

Mechel OAO  
Form 20-F  
April 26, 2017  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**Form 20-F**

**REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**OR**

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934**

**For the fiscal year ended December 31, 2016**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934**

**OR**

**SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934**

**Commission file number 001-32328**

**MECHEL PAO**

**(Exact name of Registrant as specified in its charter)**

**RUSSIAN FEDERATION**

**(Jurisdiction of incorporation or organization)**

**Krasnoarmeyskaya Street 1, Moscow 125167, Russian Federation**

**(Address of principal executive offices)**

**Alexey Lukashov, tel.: +7-495-221-8888, e-mail: [alexey.lukashov@mechel.com](mailto:alexey.lukashov@mechel.com)**

**(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)**

**Securities registered or to be registered pursuant to Section 12(b) of the Act:**

<b>Title of Each Class</b>	<b>Name of Each Exchange on Which Registered</b>
<b>COMMON AMERICAN DEPOSITARY SHARES, EACH COMMON ADS REPRESENTING TWO COMMON SHARES COMMON SHARES, PAR VALUE</b>	<b>NEW YORK STOCK EXCHANGE</b>
<b>10 RUSSIAN RUBLES PER SHARE</b>	<b>NEW YORK STOCK EXCHANGE<sup>(1)</sup></b>
<b>PREFERRED AMERICAN DEPOSITARY SHARES, EACH PREFERRED ADS REPRESENTING ONE-HALF OF A PREFERRED SHARE PREFERRED SHARES, PAR VALUE</b>	<b>NEW YORK STOCK EXCHANGE</b>
<b>10 RUSSIAN RUBLES PER SHARE</b>	<b>NEW YORK STOCK EXCHANGE<sup>(2)</sup></b>

**Securities registered or to be registered pursuant to Section 12(g) of the Act:**

**None**

**(Title of Class)**

**Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act:**

**None**

**(Title of Class)**

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

416,270,745 common shares, of which 82,266,622 shares are in the form of common ADSs as of March 31, 2017

138,756,915 preferred shares (including 55,502,766 shares held by Skyblock Limited, a wholly-owned subsidiary of Mechel), of which 9,359,432 shares are in the form of preferred ADSs as of March 31, 2017

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes No

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check One):

Large accelerated filer Accelerated filer Non-accelerated filer  
Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP International Financial Reporting Standards as issued by the International Accounting Standards Board Other

If "Other" has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

- (1) Listed, not for trading or quotation purposes, but only in connection with the registration of common ADSs pursuant to the requirements of the Securities and Exchange Commission.
- (2) Listed, not for trading or quotation purposes, but only in connection with the registration of preferred ADSs pursuant to the requirements of the Securities and Exchange Commission.

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Unless the context otherwise requires, references to Mechel refer to Mechel PAO, and references to Mechel group, our group, we, us or our refer to Mechel PAO together with its subsidiaries.

Our business consists of three segments: mining, steel and power. References in this document to segment revenues are to revenues of the segment excluding intersegment sales, unless otherwise noted. References in this document to our sales or our total sales are to third-party sales and do not include intra-group sales, unless otherwise noted.

For the purposes of calculating certain market share data, we have included businesses that are currently part of our group that may not have been part of our group during the period for which such market share data is presented.

The presentation currency of our consolidated financial statements is the Russian ruble. Before transition to IFRS, U.S. dollar was the presentation currency of our consolidated financial statements prepared under U.S. GAAP. The

reason of adopting the Russian ruble as the presentation currency in the consolidated statements

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under IFRS is to allow a greater transparency of our financial and operating performance as it more closely reflects the profile of our revenue and operating income that are mostly generated in Russian rubles.

References to Russian rubles, rubles or RUB are to the currency of the Russian Federation, references to U.S. dollars, \$ or USD are to the currency of the United States and references to euro, or EUR are to the currency of the member states of the European Union that participate in the European Monetary Union.

The term tonne as used herein means a metric tonne. A metric tonne is equal to 1,000 kilograms or 2,204.62 pounds. The term short ton is also used in this document. A short ton is equal to 907 kilograms or 2,000 pounds.

Certain amounts that appear in this document have been subject to rounding adjustments; accordingly, figures shown as totals in certain tables or in the text may not be an arithmetic aggregation of the figures that precede them.

CIS means the Commonwealth of Independent States.

The following table sets forth by business activity the official names and location of our key subsidiaries and their names as used in this document:

<b>Name as Used in This Document</b>	<b>Official Name</b>	<b>Location</b>
<b><i>Mining</i></b>		
Mechel Mining	Mechel Mining AO <sup>(1)</sup>	Russia, Moscow
Southern Kuzbass Coal Company	Southern Kuzbass Coal Company PAO <sup>(1)</sup>	Russia, Kemerovo region
Yakutugol	Yakutugol Joint-Stock Holding Company <sup>(1)</sup>	Russia, Sakha Republic
Elgaugol	Elgaugol OOO	Russia, Sakha Republic
Korshunov Mining Plant	Korshunov Mining Plant PJSC <sup>(1)</sup>	Russia, Irkutsk region
Moscow Coke and Gas Plant	Moscow Coke and Gas Plant JSC <sup>(1)</sup>	Russia, Moscow region
Mechel Coke	Mechel Coke OOO	Russia, Chelyabinsk region
Port Posiet	Port Posiet JSC <sup>(1)</sup>	Russia, Primorsk Krai
Port Temryuk	Port Mechel Temryuk OOO	Russia, Krasnodar Krai
<b><i>Steel</i></b>		
Chelyabinsk Metallurgical Plant	Chelyabinsk Metallurgical Plant PAO <sup>(1)</sup>	Russia, Chelyabinsk region
Izhstal	Izhstal OAO	Russia, Republic of Udmurtia
Urals Stampings Plant	Urals Stampings Plant PAO <sup>(1)</sup>	Russia, Chelyabinsk region
Beloretsk Metallurgical Plant	Beloretsk Metallurgical Plant AO <sup>(1)</sup>	Russia, Republic of Bashkortostan
Vyartsilya Metal Products Plant	Vyartsilya Metal Products Plant ZAO	Russia, Republic of Karelia
Mechel Nemunas	Mechel Nemunas UAB	Lithuania
Bratsk Ferroalloy Plant	Bratsk Ferroalloy Plant OOO	Russia, Irkutsk region
Port Kambarka	Port Kambarka OAO	Russia, Republic of Udmurtia





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<b>Name as Used in This Document</b>	<b>Official Name</b>	<b>Location</b>
<b><i>Power</i></b>		
Southern Kuzbass Power Plant	Southern Kuzbass Power Plant OAO	Russia, Kemerovo region
Kuzbass Power Sales Company	Kuzbass Power Sales Company OAO	Russia, Kemerovo region
Mechel Energo	Mechel Energo OOO	Russia, Chelyabinsk region
<b><i>Marketing and Distribution</i></b>		
Mechel Carbon	Mechel Carbon AG	Switzerland, Baar
Mechel Trading	Mechel Trading AG	Switzerland, Baar
Mechel Service Global	Mechel Service Global B.V.	Netherlands
Mechel Service	Mechel Service OOO	Russia, Moscow
<b><i>Other</i></b>		
Mecheltrans	Mecheltrans OOO	Russia, Moscow

- (1) The legal organizational form of our Russian subsidiaries and Mechel has been changed in accordance with the current legislation of the Russian Federation.

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**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

Matters discussed in this document may constitute forward-looking statements, as defined in the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. We wish to caution you that these statements are only predictions and that actual events or results may differ materially. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance, and underlying assumptions and other statements, which are other than statements of historical facts. The words believe, expect, anticipate, intend, estimate, forecast, project, will, may, should and similar expressions identify forward-looking statements. Forward-looking statements appear in a number of places including, without limitation, Item 3. Key Information Risk Factors, Item 4. Information on the Company and Item 5. Operating and Financial Review and Prospects, and include statements regarding:

strategies, outlook and growth prospects;

the ability to maintain and generate sufficient cash and other liquid resources to meet our operating and debt service requirements;

our ability to comply with the financial covenants in our loan agreements as well as other covenants and restrictions imposed by the existing and future financing arrangements and our ability to attract new financing or refinancing of debt, including an outcome in the ongoing debt restructuring negotiations with our lenders;

the impact of competition;

costs of our acquisitions and ability to realize expected synergies and other benefits;

capital expenditures;

demand for our products;

economic outlook and industry trends;

transactions with related parties;

regulatory compliance;

developments in our markets;

future plans and potential for future growth;

the results of any legal procedures;

the impact of regulatory initiatives; and

the strength of our competitors.

The forward-looking statements in this document are based upon various assumptions, many of which are based, in turn, upon further assumptions, including without limitation, management's examination of historical operating trends, data contained in our records and other data available from third parties. Although we believe that these assumptions were reasonable when made, these assumptions are inherently subject to significant uncertainties and contingencies which are difficult or impossible to predict and are beyond our control and we may not achieve or accomplish these expectations, beliefs or projections. See Item 3. Key Information Risk Factors for a discussion of important factors that, in our view, could cause actual results to differ materially from those discussed in the forward-looking statements.

Except to the extent required by law, neither we, nor any of our agents, employees or advisers intend or have any duty or obligation to supplement, amend, update or revise any of the forward-looking statements contained or incorporated by reference in this document.

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**PART I**

**Item 1. *Identity of Directors, Senior Management and Advisers***

Not applicable.

**Item 2. *Offer Statistics and Expected Timetable***

Not applicable.

**Item 3. *Key Information***

**Selected Financial Data**

The financial data set forth below as of December 31, 2016, 2015 and 2014, and for the years then ended, have been derived from our consolidated financial statements. Our reporting currency is the Russian ruble and we prepare our consolidated financial statements in accordance with International Financial Reporting Standards ( **IFRS** ).

The consolidated financial statements for the year ended December 31, 2015 were the first we had prepared in accordance with IFRS. The date of transition to IFRS was January 1, 2014. For periods up to and including the year ended December 31, 2014, we prepared our consolidated financial statements in accordance with U.S. GAAP. Accordingly, we have prepared financial statements that comply with IFRS applicable as of December 31, 2016, together with the comparative periods data for the years ended December 31, 2015 and 2014.

Pursuant to the transitional relief granted by the U.S. SEC in respect of the first-time adoption of IFRS, we have only provided financial statements and financial information for two fiscal years ended December 31, 2015 in the previously filed annual report for the year ended December 31, 2015 as presented under IFRS, we have provided financial statements and financial information for three fiscal years ended December 31, 2016 herein. The selected financial information as of and for the years ended December 31, 2016, 2015 and 2014 set forth below should be read in conjunction with, and is qualified in its entirety by reference to Item 5. Operating and Financial Review and Prospects and our audited consolidated financial statements and the notes thereto included in this annual report.

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Our results of operations for the periods presented are affected by disposals. See note 1(a) to the consolidated financial statements. The financial data below should be read in conjunction with, and is qualified in its entirety by reference to, our consolidated financial statements and Item 5. Operating and Financial Review and Prospects.

	<b>Year Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	<b>(In millions of Russian rubles, unless stated otherwise)</b>		
<b>Consolidated statement of profit (loss) and other comprehensive income (loss) data:</b>			
Revenue	276,009	253,141	243,992
Cost of goods sold	(146,322)	(151,334)	(153,057)
Gross profit	129,687	101,807	90,935
Total selling, distribution and operating income and (expenses), net	(86,997)	(77,555)	(90,028)
Operating profit	42,690	24,252	907
Total other income and (expense), net	(28,539)	(131,380)	(131,994)
Profit (loss) before tax from continuing operations	14,151	(107,128)	(131,087)
Income tax (expense) benefit	(4,893)	(8,322)	8,822
Profit (loss) for the year from continuing operations	9,258	(115,450)	(122,265)
(Loss) profit after tax for the year from discontinued operations, net	(426)	822	(11,702)
Profit (loss) for the year	8,832	(114,628)	(133,967)
Less: profit (loss) attributable to non-controlling interests	1,706	535	(1,263)
Profit (loss) attributable to equity shareholders of Mechel PAO	7,126	(115,163)	(132,704)
Profit (loss) for the year	8,832	(114,628)	(133,967)
Exchange differences on translation of foreign operations	431	287	1,168
Net (loss) gain on available for sale financial assets	(1)	8	2
Re-measurement losses on defined benefit plans	(23)	(194)	(127)
<b>Total comprehensive income (loss) for the year, net of tax</b>	<b>9,239</b>	<b>(114,527)</b>	<b>(132,924)</b>
Total comprehensive income (loss) attributable to non-controlling interests	1,710	537	(1,249)
Total comprehensive income (loss) attributable to equity shareholders of Mechel PAO	7,529	(115,064)	(131,675)
Earnings (loss) per share from continuing operations (in Russian rubles per share) basic and diluted	18	(278)	(290)
	(1)	2	(29)

(Loss) earnings per share from discontinued operations (in Russian rubles per share)

Basic and diluted, earnings (loss) for the year attributable to common equity shareholders of Mechel PAO	17	(277)	(319)
Cash dividends per common share			

Cash dividends per preferred share

Weighted average number of common shares	416,270,745	416,270,745	416,270,745
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**Mining segment statement of profit (loss) data<sup>(1)</sup>:**

Revenue	121,555	108,723	100,558
Cost of goods sold	(45,040)	(51,280)	(51,435)

Gross profit	76,515	57,442	49,123
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	Year Ended December 31,		
	2016	2015	2014
(In millions of Russian rubles, unless stated otherwise)			
Total selling, distribution and operating income and (expenses), net	(45,503)	(41,437)	(47,405)
Operating profit	31,012	16,005	1,718
<b>Steel segment statement of profit (loss) data<sup>(1)</sup>:</b>			
Revenue	168,893	153,004	146,867
Cost of goods sold	(126,745)	(119,610)	(115,485)
Gross profit	42,148	33,394	31,382
Total selling, distribution and operating income and (expenses), net	(30,617)	(24,868)	(32,701)
Operating profit (loss)	11,531	8,526	(1,319)
<b>Power segment statement of profit (loss) data<sup>(1)</sup>:</b>			
Revenue	40,625	41,467	39,554
Cost of goods sold	(29,047)	(30,178)	(29,215)
Gross profit	11,578	11,289	10,339
Total selling, distribution and operating income and (expenses), net	(10,877)	(11,250)	(9,922)
Operating profit	701	39	417
<b>Consolidated statement of financial position data (at period end):</b>			
Total assets	325,465	342,071	369,258
Equity attributable to equity shareholders of Mechel PAO	(260,274)	(267,803)	(154,666)
Equity attributable to non-controlling interests	7,687	5,948	8,253
Interest-bearing loans and borrowings, including interest payable, fines and penalties on overdue amounts of RUB 38,594 million, RUB 47,475 million and RUB 14,615 million as of December 31, 2016, 2015 and 2014, respectively	434,165	491,674	386,518
Non-current interest-bearing loans and borrowings	11,644	4,308	9,346
<b>Consolidated statement of cash flows data:</b>			
Net cash provided by operating activities	53,207	38,867	43,013
Net cash used in investing activities	(4,969)	(5,218)	(14,494)
Net cash used in financing activities	(45,869)	(34,433)	(34,206)
<b>Non-IFRS measures<sup>(2)</sup>:</b>			
Consolidated Adjusted EBITDA	66,164	45,730	29,759
Mining Segment Adjusted EBITDA	41,884	26,831	13,359
Steel Segment Adjusted EBITDA	23,172	17,127	14,906
Power Segment Adjusted EBITDA	1,662	2,090	1,403

- (1) Segment revenues and cost of goods sold include intersegment sales.
- (2) Adjusted EBITDA represents net profit (loss) attributable to shareholders of Mechel PAO before depreciation and depletion, foreign exchange (gain) loss, net, finance costs, including fines and penalties on overdue loans and borrowings and finance lease payments, finance income, net result on the disposal of non-current assets, impairment of goodwill and other non-current assets, write-off of accounts receivable, allowance for doubtful accounts, write-off of inventories to net realizable value, loss (profit) after tax for the year from discontinued operations, net, net result on the disposal of subsidiaries, profit (loss) attributable to non-controlling interests, income tax expense (benefit), pension service cost and actuarial loss, other related expenses, other fines and penalties, gain on write-off of accounts payable with expired legal term, other one-off items.



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Reconciliation of Adjusted EBITDA to net profit (loss) attributable to shareholders of Mechel PAO is as follows for the periods indicated:

	<b>Year Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	<b>(In millions of Russian rubles)</b>		
<b>Consolidated Adjusted EBITDA reconciliation:</b>			
Net profit (loss) attributable to shareholders of Mechel PAO	7,126	(115,163)	(132,704)
Add:			
Depreciation and depletion	13,714	14,085	14,429
Foreign exchange (gain) loss, net	(25,947)	71,106	103,176
Finance costs, including fines and penalties on overdue loans and borrowings and finance lease payments	54,240	60,452	28,110
Finance income	(1,176)	(183)	(107)
Net result on the disposal of non-current assets, impairment of goodwill and other non-current assets, write-off of accounts receivable, allowance for doubtful accounts and write-off of inventories to net realizable value	8,447	4,772	12,710
Loss (profit) after tax for the year from discontinued operations, net	426	(932)	11,702
Net result on the disposal of subsidiaries	(194)	19	89
Profit (loss) attributable to non-controlling interests	1,706	535	(1,263)
Income tax expense (benefit)	4,893	8,322	(8,822)
Pension service cost and actuarial loss, other related expenses	(171)	50	(6)
Other fines and penalties	1,396	1,598	915
Gain on write-off of accounts payable with expired legal term	(115)	(224)	(38)
Other one-off items	1,819	1,293	1,568
<b>Consolidated Adjusted EBITDA</b>	<b>66,164</b>	<b>45,730</b>	<b>29,759</b>
<b>Mining Segment Adjusted EBITDA reconciliation:</b>			
Net profit (loss) attributable to shareholders of Mechel PAO	1,797	(71,120)	(86,787)
Add:			
Depreciation and depletion	7,912	9,106	8,747
Foreign exchange (gain) loss, net	(14,960)	49,872	70,553
Finance costs, including fines and penalties on overdue loans and borrowings and finance lease payments	39,345	33,880	15,045
Finance income	(2,482)	(1,030)	(777)
Net result on the disposal of non-current assets, impairment of goodwill and other non-current assets, write-off of accounts receivable, allowance for doubtful accounts and write-off of inventories to net realizable value	2,584	900	1,357
(Profit) loss after tax for the year from discontinued operations, net		(764)	13,141
Net result on the disposal of subsidiaries			
Profit (loss) attributable to non-controlling interests	511	(444)	(971)
Income tax expense (benefit)	5,019	5,632	(8,435)
Pension service cost and actuarial loss, other related expenses	(198)	125	(5)
Other fines and penalties	556	707	755
Gain on write-off of accounts payable with expired legal term	(19)	(33)	(2)

Other one-off items	1,819		741
Mining Segment Adjusted EBITDA	41,884	26,831	13,359

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	<b>Year Ended December 31,</b>		
	<b>2016</b>	<b>2015</b>	<b>2014</b>
	<b>(In millions of Russian rubles)</b>		
<b>Steel Segment Adjusted EBITDA reconciliation:</b>			
Net profit (loss) attributable to shareholders of Mechel PAO	6,399	(41,438)	(45,356)
Add:			
Depreciation and depletion	5,435	4,650	5,391
Foreign exchange (gain) loss, net	(10,904)	21,122	32,910
Finance costs, including fines and penalties on overdue loans and borrowings and finance lease payments	17,411	25,645	12,966
Finance income	(2,234)	(344)	(390)
Net result on the disposal of non-current assets, impairment of goodwill and other non-current assets, write-off of accounts receivable, allowance for doubtful accounts and write-off of inventories to net realizable value	5,389	2,122	10,658
Profit after tax for the year from discontinued operations, net	406	(168)	(1,468)
Net result on the disposal of subsidiaries	(194)	19	89
Profit (loss) attributable to non-controlling interests	1,056	812	(408)
Income tax (benefit) expense	(265)	2,794	(374)
Pension service cost and actuarial loss, other related expenses	26	(81)	(7)
Other fines and penalties	742	890	189
Gain on write-off of accounts payable with expired legal term	(95)	(190)	(35)
Other one-off items		1,263	742
<b>Steel Segment Adjusted EBITDA</b>	<b>23,172</b>	<b>17,127</b>	<b>14,906</b>
<b>Power Segment Adjusted EBITDA reconciliation:</b>			
Net (loss) profit attributable to shareholders of Mechel PAO	(517)	(2,286)	(651)
Add:			
Depreciation and depletion	367	329	291
Foreign exchange (gain) loss, net	(83)	111	(287)
Finance costs, including fines and penalties on overdue loans and borrowings and finance lease payments	1,078	2,173	1,208
Finance income	(54)	(55)	(48)
Net result on the disposal of non-current assets, impairment of goodwill and other non-current assets, write-off of accounts receivable, allowance for doubtful accounts and write-off of inventories to net realizable value	474	1,751	696
Loss after tax for the year from discontinued operations, net	20		29
Net result on the disposal of subsidiaries			
Profit (loss) attributable to non-controlling interests	139	166	114
Income tax expense (benefit)	139	(103)	(13)
Pension service cost and actuarial loss, other related expenses	2	6	7
Other fines and penalties	98		(29)
Gain on write-off of accounts payable with expired legal term	(1)	(1)	
Other one-off items			86
<b>Power Segment Adjusted EBITDA</b>	<b>1,662</b>	<b>2,090</b>	<b>1,403</b>



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Adjusted EBITDA is a measure of our operating performance that is not required by, or presented in accordance with, IFRS. Adjusted EBITDA is not a measure of our operating performance under IFRS and should not be considered as an alternative to net income, operating income or any other performance measures derived in accordance with IFRS or as an alternative to cash flow from operating activities or as a measure of our liquidity. In particular, Adjusted EBITDA should not be considered as a measure of discretionary cash available to us to invest in the growth of our business.

