Good day, ladies and gentlemen, welcome to ALROSA’s conference call on Q3 and 9M 2016 IFRS results. I will make a few introductory notes.

Our top management team today is represented by Andrey Zharkov, CEO, and Igor Kulichik, CFO. Igor Kulichik will make a presentation and the Q&A session will be held by our CEO Andrey Zharkov. We will refer to the slides that were uploaded to the website.

As always, before we start the call, I would like to quote the disclaimer. Some of the information provided in this call may include forward-looking statements that involve risks, uncertainties and assumptions. If the risks or uncertainties ever materialize or assumptions prove incorrect, the results may differ materially from those expressed or implied by such forward-looking statements. ALROSA assumes no obligation and does not intend to update any of such forward-looking statements.

Now, I pass the floor to our CFO Igor Kulichik. Please.

Igor Kulichik (translated)

Colleagues, I am happy to welcome you to our Q3 and 9M 2016 results conference call.

The robust growth in Q1 2016, further recovery in the midstream demand for rough diamonds in Q2 and Q3 2016, coupled with the Company’s cost management initiatives have all contributed to the substantial improvements in ALROSA’s financial performance.

The Q4 2016 market demand remains stable, with October sales of USD 431 mln being on par with the previous month’s sales volumes.
ALROSA maintains its moderately conservative outlook for demand in the diamond market on the back of slack growth in diamond jewellery sales.

ALROSA’s key 9M 2016 financial highlights are shown on pages 3–4 of the presentation.

EBITDA was up 67% y-o-y to achieve RUB 150 bn, while EBITDA margin rose to 59% from 52% in 9M 2015.

Pages 5 and 6 discuss the changes in revenue. In 9M 2016, the Group's revenue grew by 48% y-o-y to RUB 255.6 bn. In USD terms, the revenue was up 29% y-o-y.

The 54% increase in revenue from diamond sales was driven by the 31% sales volumes growth, and also by the ruble weakening against the US dollar by 14% y-o-y in 9M 2016. A drop in the average price of the sold diamonds in 9M 2016 was primarily due to the Company's price cutting initiatives back in 2015.

Costs breakdown is shown on page 7. In 9M 2016, the cost of sales grew by 31% in line with the increase in diamond sales volumes.

Wages, salaries and other staff costs went up 5%, which was primarily caused by the pay level adjustments on par with the inflation rate in Russia.

The increase in depreciation was due to larger production at some of the sites of ALROSA and Severalmaz, and the commencement of production at AO Nizhne-Lenskoye’s Bolshaya Kuonamka and Talakhtakh alluvial placers.

The increase in materials costs was primarily due to the rising prices of materials, new production equipment launched at the Udachny underground mine, and expanded mining operations at AO Nizhne-Lenskoye’s alluvial placers.

Pages 8 and 9 of the presentation show EBITDA and net profit breakdown. In 9M 2016, EBITDA went up by 67% y-o-y to RUB 150 bn. The Group’s net profit grew more than three-fold y-o-y and reached RUB 116.9 bn.

Capex in 9M 2016 went down 11% as a result of further reduction in maintenance capex in line with the Group’s plan for 2016.

The relative increase in expansion capex, as you can see on page 11, is due to the development of transport infrastructure at the Verkhne-Munskoye deposit, which is located 170 km away from the settlement of Udachny.

Page 12 shows the breakdown of the Group’s free cash flow. It reached RUB 104,1 bn, which represents a considerable increase y-o-y and was driven by the growth in operating profit and the decrease in rough diamond inventories.

Currently, the rough diamond inventories stand at around 17 million carats, having dropped by more than 5 million carats year-to-date. We do not expect any further considerable decrease in diamond inventories until the year end, as in Q4, we typically see a seasonal increase in inventories due to sorting of rough diamonds mined from the alluvial deposits in summer.

The breakdown of our loans and borrowings is shown on page 13. In Q3 2016, the Group’s total debt remained flat at USD 2.7 bn.
As at 30 September 2016, net debt was USD 2.2 bn, with the leverage ratio at 0.8x. Please note that cash and cash equivalents do not include 90+ days deposits totalling more than USD 700 mln. Together with these deposits, the Company’s total liquidity cushion exceeds USD 1.2 bn that will be used to repay the loans ahead of schedule in 2016 and will serve as a source of liquidity for the Company’s 2017 expenses, including those related to dividends payouts.

