a small construction company, Granite Construction, which carries out small ad hoc construction projects such as well pads and on-site accommodation on both Licences. In 2016 Granite Construction charged the WorldAce Group US\$0.81 million (2015: US\$0.75 million) in respect of these services.

Finance Revenue

Most of the finance revenue relates to interest receivable on loans to joint ventures. During 2016 PetroNeft had interest receivable of US\$3,011,025 (2015: US\$2,826,303) on its loans to WorldAce Group and US\$234,402 (2015: US\$205,189) on its loans to Russian BD Holdings B.V.

Key Financial Metrics – WorldAce Group

Because of the equity method of consolidation that applies to PetroNeft's interest in WorldAce, it is difficult to extract meaningful metrics from the PetroNeft consolidated income statement. Therefore, the metrics below are an extraction from the audited financial statements of the WorldAce Group and give an indication as to the performance of Licence 61:

	PetroNeft's 2016 US\$'000	PetroNeft's 2015 US\$'000
Continuing operations		
Revenue	11,604	10,300
Cost of sales	(11,200)	(10,436)
Gross profit	404	(136)
Gross margin %	3.5%	(1.3%)
Administrative expenses	(1,614)	(1,519)
Impairment of oil and gas properties	-	(4,550)
Operating loss	(1,210)	(6,205)
Loss on disposal of oil and gas properties	(438)	-
Write-off of exploration and evaluation assets	(710)	-
Finance revenue	10	12
Finance costs	(3,373)	(2,572)
Loss for the year for continuing operations before taxation	(5,721)	(8,765)
Income tax	-	-
Loss for the year for continuing operations before taxation	(5,721)	(8,765)

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Chairman's Statement (*continued*)

Net Loss – WorldAce Group

The net loss of WorldAce Group for the full year decreased to US\$11,442,464 from US\$17,530,110 in 2015. The decrease in the loss for the year before taxation can be attributed to the fact that there was no impairment necessary in the year. Of the US\$6.6 million in interest payable by WorldAce, US\$3.0 million is payable to PetroNeft. Due to the lower oil price environment and a reduction in reserves at the Lineynoye oil field an impairment of oil and gas properties in the amount of US\$9.1 million was required in 2015.

Revenue, Cost of Sales and Gross Margin – WorldAce Group

Revenue from oil sales was US\$23,208,363 for the year (2015: US\$20,600,188). Cost of sales includes depreciation of US\$3,337,902 (2015: US\$2,856,469), which was higher mainly due to increased production. The gross margin improved during the year also due to higher production. Operating costs per barrel (cost of sales excluding depreciation and Mineral Extraction Tax) were lower at US\$8.04 (2015: US\$10.73 per barrel). We would expect the gross margin to improve in future periods as our facilities and field operations are fully staffed and can handle additional production from the Sibkrayevskoye oil field once it comes online. We produced 990,931 barrels of oil (2015: 737,655 barrels) in the year and sold 985,824 barrels of oil (2015: 761,123 barrels) achieving an average oil price of US\$24 per barrel (2015: US\$27 per barrel). All oil was sold on the domestic market in Russia.

Finance Costs – WorldAce Group

Finance costs of US\$6,744,948 (2015: US\$5,144,634) mainly relates to interest on loans from PetroNeft and Oil India.

Taxation – WorldAce Group

There is no tax payable in 2016 or 2015.

Current and Future Funding of PetroNeft Group

In the 2015 Annual Report we outlined that PetroNeft expected to start receiving interest due on its shareholder loans to WorldAce in the second half of 2017 once the development of the Sibkrayevskoye oil field in Licence 61 was up and running. The S-374 appraisal well drilled in 2016 at the Sibkrayevskoye oil field, to assess the true extent of the field 10km to the south of existing wells, did not encounter commercial hydrocarbons. The result of this well has led to the postponement of the commencement of the development of the Sibkrayevskoye oil field by one year pending the result of a new appraisal well, S-375, which will be drilled in the summer of 2017. As a consequence of this, the date by which PetroNeft expects to start receiving interest due on its shareholder loans to WorldAce has been extended by a minimum of 12 months from the previously guided estimate of late 2017.

Success of the S-375 well would provide assurance that there are at least two pads to be developed at Sibkrayevskoye, in which case it is expected that the development of the Sibkrayevskoye oil field will commence in 2018. The proposed first pad at Sibkrayevskoye has already been delineated by the S-370, S-372 and S-373 wells. The S-375 well is being drilled within the proposed pad 2 area which is about 2km from the existing wells that found oil and is within the same structural closure. The S-374 well was more than 10km south in a different structural lobe. The S-373 well at the proposed pad 1 area has produced oil during the last two winters at consistent rates giving further comfort to the Company of the prospects of the area.

In 2016 the Board of Oil India provided a non-binding indication of their willingness to provide a US\$25 million shareholder loan to WorldAce for the development of Sibkrayevskoye. Should the S-375 well not be successful the joint venture shareholders will need to consider other options. This could include the development of Sibkrayevskoye as a one-pad development focussed only on the area surrounding previous wells such as S-373 or it could lead to some further appraisal work. The joint venture shareholders have provided non-binding indications of their willingness to consider providing continuing support in this event, including not immediately seeking repayments of principal or payment of interest under shareholder loan agreements.