Adjusted EBITDA has limitations as an analytical tool, and should not be considered in isolation or as a substitute for analysis of our operating results as reported under IFRS. Some of these limitations are as follows:

Adjusted EBITDA does not reflect the impact of depreciation and depletion on our operating performance. The assets of our businesses which are being depreciated and depleted (including, for example, our mineral reserves) will have to be replaced in the future and such depreciation and depletion expense may approximate the cost to replace these assets in the future. By excluding such expense from Adjusted EBITDA, Adjusted EBITDA does not reflect our future cash requirements for such replacements.

Adjusted EBITDA does not reflect the impact of foreign exchange gains and losses, which may recur.

Adjusted EBITDA does not reflect the impact of finance income and finance costs, including fines and penalties on overdue loans and borrowings and finance lease payments, which are significant and could further increase if we incur more debt, on our operating performance.

Adjusted EBITDA does not reflect the impact of the net result on the disposal of non-current assets on our operating performance, which may recur.

Adjusted EBITDA does not reflect the impact of impairment of goodwill and other non-current assets, which may recur.

Adjusted EBITDA does not reflect the impact of write-off of accounts receivable, which may recur.

Adjusted EBITDA does not reflect the impact of allowance for doubtful accounts, which may recur.

Adjusted EBITDA does not reflect the impact of write-off of inventories to net realizable value, which may recur.

Adjusted EBITDA does not reflect the impact of profits and losses after tax for the year from discontinued operations.

Adjusted EBITDA does not reflect the impact of net result on the disposal of subsidiaries.

Adjusted EBITDA does not reflect the impact of profits and losses attributable to non-controlling interests on our operating performance.

Adjusted EBITDA does not reflect the impact of income tax expenses and benefits on our operating performance.

Adjusted EBITDA does not reflect the impact of pension service cost and actuarial loss, other related expenses.

Adjusted EBITDA does not reflect the impact of other fines and penalties.

Adjusted EBITDA does not reflect the impact of gain on write-off of accounts payable with expired legal term.

Adjusted EBITDA does not reflect the impact of other one-off items.

Other companies in our industry may calculate Adjusted EBITDA differently or may use it for different purposes than we do, limiting its usefulness as a comparative measure.

We compensate for these limitations by relying primarily on our IFRS operating results and using Adjusted EBITDA only supplementally. See our consolidated statement of financial position, consolidated statement of profit (loss) and other comprehensive income (loss) and consolidated statement of cash flows included elsewhere in this document.

**Table of Contents****Exchange Rates**

The following tables show, for the periods indicated, certain information regarding the official exchange rate between the ruble and the U.S. dollar, based on data published by the Central Bank of the Russian Federation (the **CBR** ).

These rates may differ from the actual rates used in preparation of our financial statements and other financial information provided herein.

Year Ended December 31,	Rubles per U.S. Dollar			
	High	Low	Average <sup>(1)</sup>	Period End
2016	83.59	60.27	67.03	60.66
2015	72.88	49.18	60.96	72.88
2014	67.79	32.66	38.42	56.26
2013	33.47	29.93	31.85	32.73
2012	34.04	28.95	31.09	30.37

(1) The average of the exchange rates on the last business day of each full month during the relevant period.

	Rubles per U.S. Dollar	
	High	Low
March 2017	59.22	56.38
February 2017	60.31	56.77
January 2017	60.66	59.15
December 2016	65.24	60.27
November 2016	65.86	63.20
October 2016	63.40	62.05

The exchange rate between the ruble and the U.S. dollar on April 26, 2017 was 55.85 rubles per one U.S. dollar.

No representation is made that the ruble or U.S. dollar amounts in this document could have been or can be converted into U.S. dollars or rubles, as the case may be, at any particular rate or at all.

**Risk Factors**

*An investment in our shares and ADSs involves a high degree of risk. You should carefully consider the following information about these risks, together with the information contained in this document, before you decide to buy our shares or ADSs. If any of the following risks actually occurs, our business, financial condition, results of operations or prospects could be materially adversely affected. In that case, the value of our shares or ADSs could also decline and you could lose all or part of your investment.*

**Risks Relating to Our Financial Condition and Financial Reporting**

*There is substantial doubt about our ability to continue as a going concern.*

As discussed in note 4 to our consolidated financial statements in Item 18. Financial Statements, because we have significant debt that we do not have the ability to repay without refinancing or restructuring, and our ability to do so is dependent upon continued negotiations with the banks, there is substantial doubt about our ability to continue as a going concern. We also note that there was a default on payments of principal and interest to certain lenders and lessors. In addition, we have been in non-compliance with certain financial and non-financial covenants in several loan agreements. See We face pressure on our liquidity, negatively influencing our working capital, which resulted from the acquisitions, substantial investment program, decrease



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in prices on commodity markets, global economic slowdown, difficulties with attracting new financing or refinancing of our debt and our need to service debt along with international sanctions against Russia and Russian state-owned banks, Our failure to comply with the payment and other obligations in our credit facilities caused some of our creditors to accelerate amounts due under their loan agreements and such failure, or like failure in the future, may cause the acceleration of our other outstanding debt, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects, If we are unable to restructure all of our indebtedness or fail to comply with the new terms of the restructured indebtedness, our lenders may claim for accelerated repayment, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects, We have a substantial amount of outstanding indebtedness with restrictive financial covenants and most shares and assets in our subsidiaries are pledged and We have not fulfilled our payment obligations under several of the group's lease agreements and a number of the respective lessors have required the return of the leased assets, which may materially adversely affect our business, financial condition, results of operations and prospects. Although as of December 31, 2016 restructuring agreements with our major lenders, such as Gazprombank, VTB Bank and Sberbank, were signed and became effective and restructuring agreements with our major lessors, such as Sberbank Leasing AO and VTB Leasing JSC, were entered into we still have a number of creditors to which the debt is overdue and such creditors could (have the legal right to) request for accelerated repayment of a significant portion of our debt and initiate legal procedures for enforcement of our debts. We do not have the resources to repay overdue debt or to enable us to comply with accelerated repayment requests immediately. Our plans, including the achievement of the restructuring with all of our lenders and aligning the servicing of our debt with new repayment schedules and projected cash flows to be generated by our group in 2017 and beyond, are discussed in Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Outlook for 2017 and note 4 to our consolidated financial statements in Item 18. Financial Statements. Our future is dependent on our ability to refinance or restructure our indebtedness successfully or otherwise address these matters. If we fail to do so for any reason, we would not be able to continue as a going concern and could potentially be forced to seek relief under applicable bankruptcy or insolvency procedures, in which case our shares and ADSs would lose all or a substantial amount of their value. However, given management's plans, our consolidated financial statements have been prepared on the basis that we will continue as a going concern entity, and no adjustments have been made in our consolidated financial statements relating to the recoverability and classification of the recorded value of assets, the amounts and classification of liabilities or any other adjustments that might result in any potential impact of us not being able to refinance our debt obligations as outlined in note 4 to our consolidated financial statements in Item 18. Financial Statements.

*We face pressure on our liquidity, negatively influencing our working capital, which resulted from the acquisitions, substantial investment program, decrease in prices on commodity markets, global economic slowdown, difficulties with attracting new financing or refinancing of our debt and our need to service debt along with international sanctions against Russia and Russian state-owned banks.*

Due, inter alia, to a substantial increase in our total indebtedness in 2007 and early 2008, together with a substantial decrease in prices on commodity markets, we experienced a liquidity shortage in late 2008 and early 2009 and in order to address the liquidity shortage during 2008 through 2011 we obtained significant loans.

Starting from the second half of 2012 and gradually worsening during 2013 and into 2014, a second phase of economic and financial difficulties unfolded. To alleviate the pressure on our liquidity, in 2013, we refinanced and restructured a number of major loans mainly with Russian state-owned banks and issued Russian ruble bonds in order to refinance our debts. Additionally, in December 2013, we restructured our \$1.0 billion pre-export facilities with a syndicate of banks.

In the first half of 2014, we experienced a shortage of liquidity and difficulties with refinancing of our debt; as a result, we failed to fulfill our payment obligations in connection with the servicing of interest and the repayment of our indebtedness. We held discussions with our creditors and applied for a standstill with respect to

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the payment of our financial obligations or a temporary reduction in servicing the loans which was not accepted. From the second half of 2014, the markets for our main products began to recover, and the depreciation of the ruble contributed to an increase in our operating profit and our available free cash flow for servicing our financial obligations. Despite of further decrease in prices on our main products during 2015 with further depreciation of the ruble we managed to maintain stable operation profit and used all earned profits for servicing of our financial obligations. We resumed making partial payments of current interest to the banks and agreed extension of the grace periods and new repayment schedules with our major creditors as well as partial capitalization of interest payments and restructuring of overdue interest and principal. In 2016, the market situation has been rapidly changing from quarter to quarter with coal prices rise over the second half of 2016 and correction of the steel prices in the third quarter of 2016. Positive dynamics of steel and coal prices allowed us to improve our financials and supported us in finalizing restructuring with majority of our creditors, including Russian state banks, bondholders and other Russian commercial banks. Our primary objective in negotiating the debt refinancing and restructuring relates to matching our projected available free cash flows with future financial and investment payments and resetting the financial covenants is to ensure a stable financial environment. We are aiming to lengthen the maturity profile and repayment grace periods of that part of our debt portfolio that currently remains not restructured.

For the year ended December 31, 2016, we had an operating income of RUB 42,690 million as compared to RUB 24,252 million for the year ended December 31, 2015. Net cash provided by operating activities was RUB 53,207 million for the year ended December 31, 2016 as compared to RUB 38,867 million for the year ended December 31, 2015. As of December 31, 2016, our total indebtedness was RUB 407,216 million, a decrease of RUB 41,292 million from December 31, 2015. The short-term portion of our total indebtedness was RUB 434,165 million as of December 31, 2016 as compared to RUB 491,674 million as of December 31, 2015. The working capital deficit amounted to RUB 441,581 million as of December 31, 2016 as compared to RUB 517,416 million as of December 31, 2015. Cash and cash equivalents as of December 31, 2016 were RUB 1,689 million as compared to RUB 3,079 million as of December 31, 2015. Our total liabilities exceeded total assets by RUB 252,588 million as of December 31, 2016.

Our ability to refinance existing debt is limited due to difficult conditions on the domestic and international capital markets and in the banking sector, together with sanctions imposed on certain Russian banks preventing them from raising additional long-term financing on the international capital markets. We have restructured major part of our debt portfolio, reduced the capital investment program and disposed of certain non-core or loss-making assets. See If we are unable to restructure all of our indebtedness or fail to comply with the new terms of the restructured indebtedness, our lenders may claim for accelerated repayment, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects and We will require a significant amount of cash to fund our capital investment program. These measures, if successful, should reduce the risk of facing a liquidity shortage in the medium term as well as allow us to reduce our debt leverage over time.

In October 2014, Moody's Investors Service downgraded our rating to Caa3 with negative outlook because of the increased risk of default under our credit facilities, high probability of a refinancing scenario and a weak coal market environment. Further, in December 2014, Moody's Investors Service added Ca-PD/LD to our rating due to litigation with VTB Bank. In March 2015, following Mechel's request, Moody's Investors Service withdrew our corporate family rating of Caa3, probability of default rating of Ca-PD/LD and long-term national scale rating of Caa2.ru. Downgrade and further absence of international rating may reduce our opportunities to raise necessary debt financing (including by accessing the debt capital markets), as well as potentially negatively impact the terms of such financing.

Any deterioration in our operating performance, including due to any worsening of prevailing economic conditions, fall in commodity prices (whether due to the cyclical nature of the industry or otherwise) and/or financial, business or

other factors (including the imposition of further international sanctions against Russian companies or individuals as well as certain industries, including steel and mining sectors), many of which are

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beyond our control, may adversely and materially affect our cash flow, liquidity and working capital position and may result in an increase in our working capital deficit and in our inability to meet our obligations as they fall due. Poor liquidity and working capital deficit could lead to debt repayments difficulties, defaults, enforcement of security and eventually insolvency. As a result we will not be able to expand our business, finance capital expenditures and would have to downgrade which could result in higher cost of borrowing. All these factors could lead to difficulties with refinancing or raising additional capital and would require further restructuring. See [Risks Relating to Our Business and Industry](#). If we are unable to restructure all of our indebtedness or fail to comply with the new terms of the restructured indebtedness, our lenders may claim for accelerated repayment, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects, [Risks Relating to Our Business and Industry](#). We operate in cyclical industries, and any local or global downturn, whether or not primarily affecting the mining and/or steel industries, may have an adverse effect on our business, financial condition, results of operations and prospects and [Risks Relating to the Russian Federation](#). The political and economic crisis in Ukraine as well as other politically related disagreements and allegations between Russia and other countries and sanctions imposed as a result thereof by the United States and the European Union may have a material adverse effect on our business, liquidity and financial condition, as well as the trading market for and value of our shares and ADSs. There is no guarantee that we would be successful in refinancing and restructuring of our debt or in raising additional capital (particularly if we fall under international sanctions preventing us from accessing foreign capital markets and supply of our products on certain export markets), or that we would be able to do so on a timely basis or on terms which are acceptable to us. Even if we were successful, the terms of such refinancing or new capital may be detrimental to holders of ADSs and shares including due to a dilution of their interest. Any such deterioration, affect or failure could have a material adverse effect on our business, financial condition, results of operations and the trading price of our ADSs and shares.

*Our failure to comply with the payment and other obligations in our credit facilities caused some of our creditors to accelerate amounts due under their loan agreements and such failure, or like failure in the future, may cause the acceleration of our other outstanding debt, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects.*

Most of the loan agreements under which we or our subsidiaries are borrowers contain various representations, undertakings, restrictive covenants and events of default. Furthermore, according to the terms of such agreements, certain of our actions aimed at developing our business and pursuing our strategic objectives, such as acquisitions, disposal of assets, corporate restructurings, investments into certain of our subsidiaries and others, require prior notice to or consent from the respective lenders. We have restrictions on our ability to pay dividends, incur additional indebtedness and make capital expenditures, as well as expand through further acquisitions and use proceeds from certain disposals.

During 2014 and 2015, VTB Bank and Sberbank decided to accelerate outstanding amounts under our credit facilities due to our payment defaults. Although we were able to settle with VTB Bank and Sberbank, such acceleration, in turn, would give our other creditors the right to trigger acceleration under their loan agreements. See [Risks Relating to Our Business and Industry](#). We may become subject to bankruptcy procedures, which may result in the inability of holders of our shares and ADSs to recover any of their investments.

In 2015, we signed agreements on restructuring of our debt with our major lenders, such as VTB Bank and Gazprombank. We also signed restructuring agreements with Sberbank in February-April 2016 which granted a grace period and extended repayments of our debt as well as waived all previous defaults. In December 2016, we signed the last set of the agreements with VTB Bank which provide extension of maturity of our credit lines until April 2022. Signing of these agreements was condition precedent to coming into effect of the similar provisions under agreements with Gazprombank and Sberbank. See [Risks Relating to Our Business and Industry](#). If we are unable to restructure all of our indebtedness or fail to comply with the new terms of the restructured indebtedness, our lenders may claim for accelerated repayment, which could lead to

cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects and Item 5. Operating and Financial Review and Prospects Restructuring of financial indebtedness.

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As of December 31, 2016, we had significant amount of overdue debt and we were in breach of certain financial and non-financial covenants in several loan agreements and defaulted on our loans allowing the relevant creditors to claim for accelerated repayment of all amounts of outstanding at any time, however we have not received any notices from the creditors as of December 31, 2016. See Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources Restrictive Covenants, Item 5. Operating and Financial Review and Prospects Description of Certain Indebtedness, Item 10. Additional Information Material Contracts and Item 13. Defaults, Dividend Arrearages and Delinquencies.

Currently we continue to be in default under a number of our facilities, mainly under credit facilities with international lenders (pre-export facility agreements and export credit agreements), and are negotiating with our lenders refinancing and restructuring thereof. Our international lenders have not so far waived their rights in respect of or granted their consent to our breaches. We have received notification on defaults under the facilities with our international lenders, however the lenders under the export credit agreements did not claim for accelerated repayment. In December 2016, pre-export facility agreements with a syndicate of banks have matured without being repaid. In February 2017, a number of lenders under pre-export facility agreements filed 14 requests for arbitration. The 14 requests claim amounts allegedly due, including during the arbitration, plus expenses and any other amounts awarded by the arbitral tribunal. See Item 8. Financial Information Litigation Debt litigation. These claims as well as the refusal of any one lender to grant or extend a waiver or amend the loan documentation, even if other lenders may have waived covenant defaults under the respective credit facilities, could result in substantially all of our indebtedness being accelerated. If our indebtedness is accelerated in full or in part, it would be very difficult in the current financing environment for us to refinance our debt or obtain additional financing, and we could lose our assets, including fixed assets and shares in our subsidiaries, if our lenders foreclose on their liens, which would adversely affect our ability to conduct our business and result in a significant decline in the value of our shares and ADSs.