This does conclude my presentation, and I suggest that we move on to the Q&A session now. Thank you.

Questions and Answers

Ksenia Mishankina – UBS

What is your optimal Net Debt / EBITDA? Do you plan to refinance any short-term debt?

Andrey Zharkov (translated)

We are comfortable with Net Debt / EBITDA within 2x. We are going to stay within 1.0x at 2016YE.

Considering refinancing and short-term loans and borrowings, next year we will prepay the Alfa-Bank loan. The respective agreement has almost been achieved.

Barry Ehrlich – Citi

Your 9M 2016 production dropped 6% y-o-y. On slide 7, if we remove depreciation from the reported cost of production, we can see that the cash cost of production rose 3% y-o-y. Taken together with the decline in production volumes, it looks like, on a unit basis, your costs rose about 10% in ruble terms.

Based on that, I have three questions.

First, do you agree with that calculation and logic?

Second, are you still planning to increase production in 2017?

Third, what are the factors that would cause unit costs to rise faster in 2017, if that is your expectation?

Andrey Zharkov (translated)

We agree with the calculations. However, there are also other drivers behind the cash cost increase (like inflation, etc.), not just reduced production volumes.

As to reduced production and its impact on cash cost, reduction in output at alluvial placers would add some 2–3% to cash costs, however, when we reduce production at our underground facilities, cash costs would rise more materially.

As for the 2017 production guidance, it will remain at least flat y-o-y or increase slightly. However, these targets are subject to our annual budgeting cycle and will be updated further on.

Nikolay Sosnovskiy – Prosperity

Two questions, first one is on the inventory levels. Can you disclose the composition of the diamond inventories at the beginning of the year and currently in terms of the split between gem quality and industrial quality diamonds?
Second, in late 2015 you substantially decreased prices (by about 15%). Now that the sales volumes have recovered, what are the potential conditions for an increase in the rough diamond prices to the previous level?

Andrey Zharkov (translated)

As for our inventory composition, the average price per carat was fluctuating during the year. At the beginning of the year, it stood at around USD 80 per carat and then dropped to USD 50–55 per carat, followed by another recovery cycle towards USD 60–70 per carat. This was due to higher-priced category demand growing and demand for cheaper category positions decreasing. Then we expanded the sales of cheaper category diamonds. The latter happened during 2H of the year after the price adjustment.

As for the overall price index, it indeed dropped by some 15% in 2015. In 2016, there were no major price adjustments; we were just rebalancing the price within the overall index, with up or down fluctuations of 2%. Speaking of potential drivers of price growth going forward, the current market priority is to maintain healthy midstream margins, so at the moment we see no reasons for major price increases.

Vahe Ovasapyan – Goldman Sachs

My first question is on the diamond market situation. ALROSA decreased sales in October vs September. De Beers demonstrated two consequential months of sales decreases, which, as I understand, could be explained by the festival season in India. Could we expect higher sales in November? Let us have a look at the diamond market: De Beers launched a new growth project, Grib continues to ramp up, and generally the market expects higher supply next year as compared to 2016. Yet neither ALROSA, nor other experts expect substantial growth in demand for diamonds. What do you think about the supply and demand balance next year? Could we expect lower prices in this environment for 2017?

My second question is on your leverage and dividends. The Company’s effective Net Debt to EBITDA ratio stands at 0.5x, if we include the 90+ days deposits in the cash and cash equivalents. I understand you are comfortable with your Net Debt to EBITDA ratio of 0.5x. So, what are you planning to do with that huge cash pile that should be generated next year, even if your payout ratio is 50%?

Andrey Zharkov (translated)

Let us start with your second question. The core spending targets for our free cash flow are deleveraging and dividends. That is how we are going to spend that liquidity cushion.

Now I will go back to your first question about the market environment. After our sales were down in 2015 and then we saw a material recovery in 2016, we expect that in 2017 the markets and the demand will be stable. We currently see no reasons for either sharp reduction or sharp increases in market demand. So our top strategic priority now is to reduce the level of inventories and try to sell as much as we produce.