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Chairman's Statement (*continued*)

The effect of the delay in receiving interest due is that PetroNeft will require additional funding to cover its operating costs during the next 12 months. Management have prepared cash flow projections for the period to 31 December 2018 which indicate a shortfall of funds by the end of quarter one 2018, and a cumulative shortfall of approximately US\$1 million by 31 December 2018, irrespective of the success of S-375.

The Company is currently in confidential discussions pursuing several options in order to meet this potential shortfall. These include the potential sale or farmout of Licence 67, short term debt financing from a related corporate entity and the acquisition of producing and non-producing assets in share for share type transactions. The Board believe that the first two options can be completed in a short timeframe. In relation to the latter option, the Company has signed non-disclosure agreements and opened data rooms. As there are delaying factors, including regulatory requirements, around a share for share type transaction, the timeframe to close such a transaction could be several months following binding agreement between the parties.

The Directors are satisfied that the options being pursued are progressing well and are confident the funding gap can be solved.

The successful development of S-375 and the potential shortfall in funds represent material uncertainties that may cast significant doubt upon the Group's and the Company's ability to continue as a going concern as described in Note 2 to the Final Results.

Summary

2016 was a mixed year for PetroNeft with positives and negatives coming from a busy work programme. The lessons learned from the 2015 programme of horizontal wells bore good results at Arbuzovskoye leading to a 35% increase in production. The result of the S-374 well at Sibkrayevskoye has led us to delay the commencement of the Sibkrayevskoye development pending the result of the S-375 well. Our industry is continuing to go through tough times at present but we have future development targets such as Sibkrayevskoye that will still be profitable at current reduced oil prices.

Annual Report and AGM

The annual report will be mailed to shareholders and published on the Company's website (www.petroneft.com) on 30 June 2017. The AGM will be held in Dublin on 15 September 2017.

Finally, I know that I speak for all the Directors, management and staff of the Group in giving sincere thanks to our shareholders, both old and new, for your continued support throughout the past year.

David Golder
Non-Executive Chairman

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Consolidated Income Statement

For the year ended 31 December 2016

	<i>Note</i>	2016 US\$	2015 US\$
<i>Continuing operations</i>			
Revenue		2,279,585	2,398,314
Cost of sales		<u>(2,038,209)</u>	<u>(2,370,949)</u>
Gross profit		241,376	27,365
Administrative expenses		(2,154,699)	(1,379,506)
Exchange gain/(loss) on intra-Group loans		<u>77,458</u>	<u>(284,449)</u>
Operating loss		(1,835,865)	(1,636,590)
Share of joint venture's net loss - WorldAce Investments Limited		(5,721,232)	(8,765,055)
Share of joint venture's net loss - Russian BD Holdings B.V.		(288,198)	(314,859)
Finance revenue		<u>3,247,876</u>	<u>3,041,587</u>
Loss for the year for continuing operations before taxation		(4,597,419)	(7,674,917)
Income tax expense		(830,241)	(799,466)
Loss for the year attributable to equity holders of the Parent		<u>(5,427,660)</u>	<u>(8,474,383)</u>
Loss per share attributable to ordinary equity holders of the Parent			
Basic and diluted - US dollar cent	4	(0.77)	(1.20)

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2016

	2016 US\$	2015 US\$
Loss for the year attributable to equity holders of the Parent	(5,427,660)	(8,474,383)
<i>Other comprehensive income to be reclassified to profit or loss in subsequent years:</i>		
Currency translation adjustments - subsidiaries	25,298	265,640
Share of joint ventures' other comprehensive income - foreign exchange translation differences	<u>7,741,440</u>	<u>(12,474,502)</u>
Total comprehensive profit/(loss) for the year attributable to equity holders of the Parent	<u>2,339,078</u>	<u>(20,683,245)</u>

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Consolidated Balance Sheet

As at 31 December 2016

		2016	2015
	Note	US\$	US\$
Assets			
Non-current Assets			
Property, plant and equipment	5	143,466	181,703
Equity-accounted investment in joint ventures - WorldAce Investments Limited	6	-	-
Equity-accounted investment in joint ventures - Russian BD Holdings B.V.	7	-	-
Financial assets - loans and receivables	8	47,713,421	42,883,861
		<u>47,856,887</u>	<u>43,065,564</u>
Current Assets			
Inventories	9	28,973	54,302
Trade and other receivables	10	1,143,904	1,842,128
Cash and cash equivalents	11	319,618	1,284,212
		<u>1,492,495</u>	<u>3,180,642</u>
Total Assets		<u>49,349,382</u>	<u>46,246,206</u>
Equity and Liabilities			
Capital and Reserves			
Called up share capital	13	9,429,182	9,429,182
Share premium account		140,912,898	140,912,898
Share-based payments reserve		6,796,540	6,796,540
Retained loss		(80,202,450)	(74,774,790)
Currency translation reserve		(31,118,410)	(38,885,148)
Other reserves		336,000	336,000
Equity attributable to equity holders of the Parent		<u>46,153,760</u>	<u>43,814,682</u>
Non-current Liabilities			
Deferred tax liability		2,113,541	1,286,378
		<u>2,113,541</u>	<u>1,286,378</u>
Current Liabilities			
Trade and other payables	12	1,082,081	1,145,146
		<u>1,082,081</u>	<u>1,145,146</u>
Total Liabilities		<u>3,195,622</u>	<u>2,431,524</u>
Total Equity and Liabilities		<u>49,349,382</u>	<u>46,246,206</u>