Our ability to continue to comply with our financial and other loan covenants in the future and to continue to service and refinance our indebtedness will depend on our results of operations and our ability to generate cash in the future and attract new financing and refinance the existing indebtedness, which will depend on several factors, including lenders credit decisions, limitations on the ability of Russian companies to access international capital markets as a result of a tightening of international sanctions against Russian companies and individuals and general economic, financial, competitive, legislative and other factors that are beyond our control. We cannot assure you that any breach of financial and other covenants in our loan agreements, including defects in security, will not result in new demands from our lenders for acceleration of our loan repayment obligations or related litigation, including as a result of cross-defaults. If we fail to comply with our financial and other covenants contained in any of our loan agreements, including compliance with financial ratios and other covenants, or fail to obtain prior consent of lenders for certain actions, or fail to obtain extensions or waivers in respect of any breaches of our loan agreements or amend our loan agreements, such failure would constitute an event of default under the relevant loan agreement and a cross-default under most of the others. Any event of default under our loan agreements could result in acceleration of repayment of principal and interest under the relevant loan agreement and, via cross-default provisions, under our other facilities, reduced opportunities for future borrowing, debt service obligations in excess of our ability to pay, liability for damages or inability to further develop our business and pursue our strategic objectives, any of which could have a material adverse effect on our business, financial condition, results of operations and prospects.

*If we are unable to restructure all of our indebtedness or fail to comply with the new terms of the restructured indebtedness, our lenders may claim for accelerated repayment, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects.*

We have a number of facilities with Russian and international lenders which we have been in non-compliance. We are negotiating restructuring of indebtedness under these agreements in order to extend the repayment schedule and final maturity as well as to decrease our current interest payments. If we fail to negotiate



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restructuring of these agreements, lenders thereunder could claim acceleration of repayment which we may not be able to make. This could lead to cross-default under other agreements and could have a material adverse effect on our business, financial condition, results of operation and prospects.

We have signed restructuring agreements with our major Russian lenders which became effective during the period from October 2015 to December 2016. See Item 5. Operating and Financial Review and Prospects Restructuring of financial indebtedness.

Our major lenders, such as Gazprombank, VTB Bank and Sberbank, require that all the loans provided to our subsidiaries shall be secured with the suretyship or pledge of assets of Mechel PAO. In accordance with the Joint-Stock Companies Law, such transactions exceeding 2% (10% starting from January 1, 2017) of the balance sheet value of the company's assets determined under Russian accounting standards require participation and obtaining of approval from a majority of disinterested shareholders of the company. Such security is an additional guarantee for our lenders which they require for restructuring of our debt. On March 4, 2016, we convoked the extraordinary general shareholders' meeting to approve a number of interested party transactions but we did not manage to obtain the required quorum to approve such transaction. Although we managed to obtain the required quorum on May 26, 2016 and February 27, 2017, we cannot predict whether we could obtain such shareholders' approval in order to secure our loans in the future or we could get a waiver from the banks for the amendment of the security structure.

During 2016, we have successfully restructured our ruble bonds, however we might need to negotiate with the bondholders extension of maturities thereof and new amortization schedules in case of liquidity shortage in the future. If we fail to agree with the bondholders on a restructuring and we will not have liquidity to finance buy-back of these bonds, payment default will occur. Payment default under any of ruble bonds may result in cross-default under all other bond issues as well as cross-default under restructured credit facilities. The bondholders also could litigate us after the restructuring and this could lead to termination of the restructuring.

If we fail to comply with the new terms and conditions, our lenders could claim acceleration of repayment which we may not be able to make and enforce the security which had been pledged to those banks. See We have a substantial amount of outstanding indebtedness with restrictive financial covenants and most shares and assets in our subsidiaries are pledged. This could further lead to cross-default under other agreements and could have a material adverse effect on our business, financial condition, results of operation and prospects.

We still have a number of facilities with international lenders to be restructured in order to extend the repayment schedule and final maturity. In February 2017, a number of lenders under pre-export facility agreements filed requests for arbitration with the London Court of International Arbitration ( **LCIA** ). See Item 8. Financial Information Litigation Debt litigation. These recent claims trigger an event of default and cross-default under various loan agreements and our lenders may claim for accelerated repayments. We have requested our major Russian lenders to waive cross-default provisions in this respect, however we have no clarity when and whether such waivers will be granted. If no waivers are granted, lenders will have a right to claim for immediate acceleration of our indebtedness. We do not have the resources to repay overdue debt or to enable us to comply with accelerated repayment requests immediately. See also Our failure to comply with the payment and other obligations in our credit facilities caused some of our creditors to accelerate amounts due under their loan agreements and such failure, or like failure in the future, may cause the acceleration of our other outstanding debt, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects.

*We have a substantial amount of outstanding indebtedness with restrictive financial covenants and most shares and assets in our subsidiaries are pledged.*

We have a substantial amount of outstanding indebtedness, primarily consisting of debt we incurred in connection with the financing of our acquisitions of Yakutugol and Oriel Resources in 2007 and 2008, as well as debt we incurred to finance our investment program in recent years, including the development of the Elga coal deposit and the universal rolling mill installation, and our working capital needs which have been significant in

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recent years due to the depressed demand and volatile pricing for our main products. Most of this debt has restrictive financial covenants. See Item 5. Operating and Financial Review and Prospects Restrictive Covenants, Item 5. Operating and Financial Review and Prospects Description of Certain Indebtedness and Item 10. Additional Information Material Contracts. As of December 31, 2016, our consolidated total debt, including finance lease obligations and the put option of Gazprombank, was RUB 492,602 million, of which RUB 444,340 million was short-term debt (including RUB 427,350 million with loan covenant violations, of which RUB 260,653 million was long-term debt reclassified to short-term debt due to defaults and cross-defaults under our loan agreements). Our finance costs for the year ended December 31, 2016 were RUB 54,240 million, net of the amount capitalized.

In order to secure bank financings, we have pledged shares in certain our subsidiaries, including 100%-1 share of Yakutugol, 75%+4 shares of Southern Kuzbass Coal Company, 91.66% of Chelyabinsk Metallurgical Plant, 50%+2 shares of common shares of Beloretsk Metallurgical Plant, 80%+3 shares of Korshunov Mining Plant, 62.5% of Mechel Mining, 80%-5 shares of Urals Stampings Plant, 33.33%+1 share of common shares of Izhstal, 25%+1 share of Port Posiet, 50.99% of Elgaugol, 25% of registered capital of Mecheltrans, 100% of registered capital of Fincom-invest OOO, 25% of registered capital of Port Temryuk, 25% of registered capital of Bratsk Ferroalloy Plant, 1.99% of registered capital of MecheltransVostok OOO and 1.99% of registered capital of Elga-road OOO as of December 31, 2016. In January 2017, we pledged 5% of all issued preferred shares of Mechel. Also, property, plant and equipment and certain other assets of our subsidiaries are pledged to the lenders. As of December 31, 2016, the carrying value of property, plant and equipment, inventory and accounts receivable pledged under our loan agreements amounted to RUB 120,953 million. See note 10.1(h) to the consolidated financial statements. Should we be in payment defaults, breaches of covenants and restrictions under our financial agreements and fail to receive waivers, the security may be enforced, which could have a material adverse effect on our business, financial condition, results of operations and prospects. For a description of defaults and acceleration events, see Our failure to comply with the payment and other obligations in our credit facilities caused some of our creditors to accelerate amounts due under their loan agreements and such failure, or like failure in the future, may cause the acceleration of our other outstanding debt, which could lead to cross-default under other borrowings and have a material adverse effect on our business, financial condition, results of operations and prospects.

Our ability to make payments on our indebtedness depends upon our operating performance, which is subject to general economic and market conditions, commodity prices, and financial, business and other factors (including the maintenance or extension of international sanctions against Russian companies and individuals as well as sanctions imposed on certain industrial sectors), many of which we cannot control. See We face pressure on our liquidity, negatively influencing our working capital, which resulted from the acquisitions, substantial investment program, decrease in prices on commodity markets, global economic slowdown, difficulties with attracting new financing or refinancing of our debt and our need to service debt along with international sanctions against Russia and Russian state-owned banks.

Among other things, high levels of indebtedness, the restrictive financial covenants in our credit facilities and breaches thereof as well as default on our loans, could potentially: (1) limit our ability to raise capital through debt financing; (2) limit our flexibility to plan for, or react to, changes in the markets in which we compete; (3) disadvantage our group relative to our competitors with superior financial resources; (4) lead to a loss of assets pledged as security; (5) render us more vulnerable to general adverse economic and industry conditions; (6) require us to dedicate all or a substantial part of our cash flow to service our debt; and (7) limit or eliminate our ability to pay dividends.

*We may become subject to bankruptcy procedures, which may result in the inability of holders of our shares and ADSs to recover any of their investments.*

Our future is dependent on our ability to refinance, restructure and service our indebtedness successfully. If we fail to do so for any reason, we could be forced to seek relief under applicable bankruptcy procedures, in which case our shares and ADSs may lose all or substantial amount of their value. See [Table of Contents](#) There is substantial doubt about our ability to continue as a going concern.

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Our creditors, including the Federal Tax Service of the Russian Federation, may file a bankruptcy petition with a court seeking to declare us insolvent if we are unable to make payments to our creditors in excess of 300,000 rubles within three months of such payments becoming due. In most cases, for such petition to be accepted, the outstanding indebtedness must be confirmed by a separate court decision or arbitral award that has already entered into force. However, under recent amendments to the Federal Law No. 127-FZ On Insolvency (Bankruptcy) dated October 26, 2002 (the **Bankruptcy Law**), financial (credit) organizations, which include our major creditors, may file a petition for bankruptcy without such separate court decision. In this case, the financial organization is required to notify the debtor and its creditors in writing at least 15 days from the date of publication of the bankruptcy petition in the Unified Federal Register of Information on Facts of Business Activity of Legal Entities. On March 7, 2015, VTB Bank published a notification of its intention to initiate bankruptcy proceedings against us. On March 12, 2015, VTB Bank further informed our main creditors of its intention to proceed with such bankruptcy petition. The restructuring documents have been signed in September 2015 and currently there is no further development regarding this issue from VTB Bank side. On April 24, 2015, VTB Bank and VTB Capital Plc filed a claim with the High Court of Justice Queen's Bench Division Commercial Court in England seeking for injunctive relief under pre-export facility agreements with a syndicate of banks. This claim and court proceedings were put on hold until June 1, 2017. VTB Bank and VTB Capital Plc terminated Russian court proceedings and recalled all of their Russian claims against us in October 2015, once restructuring agreements with VTB Bank became effective. See Item 8. Financial Information Litigation Debt litigation. If any other creditor initiates court proceedings seeking to declare us insolvent or if the bank is granted with aforementioned preliminary injunctions, it could have a material adverse effect on our prospects and on the value of our shares and ADSs and may ultimately result in the inability of holders of our shares and ADSs to recover any of their investments.

From time to time, the group's suppliers, services providers and other third parties which we may owe operating debt to may file bankruptcy claims based on the formal debt limit provided by the Bankruptcy Law, however, we settle such claims before court consideration. Nevertheless, the overall debt of our group companies is still substantial. Therefore, there is a risk that our creditors (including suppliers, services providers, etc.) may file bankruptcy petitions, and our shareholders and ADS holders may lose all or substantial part of their investment.

The Bankruptcy Law is still developing and it remains subject to varying interpretations. While the Bankruptcy Law establishes the principle of adequate protection of creditors, debtors, shareholders and other stakeholders in bankruptcy, it often fails to provide instruments for such protection that are available in other jurisdictions with more developed bankruptcy procedures. Bankruptcy proceedings in Russia are often not conducted in the best interests of shareholders or creditors. In addition, Russian courts that conduct bankruptcy proceedings may be subject to a greater degree of political interference and may employ a more formalistic, and less commercially sophisticated, approach to rendering decisions than like court in other jurisdictions. Russian insolvency proceedings in the past have shown a bias towards liquidation and not rehabilitation or restructuring.

The Bankruptcy Law provides for the following order of priority for the satisfaction of creditor claims: (i) personal injury claims; (ii) employment claims (wages and severance payments) and royalty claims under copyright agreements; and (iii) all other claims. The claims of secured creditors are satisfied in accordance with a special procedure, that is, out of the proceeds of sale of the pledged or mortgaged assets. Equity claims of shareholders or ADSs holders may be satisfied only if any assets remain after all creditors have been paid in full. Therefore, there is a risk that our shareholders and ADS holders may lose all or substantial part of their investment. This risk is even more significant for ADS holders whose status in the bankruptcy proceedings is unclear.

*We have not fulfilled our payment obligations under several of the group's lease agreements and a number of the respective lessors have required the return of the leased assets, which may materially adversely affect our business, financial condition, results of operations and prospects.*

Some of our group companies have entered into various lease agreements with different leasing companies for the mining equipment, trucks, railcars, etc.

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Each of the lease agreements has a certain payment schedule. Starting from the second quarter of 2014, we began to delay the regular payments under several of these lease agreements. According to the Civil Code of the Russian Federation, as amended (the **Civil Code**), and the Federal Law No. 164-FZ On Financial Leasing dated October 29, 1998, as amended, a lessor is generally entitled to apply to a court for the early termination of a lease agreement if the lessee fails to make two consecutive payments under the lease agreement. The lessor is required to notify the lessee in writing and request fulfillment of its obligations under the lease agreement within a reasonable time before applying to the court.

The lease agreements we have entered into generally provide for a stricter procedure, whereby the lessor is also entitled to terminate the contract unilaterally, without applying to the court, by way of sending a notification to the lessee in case of non-payment within a specified period of time. The lessor is entitled to receive penalties in case of a delay in payment and early termination of the lease agreement due to the lessee's default. Upon termination of the lease agreement, the lessor is entitled to request the return of the leased equipment. If the lessee fails to return the equipment, the lessor is entitled to receive rental payments covering the time of the delay and compensation for damages if not covered by rental payments.

In particular, we failed to fulfill our payment (as well as certain other) obligations under the lease agreements with Sberbank Leasing AO. Between May and August 2014, we received payment demands from Sberbank Leasing AO, requiring us to settle the overdue amounts under the respective lease agreements. In September-October 2014, Sberbank Leasing AO filed lawsuits for the recovery of the overdue amounts under the lease agreements concluded with Korshunov Mining Plant, Mechel Materials, Yakutugol, Southern Kuzbass Coal Company and Metallurgshakhtspetsstroy. In February 2015, Sberbank Leasing AO sent termination notices to the lessees under the respective lease agreements for the total amount of 4.2 billion rubles. According to such notices, unless the payments are made within 15 days from the date of the notice, the respective lease agreements shall be deemed terminated. The payments were not made, and in April 2015, Sberbank Leasing AO requested through the courts accelerated repayment of amounts due under the lease agreements as well as the return of the leased assets. During the period from December 2015 to May 2016, we signed settlement agreements with Sberbank Leasing AO which waived our previous defaults and restructured our future payment schedules. The settlement agreements became effective in 2016. We have further signed new versions of certain settlement agreements revising payment schedules and we expect their approval by the court in April-May 2017.

During the period from May to August 2015, following our failure to fulfill payment obligations under the respective lease agreements, Caterpillar Financial OOO sent termination notices to the lessees (Yakutugol, Mechel Engineering, Korshunov Mining Plant, Mechel Materials, Metallurgshakhtspetsstroy, Tomusinsky Open Pit and Southern Kuzbass Coal Company). We have not settled the claims and Caterpillar Financial OOO filed lawsuits with the court against our subsidiaries and Mechel (as the guarantor under four lease agreements) seeking termination of lease agreements, withdrawal of leasing assets and recovery of debt in an aggregate amount of approximately \$5.0 million and 313.9 thousand. In July 2016, Caterpillar Financial OOO filed another lawsuit seeking recovery of debt and withdrawal of a leasing asset. Currently, these lawsuits are considered by the courts of various instances while we continue negotiations with Caterpillar Financial OOO.

During the period from May to November 2016, VTB Leasing JSC filed several lawsuits with the court against Mecheltrans seeking recovery of debt under lease payments and the court sustained the plaintiff's claims. We repaid part of the debt and signed settlement agreements for the remaining overdue debt. As of the date hereof, all settlement agreements have been approved by the court. See Item 8. Financial Information Litigation Debt litigation for a description of the court proceedings mentioned above.

During 2016, we breached payment schedules with Sberbank Leasing AO, Caterpillar Financial OOO, VTB Leasing JSC and Gazprombank Leasing JSC, however we managed to substantially decrease our overdue lease payments and agreed on the repayment profile of the remaining overdue debts. As of December 31, 2016, we fully repaid the overdue lease payments to Gazprombank Leasing JSC.



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In the event the leased equipment is returned to the lessor, there is a risk that our operating activities (for the group companies that are lessees under the delinquent leases) will be adversely affected, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

*We will require a significant amount of cash to fund our capital investment program.*

Our business requires maintenance capital expenditures in order to maintain production levels adequate to meet the demand for our products, as well as other capital expenditures to implement our business strategy. We spent 4,570 million rubles during 2016 on our capital expenditures (including 2,060 million rubles in maintenance capital expenditures). In planning for 2017, we followed our current investment policy focusing only on those items that are either close to completion or are of major importance for our operations. Our capital investment program currently contemplates capital spending of up to 12,544 million rubles in 2017 (including up to 6,412 million rubles in maintenance capital expenditures). A considerable part of the planned capital expenditures relate to the renewal of mining-and-transport equipment and to the development of the Elga coal deposit. The Elga capital expenditures are planned in the amount of approximately 5.8 billion rubles to be financed from our own funds in 2017-2019. Overall, we plan to spend up to 35.7 billion rubles for the three-year period of 2017-2019 on capital investments (including up to 17.7 billion rubles in maintenance capital expenditures). See Item 4. Information on the Company Capital Investment Program.

Our ability to undertake and fund planned capital expenditures will depend on our ability to generate cash in the future and access debt financing. Lack of liquidity may jeopardize capital expenditure plans, see We face pressure on our liquidity, negatively influencing our working capital, which resulted from the acquisitions, substantial investment program, decrease in prices on commodity markets, global economic slowdown, difficulties with attracting new financing or refinancing of our debt and our need to service debt along with international sanctions against Russia and Russian state-owned banks. This, to a certain extent, is subject to general economic and market conditions, financial, competitive, legislative, regulatory and other factors (including the status of international sanctions against Russian companies and individuals as well as sanctions imposed on certain types of products in different sectors) that are beyond our control. Raising debt financing for our capital expenditures on commercially reasonable terms may be particularly challenging given our current high levels of indebtedness and restrictive covenants imposed under the loan agreements. Any deterioration in our operating performance, including due to any worsening of economic conditions, fall in commodity prices and/or financial, business or other factors, many of which are beyond our control, may adversely and materially affect our cash flow which may leave us unable to conduct our capital expenditure plans as necessary or required, which could adversely affect our operating facilities and ability to comply with applicable regulations.