Ksenia Mishankina – UBS

Can you please provide guidance for capex and volumes of gem-quality diamonds to be sold in 2017?

Andrey Zharkov (translated)

Our capex for 2017 is going to stay flat. We see no prerequisites for sharp growth in capex. As for our sales volumes, they are also going to stay flat. However, the budgeting cycle for 2017 is now in progress. After
our Supervisory Board approves the budget and business plan for 2017 we will duly disclose this to the market community.

Ksenia Mishankina – UBS

When you are talking about flat capex in 2017, is that in ruble terms?

Andrey Zharkov (translated)

Yes, that is in rubles. Please note that the budgeting cycle is not yet over. As a ballpark number, we are going to keep it at RUB 32 bn, which is flat as compared to 2016. We will update you as soon as any adjustments are there.

Alexandra Falkova – Sberbank

Could you give us an update on the capex number for this year? As far as I remember, your previous guidance was around RUB 38.9 bn for 2016, and in 9M 2016, the actual capex is only around RUB 21 bn. Should we expect any considerable reduction of capex vs your previous plans or a kind of spillover of capex to 2017?

Andrey Zharkov (translated)

Our capex levels next year are going to stay flat vs 2016 because of some spillover of capex related to Verkhne-Munskoye deposit. Due to weather conditions some of the development works at Verkhne-Munskoye are going to migrate to next year. So, our capex for 2016 is going to be some 15% down vs the 2016 budget and about 8% down y-o-y. This will be rolled over to 2017 and hence, again, the 2017 capex is going to stay flat vs the 2016 budget.

Boris Sinitsyn – VTB Capital

The first question is on your inventory reduction. It seems like you have managed to reduce your diamond inventory by 2.9 mln carats so far this quarter. Correct me if I am wrong, I am comparing the level of current stockpile and the level as of the end of Q3 2016, which is impressive. So, do you expect a marginal build-up in inventory in December could you reiterate your annual production guidance for this year. The second question is whether you expect any changes in product mix next year, and, if you do, what could be the effect on your average realised price, all other factors being fixed? The third question is on your export duty cancellation. I understand Q4 2016 will be the first quarter of no duty. How does it work, assuming that you do not increase your prices for diamond sales? Would you still benefit from export duty reduction and still receive some amount of cash as a result of this reduction or would you need to increase prices in order to get this benefit?

Andrey Zharkov (translated)

As for your first question about inventories. At 2016YE, we expect our inventories to be down about 10% y-o-y.

As for the product mix and demand-linked fluctuations, I can say that demand is constantly evolving category to category. In 2016, for example, we saw a brisk demand for higher-priced categories of rough diamonds. However, in India they launch a number of marketing projects to stimulate demand for cheaper-priced categories. So, this is a living thing. The demand is constantly fluctuating and equalizing, and for 2017, we do not expect any specific shifts or moves in the product mix demand.
As for the export duty, it was indeed cancelled as of 1 September 2016. However, the prices in the global market will not grow as a result of this. The prices got equalized in the global market and the domestic market. Actually, it was the domestic market that was brought to the level of the international market price. Effectively, we will be saving on the export duty expenses going forward.

**Boris Sinitsyn – VTB Capital**

Thank you very much. Could you reiterate that the production guidance of 37 mln carats is still intact for this year?

**Andrey Zharkov (translated)**

Yes, we do reiterate our production guidance for this year to stand at 37 mln carats.

**Dan Shaw – Morgan Stanley**

Do you expect to see any impact on demand from India given a change in the availability of banknotes and a potential impact on liquidity in the system?

**Andrey Zharkov (translated)**

Yes, we do expect some impact on demand in the short-term, I mean, on the horizon of 3–5 months. There is a monetary reform, you have mentioned going on in India, and we expect that it will affect the cheaper-priced categories that are polished and then sold inside India.

**Andrey Zharkov (translated)**

Thank you very much to all of you for taking part in our Q3 and 9M 2016 results call. We hope, we have answered all your questions. In case any further questions arise, please feel free to reach out to our IR team and we will be happy to take your further questions. Thank you.