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Consolidated Statement of Changes in Equity

For the year ended 31 December 2016

	Called up share capital US\$	Share premium account US\$	Share-based payment and other reserves US\$	Currency translation reserve US\$	Retained loss US\$	Total US\$
At 1 January 2015	9,429,182	140,912,898	7,099,745	(26,676,286)	(66,300,407)	64,465,132
Loss for the year	-	-	-	-	(8,474,383)	(8,474,383)
Currency translation adjustments - subsidiaries	-	-	-	265,640	-	265,640
Share of joint ventures' other comprehensive income - foreign exchange translation differences	-	-	-	(12,474,502)	-	(12,474,502)
Total comprehensive loss for the year	-	-	-	(12,208,862)	(8,474,383)	(20,683,245)
Share-based payment expense	-	-	32,795	-	-	32,795
At 31 December 2015	9,429,182	140,912,898	7,132,540	(38,885,148)	(74,774,790)	43,814,682
At 1 January 2016	9,429,182	140,912,898	7,132,540	(38,885,148)	(74,774,790)	43,814,682
Loss for the year	-	-	-	-	(5,427,660)	(5,427,660)
Currency translation adjustments - subsidiaries	-	-	-	25,298	-	25,298
Share of joint ventures' other comprehensive income - foreign exchange translation differences	-	-	-	7,741,440	-	7,741,440
Total comprehensive profit for the year	-	-	-	7,766,738	(5,427,660)	2,339,078
At 31 December 2016	9,429,182	140,912,898	7,132,540	(31,118,410)	(80,202,450)	46,153,760

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Consolidated Cash Flow Statement

For the year ended 31 December 2016

	2016 US\$	2015 US\$
Operating activities		
Loss before taxation	(4,597,419)	(7,674,917)
Adjustment to reconcile loss before tax to net cash flows		
Non-cash		
Depreciation	68,568	97,673
Share of loss in joint ventures	6,009,430	9,079,914
Share-based payment expense	-	32,795
Finance revenue	(3,247,876)	(3,041,587)
Working capital adjustments		
Decrease/(increase) in trade and other receivables	860,444	(548,351)
Decrease/(increase) in inventories	25,330	(39,122)
(Decrease)/increase in trade and other payables	(59,474)	31,428
Income tax paid	(16,650)	(25,832)
Net cash flows used in operating activities	(957,647)	(2,087,999)
Investing activities		
Purchase of property, plant and equipment	-	(19,059)
Loan facilities advanced to joint venture undertakings	(10,000)	-
Interest received	2,449	10,095
Net cash used in investing activities	(7,551)	(8,964)
Net decrease in cash and cash equivalents	(965,198)	(2,096,963)
Translation adjustment	604	(11,594)
Cash and cash equivalents at the beginning of the year	1,284,212	3,392,769
Cash and cash equivalents at the end of the year	319,618	1,284,212

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Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

1. Basis of Accounting and Presentation of Financial Information

While the financial information included in this announcement has been prepared in accordance with the Group's accounting policies under International Financial Reporting Standards ("IFRS") as adopted by the European Union, this announcement does not itself contain sufficient information to comply with IFRS. The Company is distributing the full financial statements that comply with IFRS on 30 June 2017.

The financial information set out above does not constitute the Company's statutory accounts for the years ended 31 December 2016 or 2015, but is derived from those accounts. Statutory accounts for 2015 have been delivered to the Registrar of Companies and those for 2016 will be delivered following the Company's annual general meeting. The auditors have reported on those accounts. Both reports were unmodified but the 2016 report did draw attention to going concern issues by way of emphasis of matter.

Adoption of IFRS and International Financial Reporting Interpretations Committee (IFRIC) interpretations

A number of amendments to existing IFRS (principally related to clarifications and refinements of definitions) became effective for, and have been applied in preparing, these Financial Statements. The application of these amendments did not result in material changes to the results or financial position of the Group or the Company.

2. Going Concern

PetroNeft is facing a potential funding shortfall in 2018 due to the delay in the commencement of the Sibkrayevskoye oil field development. The effect of this delay is to also delay the commencement of payments to PetroNeft of interest due to it under shareholder loan agreements with WorldAce. The effect of this is that PetroNeft will require additional funding to meet its operating costs during the next 12 months.

The S-374 appraisal well drilled at Sibkrayevskoye oil field in Licence 61 in 2016 did not encounter commercial hydrocarbons. The result of this well has led to the postponement of the commencement of the development of the Sibkrayevskoye oil field by one year pending the result of a new appraisal well, S-375, which will be drilled in the Summer of 2017. As a consequence of this, the date by which PetroNeft expects to start receiving interest due on its shareholder loans to WorldAce has been extended by a minimum of 12 months from the previously guided estimate of late 2017.