*Changes in the exchange rate of the ruble against the U.S. dollar and in interest rates may materially adversely affect our business, financial condition and results of operations.*

Part of our sales are denominated in U.S. dollars, whereas the majority of our direct costs are incurred in rubles. In addition, we have foreign currency loans that are denominated mainly in U.S. dollars. Depreciation in real terms of the ruble against the U.S. dollar may result in a decrease in our costs relative to our export revenues assuming stable level of prices for our products. Also depreciation in real terms of the ruble against the U.S. dollar may result in a reduction in our ability to service debt obligations denominated in foreign currencies in case of sharp decline in sales in general and sales denominated in foreign currencies in particular. Conversely, appreciation in real terms of the ruble against the U.S. dollar may materially adversely affect our results of operations if the prices we are able to charge for our products do not increase sufficiently to compensate for the increase in real terms in our ruble-denominated expenditures. In 2015, the ruble depreciated against foreign currencies, decreasing to 72.88 rubles per one U.S. dollar on December 31, 2015. In 2016, the ruble-U.S. dollar exchange rate was very volatile, reaching RUB 60.66 as at

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December 31, 2016 and strengthened by 16.8% from December 31, 2015. As of March 31, 2017, the ruble-U.S. dollar exchange rate was 56.38 (a 16.6% decline compared to March 31, 2016) and the ruble-euro exchange rate was 60.60 (a 20.8% decline compared to March 31, 2016), according to the CBR.

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In an effort to protect the country's foreign currency reserves from substantial depletion, the CBR moved to a free floating exchange rate regime on November 20, 2014. In response to continuing ruble depreciation, the CBR in an unexpected, emergency meeting increased its key rate, which determines the borrowing costs for commercial banks, from 10.5% to 17% subsequently lowering the rate to 9.75% during 2015-2017. Upon restructuring, interest rates under our ruble-denominated facilities with Russian state banks are linked to the CBR key rate (plus a margin above the key rate). Should the CBR key rate increase again, or should interest rates under our existing facility agreements otherwise increase, we will face higher borrowing costs, which could have a material adverse effect on our business, cash flows, financial condition, results of operations and prospects.

*Inflation could increase our costs and decrease operating margins.*

In 2016, 2015 and 2014, the inflation rate in Russia was 5.4%, 12.9% and 11.4%, respectively, according to the Russian Federal State Statistics Service ( **Rosstat** ). The increase of inflation in 2014 followed by further increase in 2015 may be attributed to international sanctions imposed on Russian companies and individuals, the significant fall in the ruble against the U.S. dollar and euro and high growth of prices on consumer goods and services. A record low level of inflation in Russia in 2016 was due to the tight monetary policy of the CBR and slowing growth of prices on consumer goods and services. Inflation increases our operating costs on monetary items, which are sensitive to rises in the general price level in Russia, including fuel and energy costs, cost of production services and salaries (as under existing collective agreements wage indexation is carried out taking into account inflation). Inflation could also potentially increase the prices we can charge for our products. The impact of inflation on our operating margins depends on whether we can charge higher prices corresponding with the increase in costs. Nevertheless, there is a high risk that inflation will have an overall negative impact on our operating margins.

*If limitations on the conversion of rubles into foreign currencies in Russia are imposed, this could cause us to default on our obligations.*

Part of our indebtedness and part of our capital expenditures are payable in various foreign currencies, including the U.S. dollar and euro. Russian legislation currently permits the conversion of ruble revenues into foreign currency without limitation. If the Russian authorities were to impose limitations on the convertibility of the ruble or other restrictions on operations with rubles and foreign currencies in the event of an economic crisis or otherwise, there may be delays or other difficulties in converting rubles into foreign currency to make a payment or delays in or restrictions on the transfer of foreign currency. This, in turn, could limit our ability to meet our payment and debt obligations, which could result in the loss of suppliers, acceleration of debt obligations and cross-defaults and, consequently, have a material adverse effect on our business, financial condition, results of operations and prospects.

*Our business could be materially adversely affected if creditors of certain of our subsidiaries accelerate their debt.*

If we decide to merge certain subsidiaries for operational reasons from time to time, under Russian law such mergers are considered to be a reorganization and the merged subsidiaries are required to publish the information regarding this reorganization twice: the first publication due at the beginning of the reorganization and the second to follow one month after the first publication. Russian law also provides that, for a period of 30 days after the date of latest publication, the creditors of merging subsidiaries have a right to file a claim seeking acceleration of the reorganized subsidiaries' indebtedness and demand reimbursement for applicable losses, except in cases where the creditors have adequate security or are provided with adequate security within 30 days after filing of such claim. In the event that we undertake any such merger and all or part of our subsidiaries' indebtedness is accelerated, we and such subsidiaries may not have the ability to raise the funds necessary for repayment, which could have a material adverse effect on our business, financial condition, results of operations and prospects.



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*Russian law restrictions on depositary receipt programs limit our access to equity capital and constrain our refinancing options.*

Russian companies are limited in their ability to place shares in circulation outside of Russia, including in the form of depositary receipts such as our common American Depositary Shares ( **common ADSs** ) and our global depositary shares representing our common shares ( **GDSs** ), as well as our preferred American Depositary Shares representing our preferred shares ( **preferred ADSs**, and together with the common ADSs, the **ADSs** ) due to Russian securities regulations. We have received permission from the Russian Federal Financial Markets Service ( **FFMS** ) for up to 40% of our common shares to be circulated abroad through depositary receipt programs, which was the maximum amount allowed at that time. Later we also received FFMS permission for a total of 41,627,074 preferred shares to be circulated through depositary receipt programs, representing 30% of the total number of issued preferred shares, which was the maximum amount allowed at that time. Currently, Russian securities regulations provide that no more than 25% of the total number of a Russian company's shares may be placed and circulated abroad through depositary receipt programs or otherwise. It is unclear whether the FFMS's approvals of higher amounts prior to the establishment of this lower limit will be allowed to remain in place. As of December 31, 2016, our common ADSs and GDSs together accounted for approximately 33% of our common shares, and accordingly we believe we cannot raise additional equity financing through placement of common shares in the form of depositary receipts. If the current limit is enforced Deutsche Bank Trust Company Americas (the **depositary** ) may be forced to cancel some of our common ADSs and GDSs and deliver a corresponding number of the underlying common shares to holders of common ADSs or GDSs. The Russian government or its agencies may also impose other restrictions on international financings by Russian issuers.

*We had in the past material weaknesses in our internal control over financial reporting, and we make no assurances that additional material weaknesses will not be identified in the future.*

Management identified a material weakness in our internal control over financial reporting as defined in the Exchange Act Rule 12b-2 and Rule 1-02 of Regulation S-X that affected our financial statements for the year ended December 31, 2016. The material weakness in our internal control over financial reporting identified as of December 31, 2016 is described in Item 15. Controls and Procedures. Due to the effect of this material weakness, our auditors have opined that we have not maintained effective internal control over financial reporting as of December 31, 2016 under Section 404 of the Sarbanes-Oxley Act of 2002. Our auditors have also opined that we did not maintain effective internal control over financial reporting as of each of December 31, 2006, 2007, 2008, 2009, 2010, 2011 and 2015 due to the effect of the material weaknesses identified as of those dates.

Notwithstanding the steps we have taken and continue to take that are designed to remedy the material weakness identified in Item 15. Controls and Procedures, we may not be successful in remedying this material weakness in the near or long term and we make no assurances that additional significant deficiencies or material weaknesses in our internal control over financial reporting will not be identified in the future. Our failure to implement and maintain effective internal control over financial reporting could result in errors in our financial statements that could result in a restatement of financial statements, cause us to fail to meet our reporting obligations and cause investors to lose confidence in our reported financial information, leading to a decline in the market price of our shares and ADSs.

*We may incur impairments to goodwill or other non-current assets which could negatively affect our future profits.*

We assess, at each reporting date, whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, we estimate the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or a cash-generating unit's fair value less costs of disposal and its value in use. The recoverable amount is determined for an individual asset, unless the asset



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does not generate cash inflows that are largely independent of those from other assets or groups of assets. When the carrying amount of an asset or a cash-generating unit exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In assessing value in use, we use assumptions that include estimates regarding the discount rates, growth rates and expected changes in selling prices, sales volumes and operating costs, as well as capital expenditures and working capital requirements during the forecasted period. The estimated future cash flows expected to be generated by the asset, when the quoted market prices are not available, are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. The growth rates are based on our growth forecasts, which are largely in line with industry trends. Changes in selling prices and direct costs are based on historical experience and expectations of future changes in the market. In determining fair value less costs of disposal, recent market transactions are taken into account.

We base our impairment calculation on detailed budgets and forecast calculations, which are prepared separately for each of our group's cash-generating units to which the individual assets are allocated. These budgets and forecast calculations generally cover a period of five years. A long-term growth rate is calculated and applied to project future cash flows after the fifth year.

For a cash-generating unit involved in mining activity future cash flows include estimates of recoverable minerals that will be obtained from proved and probable reserves, mineral prices (considering current and historical prices, price trends and other related factors), production levels, capital and reclamation costs, all based on the life of mine models prepared by our engineers.

Impairment losses of continuing operations are recognized in the consolidated statement of profit (loss) and other comprehensive income (loss) in expense categories consistent with the function of the impaired asset.

For assets excluding goodwill, an assessment is made at each reporting date to determine whether there is an indication that previously recognized impairment losses no longer exist or have decreased. If such indication exists, we estimate the asset's or the cash-generating unit's recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognized. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the consolidated statement of profit (loss) and other comprehensive income (loss) unless the asset is carried at a revalued amount, in which case, the reversal is treated as a revaluation increase.

Goodwill is tested for impairment annually as of December 31 and when circumstances indicate that the carrying value may be impaired.

Impairment is determined for goodwill by assessing the recoverable amount of each cash-generating unit (or group of cash-generating units) to which the goodwill relates. When the recoverable amount of the cash-generating unit is less than its carrying amount, an impairment loss is recognized. Impairment losses relating to goodwill cannot be reversed in future periods.

Based on the results of the impairment analysis of goodwill we performed as of December 31, 2016, impairment loss of RUB 2,930 million was recognized. According to the results of the impairment analysis of non-current assets as of December 31, 2016, impairment loss of RUB 2,272 million was recognized. See note 18 to the consolidated financial statements.

The amount of goodwill on our balance sheet as of December 31, 2016 that is subject to impairment analysis in the future is RUB 18,355 million or 6% of our total assets. This amount includes goodwill of Yakutugol,



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Southern Kuzbass Power Plant, Kuzbass Power Sales Company and Port Posiet of RUB 13,399 million, RUB 2,382 million, RUB 1,026 million and RUB 756 million, respectively, as of December 31, 2016. See note 18 to the consolidated financial statements.

Based on the results of the impairment analysis of goodwill we performed as of December 31, 2015, impairment loss of RUB 1,444 million was recognized. According to the results of the impairment analysis of non-current assets, impairment loss of non-current assets of RUB 5,983 million was recognized. See note 18 to the consolidated financial statements. Based on comparison of carrying value and recoverable value as of December 31, 2015, excess of recoverable value over carrying value was identified therefore reversal of previously recoded impairment loss as of December 31, 2014 was recognized in the amount of RUB 5,966 million.

We continue to monitor relevant circumstances, including consumer levels, general economic conditions and market prices for our products, and the potential impact that such circumstances might have on the valuation of our goodwill and non-current assets. It is possible that changes in such circumstances, or in the numerous variables associated with our judgments, assumptions and estimates made in assessing the appropriate valuation of goodwill and recoverable value of non-financial assets, could in the future require us to further reduce our goodwill and non-financial assets and record related non-cash impairment charges. If we are required to record additional impairment charges, this could have a material adverse impact on our results of operations or financial position.

*Given the competition for qualified accounting personnel in Russia, we may be unable to retain our key accounting staff, which could disrupt our ability to timely and accurately report IFRS financial information.*

Our subsidiaries maintain their books and records in local currencies and prepare accounting reports in accordance with local accounting principles and practices. In particular, each of our Russian subsidiaries maintains its books in rubles and prepares separate unconsolidated financial statements in accordance with Russian accounting standards. For every reporting period, we translate, adjust and combine these Russian statutory financial statements to prepare consolidated financial statements in accordance with IFRS. This is a time-consuming task requiring us to have accounting personnel experienced in internationally accepted accounting standards. We believe there is a shortage in Russia of experienced accounting personnel with knowledge of internationally accepted accounting standards. Moreover, there is high demand for such personnel as many Russian companies prepare financial statements on the basis of internationally accepted accounting standards. Such competition may make it difficult for us to hire and retain such personnel, and our accounting staff may have high turnover.

***Risks Relating to Our Business and Industry***

*We operate in cyclical industries, and any local or global downturn, whether or not primarily affecting the mining and/or steel industries, may have an adverse effect on our business, financial condition, results of operations and prospects.*

Our mining segment sells coal (metallurgical and steam), iron ore concentrate and coke. These commodities are traded in markets throughout the world and are influenced by various factors beyond our control, such as global economic cycles and economic growth rates. Prices of these products have varied significantly in the past and could vary significantly in the future. For example, in 2016, coal prices were highly volatile due to coal supply management policy in China which has caused a fall in production that has driven a rise in prices, despite demand dropping globally. After a sharp rise of coal prices in July-November 2016, Chinese government made some changes to the coal production policy allowing Chinese companies to produce more coal and prices started to decline.

Our steel segment sells steel products, including semi-finished products, long products of a wide range of steel grades, carbon and stainless flat products, wire products, forgings and stampings and others, as well as

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ferrosilicon. Ferrosilicon is primarily used in the manufacture of steel and its market demand generally follows the cycles of the steel industry. The steel industry is highly cyclical in nature because the industries in which steel customers operate are subject to changes in general economic conditions. The demand for steel products thus generally correlates to macroeconomic fluctuations in the economies in which steel producers sell products, as well as in the global economy. The prices of steel products are influenced by many factors, including demand, worldwide production capacity, capacity-utilization rates, raw materials costs, exchange rates, trade barriers and improvements in steel-making processes. Steel prices have experienced, and in the future may experience, significant fluctuations as a result of these and other factors, many of which are beyond our control. For example, in 2015, steel market in China experienced turbulence as the steel prices collapsed and the demand decreased. Although the demand for steel in China has gradually started to recover through 2016 and the steel prices follow this trend, they remain volatile and far from the peak levels.

Our power segment generates and supplies power resources. Power demand in Russia depends on its consumption by the industrial sector. In Russia, the steel and mining industries are major consumers of power and the level of production of steel and mining companies impact demand for power. Market demand for the power produced by our power segment is affected by many of the same factors and cycles that affect our mining and metals businesses.

As a result of the 2008-2009 global economic crisis and the subsequent 2010-2011 global economic slowdown, the demand and prices for our products sharply declined. The continuing stagnation of the economy of the European region, the 2012-2016 economic slowdowns in the Asian region, primarily in China, as well as the existing uncertainty as to global economic recovery in the near future and international sanctions against Russia and Russian individuals or businesses may have adverse consequences for our customers and our business as a whole. See [Risks Relating to the Russian Federation](#). The political and economic crisis in Ukraine as well as other politically related disagreements and allegations between Russia and other countries and sanctions imposed as a result thereof by the United States and the European Union may have a material adverse effect on our business, liquidity and financial condition, as well as the trading market for and value of our shares and ADSs.

Prices for our products, including coal, iron ore, metals, ferrosilicon and power, as well as the prices of coal, iron ore, ferroalloys, power and natural gas and other commodities and materials we purchase from third parties for the production of our products, fluctuate substantially over relatively short periods of time and expose us to commodity price risk. We do not use options, derivatives or swaps to manage commodity price risk. We use our vertically integrated business model and intersegment sales, as well as short-term and long-term purchase and sales contracts with third party suppliers and customers, to manage such risk. In addition, the length and pricing terms of our sales contracts on certain types of products are affected and can be regulated by orders issued by Russian antimonopoly authorities. In particular, pursuant to a directive issued to us by the Russian Federal Antimonopoly Service ( **FAS** ) in August 2008, we entered into long-term contracts for supply of certain grades of our coking coal with a formula of price calculation and with fixed volumes for the entire period of the contract. See [Antimonopoly regulation could lead to sanctions with respect to the subsidiaries we have acquired or established or our prices, sales volumes and business practices](#). Terms of sales of other types of our products may also be affected by regulations of the authorities. We cannot assure you that our strategies and contracting practices will be successful in managing our pricing risk or that they will not result in liabilities. If our strategies to manage commodity price risk and the impact of business cycles and fluctuations in demand are not successful, it could have a material adverse effect on our business, financial condition, results of operations and prospects.

*The steel and mining industries are highly competitive, and we may not be able to compete successfully.*

We face competition from Russian and international steel and mining companies. Consolidation in the steel and mining sectors globally has led to the creation of several large producers, some of which have greater financial

resources and more modern facilities than our group. We also face price-based competition from

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producers in emerging market countries, including, in particular, Brazil (in the export of raw materials for metallurgy) and China, Ukraine, Belarus, Turkey and Kazakhstan (in the export of semi-finished products and rolled products). Increased competition could result in more competitive pricing and reduce our operating margins.

Our competitiveness is based in part on our operations in Russia having a lower cost of production than competitors in higher-cost locations. We have been facing a consistent upward trend in the past several years in production costs, particularly with respect to wages and transportation. For example, our rail transportation costs increased consistently during previous years with the more recent rail tariff increases of 10.0% in 2015 and 9.0% in 2016. Starting from January 29, 2015, railway export tariffs for all goods were increased by additional 13.4%, except for certain grades of coal and middlings for which additional indexation amounted to only 1.3%. In 2017, railway tariffs were increased by 6.08%. See A limited capacity of the railway infrastructure and an increase in railway tariffs expose us to uncertainties regarding transportation costs of raw materials and steel products, Increasing costs of electricity, natural gas and labor could materially adversely affect our operating margins and Inflation could increase our costs and decrease operating margins. If these production costs continue to increase in the jurisdictions in which we operate, our competitive advantage will be diminished, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

*Changes in our estimates of reserves or failure to implement mine development plans could result in lower than expected revenues, higher than expected costs or decreased operating margins.*

We base our reserve information on engineering, economic and geological data which is assembled, analyzed and reviewed by our staff, which includes various engineers and geologists, annually and which is reviewed by independent mining engineers as of the acquisition dates as part of business combinations. The reserve estimates as to both quantity and quality are periodically updated to reflect production from reserves and new drilling, engineering or other data received. There are numerous uncertainties inherent in estimating quantities and qualities and the costs to mine recoverable reserves, including many factors beyond our control. Estimates of economically recoverable reserves and net cash flows necessarily depend upon a number of variable factors and assumptions, such as geological and mining conditions which may not be fully identified by available exploration data or which may differ from our experience in current operations, projected rates of production in the future, historical production from the area compared with production from other similar producing areas, the assumed effects of regulation and taxes by governmental agencies and assumptions concerning prices, operating costs, mining technology improvements, mineral extraction and excise tax, development costs and reclamation costs, all of which may vary considerably from actual results. In addition, it may take many years from the initial phase of drilling before production is possible. During that time, the economic feasibility of exploiting a discovery may change as a result of changes in the market price of the relevant commodity. Mine development plans may have to be revised due to geological and mining conditions and other factors described above, as well as due to shortages in capital funding. Our planned development projects also may not result in significant additional reserves and we may not have continuing success developing new mines or expanding existing mines beyond our existing reserves.