Success of the S-375 well would provide assurance that there are at least two pads to be developed at Sibkrayevskoye, in which case it is expected that the development of the Sibkrayevskoye oil field will commence in 2018. The proposed first pad at Sibkrayevskoye has already been delineated by the S-370, S-372 and S-373 wells. The S-375 well is being drilled within the proposed pad 2 area which is about 2km from the existing wells that found oil and is within the same structural closure. The S-374 well was more than 10km south in a different structural lobe. The S-373 well at the proposed pad 1 area has produced oil during the last two winters at consistent rates giving further comfort to the Company of the prospects of the area.

In 2016 the Board of Oil India provided a non-binding indication of their willingness to provide a US\$25 million shareholder loan to WorldAce for the development of Sibkrayevskoye. Should the S-375 well not be successful the joint venture shareholders will need to consider other options. This could include the development of Sibkrayevskoye as a one-pad development focussed only on the area surrounding previous wells such as S-373 or it could lead to some further appraisal work. The joint venture shareholders have provided non-binding indications of their willingness to consider providing continuing support in this event, including not immediately seeking repayments of principal or payment of interest under shareholder loan agreements.

Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

2. Going Concern (continued)

The Group has analysed its cash flow requirements through to 31 December 2018 in detail. The cash flow includes estimates for a number of key variables including timing of cash flows of expenditure and management of working capital, and the Directors believe that the Group's cash flow forecasts represent the best estimate of the actual cash flows over the forecast period at the date of approval of the financial statements. The cash flow is stress tested to assess the adverse effect arising from reasonable changes in circumstance. The cash flow projections for the period to 31 December 2018 indicate a potential shortfall of funds by the end of quarter one in 2018.

The Company is currently in confidential discussions pursuing several options in order to meet this potential shortfall. These include the potential sale or farmout of Licence 67, short term debt financing from a related corporate entity and the acquisition of producing and non-producing assets in share for share type transactions. The Board believe that the first two options can be completed in a short timeframe. In relation to the latter option, the Company has signed non-disclosure agreements and opened data rooms. As there are delaying factors, including regulatory requirements, around transferring licences and in a share for share type transaction, the timeframe to close such a successful transaction could be at least six months following binding agreement between the parties. The Board is confident that one of these options will bring a solution.

The successful development of S-375 and the potential shortfall in funds represent material uncertainties that may cast significant doubt upon the Group and the Company's ability to continue as a going concern. Nevertheless, after making enquiries, and considering the uncertainties described above, the Directors are confident that the Group and the Company will have adequate resources to continue in operational existence for the foreseeable future. For these reasons, they continue to adopt the going concern basis in preparing the annual report and accounts.

Accordingly, these financial statements do not include any adjustments to the carrying amount or classification of assets and liabilities that would result if the Group or Company was unable to continue as a going concern.

3. Segment information

At present the Group has one reportable operating segment, which is oil exploration and production through its joint venture undertakings. As a result, there are no further disclosures required in respect of the Group's reporting segment.

The risk and returns of the Group's operations are primarily determined by the nature of the activities that the Group engages in, rather than the geographical location of these operations. This is reflected by the Group's organisational structure and the Group's internal financial reporting systems.

Management monitors and evaluates the operating results for the purpose of making decisions consistently with how it determines operating profit or loss in the consolidated financial statements.

Geographical segments

Although the joint venture undertakings WorldAce Investments Limited and Russian BD Holdings B.V. are domiciled in Cyprus and the Netherlands, the underlying businesses and assets are in Russia. Substantially all of the Group's sales and capital expenditures are in Russia.

Assets are allocated based on where the assets are located:

	2016	2015
	US\$	US\$
Non-current assets		
Russia	47,854,604	43,062,084
Ireland	2,283	3,480
	47,856,887	43,065,564

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Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

4. Loss per Ordinary Share

Basic loss per Ordinary Share amounts are calculated by dividing net loss for the year attributable to ordinary equity holders of the Parent by the weighted average number of Ordinary Shares outstanding during the year. Basic and diluted earnings per Ordinary Share are the same as the potential Ordinary Shares are anti-dilutive.

	2016 US\$	2015 US\$
Numerator		
Loss attributable to equity shareholders of the Parent for basic and diluted loss	(5,427,660)	(8,474,383)
	<u>(5,427,660)</u>	<u>(8,474,383)</u>
Denominator		
Weighted average number of Ordinary Shares for basic and diluted earnings per Ordinary Share	707,245,906	707,245,906
Diluted weighted average number of shares	<u>707,245,906</u>	<u>707,245,906</u>
Loss per share:		
Basic and diluted - <i>US dollar cent</i>	(0.77)	(1.20)

The Company has instruments in issue that could potentially dilute basic earnings per Ordinary Share in the future, but are not included in the calculation for the reasons outlined below:

- Employee Share Options – These potential Ordinary Shares are anti-dilutive for the years ended 31 December 2016 and 2015.
- Warrants – All remaining warrants expired during 2015.