The financial performance of our mining segment depends substantially on our ability to mine coal reserves that have the geological characteristics that enable them to be mined at competitive costs and to meet the quality needed by our customers. Actual tonnage recovered from identified reserve areas or properties and revenues and expenditures with respect to our reserves may vary materially from estimates. Replacement reserves may not be available when required or, if available, may not be capable of being mined at costs comparable to those characteristic of the depleting mines. Our ability to obtain other reserves through acquisitions in the future could be limited by restrictions under our existing or future loan agreements, competition from other mining companies for attractive properties, the lack of suitable acquisition candidates or the inability to acquire mining properties on commercially reasonable terms. Furthermore, we may not be able to mine all of our reserves as profitably as we do at our current operations due to

increases in wages, power and fuel prices and other factors.

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Therefore, changes in our estimates of reserves or failure to implement mine development plans could result in lower than expected revenues, higher than expected costs or decreased operating margins.

*The development of the Elga coal deposit is subject to certain risks due to the substantial amount of capital costs involved in developing the required infrastructure.*

The risks associated with the development of the Elga coal deposit have the potential to impact the project's legal or economic viability. Key risks that have been identified include the following: (1) the early termination, suspension or restriction of the right of subsoil use of the Elga coal deposit in case of violation of the requirements of the deposit development technical plan; (2) the project requires significant capital expenditures to develop the required production and washing facilities and infrastructure, and increases in planned capital and operating costs could make the project uneconomical because of the project's sensitivity to these costs; (3) the economic viability of the project is dependent upon the full use of the rail line; (4) the project is very sensitive to market prices for coal because of the high initial capital costs; and (5) the insufficient capacity of ports in the Russian Far East where the Elga deposit is located may limit the distribution of coal mined at the Elga deposit. In addition, capital expenditures for the rail line were not considered in the calculation of reserves estimates as we do not plan to use the rail line solely for delivery of coal from the Elga deposit. The realization of any of these risks could have a material adverse effect on our business, financial condition, results of operations and prospects. While we have already invested approximately 73.7 billion rubles in the development of the Elga coal deposit (out of which approximately 64.3 billion rubles was invested in the construction of the rail line), its further development requires a substantial amount of investment. Based on the expected financial capabilities of the group in view of the current and projected market conditions for our main products, we plan to invest in Elga from our own funds approximately 5.8 billion rubles in 2017-2019. In 2013 and 2014, our subsidiary Elgaugol and State Corporation Bank for Development and Foreign Economic Affairs (Vnesheconombank) (**Vnesheconombank**) signed a \$150.0 million bridge loan agreement and a \$2.5 billion main project financing loan agreements for the development of the Elga coal deposit. As of December 31, 2016, the principal amount outstanding under the loan agreements was \$167.3 million, with overdue principal in the amount of \$146.4 million and overdue interest in the amount of \$6.2 million. Disbursement under the main project financing loan agreements was subject to fulfillment of conditions precedent. Elgaugol has not fulfilled these conditions and Vnesheconombank has suspended the financing. We hold negotiations with Vnesheconombank with respect to restructuring of the bridge loan and possibility of further financing of the Elga project.

*Successful implementation of our strategy to expand our special steel long products sales and coal sales depends on our ability to increase our export sales of these products.*

Our strategy to expand our special steel long products sales is dependent on our ability to increase our exports of these products to other countries. Likewise, our strategy to increase our sales of coal, particularly high-grade coking coal and PCI, is substantially dependent on our ability to increase our production and exports of these products through ports in the Russian Far East to other countries, particularly Japan, China, South Korea and other Pacific Rim countries. We face a number of obstacles to this strategy, including oversupply and low demand, trade barriers and sales and distribution challenges, as well as restrictions imposed by antimonopoly legislation. See Antimonopoly regulation could lead to sanctions with respect to the subsidiaries we have acquired or established or our prices, sales volumes and business practices.

Currently, key ports in the Russian Far East have limited cargo-handling capacity, lack adequate port facilities and have old and worn-out equipment. In particular, the limited capacity of the railways connecting to these ports is a critical impediment to the further development of port infrastructure and the entire transportation system in the Russian Far East. Increasing the capacity of the ports in the Russian Far East is one of the key issues identified in the Transportation Strategy of the Russian Federation. Existing railway sections must be reconstructed, the logistics

structure improved and the actions of the cargo owners, the ports management and Russian Railways, an open joint-stock company wholly owned by the Russian government, must be better coordinated. In addition, the shortage of the locomotive fleet of Russian Railways due to its worn-out state and



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frequent breakdowns, as well as major track repairs by Russian Railways in the summer months result in restriction on cargo volumes and increase in delivery time. Slowdown in train movements in the winter months has a negative impact on the state of bulk cargo as freezing occurs due to low temperatures which further reduces the rate of discharge in ports and leads to congestion of railcars in the railway network.

In particular, the total current annual capacity of the Baikal-Amur Mainline to which our Elga deposit is connected by our private rail line, was increased to 23 million tonnes in 2016 and upon implementation of a set of actions set forth in the Federal Target Program Development of Transport System of Russia (2010-2020) is expected to increase up to 33 million tonnes per year by 2018. However, in order to comply with the general declared volumes for cargo transportation on the Baikal-Amur Mainline, its capacity will need to be further expanded to meet, among others, our needs when Elga Open Pit reaches its full planned annual production capacity of 28.2 million tonnes of saleable coal in 2027. In addition, Russian Railways increased the capacity of the Komsomolsk-on-Amur-to-Sovetskaya Gavan segment, which connects the Baikal-Amur Mainline to Port Vanino, to 42.3 million tonnes in 2016. However, this increase may not be sufficient as other cargo shippers may also substantially increase their cargo volumes on the Baikal-Amur and Trans-Siberian Mainlines and further in the direction from Komsomolsk-on-Amur to Sovetskaya Gavan transportation hub. We cannot guarantee that the development projects by Russian Railways will proceed according to current plans, particularly in light of international sanctions against Russian companies and individuals. In addition, there is acute competition among Russian coal exporters for existing port capacity. In light of this shortage, Russian coal producers have endeavored to acquire ports or separate terminals to ensure the export of their products.

Our ability to increase coking coal export volumes is also limited by requirements to first satisfy Russian domestic coal demand, pursuant to a FAS directive issued to us in August 2008. See Antimonopoly regulation could lead to sanctions with respect to the subsidiaries we have acquired or established or our prices, sales volumes and business practices. Failure to successfully manage the obstacles and tasks involved in the implementation of our export sales strategy could have a material adverse effect on our business, financial condition, results of operations and prospects.

*In the event the title to the shares of any company we acquired is successfully challenged, we risk losing our ownership interest in that company or its assets.*

Almost all of our Russian assets consist of companies formed during the course of Russian privatizations in the 1990s and early 2000s and generally we acquired shares in these companies from third parties after their respective privatizations. Given that Russian privatization legislation is vague, many privatizations are vulnerable to challenge. The Russian statute of limitations for challenging privatization transactions is generally three years since the date when performance of the transaction began. If a person presenting the claim was not a party to the transaction, the statute of limitations runs from the date when such person found out or should have found out that performance of the transaction was initiated. The statute of limitations generally cannot exceed 10 years from the commencement of performance of the transaction, although recent court practice suggests this limit does not apply if a claimant was not aware of a violation and if it is determined that, in accordance with general principles of justice, the statute of limitations concept cannot be otherwise relied on to allow the legalization of unlawfully acquired property. As noted above, most of our subsidiaries were privatized more than 10 years ago. In the event that any title to, or our ownership stakes in, any of the privatized companies acquired by us is subject to challenge as having been improperly privatized and we are unable to defeat this claim, we risk losing our ownership interest in the company or its assets, which could materially adversely affect our business, financial condition, results of operations and prospects.

In addition, under Russian law transactions in shares may be invalidated on many grounds, including a sale of shares by a person without the right to dispose of such shares, breach of interested party and/or major transaction rules and/or the terms of transaction approvals issued by governmental authorities, or failure to register the share transfer in the

securities register. As a result, defects in earlier transactions with shares of our subsidiaries (where such shares were acquired from third parties) may cause our title to such shares to be subject to challenge.

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*Our business could be adversely affected if we fail to obtain or extend necessary subsoil licenses and permits or fail to comply with the terms of our subsoil licenses and permits.*

Our business depends on the continuing validity of our subsoil licenses and the issuance of new and extended subsoil licenses and our compliance with the terms thereof. In particular, in estimating our reserves, we have assumed that we will be able to renew our Russian subsoil licenses as and when necessary in the ordinary course of business so that we will be able to exploit the resources under such licenses for the operational life of the relevant subsoil plot. See Item 4. Information on the Company Regulatory Matters Subsoil Licensing in Russia Extension of licenses and Mining Segment Mineral reserves. However, license extension is subject to the licensee being in compliance with the terms of the license. Our experience with license extensions and publicly available information about current market practice and available court practice suggest that regulatory authorities tend to focus on such terms of the license as production levels, operational milestones and license payments, which are considered to be material terms of the license. Nevertheless, there is no assurance that this approach will be consistently applied by the regulatory authorities and the courts and that there will be no changes to this approach in the future. Regulatory authorities exercise considerable discretion in the timing of license issuance, extension of licenses and monitoring licensees' compliance with license terms. Subsoil licenses and related agreements typically contain certain environmental, safety and production commitments. See Item 4. Information on the Company Regulatory Matters Subsoil Licensing in Russia Maintenance and termination of licenses. If regulatory authorities determine that we have violated the material terms of our licenses, it could lead to rejection in license extension or suspension or termination of our subsoil licenses, and to administrative and civil liability. In addition, requirements imposed by relevant authorities may be costly to implement and result in delays in production. Our subsoil licenses expire on dates falling in 2019 through 2037. See the tables setting forth expiry dates of our Russian subsoil licenses in Item 4. Information on the Company Mining Segment and reserves information. Accordingly, these factors may seriously impair our ability to operate our business and realize our reserves which could have a material adverse effect on our business, financial condition, results of operations and prospects.

We are currently in compliance with the material terms of our Russian subsoil licenses, except for the following. We failed to commence commercial coal production at the Raspadsk license area (part of Olzherassky Open Pit) in 2009 as required by the license due to unfavorable mine economics, but expect to commence such production in the fourth quarter of 2018 provided coal prices recover sufficiently. In addition, we commenced preparation for the commercial development of the Yerunakovsk-1, Yerunakovsk-2 and Yerunakovsk-3 license areas, but failed to commence commercial production at these license areas in 2011 as required by the licenses due to unfavorable mine economics. Moreover, we cannot fully develop the deposit at the Yerunakovsk-3 license area due to the presence of a third-party sludge pond in this area. Furthermore, we failed to commence commercial coal production at the Olzherassk license area (Olzherasskaya-Glubokaya Underground) due to unfavorable mine economics and the significant capital investments required to develop this license area. The Yerunakovsk-2, Yerunakovsk-3 and Olzherassk (Olzherasskaya-Glubokaya Underground) license areas are not counted for the purposes of our coal reserves.

*Increasing costs of electricity, natural gas and labor could materially adversely affect our operating margins.*

In 2016, our Russian operations purchased approximately 4.7 billion kilowatt-hours ( **kWh** ) of electricity at a total cost of 13.2 billion rubles, implying an average cost of 2.4 rubles per kWh. According to the Ministry of Economic Development of the Russian Federation, the average increase in market prices on the retail electricity market was 7.9% in 2016, and is expected to be 6.5% in 2017. Further price increases for electricity may also occur in the future due to the increase in fuel prices.

Our Russian operations also purchase significant amounts of natural gas, primarily for the production of power resources at our own co-generation facilities, from Novatek PAO ( **Novatek** ), Russia's largest independent producer of

natural gas, Rosneft Oil Company ( **Rosneft** ), the leader of Russia's petroleum industry, and Gazprom PAO ( **Gazprom** ), the government-controlled dominant gas producer and the owner of

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the unified gas supply system of Russia. Domestic natural gas prices are regulated by the Russian government. In 2016, we purchased approximately 1.8 billion cubic meters of gas at a total cost of approximately 6.9 billion rubles. Russian domestic natural gas prices are significantly below Western European levels, which provides us with a cost advantage over our competitors, an advantage which may diminish as Russian domestic gas prices approach Western European levels. Starting from July 1, 2015, the Russian Federal Tariff Service set wholesale prices of gas produced by Gazprom for domestic consumers on the territory of the Russian Federation, except for households, in the range of 2,395 rubles to 4,906 rubles as compared to prices set for the previous period which were set starting from January 1, 2014 in the range of 2,228 rubles to 4,675 rubles per thousand cubic meters, depending on the region of the Russian Federation where the gas is purchased. In 2016, gas prices were not increased and remained at the level of 2015.

Following raw materials used in the production process and energy-related costs, our labor costs are the next most significant operational cost. Labor costs in Russia have historically been significantly lower than those in the more developed market economies of North America and Western Europe for similarly skilled employees. According to Rosstat, after adjusting for inflation, the average wage in the Russian Federation has risen at the annual rate of 1.2% and 4.8% in 2014 and 2013, respectively. In 2015, the average wage has decreased by 9.0%, according to Rosstat. In 2016, the average wage has increased by 0.7%, according to Rosstat. Labor costs in Russia are indexed to and adjusted for inflation, which means that in the future labor costs may rise and our advantage with respect to our competitors with foreign operations that have historically had to pay higher average wages than those paid in Russia may be reduced.

Higher costs of electricity, natural gas and labor could negatively impact our operating margins, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

*A limited capacity of the railway infrastructure and an increase in railway tariffs expose us to uncertainties regarding transportation costs of raw materials and steel products.*

Railway transportation is our principal means of transporting raw materials and steel products to our facilities and to customers in Russia and abroad. The Russian rail system is controlled by Russian Railways, which is a state-sanctioned monopoly responsible for the management of all Russian railroads. The Russian government sets domestic rail freight prices and the terms of transportation, including the terms related to the type of rolling stock to be used for transportation of certain types of cargo and the estimated minimum tonnage for the purposes of determining the applicable tariff. These rail freight prices are subject to annual adjustment based on, among other factors, inflation and the funding requirements of Russian Railways' capital investment program, which is in turn affected by the acute need to upgrade track infrastructure and passenger- and cargo-handling facilities.

The most significant railcar owners are Freight One JSC, Federal Freight JSC, NefteTransService, Globaltrans and Freight Company Novotrans. Our cargoes are currently transported in the railcars owned by our subsidiary Mecheltrans or third party railcar owners, mainly to transport coal products and iron ore concentrate. Mecheltrans works with third party railcar owners to arrange for transportation and forwarding of cargoes with their railcars. In 2016, our freight volume transported by third party railcar owners amounted to 28.0 million tonnes, for which we paid 8.6 billion rubles.

In 2016, railway tariffs were indexed by 9.0%. Starting from January 1, 2017, railway tariffs have increased by an additional 6.08%. Along with the growth of tariff levels, a disruption in the transportation of our raw materials and products may occur. In 2016, due to the ban to increase the service life of railcars, the open car fleet of Russian Railways decreased sharply while traffic volumes remained unchanged. In the summer of 2016, the shortage of railcars increased as a result of scheduled track repairs. The shortage of the rolling stock led to a significant increase in prices of rolling stock operators' services and a reduction in volume of transported cargo, including our cargo. All of

the above factors may preserve in the future and negatively impact our operating margins, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

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*We face certain trade restrictions in the export of ferrosilicon to the European Union.*

In February 2008, an antidumping duty in the amount of 17.8% was imposed on exports to the European Union of ferrosilicon produced by our subsidiary Bratsk Ferroalloy Plant for a period of five years. In February 2013, the European Commission initiated an expiry review of the antidumping measures applicable to imports of ferrosilicon. In April 2014, the antidumping duty was extended for another five years. We may face additional antidumping duties and other trade restrictions in the European Union, the United States and other markets in the future. See Item 4. Information on the Company Steel Segment Trade restrictions.

*We benefit from Russia's tariffs and duties on imported steel, many of which have been reduced upon Russia's WTO membership and may be eliminated in the future.*

Russia has in place import tariffs with respect to certain imported steel products. These tariffs generally amount to 5-15% of the value of the imports. Almost all of our sales of steel products in Russia were protected by these import tariffs in 2016. The Republic of Belarus, the Republic of Kazakhstan and the Russian Federation entered into a Customs Union and implemented a Common Customs Tariff, which came into force on January 1, 2010, reducing import duties on stainless rolled products from 15% to 10%. Further, the Republic of Belarus, the Republic of Kazakhstan and the Russian Federation established the Eurasian Economic Union which was enlarged in 2015 to include the Republic of Armenia and the Kyrgyz Republic. Creation of the Customs Union, as well as other actions and decisions of Russian authorities in respect of tariffs and duties, can lead to further reduction of import duties.

On November 20, 2013, the Eurasian Economic Commission initiated an antidumping investigation against imports of steel bars originating in Ukraine. In March 2016, the investigation was completed resulting in the imposition of antidumping duties for a period of five years. Therefore, we benefit from protection of the Eurasian Economic Union's market from low-priced import of steel bars.

Upon Russia's entry into the World Trade Organization ( **WTO** ), the import tariffs and duties of Russia were reduced or eliminated, depending on the type of steel products. In particular, according to the WTO accession terms Russian import duties on most types of steel products have been reduced to 5%, causing increased competition in the Russian steel market from foreign producers and exporters.

*Our exports to the European Union are subject to REACH regulations.*

Chemical substances contained in some of our products, as well as by-products and waste, which we export to or produce in the European Union are subject to regulation (EC) No 1907/2006 on registration, evaluation, authorization and restrictions of use of chemicals ( **REACH** ). Under REACH, we must provide a registration dossier for such substances to the European Chemicals Agency ( **ECHA** ). In addition, we must provide the information about the registered substances usage and utilization to the competent authorities of the E.U. Member States and downstream users upon request. We believe that we are in compliance with current REACH requirements and we will have to maintain certain resources to ensure compliance with further developing REACH requirements.

REACH provides for a special authorization regime for substances of high concern, including those that are identified from scientific evidence as causing probable serious effects to humans or the environment on a case-by-case basis. To obtain authorization, a manufacturer of substances of high concern is generally required to demonstrate that the risk from the use of the substance is adequately controlled. All substances under the authorization regime are subject to restrictions with respect to manufacture, placing on the market or use. The European Commission may amend or withdraw the authorization, even one given for adequate control, if suitable substitutes have become available. Currently, none of our products contain substances which may be subject to the authorization regime. There is no

assurance that our products will not be subject to further restrictions or bans if any substance of high concern is detected in our products in excess of statutory thresholds, which could have a material adverse effect on our business, financial condition, results of operations and prospects.



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The European Commission has planned several revisions of the REACH regulation by 2019. Compliance with changes to the existing regulations may lead to increased costs, modifications in operating practices and/or further restrictions affecting our products. Any such changes and/or modifications could have a material adverse effect on our business, financial condition, results of operations and prospects.

*We are subject to mining risks.*

Our operations, like those of other mining companies, are subject to all of the hazards and risks normally associated with the exploration, development and production of natural resources, any of which could result in production shortfalls or damage to persons or property.

In particular, hazards associated with our open pit mining operations include, but are not limited to: (1) flooding of the open pit; (2) collapses of the open pit wall; (3) accidents associated with the operation of large open pit mining and rock transportation equipment; (4) accidents associated with the preparation and ignition of large-scale open pit blasting operations; (5) deterioration of production quality due to weather; and (6) hazards associated with the disposal of mineralized waste water, such as groundwater and waterway contamination.

Hazards associated with our underground mining operations include but are not limited to: (1) underground fires and explosions, including those caused by flammable gas; (2) cave-ins or ground falls; (3) emissions of gases and toxic chemicals; (4) flooding; (5) sinkhole formation and ground subsidence; and (6) other accidents and conditions resulting from drilling, blasting and removing and processing material from an underground mine, including due to human error.

We are at risk of experiencing any and all of these hazards. The occurrence of such hazards could delay production, increase production costs, result in injury to persons or death, and damage to property, as well as liability for us. For example, in 2008, there were two accidents at V.I. Lenina Underground which involved multiple casualties, and one of the accidents resulted in five fatalities. In 2010 through 2012, there were a number of occasions of self-heating and spontaneous ignition of coal as well as an increase of coal dust levels, each of which resulted in the temporary suspension of mining operations at the longwalls of Sibirginskaya Underground, V.I. Lenina Underground and Olzherasskaya-Novaya Underground. There were no casualties involved in any of these occasions. In 2013-2016, there were also a number of occasions which caused the temporary suspension of mining operations, but had no significant effect on our business. We implemented measures to cure the causes of these occasions and we are implementing measures aimed at preventing accidents and occasions in the future and we are cooperating with the competent governmental authorities, in particular, the Russian Federal Service for Ecological, Technological and Nuclear Supervision ( **Rostekhnadzor** ).

The risk of occurrence of these hazards is also exacerbated by the significant level of wear of the equipment of our mining enterprises. We are conducting a program of phased replacement and refurbishment of obsolete equipment in order to meet safety requirements at our most hazardous facilities.

*Abnormal weather conditions and natural hazards could negatively impact our business.*

Our production facilities are located in different climate and weather conditions, and abnormal weather changes and natural hazards could affect their operations. Interruptions in electricity supply and transport communication could lead to delays in deliveries of raw materials to our production facilities and finished products to consumers, as well as a suspension of production. For example, in 2016, a 50 meters long wash-out of railway track on the Ulak-Elga rail line occurred as a result of heavy rains. Coal transportation from the Elga deposit was interrupted for 4 days until the full restoration of the railway. In addition, the existence of abnormally low temperatures for a long period of time may

limit the work of the port infrastructure, crane equipment and mining-and-transport equipment. For example, in 2013, operations at our open pit mines in Russia were suspended for a period of 2 to 16 days. The negative impact of such abnormal or extreme climate and weather conditions may have an adverse effect on our business, financial condition, results of operations and prospects.

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*More stringent environmental laws and regulations or more stringent enforcement or findings that we have violated environmental laws and regulations could result in higher compliance costs and significant fines and penalties, cleanup costs and compensatory damages, or require significant capital investment, or even result in the suspension of our operations, which could have a material adverse effect on our business, financial condition, results of operations and prospects.*

Our operations and properties are subject to environmental laws and regulations in the jurisdictions in which we operate. For instance, our operations generate large amounts of pollutants and waste, some of which are hazardous, such as benzapiren, sulfur oxide, sulfuric acid, nitrogen ammonium, sulfates, nitrites and phenicols. Some of our operations result in the creation of sludges, including sludges containing base elements such as chromium, copper, nickel, mercury and zinc. The creation, storage and disposal of such hazardous waste is subject to environmental regulations, including the requirement to perform decontamination and reclamation, such as cleaning up highly hazardous waste oil and iron slag. In addition, pollution risks and related cleanup costs are often impossible to assess unless environmental audits have been performed and the extent of liability under environmental and civil laws is clearly determinable. Furthermore, new and more stringent regulations have been introduced in a number of countries in response to the impacts of climate change. See Increased regulations associated with climate change and greenhouse gas emissions may give rise to increased costs and may adversely impact our business and markets.

Generally, there is a greater awareness in Russia of damage caused to the environment by industry than existed during the Soviet era. At the same time, environmental legislation in Russia is generally weaker and less stringently enforced than in the European Union or the United States. However, recent Russian government initiatives indicate that Russia will introduce new water, air and soil quality standards and increase its monitoring and fines for non-compliance with environmental rules, and environmental concerns are increasingly being voiced at the local level. For example, Resolution No. 1029 of the Government of the Russian Federation dated September 28, 2015 On approval of criteria for attribution of objects having a negative impact on the environment to objects of I, II, III and IV category, sets criteria for the classification of objects that have a negative impact on the environment into the four categories. The first category includes objects that have a significant negative impact on the environment and relate to fields of application of the best available technology and the fourth category includes objects that have minimal environmental impact. Certain of our production facilities can be attributed to the first category of objects that have a negative impact on the environment.

Based on the current regulatory environment in Russia and elsewhere where we conduct our operations, as of December 31, 2016, we have not created any reserves for environmental liabilities and compliance costs, other than an accrual in the amount of RUB 3,678 million for rehabilitation provision. Any change in this regulatory environment could result in actual costs and liabilities for which we have not provided. We estimated the total amount of capital investments to address environmental concerns at our various subsidiaries at RUB 647 million as of December 31, 2016. These amounts are not accrued in the consolidated financial statements until actual capital investments are made. See note 28 to the consolidated financial statements.

In the course, or as a result, of an environmental investigation by Russian governmental authorities, courts can issue decisions requiring part or all of the production at a facility that has violated environmental standards to be halted for a period of up to 90 days. We have been cited in Russia for various violations of environmental regulations in the past and we have paid certain fines levied by regulatory authorities in connection with these infractions. In June 2013, the Russian Federal Service for the Supervision of Natural Resources ( **Rosprirodnadzor** ) claimed 398.6 million rubles from Beloretsk Metallurgical Plant as compensation for damages caused by discharging waste water into the river Belaya and Beloretsk storage reservoir. This claim was resolved by means of a settlement agreement approved by the arbitrazh court according to which Beloretsk Metallurgical Plant was obliged to reconstruct a waste treatment facilities system by December 31, 2016. In November 2016, Beloretsk Metallurgical Plant applied for a stay of

execution and the court ruled to complete the reconstruction in the period up to December 31, 2023. In February 2015, Rosprirodnadzor filed a similar claim in the amount of 195.3 million rubles against Beloretsk Metallurgical Plant. In accordance with the court's decision, Beloretsk Metallurgical Plant is obliged to perform a set of measures for equipment modernization until July 1,

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2017. See Item 8. Financial Information Litigation Environmental and safety. Though our production facilities have not been ordered to suspend operations due to environmental violations during the respective periods since we acquired or established them, there are no assurances that environmental protection authorities will not seek such suspensions in the future. In the event that production at any of our facilities is partially or wholly suspended due to this type of sanction, our business, financial condition, results of operations and prospects could be materially adversely affected.

*Increased regulations associated with climate change and greenhouse gas emissions may give rise to increased costs and may adversely impact our business and markets.*

Through our mining and power segments, we are a major producer of carbon-related products such as coal, coal concentrate and energy. Coal and coal-based energy are also significant inputs in many of the operations of our steel segment. A major by-product of the underground mining of coal is methane (CH<sub>4</sub>) and a major by-product of coal burning is carbon dioxide (CO<sub>2</sub>), both of which are considered to be greenhouse gases and generally a source of concern in connection with global warming and climate change.

The December 1997 Kyoto Protocol established a set of greenhouse gas emission targets for developed countries that have ratified the Kyoto Protocol. In order to give the countries a certain degree of flexibility in meeting their emission reduction targets, the Kyoto Protocol developed mechanisms allowing participating countries to earn and trade emissions credits by way of implementing projects aimed at meeting the Kyoto Protocol targets. The European Union has established greenhouse gas regulations and many other countries are in the process of doing so. The European Union Emissions Trading System ( EU ETS ) has had an impact on greenhouse gas and energy-intensive businesses based in the European Union. Our operations in Lithuania are currently subject to the EU ETS, as are our E.U. based customers.

The Russian Federation ratified the Kyoto Protocol in 2005 and since October 2009 Russia has established a legal procedure for implementing trading mechanisms provided under the Kyoto Protocol. However, in 2012, Russia refused to sign up for the second period of limits set to begin in 2013 and remain in effect until 2020.

In December 2015 at the Paris climate conference, 196 countries adopted the United Nations Framework Convention on Climate Change which is due to enter into force in 2020. The agreement sets out a global action plan to avoid climate change. As stated by Mr. Putin during his speech at the Paris conference, Russia expects to decrease greenhouse gas emissions to 70% of the 1990 level by 2030. Furthermore, the Russian Federation shall develop a long-term plan to reduce greenhouse gas emissions and shall establish a strategy on adaptation to climate change. In July 2015, Ministry of Natural Resources and Ecology of the Russian Federation has approved guidelines for the quantification of the amount of greenhouse gas emissions by organizations conducting business and other activities in Russia.

Further Russia's steps on implementation of the United Nations Framework Convention on Climate Change could restrict our operations and/or impose significant costs or obligations on us, including requiring additional capital expenditures, modifications in operating practices, and additional reporting obligations. These regulatory programs may also have a negative effect on our production levels, profit and cash flows and on our suppliers and customers, which could result in higher costs and lower sales. Finally, we note that even without further legislation or regulation of greenhouse gas emissions, increased awareness and any adverse publicity in the global marketplace about the greenhouse gasses emitted by companies in the steel manufacturing industry could harm our reputation and reduce customer demand for our products.

*Failure to comply with existing laws and regulations could result in substantial additional compliance costs or various sanctions which could materially adversely affect our business, financial condition, results of operations and prospects.*

Our operations and properties are subject to regulation by various government entities and agencies in connection with obtaining and renewing various licenses, permits, approvals and authorizations, as well as with

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ongoing compliance with existing laws, regulations and standards. See Item 4. Information on the Company Regulatory Matters Licensing of Operations in Russia. Governmental authorities in countries where we operate exercise considerable discretion in matters of enforcement and interpretation of applicable laws, regulations and standards, the issuance and renewal of licenses, permits, approvals and authorizations, and in monitoring licensees compliance with the terms thereof which may result in unexpected audits, criminal prosecutions, civil actions and expropriation of property. For example, in November 2015, the Ministry for Investment and Development of the Republic of Kazakhstan unilaterally terminated the contract for the silicate nickel ore production at the Shevchenko deposit in Kazakhstan's Kostanay region entered into in connection with the subsoil license for the Shevchenko deposit due to non-compliance with the terms of the contract. Governmental authorities have the right to, and frequently do, conduct periodic inspections of our operations and properties throughout the year.

Our failure to comply with existing laws and regulations or to obtain and comply with all approvals, authorizations and permits required for our operations or findings of governmental inspections may result in the imposition of fines or penalties or more severe sanctions including the suspension, amendment or termination of our licenses, permits, approvals and authorizations or in requirements that we cease certain of our business activities, or in criminal and administrative penalties applicable to our officers. Arbitrary government actions directed against other Russian companies (or the consequences of such actions) may generally impact on the Russian economy, including the securities market. Any such actions, decisions, requirements or sanctions could increase our costs and materially adversely affect our business, financial condition, results of operations and prospects.

*The concentration of our shares with our largest shareholders will limit your ability to influence corporate matters and transactions with largest shareholders may present conflicts of interest, potentially resulting in the conclusion of transactions on less favorable terms than could be obtained in arm's length transactions.*

Our Chairman, Igor Zyuzin may be deemed to be the beneficial owner of approximately 36.34% of our common shares. In addition, our Chairman's wife and children, Mrs. Irina Zyuzina and Ms. Ksenia Zyuzina and Mr. Kirill Zyuzin, together may be deemed to be the beneficial owners of approximately 18.70% of our common shares each separately. Therefore, Mr. Igor Zyuzin and Mrs. Irina Zyuzina together beneficially own 55.04% of our common shares. See Item 7. Major Shareholders and Related Party Transactions. Except in certain cases as provided by the Federal Law On Joint-Stock Companies, dated December 26, 1995, as amended (the **Joint-Stock Companies Law**), resolutions at a general shareholders' meeting are adopted by a majority of the voting stock at a meeting where shareholders holding more than half of the voting shares are present or represented. Accordingly, Mr. Zyuzin and his family members have the power to control the outcome of most matters to be decided by a majority of the voting stock present at a general shareholders' meeting and can control the appointment of the majority of directors and the removal of all of the elected directors if they act in concert. In addition, our largest shareholders are likely to be able to take actions, which require a three-quarters supermajority of the voting stock present at such a general shareholders' meeting, such as amendments to our charter, reorganization, significant sales of assets and other major transactions, if other shareholders do not participate in such meeting. Thus, our largest shareholders can take actions that you may not view as beneficial or prevent actions that you may view as beneficial, and as a result, the value of our common shares and ADSs could be materially adversely affected.

We have also engaged and will likely continue to engage in transactions with related parties, including our largest shareholder, which may present conflicts of interest, potentially resulting in the conclusion of transactions on less favorable terms than could be obtained in arm's length transactions. See Item 7. Major Shareholders and Related Party Transactions Related Party Transactions.

*Our competitive position and future prospects depend on our senior management team.*

Our ability to maintain our competitive position and to implement our business strategy is dependent on the performance of our senior management team and, in particular, Mr. Zyuzin, our Chairman and largest



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shareholder. Competition in Russia, and in the other countries where we operate, for senior management personnel with relevant expertise is intense due to the small number of qualified individuals. The loss or decline in the services of members of our senior management team or an inability to attract, retain and motivate qualified senior management personnel could have a material adverse effect on our business, financial condition, results of operations and prospects.

*Antimonopoly regulation could lead to sanctions with respect to the subsidiaries we have acquired or established or our prices, sales volumes and business practices.*

Our business has grown substantially through the acquisition and founding of companies, many of which required the prior approval or subsequent notification of the FAS or its predecessor agencies. Relevant legislation restricts the acquisition or founding of companies by legal entities or individuals acting alone or jointly with their group of persons without such approval or notification. This legislation is vague in certain parts and subject to varying interpretations. If the FAS were to conclude that a company was acquired or created in contravention of applicable legislation and that competition has been or could be limited as a result, it could seek redress, including invalidating the transactions that led to or could lead to the limitation of competition, obliging the acquirer or founder to perform activities to restore competition, and seeking the dissolution of the new company created as a result of reorganization. Any of these actions could materially adversely affect our business, financial condition, results of operations and prospects.

In 2008, the FAS issued a number of directives to our companies placing certain restrictions on our business practices. On May 13, 2008, the FAS issued a directive ordering Mechel and Southern Kuzbass Coal Company, as a group of companies holding a dominant position in the Russian coking coal market, to fulfill the following requirements:

to avoid the unjustified reduction of production volumes and product range at Southern Kuzbass Coal Company;

to provide, to the extent possible, equal supply terms to all customers without discrimination against companies not forming part of this group of companies;

not to restrict other companies from supplying coking coal to the same geographical area of operations; and

to notify the FAS prior to any increase in domestic prices of coking coal and coking coal concentrate, if such increase amounts to more than 10% of the relevant price used 180 days before the date such increase is planned to take place, with submission to the FAS of the financial and economic reasoning for the planned increase of prices.

In connection with the establishment of Mechel Mining, the subsidiary into which we consolidated certain of our mining assets, we received a directive from the FAS dated June 23, 2008, which contains requirements as to the activities of Mechel Mining and its subsidiaries Yakutugol and Southern Kuzbass Coal Company, as a group of companies holding a dominant position in the Russian coking coal market. The requirements are the same as those described above.

In August 2008, as a result of an antimonopoly investigation into the business of our subsidiaries Mechel Trading House, Southern Kuzbass Coal Company, Yakutugol and Mechel Trading, the FAS found them to have abused their

dominant position in the Russian market for certain grades of coking coal concentrate. The FAS issued a directive requiring these subsidiaries and their successors to, among others, refrain from taking any action in the Russian market for certain grades of coking coal concentrate which would or may preclude, limit or eliminate competition and/or violate third parties' interests, including fixing and maintaining a monopolistically high or low price, refusing or avoiding to enter into an agreement with certain buyers without good economic or technological reasons where the production or supply of the relevant grades of coking coal concentrate is possible and creating discriminatory conditions for buyers. Furthermore, material fines were imposed on Mechel Trading House, Southern Kuzbass Coal Company and Yakutugol.

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In the event of a breach of the terms of business conduct set forth by the FAS, the FAS may seek to impose fines for violations of antimonopoly and administrative legislation. Such fines may include an administrative fine of an amount from 300 thousand to one million rubles or, if such violation has led or may lead to the prevention, limitation or elimination of competition, an administrative fine of up to 15% of the proceeds of sale of all goods, works and services on the market where such violation was committed, but not more than 2% of gross proceeds of sale of all goods, works and services. Russian legislation also provides for criminal liability for violations of antimonopoly legislation in certain cases. Furthermore, for systematic violations, a court may order, pursuant to a suit filed by the FAS, a compulsory split-up or spin-off of the violating company, and no affiliation can be preserved between the new entities established as result of such a mandatory reorganization. The imposition of any such liability on us or our subsidiaries could materially adversely affect our business, financial condition, results of operations and prospects.

In 2016, the FAS conducted large-scale inspections of companies engaged in loading, unloading and storage of cargoes in ports of the Russian Federation concerning justification of applied tariffs for services. Based on the findings, proceedings for violation of antimonopoly legislation were initiated in respect of a number of companies. Our group companies which provide services of loading, unloading and storage of cargoes in ports were not subject to proceedings for violation of antimonopoly legislation, however the inspections are ongoing. The FAS is also considering repeated introduction of government regulation of tariffs for services of loading, unloading and storage of cargoes in ports which could have a material adverse effect on our business, financial condition, results of operations and prospects.

Negative publicity associated with any antimonopoly, administrative, criminal or other investigation or prosecution carried out with respect to our business practices, regardless of the outcome, could damage our reputation and result in a significant drop in the price of our shares and ADSs and could materially adversely affect our business, financial condition, results of operations and prospects.