PetroNeft Resources plc

Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

5. Property, Plant and Equipment

	Plant and machinery US\$
Cost	
At 1 January 2015	996,588
Additions	19,059
Translation adjustment	(215,247)
At 1 January 2016	800,400
Translation adjustment	145,468
At 31 December 2016	945,868
Depreciation	
At 1 January 2015	674,786
Charge for the year	97,673
Translation adjustment	(153,762)
At 1 January 2016	618,697
Charge for the year	68,568
Translation adjustment	115,137
At 31 December 2016	802,402
Net book values	
At 31 December 2016	143,466
At 31 December 2015	181,703

PetroNeft Resources plc

Notes to the Preliminary Financial Statements

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6. Equity-accounted Investment in Joint Venture – WorldAce Investments Limited

PetroNeft Resources plc has a 50% interest in WorldAce Investments Limited, a jointly controlled entity which holds 100% of LLC Stimul-T, an entity involved in oil and gas exploration and the registered holder of Licence 61. The interest in this joint venture is accounted for using the equity accounting method. WorldAce Investments Limited is incorporated in Cyprus and carries out its activities, through LLC Stimul-T, in Russia.

	Share of net assets US\$
At 1 January 2015	10,865,156
Elimination of unrealised profit on intra-Group transactions	(29,326)
Retained loss	(8,765,055)
Translation adjustment	(11,587,393)
Credited against loans receivable from WorldAce Investments Limited (Note 8)	9,516,618
At 1 January 2016	-
Elimination of unrealised loss on intra-Group transactions	(157,876)
Retained loss	(5,721,232)
Translation adjustment	7,149,140
Debited to loans receivable from WorldAce Investments Limited (Note 8)	(1,270,032)
At 31 December 2016	-

The balance sheet position of WorldAce Investments Limited shows net liabilities of US\$25,915,002 following a loss in the year of US\$11,442,464 together with a positive currency translation adjustment of US\$14,298,281. PetroNeft's 50% share is included above and results in a negative carrying value of US\$8,246,586. Therefore, the share of net assets is reduced to Nil and, in accordance with IAS 28 *Investments in Associates and Joint Ventures*, the amount of US\$8,246,586 is deducted from other assets associated with the joint venture on the Balance Sheet which are the loans receivable from WorldAce Investments (see Note 8).

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Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

6. Equity-accounted Investment in Joint Venture – WorldAce Investments Limited (continued)

Additional financial information in respect of PetroNeft's 50% interest in the equity-accounted joint venture entity is disclosed below:

	2016 US\$	2015 US\$
<i>Continuing operations</i>		
Revenue	11,604,182	10,300,094
Cost of sales	(11,199,845)	(10,435,521)
Gross profit/(loss)	404,337	(135,427)
Administrative expenses	(1,614,435)	(1,519,005)
Impairment of oil and gas properties	-	(4,550,000)
Operating loss	(1,210,098)	(6,204,432)
Loss on disposal of oil and gas properties	(438,034)	-
Write-off of exploration and evaluation assets	(710,047)	-
Finance revenue	9,421	11,694
Finance costs	(3,372,474)	(2,572,317)
Loss for the year for continuing operations before taxation	(5,721,232)	(8,765,055)
Income tax expense	-	-
Loss for the year	(5,721,232)	(8,765,055)
Loss for the year	(5,721,232)	(8,765,055)
<i>Other comprehensive income to be reclassified to profit or loss in subsequent years:</i>		
Currency translation adjustments	7,149,140	(11,587,393)
Total comprehensive profit/(loss) for the year	1,427,908	(20,352,448)

The currency translation adjustment results from the movement of the Russian Rouble during the year. All Russian Rouble carrying values in Stimul-T, the 100% subsidiary of WorldAce are converted to US Dollars at each period end. The resulting gain or loss is recognised through other comprehensive income and transferred to the currency translation reserve. The Russian Rouble appreciated significantly against the US Dollar during the year from RUB73.3:US\$1 at 31 December 2015 to RUB60.9:US\$1 at 31 December 2016.

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Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

6. Equity-accounted Investment in Joint Venture – WorldAce Investments Limited (continued)

	2016 US\$	2015 US\$
Non-current Assets		
Oil and gas properties	37,945,273	27,646,307
Property, plant and equipment	199,338	197,826
Exploration and evaluation assets	7,556,920	6,044,036
Assets under construction	932,631	2,345,358
	46,634,162	36,233,527
Current Assets		
Inventories	536,685	257,857
Trade and other receivables	176,318	259,142
Cash and cash equivalents	40,415	153,198
	753,418	670,197
Total Assets	47,387,580	36,903,724
Non-current Liabilities		
Provisions	(433,573)	(273,278)
Interest-bearing loans and borrowings	(56,686,519)	(48,366,752)
	(57,120,092)	(48,640,030)
Current Liabilities		
Trade and other payables	(3,224,989)	(2,649,103)
	(3,224,989)	(2,649,103)
Total Liabilities	(60,345,081)	(51,289,133)
Net Liabilities	(12,957,501)	(14,385,409)

Capital commitments

	2016 US\$	2015 US\$
Details of capital commitments at the balance sheet date are as follows:		
Contracted for but not provided in the financial statements	1,080,620	1,236,788

PetroNeft Resources plc

Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

6. Equity-accounted Investment in Joint Venture – WorldAce Investments Limited (continued)

Future minimum rentals payable under non-cancellable operating leases at the balance sheet date are as follows:

	2016 US\$	2015 US\$
Within one year	57,039	39,459
After one year but not more than five years	219,319	150,274
More than five years	414,738	326,079
	<u>691,096</u>	<u>515,812</u>

The above capital commitments in the joint venture are incurred jointly with Oil India International B.V. The Group has a 50% share of these commitments.

7. Equity-accounted Investment in Joint Venture - Russian BD Holdings B.V.

PetroNeft Resources plc has a 50% interest in Russian BD Holdings B.V., a jointly controlled entity which holds 100% of LLC Lineynoye, an entity involved in oil and gas exploration and the registered holder of Licence 67. The interest in this joint venture is accounted for using the equity accounting method. Russian BD Holdings B.V. is incorporated in the Netherlands and carries out its activities in Russia.

	Share of net assets US\$
At 1 January 2015	365,178
Retained loss	(314,859)
Translation adjustment	(887,109)
Credited against loans receivable from Russian BD Holdings BV (Note 8)	836,790
At 1 January 2016	-
Retained loss	(288,198)
Translation adjustment	592,300
Debited to loans receivable from Russian BD Holdings BV (Note 8)	(304,102)
At 31 December 2016	-

The balance sheet position of Russian BD Holdings B.V. shows net liabilities of US\$1,065,376 following a loss in the year of US\$576,396 together with a positive currency translation of US\$1,184,600. PetroNeft's 50% share is included above and results in a negative carrying value of US\$532,688. Therefore, the share of net assets is reduced to Nil and, in accordance with IAS 28 *Investments in Associates and Joint Ventures*, the amount of US\$532,688 is deducted from other assets associated with the joint venture on the Balance Sheet which are the loans receivable from Russian BD Holdings B.V. (Note 8).

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Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

7. Equity-accounted Investment in Joint Venture - Russian BD Holdings B.V. (continued)

Additional financial information in respect of PetroNeft's 50% interest in the equity-accounted joint venture entity is disclosed below:

	2016 US\$	2015 US\$
Revenue	-	-
Cost of sales	-	-
Gross profit	-	-
Administrative expenses	(66,718)	(106,224)
Operating loss	(66,718)	(106,224)
Finance revenue	294	434
Finance costs	(239,079)	(209,069)
Loss for the year for continuing operations before taxation	(305,503)	(314,859)
Taxation	17,305	-
Loss for the year	(288,198)	(314,859)
Loss for the year	(288,198)	(314,859)
<i>Other comprehensive income to be reclassified to profit or loss in subsequent years:</i>		
Currency translation adjustments	592,300	(887,109)
Total comprehensive profit/(loss) for the year	304,102	(1,201,968)
	2016 US\$	2015 US\$
Non-current assets	4,069,104	3,327,327
Current assets	198,788	71,104
Total assets	4,267,892	3,398,431
Non-current liabilities	(4,512,667)	(4,034,780)
Current liabilities	(287,913)	(200,441)
Total liabilities	(4,800,580)	(4,235,221)
Net Liabilities	(532,688)	(836,790)

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Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

7. Equity-accounted Investment in Joint Venture - Russian BD Holdings B.V. (continued)

Future minimum rentals payable under non-cancellable operating leases at the balance sheet date are as follows:

	2016 US\$	2015 US\$
Within one year	2,524	2,091
After one year but not more than five years	7,898	6,706
More than five years	25,751	22,010
	<u>36,173</u>	<u>30,807</u>

There were no capital commitments as at 31 December 2016 or 31 December 2015.

8. Financial assets - loans and receivables

	2016 US\$	2015 US\$
Loans to WorldAce Investments Limited (Note 14)	52,235,829	49,224,805
Less: share of WorldAce Investments Limited loss (Note 6)	<u>(8,246,586)</u>	<u>(9,516,618)</u>
	<u>43,989,243</u>	<u>39,708,187</u>
Loans to Russian BD Holdings B.V. (Note 14)	4,256,866	4,012,464
Less: share of Russian BD Holdings B.V. loss (Note 7)	<u>(532,688)</u>	<u>(836,790)</u>
	<u>3,724,178</u>	<u>3,175,674</u>
	<u>47,713,421</u>	<u>42,883,861</u>

The Company has granted a loan facility to its joint venture undertaking WorldAce Investments Limited of up to US\$45 million. This loan facility is US\$ denominated and unsecured. Interest currently accrues on the loan at USD LIBOR plus 6.0% but the Company has agreed not to seek payment of interest until 2018 at the earliest. The loan is set to mature on 31 December 2022. As at 31 December 2016 the loan was fully drawn down. The loan from the Company to Russian BD Holdings is repayable on demand. Interest currently accrues on the loan at USD LIBOR plus 5.0% per annum.

9. Inventories

	2016 US\$	2015 US\$
Materials	28,973	54,302
	<u>28,973</u>	<u>54,302</u>

PetroNeft Resources plc

Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

10. Trade and other receivables

	2016 US\$	2015 US\$
Other receivables	155,651	147,641
Receivable from jointly controlled entities (Note 14)	920,390	1,628,667
Advances to contractors	8,047	3,708
Prepayments	59,816	62,112
	<u>1,143,904</u>	<u>1,842,128</u>

Other receivables are non-interest-bearing and are normally settled on 60-day terms.