*In the event that the minority shareholders of our subsidiaries were to successfully challenge past interested party transactions or do not approve interested party transactions in the future, we could be limited in our operational flexibility.*

We own less than 100% of the equity interests in some of our subsidiaries. In addition, certain of our wholly-owned subsidiaries have previously had other shareholders. We and our subsidiaries have carried out, and continue to carry out, transactions among our companies which may be deemed controlling or controlled entities in relation to each other, as well as transactions with other parties which may be considered to be interested party transactions under Russian law, requiring approval by disinterested directors, disinterested independent directors or disinterested shareholders depending on the nature and value of the transaction and the parties involved. The provisions of Russian law defining which transactions must be approved as interested party transactions are subject to different interpretations, and these transactions may not always have been properly approved, including by former shareholders. We cannot make any assurances that our and our subsidiaries' applications of these rules will not be subject to challenge by shareholders. Any such challenges, if successful, could result in the invalidation of transactions, which could have a material adverse effect on our business, financial condition, results of operations and prospects.

In addition, Russian law requires a three-quarters majority of the voting stock present at a general shareholders meeting to approve certain matters, including, for example, charter amendments, reorganizations, major transactions involving property in excess of 50% of the balance sheet value of the company's assets, acquisition by the company of outstanding shares and certain share issuances. In some cases, minority shareholders may not approve interested party transactions requiring their approval or other matters requiring approval of minority shareholders or supermajority approval. In the event that these minority shareholders were to successfully challenge past interested party transactions, or do not approve interested party transactions or other matters in the future, we could be limited in our

operational flexibility and our business, financial condition, results of operations and prospects could be materially adversely affected.

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*Minority shareholder lawsuits, if resolved against our group companies, could have a material adverse effect on our financial condition and results of operations.*

Russian corporate law allows minority shareholders holding in aggregate at least 1% of the voting shares to have standing to bring claims against the company challenging decisions of its governing bodies. These features of Russian corporate law are often abused by minority shareholders, who can bring claims in local courts seeking injunctions and other relief for which, in some cases, we may not receive notice. Any such actions by minority shareholders, if resolved against our group companies, could have a material adverse effect on our business, financial condition, results of operations and prospects. See Item 8. Financial Information Litigation Securities litigation.

*A majority of our employees are represented by trade unions, and our operations depend on good labor relations.*

As of December 31, 2016, approximately 59% of all our employees were represented by trade unions. Although we have not experienced any business interruption at any of our companies as a result of labor disputes from the dates of their respective acquisition by us and we consider our relations with our employees to be good, under Russian law unions have the legal right to strike and other Russian companies with large union representation periodically face interruptions due to strikes, lockouts or delays in renegotiations of collective bargaining agreements. Our businesses could also be affected by similar events if our relationships with our labor force and trade unions worsen in the future. We have extended the industry agreements for coal and ore mining and smelting industries and have renegotiated most related collective bargaining agreements. If we are unable to prolong collective bargaining agreements on similar conditions in the future or our employees are dissatisfied with the terms of the collective bargaining agreements and undertake any industrial action, it could have material adverse effects on our business, financial condition, results of operations and prospects.

*We do not carry the types of insurance coverage customary in more economically developed countries for a business of our size and nature, and a significant adverse event could result in substantial property loss and inability to rebuild in a timely manner or at all.*

The insurance industry is still developing in Russia, and many forms of insurance protection common in more economically developed countries are not available in Russia on comparable terms, including coverage for business interruption. At present, most of our Russian production facilities are not insured, and we have no coverage for business interruption or for third-party liability, other than insurance required under Russian law, collective agreements, loan agreements or other undertakings. Some of our international production facilities are not covered by comprehensive insurance typical for such operations in Western countries. We cannot assure you that the insurance we have in place is adequate for the potential losses and the liability we may suffer.

Since most of our production facilities lack insurance covering their property, if a significant event were to affect one of our facilities, we could experience substantial financial and property losses, as well as significant disruptions in our production activity, for which we would not be compensated by business interruption insurance.

Since we do not maintain separate funds or otherwise set aside reserves for these types of events, in case of any such loss or third-party claim for damages we may be unable to seek any recovery for lost or damaged property or compensate losses due to disruption of production activity. Any such uninsured loss or event may have a material adverse effect on our business, financial condition, results of operations and prospects.

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*If transactions, corporate decisions or other actions of members of our group and their predecessors-in-interest were to be challenged on the basis of non-compliance with applicable legal requirements, the remedies in the event of any successful challenge could include the invalidation of such transactions, corporate decisions or other actions or the imposition of other liabilities on such group members.*

Businesses of our group, or their predecessors-in-interest at different times, have taken a variety of actions relating to the incorporation of entities, share issuances, share disposals and acquisitions, mandatory buy-out offers, acquisition and valuation of property, including land plots, interested party transactions, major transactions, decisions to transfer licenses, meetings of governing bodies, other corporate matters and antimonopoly issues that, if successfully challenged on the basis of non-compliance with applicable legal requirements by competent state authorities, counterparties in such transactions or shareholders of the relevant members of our group or their predecessors-in-interest, could result in the invalidation of such actions, transactions and corporate decisions, restrictions on voting rights or the imposition of other liabilities. As applicable laws of the jurisdictions where our group companies are located are subject to varying interpretations, we may not be able to defend successfully any challenge brought against such actions, decisions or transactions, and the invalidation of any such actions, transactions and corporate decisions or imposition of any restriction or liability could have a material adverse effect on our business, financial condition, results of operations and prospects.

*Terrorist attacks and threats, escalation of military activity, as well as massive cyber attacks or incidents, and government regulation in response to such attacks or acts of war may negatively affect our business, financial condition, results of operations and prospects.*

Terrorist attacks and threats, escalation of military activity, as well as massive cyber attacks or incidents, and an increase in government regulation in response to such attacks or acts of war may negatively affect our business. There could be delays or losses in transportation and deliveries of our products to our customers, increased government regulation and decreased sales due to disruptions in the businesses of our customers. It is possible that any such occurrences could have a material adverse effect on our business, financial condition, results of operations and prospects.

*We have used certain information in this document that has been sourced from third parties.*

We have sourced certain information contained in this document from independent third parties, including private companies, government agencies and other publicly available sources. We believe these sources of information are reliable and that the information fairly and reasonably characterizes the industry in countries where we operate. However, although we take responsibility for compiling and extracting the data, we have not independently verified this information. In addition, the official data published by Russian federal, regional and local governments may substantially differ from those of Western countries. Official statistics may also be produced on different bases than those used in Western countries.

### ***Risks Relating to Our Shares and the Trading Market***

*The price of our shares and ADSs could be volatile and could drop unexpectedly, making it difficult for investors to resell our shares or ADSs at or above the price paid.*

The price at which our shares and ADSs trade is influenced by a large number of factors, some of which are specific to us and our operations and some of which are related to the mining and steel industries and equity markets in general. As a result of these factors, investors may not be able to resell their shares or ADSs at or above the price paid for them. In particular, the following factors, in addition to other risk factors described in this section, may have a

material impact on the market price of our shares and ADSs:

investor perception of us as a company;

actual or anticipated fluctuations in our revenues or operating results;

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announcement of intended acquisitions, disposals or financings, or speculation about such acquisitions, disposals or financings;

changes in our dividend policy, which could result from changes in our cash flow and capital position;

sales of blocks of our common shares, common ADSs, preferred shares or preferred ADSs by significant shareholders, including the Justice persons;

price and timing of any refinancing of our indebtedness;

potential litigation involving us;

changes in financial estimates and recommendations by securities research analysts;

fluctuations in Russian and international capital markets, including those due to events in other emerging markets;

the performance of other companies operating in similar industries;

regulatory developments in the markets where we operate, especially Russia and the European Union;

international political and economic conditions, including the effects of fluctuations in foreign exchange rates, interest rates and oil prices and other events such as terrorist attacks, military operations, changes in governments and relations between countries, international sanctions, particular those currently in place against certain Russian companies and individuals, natural disasters and the uncertainty related to these developments;

news or analyst reports related to markets or industries in which we operate; and

general investor perception of investing in Russia.

As a result of deteriorating market conditions in 2014 for our main products, together with our high leverage, our shares and ADSs price dropped significantly in 2014, and ADSs started trading below one U.S. dollar and thus became non-compliant with the NYSE continuous listing standards. On February 27, 2015, the 30 trading-day average closing price of ADSs amounted to \$1.26 per ADS. As a result, we received official notice from the NYSE on March 2, 2015 that our ADSs came back into compliance with the listing standards.



On August 19, 2015, we received an official notice from the NYSE stating that the price for Mechel ADSs had fallen below the \$1.00 threshold and we were required to bring our share price and average share price back above one U.S. dollar within six months from the date of receipt of the notice. In order to regain compliance with the NYSE requirements, we changed the ratio of our ADSs from one ADS per one common share to one ADS per two common shares, which became effective on January 12, 2016. As a result, we received official notice from the NYSE on February 1, 2016 that our ADSs came back into compliance with the listing standards.

*Our ability to pay dividends depends primarily upon receipt of sufficient funds from our subsidiaries.*

Because we are a holding company, our ability to pay dividends depends primarily upon receipt of sufficient funds from our subsidiaries. Under Russian law, dividends may be declared and paid only out of net profits calculated under Russian accounting standards and as long as certain conditions have been met, including if the value of the net assets, calculated under Russian accounting standards, is not less (and would not become less as a result of the proposed dividend payment) than the sum of the charter capital, the reserve fund and the difference between the liquidation value and the par value of the issued and outstanding preferred shares. See Item 10. Additional Information Charter and Certain Requirements of Russian Legislation Description of Capital Stock Dividends. Currently, some of our subsidiaries do not meet this criteria and cannot approve payment of, or pay dividends. See Risks Relating to the Russian Federation One or more of our subsidiaries could be forced into liquidation on the basis of formal non-compliance with certain requirements of Russian law, which could materially adversely affect our business, financial condition, results of operations and prospects.

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Furthermore, the payment of dividends by our subsidiaries and/or our ability to repatriate such dividends may, in certain instances, be subject to taxes, statutory restrictions, retained earnings criteria, and covenants in our subsidiaries financing arrangements and are contingent upon the earnings and cash flow of those subsidiaries. See note 25 to the consolidated financial statements. In addition, loan agreements which we have restructured contain restrictions on the payment of dividends on our common and preferred shares. See Item 8. Financial Information Dividend Distribution Policy.

*Upon introduction of a new system of recording the depositary's rights to the shares underlying depositary receipts, the depositary is required to disclose information on ADS and GDS owners in order to exercise voting rights and receive dividends with respect to the shares underlying ADSs and GDSs.*

Effective January 1, 2013, a new system of recording the depositary's rights to the shares underlying depositary receipts was introduced by the Federal Law No. 415-FZ of December 7, 2011, as amended on December 29, 2012 ( **Federal Law No. 415-FZ** ). Pursuant to the new system, the underlying shares are no longer recorded at the depositary's owner's account opened with a Russian custodian holding a depo account of nominee holder with the issuer's shareholder register. Instead, the underlying shares are now recorded at a depo account of depositary programs opened with a Russian custodian which in its turn has a depo account of nominee holder opened with the central depositary. On November 6, 2012, the FFMS granted JSC National Settlement Depositary ( **NSD** ) the status of Russian central depositary. Starting from November 6, 2013, the depo accounts of depositary programs should be opened for depositaries, and shares represented by depositary receipts should be recorded in depo accounts of depositary programs.

In addition to the new recording system, the Federal Law No. 415-FZ also sets forth new obligations for a depositary to disclose information on depositary receipt owners in order to exercise voting rights with respect to the shares represented by depositary receipts. The CBR by its Directive No. 3680-U dated June 15, 2015 sets forth the requirements for the provision of information about the depositary receipt owners. Such information is provided to the issuer in the form of a list of persons who exercise the rights under the depositary receipts. The list is provided to the issuer by the foreign depositary which opens the depo account of depositary programs. The list is provided for the preparation and holding of a shareholders' meeting. Furthermore, any obligations of the depositary to disclose information on depositary receipt owners in order to receive dividends were abolished effective January 1, 2014 pursuant to the Federal Law No. 282-FZ of December 29, 2012, as amended ( **Federal Law No. 282-FZ** ). Under the Federal Law No. 282-FZ, the payment of dividends on the shares represented by depositary receipts is made to the foreign depositary which opens the depo account of depositary programs.

Currently, it is not clear whether the term depositary receipt owner means a holder registered on the records of the depositary, a securities intermediary or a beneficial owner of a depositary receipt. As a result, the scope of the above reporting obligations, which may affect the rights of our ADS and GDS holders, also remains uncertain. We cannot assure you that the Federal Law No. 415-FZ and the other regulations by the CBR, to which the powers of the FFMS were delegated, will be compatible with the way in which depositary receipt programs were customarily operated in the past or with foreign confidentiality regulations, or that the new requirements will not impose additional burdens upon the depositary, ADS and GDS holders or their respective securities intermediaries, any of which may cause investments in our ADSs to be seen as less attractive.

In addition, the Federal Law No. 282-FZ requires the foreign depositary to take all reasonable steps to provide information on depositary receipt owners to the issuer, state arbitrazh courts, the CBR and governmental investigative authorities upon their request, and depositary receipt owners may not refuse to provide such information in response to the depositary if so requested. The CBR is entitled to demand the depositary to cure any breach of such disclosure requirements, and if the depositary fails to cure, the CBR may suspend or limit any operations with depo accounts of

depository receipt program for up to six months with respect to the number of securities not exceeding the number of securities for which the obligation to provide information has not been fulfilled. It is unclear how the CBR will use these new regulatory powers. Any suspension of or limitation on our ADS or GDS programs could have a material adverse effect on the value of the ADSs.

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*The depositary may be required to take certain actions due to Russian law requirements which could adversely impact the liquidity and the value of the shares and ADSs.*

If at any time the depositary believes that the shares deposited with it against the issuance of ADSs represent (or, upon accepting any additional shares for deposit, would represent) a percentage of shares which exceeds any threshold or limit established by any applicable law, directive, regulation or permit, or satisfies any condition for making any filing, application, notification or registration or obtaining any approval, license or permit under any applicable law, directive or regulation, or taking any other action, the depositary may (1) close its books to deposits of additional shares in order to prevent such thresholds or limits being exceeded or conditions being satisfied or (2) take such steps as are, in its opinion, necessary or desirable to remedy the consequences of such thresholds or limits being exceeded or conditions being satisfied and to comply with any such law, directive or regulation, including, causing *pro rata* cancellation of ADSs and withdrawal of underlying shares from the depositary receipt program to the extent necessary or desirable to so comply. Any such circumstances may affect the liquidity and the value of the shares and ADSs.

*Voting rights with respect to the shares represented by our ADSs are limited by the terms of the relevant deposit agreement for the ADSs and relevant requirements of Russian law.*

ADS holders have no direct voting rights with respect to the shares represented by the ADSs. They can only exercise voting rights with respect to the shares represented by ADSs in accordance with the provisions of the deposit agreements relating to the ADSs and relevant requirements of Russian law. Therefore, there are practical limitations upon the ability of ADS holders to exercise their voting rights due to the additional procedural steps which are involved. Our charter require us to notify shareholders not less than 30 days prior to the date of any meeting of shareholders and at least 50 days prior to the date of an extraordinary meeting to elect our Board of Directors. Within specified time limits, the notification of the convocation of the general shareholders meeting shall be sent to each person entitled to participate in the general shareholders meeting by post or delivered to each of the above persons against signature in accordance with the procedure prescribed by our charter and published on our site [www.mechel.ru](http://www.mechel.ru) in the information and telecommunication network Internet, or in the newspaper *Rossiyskaya Gazeta* and on our site [www.mechel.ru](http://www.mechel.ru) in the information and telecommunication network Internet or on our site [www.mechel.ru](http://www.mechel.ru) in the information and telecommunication network Internet. Our common shareholders, as well as our preferred shareholders in cases when they have voting rights, are able to exercise their voting rights by either attending the meeting in person or voting by power of attorney.

For ADS holders, in accordance with the deposit agreements, we will provide the notice to the depositary. The depositary has in turn undertaken, as soon as practicable thereafter, to mail to ADS holders notice of any such meeting of shareholders, copies of voting materials (if and as received by the depositary from us) and a statement as to the manner in which instructions may be given by ADS holders. To exercise their voting rights, ADS holders must then timely instruct the depositary how to vote their shares. As a result of this extra procedural step involving the depositary, the process for exercising voting rights may take longer for ADS holders than for holders of shares. ADSs for which the depositary does not receive timely voting instructions will not be voted at any meeting.

In addition, although securities regulations expressly permit the depositary to split the votes with respect to shares underlying the ADSs in accordance with instructions from ADS holders, there is little court or regulatory guidance on the application of such regulations, and the depositary may choose to refrain from voting at all unless it receives instructions from all ADS holders to vote the shares in the same manner. Holders of ADSs may thus have significant difficulty in exercising voting rights with respect to the shares underlying the ADSs. There can be no assurance that holders and beneficial owners of ADSs will: (1) receive notice of shareholder meetings to enable the timely return of voting instructions to the depositary; (2) receive notice to enable the timely cancellation of ADSs in respect of shareholder actions; or (3) be given the benefit of dissenting or minority shareholders rights in respect of an event or

action in which the holder or beneficial owner has voted against, abstained from voting or not given voting instructions.

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*ADS holders may be unable to repatriate their earnings.*

Dividends that we may pay in the future on the shares represented by the ADSs will be declared and paid to the depositary in rubles. Such dividends will be converted into U.S. dollars by the depositary and distributed to holders of ADSs, net of the fees and charges of, and expenses incurred by, the depositary, together with taxes withheld and any other governmental charges. The ability to convert rubles into U.S. dollars is subject to the currency markets. Although there is an active market for the conversion of rubles into U.S. dollars, including the interbank currency exchange and over-the-counter and currency futures markets, the functioning of this market in the future is not guaranteed and, in particular may be negatively impacted by any future imposition of exchange controls imposed by the Russian authorities in an effort to stabilize the value of the ruble.

*ADS holders may not be able to benefit from the United States-Russia income tax treaty.*

Under Russian tax legislation, dividends paid to a non-resident holder of shares of a Russian company generally will be subject to a 15% withholding tax. This tax rate may potentially be reduced to 10% or 5% for U.S. holders of the shares that are legal entities and organizations and to 10% for U.S. holders of the shares that are individuals under the Convention between the United States of America and the Russian Federation for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and Capital (the **United States-Russia income tax treaty** ), provided a number of conditions are satisfied. In connection with the enactment of amendments to Russian tax legislation, effective from January 1, 2014, the reduced tax rate of 5% established in accordance with certain provisions of the United States-Russia income tax treaty does not apply on dividend payments under ADSs. The general rate of 10% which is established by the treaty and does not account for benefits applies, subject to the submission of certain information to the tax agent. If such information has not been submitted to the tax agent in the prescribed manner and in a certain period of time, a tax rate of 30% is applied. Thus, the tax agent may be obliged to withhold tax at higher non-treaty rates when paying out dividends, and U.S. ADS holders may be unable to benefit from the United States-Russia income tax treaty. ADS holders may apply for a refund of a portion of the tax withheld under an applicable tax treaty, however, this process may be time-consuming and no assurance can be given that the Russian tax authorities will grant a refund. See Item 10. Additional Information Taxation Russian Income and Withholding Tax Considerations for additional information.