11. Cash and Cash Equivalents

	2016 US\$	2015 US\$
Cash at bank and in hand	319,618	1,284,212
	<u>319,618</u>	<u>1,284,212</u>

Bank deposits earn interest at floating rates based on daily deposit rates. Short-term deposits are made for varying periods of between one day and one month depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates.

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Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

12. Trade and other payables

	2016 US\$	2015 US\$
Trade payables	337,208	238,570
Trade payables to jointly controlled entity (Note 14)	108,338	239,228
Corporation tax	55,750	59,087
Oil taxes, VAT and employee taxes	56,165	78,293
Other payables	318,074	212,141
Accruals	206,546	317,827
	1,082,081	1,145,146

The Directors consider that the carrying amount of trade and other payables approximates their fair value.

Trade and other payables are non-interest-bearing and are normally settled on 60-day terms.

Trade payables and accruals principally comprise amounts outstanding for trade purchases and ongoing costs.

13. Share capital - Group and Company

Authorised

1,000,000,000 (2015: 1,000,000,000) Ordinary Shares of €0.01 each

2016 €	2015 €
10,000,000	10,000,000
10,000,000	10,000,000

Allotted, called up and fully paid equity

At 1 January 2015

At 1 January 2016

At 31 December 2016

Number of Ordinary Shares	Called up share capital US\$
707,245,906	9,429,182
707,245,906	9,429,182
707,245,906	9,429,182

PetroNeft Resources plc

Notes to the Preliminary Financial Statements

For the year ended 31 December 2016

14. Related party disclosures

Transactions with joint ventures

PetroNeft Resources plc had the following transactions with its joint ventures during the years ended 31 December 2016 and 2015:

	Russian BD Holdings BV Group US\$	WorldAce Investments Limited Group US\$
Receivable by PetroNeft Group at 1 January 2015	3,882,578	47,341,766
Transactions during the year	183,333	2,670,250
Interest accrued in the year	205,189	2,826,303
Payments for services made during the year	(29,781)	(2,483,727)
Share of joint venture's translation adjustment	(836,790)	(9,516,618)
Translation adjustment	(14,821)	45,618
At 1 January 2016	3,389,708	40,883,592
Advanced during the year	10,000	-
Transactions during the year	159,260	2,622,188
Interest accrued in the year	234,402	3,011,025
Payment for services made during the year	(10,821)	(3,426,007)
Share of joint venture's translation adjustment	304,102	1,270,032
Translation adjustment	(5,769)	83,761
At 31 December 2016	4,080,882	44,444,591
Balance at 31 December 2015 comprised of:		
Loan facility advanced	3,175,674	39,708,187
Trade and other receivables	214,034	1,414,633
Trade Payables	-	(239,228)
	3,389,708	40,883,592
Balance at 31 December 2016 comprised of:		
Loans receivable	3,724,178	43,989,243
Trade and other receivables	356,704	563,686
Trade and other payables	-	(108,338)
	4,080,882	44,444,591

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For the year ended 31 December 2016

14. Related party disclosures (continued)

Remuneration of key management

Key management comprise the Directors of the Company, the Vice Presidents of Business Development and Operations, the General Director and the Executive Director of the Russian subsidiary LLC Dolomite, along with both the Chief Geologist and Chief Engineer of LLC Dolomite. Their remuneration during the year was as follows:

Remuneration of key management

	2016 US\$	2015 US\$
Compensation of key management	1,923,326	1,715,340
Contributions to defined contribution pension plan	69,308	89,917
Share-based payment expense	-	15,401
	<u>1,992,634</u>	<u>1,820,658</u>

The total amount of unpaid fees and expenses due to Directors as at 31 December 2016 was US\$54,021 (2015: US\$143,536).

Details of transactions between the Group and other related parties are disclosed below.

Transactions with HGR Consulting Limited

Paul Dowling, Secretary and Chief Financial Officer of PetroNeft, provides his services through HGR Consulting Limited ("HGR") from May 2016. Services provided by HGR during 2016 amounted to US\$199,035. An amount of US\$116,031 was owed to HGR at 31 December 2016.

Transactions with TBNG Group

Vakha Sobraliev, Director of PetroNeft until his resignation on 18 September 2015, is the principal of LLC Tomskburneftegaz ("TBNG"), a company which has drilled production and exploration wells for the Group. Various contracts for drilling have been awarded to TBNG in recent years. All drilling contracts with TBNG are "turnkey" contracts whereby TBNG assumes substantially all liabilities in relation to the health and safety, environmental and other risks associated with drilling operation. As part of this arrangement WorldAce Group companies also occasionally sell sundry goods and services to TBNG. Other companies related to TBNG also provide some services to the Group such as transportation, power management and repairs. The following is a summary of the transactions:

	TBNG Group From 1 January to 18 September 2015 US\$
Maximum value of new contracts awarded during the period	1,778,324
Paid during the period for drilling and related services	5,379,260
Paid during the period for other services	2,023
Amount due to TBNG and related companies at period end	-
Received during the period for sundry goods and services	98,789
Amount due from TBNG and related companies at period end	<u>-</u>

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14. Related party disclosures (*continued*)

Other PetroNeft Group companies provided various services to TBNG Group during the period from 1 January to 18 September 2015 amounting to US\$536. An amount of US\$Nil was outstanding from TBNG Group at 18 September 2015.

The Group has an indirect 50% interest in Lineynoye which in turn is 100% owned by the jointly controlled entity Russian BD Holdings B.V. Lineynoye also entered into some transactions with TBNG and related companies as follows:

	TBNG Group From 1 January to 18 September 2015 US\$
Maximum value of new contracts awarded during the period	-
Paid during the period for drilling and related services	-
Paid during the period for other services	-
Amount due to TBNG and related companies at period end	-
Received during the period for sundry goods and services	4,114
Amount due from TBNG and related companies at period end	-

15. Important Events after the Balance Sheet Date

In March 2017, Oil India agreed to provide 100% funding for the agreed Licence 61 work programme in 2017. A loan of US\$4 million was agreed with the joint venture company, WorldAce Investments Limited, to fund the 2017 programme. The loan is unsecured and capital repayments commence in October 2019. Should there be a significant change in the management of PetroNeft while the loan is outstanding then Oil India may seek early repayment in full. In such circumstances PetroNeft would need to provide its 50% share of the amount outstanding.

16. Board approval

This announcement was approved by the Board of Directors of PetroNeft Resources plc on 27 June 2017.

PetroNeft Resources plc

Glossary

1P	Proved reserves according to SPE standards.
2P	Proved and probable reserves according to SPE standards.
3P	Proved, probable and possible reserves according to SPE standards.
AGM	Annual General Meeting.
AIM	Alternative Investment Market of the London Stock Exchange.
AMI	Area of Mutual Interest.
Arawak	Arawak Energy Russia B.V.
bbl	Barrel.
Belgrave Naftogas	Belgrave Naftogas B.V., a member of the Arawak group of companies
bfpd	Barrels of fluid per day.
boe	Barrel of oil equivalent.
bopd	Barrels of oil per day.
Company	PetroNeft Resources plc.
CPF	Central Processing Facility.
CSR	Corporate and Social Responsibility.
Custody Transfer Point	Facility/location at which custody of oil transfers to another operator.
Dolomite	LLC Dolomite, a 100% subsidiary of PetroNeft registered in the Russian Federation
DST	Drill stem test.
ESM	Enterprise Securities Market of the Irish Stock Exchange.
ESP	Electric Submersible Pump
Exploration resources	An undrilled prospect in an area of known hydrocarbons with unequivocal four-way dip closure at the reservoir horizon.
Granite Construction	LLC Granite Construction, a 100% subsidiary of PetroNeft registered in the Russian Federation
Group	The Company and its joint ventures and subsidiary undertakings.
HSE	Health, Safety and Environment.
IAS	International Accounting Standard.
IFRIC	IFRS Interpretations Committee.
IFRS	International Financial Reporting Standard.
km	Kilometres.
km ² / sq km	Square kilometres.
KPI	Key Performance Indicator.
Licence 61	The Exploration and Production Licence in the Tomsk Oblast, Russia owned by the joint venture company WorldAce Investments Limited. It contains seven known oil fields, Lineynoye, Tungolskoye, West Lineynoye, Arbuzovskoye, Kondrashevskoye, Sibkrayevskoye and North Varyakhskoye and 27 Prospects and Leads that are currently being explored.
Licence 61 Farmout	An agreement whereby Oil India Limited subscribed for shares in WorldAce, the holding company for Stimul-T, the entity which holds Licence 61 and all related assets and liabilities, and following, PetroNeft and Oil India Limited both hold 50% of the voting shares, and through the shareholders agreement, both parties have joint control of WorldAce with PetroNeft as operator
Licence 67	The Exploration and Production Licence in the Tomsk Oblast, Russia owned by the joint venture company Russian BD Holdings B.V. It contains two oil fields, Ledovoye and Cheremshanskoye and several potential prospects.

PetroNeft Resources plc

Glossary (continued)

Lineynoye	Limited Liability Company Lineynoye, a wholly owned subsidiary of Russian BD Holdings B.V., registered in the Russian Federation.
m	Metres.
mmbbls	Million barrels.
mmbo	Million barrels of oil.
Natlata	Natlata Partners Limited, a significant shareholder of PetroNeft.
Oil pay	A formation containing producible hydrocarbons.
P1	Proved reserves according to SPE standards.
P2	Probable reserves according to SPE standards.
P3	Possible reserves according to SPE standards.
PetroNeft	PetroNeft Resources plc.
Russian BD Holdings B.V.	Russian BD Holdings B.V., a company owned 50% by PetroNeft and registered in the Netherlands.
SPE	Society of Petroleum Engineers.
Spud	To commence drilling a well.
Stimul-T	Limited Liability Company Stimul-T, a wholly owned subsidiary of WorldAce, based in the Russian Federation.
TSR	Total Shareholder Return.
VAT	Value Added Tax.
WAEP	Weighted Average Exercise Price.
WorldAce	WorldAce Investments Limited, a company owned 50% by PetroNeft, registered in Cyprus.
WorldAce Group	WorldAce Investments Limited and its 100% subsidiary LLC Stimul-T