*Capital gains from the sale of ADSs may be subject to Russian profit tax.*

Under Russian tax legislation, gains realized by foreign organizations from the disposition of Russian shares and securities, as well as financial instruments derived from such shares, with the exception of shares that are traded on an organized securities market, may be subject to Russian profit tax or income tax if more than 50% of our assets directly or indirectly consist of immovable property located in Russia. Gains arising from the sale on foreign exchanges (foreign market operators) of securities or derivatives circulated on such exchanges are not considered Russian source income.

However, no procedural mechanism currently exists to withhold and remit this tax with respect to sales made to persons other than Russian companies and foreign companies with a registered permanent establishment in Russia. Gains arising from the disposition on foreign stock exchanges of the foregoing types of securities listed on these exchanges are not subject to taxation in Russia.

Gains arising from the disposition of the foregoing types of securities and derivatives outside of Russia by U.S. holders who are individuals not resident in Russia for tax purposes will not be considered Russian source income and will not be taxable in Russia. Gains arising from disposition of the foregoing types of securities and derivatives in Russia by U.S. holders who are individuals not resident in Russia for tax purposes may be subject to a withholding tax

in Russia based on an annual tax return, which they may be required to submit with the Russian tax authorities.

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*Holders of ADSs may have limited recourse against us and our directors and executive officers because most of our operations are conducted outside the United States and all of our directors and executive officers reside outside the United States.*

Our presence outside the United States may limit ADS holders' legal recourse against us. Mechel is incorporated under the laws of the Russian Federation. Our directors and executive officers reside outside the United States, principally in Russia. A substantial portion of our assets and the assets of most of our directors and executive officers are located outside the United States. As a result, holders of our ADSs may be limited in their ability to effect service of process within the United States upon us or our directors and executive officers or to enforce in a U.S. court a judgment obtained against us or our directors and executive officers in jurisdictions outside the United States, including actions under the civil liability provisions of U.S. securities laws. In addition, it may be difficult for holders of ADSs to enforce, in original actions brought in courts in jurisdictions outside the United States, liabilities predicated upon U.S. securities laws.

There is no treaty between the United States and the Russian Federation providing for reciprocal recognition and enforcement of foreign court judgments in civil and commercial matters. These limitations may deprive investors of effective legal recourse for claims related to investments in the ADSs. The deposit agreements provide for actions brought by any party thereto against us to be settled by arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association, provided that any action under the U.S. federal securities laws or the rules or regulations promulgated thereunder may, but need not, be submitted to arbitration. The Russian Federation is a party to the United Nations (New York) Convention on the Recognition and Enforcement of Foreign Arbitral Awards, but it may be difficult to enforce arbitral awards in the Russian Federation due to a number of factors, including the inexperience of Russian courts in international commercial transactions, official and unofficial political resistance to enforcement of awards against Russian companies in favor of foreign investors and Russian courts' inability to enforce such orders.

*We and the Justice persons may offer additional preferred shares and preferred ADSs in the future, and these and other sales may adversely affect the market price of the preferred shares and preferred ADSs.*

As of March 31, 2017, of the 138,756,915 issued preferred shares, 40% are held by our wholly-owned subsidiary Skyblock Limited, the remaining preferred shares are held by the public and may be held by James C. Justice II, James C. Justice III, James C. Justice Companies Inc. and Jillean L. Justice (collectively, the **Justice persons**). The Justice persons disposed or may dispose of all or part of the remaining preferred shares they held through one or more offerings or broker trades. It is also possible that we may decide to offer additional preferred shares and preferred ADSs through public offering or broker trades in the future, including preferred shares held by Skyblock Limited. Additional offerings or sales of preferred shares and preferred ADSs by us or the Justice persons, or the public perception that such offerings or sales may occur, could have an adverse effect on the market price of our preferred shares and preferred ADSs.

***Risks Relating to the Russian Federation***

*Emerging markets such as Russia are subject to greater risks than more developed markets, and financial turmoil in developed or other emerging markets could have a material adverse effect on our business and could cause the value of our shares and ADSs to fluctuate widely.*

Investors in emerging markets such as the Russian Federation should be aware that these markets are subject to greater risk than more developed markets, including in some cases significant legal, economic and political risks. Investors should also note that the value of securities of Russian companies is subject to rapid and wide fluctuations



due to various factors. The emergence of new tensions between Russia and other countries, imposed sanction by Russian Federation on some countries and vice versa may lead to outflow of the investors from the market, quick and huge sales of Russian assets which will result in reductions in the price of Russian securities. We cannot assure you that any such developments will not have a material adverse effect on our business, financial condition, results of operations and prospects, and the value of our shares and ADSs is expected to be highly volatile while tension between Russian and other countries remains unresolved and/or the Russian economy continues to deteriorate.

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Investors should also note that emerging markets such as the Russian Federation are subject to rapid change and that the information set forth in this document may become outdated relatively quickly. Moreover, financial turmoil in any emerging market country tends to affect adversely the value of investments in all emerging market countries as investors move their money to more stable, developed markets. As has happened in the past, financial problems or an increase in the perceived risks associated with investing in emerging economies could dampen foreign investment in the Russian Federation and adversely affect the Russian economy. In addition, during such times, companies that operate in emerging markets can face liquidity constraints as foreign funding sources become less available. Accordingly, investors should exercise particular care in evaluating the risks involved and must decide for themselves whether, in light of those risks, their investment is appropriate. Generally, investment in emerging markets is only suitable for sophisticated investors who fully appreciate the significance of the risks involved.

*Domestic, regional and international political and diplomatic conflicts could create an uncertain operating environment that could adversely affect our business and hinder our long-term planning ability.*

Russia has endured ethnic, religious, historical and other divisions, which have, on occasion, given rise to tensions and, in certain cases, diplomatic and military conflict, both internally and with other countries.

For example, the Russian Federation was involved in armed conflict with Georgia in August 2008, and differing views on the Georgia conflict have had an impact on the relationship between the Russian Federation, the European Union, the United States and certain former Soviet Union countries. In addition, the relationship between Ukraine and the Russian Federation has in the recent past been subject to significant strain for a number of reasons, including Ukraine's failure to pay and accumulation of payment arrears relating to the supply of energy resources, Ukraine's possible accession to NATO and the European Union. More recently, Russia's relations with Ukraine have reached an historic post-Soviet low point following renewed political instability in Ukraine that resulted in the departure from office of Mr. Yanukovich (Ukraine's former president), Russia's role in the subsequent accession of Crimea and Sevastopol to Russia, and widespread accusations that Russia is actively involved in or otherwise supporting insurgents in eastern Ukraine in their struggle against Ukraine's central authorities. This has resulted in a substantial deterioration in Russia's relations with the United States, the European Union and other countries such as Canada, Japan and Australia, and has led to the imposition of sanctions against certain Russian individuals and entities and has contributed to certain volatility in the Russian economy and a deterioration in Russia's macroeconomic condition and prospects. See **Risks Relating to the Russian Federation** The political and economic crisis in Ukraine as well as other politically related disagreements and allegations between Russia and other countries and sanctions imposed as a result thereof by the United States and the European Union may have a material adverse effect on our business, liquidity and financial condition, as well as the trading market for and value of our shares and ADSs. If such tensions intensify or new tensions emerge between the Russian Federation and Ukraine, Georgia, the European Union, the United States or any other countries, leading potentially to the imposition of further trade sanctions or embargoes, the Russian economy will likely experience further volatility and deterioration.

In September 2015, the Russian Federal Council approved the use of Russian forces in Syria, following a formal request from the Syrian government. Operations in Syria commenced in late September 2015 and are continuing as at the date hereof. Furthermore, in November 2015, the Turkish air force shot down a Russian strike aircraft over the territory of Syria, which resulted in tensions between Russia and Turkey and led to imposition of wide range of sanctions by Russia against Turkey, which were partially removed in the second half of 2016 and beginning of 2017. Russian involvement in the conflict in Syria could further lead to the escalation of geopolitical situation and the deterioration of relationship between the Russian Federation and other countries.

Many of the aforementioned events have adversely affected the Russian economy and the Russian financial and banking markets, increased capital outflows, as well as worsened general business and investment climate in Russia.

The Russian stock exchanges have experienced heightened volatility, Russia's credit markets have tightened, and the exchange rate of the ruble against the U.S. dollar and other currencies has depreciated

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significantly. See Risks Relating to Our Financial Condition and Financial Reporting Changes in the exchange rate of the ruble against the U.S. dollar and in interest rates may materially adversely affect our business, financial condition and results of operations.

In part as a result of political tensions, international sanctions, ruble volatility and drop in the oil price, in January 2015, Standard & Poor's lowered the long- and short-term Russian Federation's foreign currency rating to BB+/B from BBB-/A-3 and local currency rating to BBB-/A-3 from BBB/A-2, both with a negative outlook. In September 2016, Standard & Poor's confirmed the Russian Federation's ratings and revised the outlook from negative to stable. In March 2017, the Russian Federation's ratings were confirmed at previous levels (BB+/B for foreign currency and BBB-/A-3 for local currency) with outlook changed to positive. In January 2015, Moody's Investors Service lowered Russia's government bond rating to Baa3 from Baa2, further downgrading it in February 2015 to Ba1, with a negative outlook. In February 2017, Moody's confirmed Russia's Ba1 rating and revised the outlook from negative to stable. In January 2015, Fitch downgraded the Russian Federation's long-term foreign and local currency Issuer Default Rating to BBB- with a negative outlook. In October 2016, Fitch confirmed the Russian Federation's ratings and revised the outlook from negative to stable. In March 2017, the Russian Federation's ratings were confirmed at BBB- with a stable outlook.

The risks associated with these events or potential future events could materially and adversely affect the investment environment and overall consumer confidence in the Russian Federation, which in turn could have a material adverse effect on our business, financial condition, results of operations and prospects.

*The political and economic crisis in Ukraine as well as other politically related disagreements and allegations between Russia and other countries and sanctions imposed as a result thereof by the United States and the European Union may have a material adverse effect on our business, liquidity and financial condition, as well as the trading market for and value of our shares and ADSs.*

In connection with the ongoing events in Ukraine, the United States and the European Union (as well as certain other countries) have imposed sanctions on certain Russian and Ukrainian persons and entities. Furthermore, in December 2016, President Obama announced sanctions against Russia's intelligence and security services, the Main Intelligence Directorate (GRU) and the Federal Security Service (FSB), as well as other entities and individuals associated with the GRU in connection with certain allegations of tampering with the political process in the United States by those entities. Furthermore, the United States Senate proposed further legislation to impose sanctions on Russia, as of the date hereof the discussions are still ongoing.

No individual or entity within our group has been designated with sanctions. Additional designations may be made, or additional categories of sanctions may be created, at any time, and we can give no assurance that any member of our group, or individuals holding positions in our group, will not be affected by future sanctions designations. The U.S. regulations identify metals and mining as an example of a sector that may be identified for sectoral sanctions, however, at this time, no such identification has been made. U.S. law also provides that persons that have materially assisted, sponsored or provided financial, material or technological support for, or goods or services to or in support of any targeted person or activity may be designated for sanctions. Mechel, like a large number of Russian companies, has commercial relationships with entities that are subject to U.S. sanctions.

Furthermore, certain entities within our group are E.U. persons. These entities are therefore required to comply with the E.U. sanctions regime, including not conducting business with any sanctioned persons. Most of the group's entities, however, are neither U.S. persons nor E.U. persons, and therefore are restricted in dealings with sanctioned persons only to the extent those dealings are subject to U.S. and/or E.U. jurisdiction. However, the United States takes a broad view with respect to its sanctions jurisdiction, and there can be no assurance that compliance issues under applicable

U.S. and/or E.U. sanctions laws and regulations will not arise with respect to us or our personnel. In particular, sanctions against Russia and Russian subjects are very recent, their scope and

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consequences remain subject to interpretation by competent authorities and courts in the United States and the European Union, and no assurance can be given that a broader interpretation may not affect any of the group entities. Non-compliance with applicable sanctions could result in, among other things, the inability of the relevant group entities to contract with U.S. and/or E.U. governments or their agencies, civil or criminal liability of such entities and/or their personnel under U.S. and/or E.U. law, the imposition of significant fines, and negative publicity and reputational damage. In addition, should our dealings with sanctioned counterparties become material, our ability to transact with U.S. or E.U. persons could be affected. As a result, our ability to raise funding from international financial institutions or the international capital markets may be inhibited.

Further tensions between Russia and other countries and any escalation of related tensions between Russia and the United States and/or the European Union, the imposition of further sanctions, or continued uncertainty regarding the scope thereof, could have a prolonged adverse impact on the Russian economy, particularly levels of disposable income, consumer spending and consumer confidence, as well as the ability of Russian banks to sustain required liquidity levels and comply with their financial obligations. These impacts could be more severe than those experienced to date. In particular, should either the United States or the European Union expand their respective sanctions on our existing or future clients, suppliers or other counterparties, a large sector of the Russian economy or otherwise, such an expansion could result in our dealings with designated persons, if any, being materially adversely impacted, the suspension or potential curtailment of business operations between us and the designated persons could occur, and substantial legal and other compliance costs and risks on our business operations could emerge.

Moreover, if we become subject to U.S. or E.U. sanctions, we may become unable to deal with persons or entities bound by the relevant sanctions, including international financial institutions and rating agencies, transact in U.S. dollars, raise funds from international capital markets, acquire equipment from international suppliers, or access our assets held abroad. Should any sector in which we operate become subject to so-called sectoral sanctions, in either of the United States or the European Union, the relevant clearing systems, brokers and other market participants as well as the New York Stock Exchange ( **NYSE** ) may refuse to permit trading in or otherwise facilitate transfers of the ADSs. Furthermore, investors in our shares or ADSs may be restricted in their ability to sell, transfer or otherwise deal in or receive distributions with respect to our shares or ADSs, either because the investor or (in the case of ADSs) the depository is subject to the jurisdiction of an applicable sanctions regime, which could make such shares or ADSs partially or completely illiquid and have a material adverse effect on their market value.

An expansion of sanctions as set forth above would likely have a material adverse impact on our business, financial condition, results of operations or prospects.

***Economic risks***

*Economic instability in Russia could adversely affect our business and the value of our shares and ADSs.*

The Russian economy has experienced various risks in the past, including high state debt, high interest rates, devaluation of the national currency and others, as well as positive trends, such as annual increases in the gross domestic product ( **GDP** ), a relatively stable ruble, strong domestic demand, rising real wages and reduced rates of inflation. However, the positive trends were interrupted by the global financial crisis in late 2008, which led to a substantial decrease in the GDP's growth rate, ruble depreciation and a decline in domestic demand. The Russian government took certain anti-crisis measures using the stabilization fund and hard currency reserves in order to soften the impact of the economic crisis on the Russian economy and support the value of the ruble. The emerging market economies, including Russia, began to experience a new economic slowdown in 2013, which together with political and other disturbances in emerging markets have introduced additional uncertainty in the overall outlook for growth of the global economy. Growth in the Russian economy has slowed down considerably, recording GDP growth of

0.6% in 2014 and further decline of 3.7% in 2015 and 0.2% in 2016, according to Rosstat. The deterioration of Russian economy in recent years is resulted from an array of factors,

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including negative investor sentiment arising from the disturbances in eastern Ukraine, international sanctions imposed on Russian companies and individuals, substantial depreciation of the ruble against major world currencies and the precipitous drop in oil prices. See **Risks Relating to the Russian Federation** The political and economic crisis in Ukraine as well as other politically related disagreements and allegations between Russia and other countries and sanctions imposed as a result thereof by the United States and the European Union may have a material adverse effect on our business, liquidity and financial condition, as well as the trading market for and value of our shares and ADSs. Further economic instability in Russia could have a material adverse effect on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.

*The Russian banking system is still developing, and another banking crisis or international sanctions could place severe liquidity constraints on our business.*

A substantial portion of our loans are from Russian banks, including state-owned banks such as Sberbank, VTB Bank and Gazprombank, who in recent years have extended the maturity of our loans, waived breaches of financial covenants and reset our financial covenants to give us more flexibility to operate our business. Such banks may not exhibit the same degree of flexibility with respect to our financings as they have in the past due to the imposition of international sanctions against them. Moreover, we rely on the Russian banking system to complete various day-to-day fund transfers and other actions required to conduct our business with customers, suppliers, lenders and other counterparties.

Despite progress achieved in recent years, the Russian banking system suffers from international sanctions imposed against state-owned banks, weak depositor confidence, high concentration of exposure to certain borrowers and their affiliates, poor credit quality of borrowers and related party transactions. In response to ruble depreciation and decline in Russian economy the CBR progressively increased its key rate in 2014 from 5.5% to 17%, which resulted in substantial volatility and liquidity shortages on the domestic financial and interbank market. The CBR proceeded to gradually reduce its key rate to 9.75% throughout 2015-2017 and introduced other measures aimed at supporting Russian banking system. Although these measures resulted in partial stabilization of the banking system and assisted some Russian banks in withstanding the recent volatility on the currency and financial markets, the Russian banking system continues to experience financial difficulties and could continue to worsen in the near future due to the impact of international sanctions and general instability of global economy and domestic financial market.

A banking or liquidity crisis or the bankruptcy or insolvency of the banks which lend to us or in which we hold our funds or use for banking transactions could have a material adverse effect on our business, results of operations, financial condition and prospects.

*The infrastructure in Russia needs significant improvement and investment, which could disrupt normal business activity.*

The infrastructure in Russia largely dates back to the Soviet era and has not been adequately funded and maintained since the dissolution of the Soviet Union. Particularly affected are the rail and road networks, power generation and transmission systems, communication systems and building stock. The deterioration of the infrastructure in Russia harms the national economy, disrupts the transportation of goods and supplies, adds costs to doing business and can interrupt business operations. These factors could have a material adverse effect on our business, financial condition, results of operations and prospects.

*The Russian economy and the value of our shares and ADSs could be materially adversely affected by fluctuations in the global economy.*



The global economic crisis, social and political instability in some Middle East countries and in Ukraine, Chinese economic slowdown followed by Chinese market's crash and decline in demand and dramatic fall in oil prices and other negative developments in various countries have resulted in increased volatility in the capital

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markets in many countries, including Russia. As has happened in the past, financial problems in emerging market economies or an increase in the perceived risks associated with investing in emerging market economies could dampen foreign investment in Russia, and Russian businesses could face severe liquidity constraints, further materially adversely affecting the Russian economy. In addition, because Russia produces and exports large amounts of oil, the Russian economy is especially vulnerable to the price of oil on the world market and a decline in the price of oil or international sanctions against the Russian oil industry could slow or disrupt the Russian economy or undermine the value of the ruble against foreign currencies. During the period from December 15, 2014 to December 14, 2015, the average price for Urals crude oil in the Mediterranean and Rotterdam petroleum markets fell by 24.6%, from \$381.8 per tonne to \$287.7 per tonne, according to the Ministry of Economic Development of the Russian Federation. Although during the period from December 15, 2015 to December 14, 2016 the average price for Urals crude oil has risen by 47.3%, prices for petroleum feedstock remain highly volatile. The ruble's value against major world currencies has fallen significantly in 2015 and although ruble has recovered during 2016 and beginning of 2017 it still remains highly volatile. See Risks Relating to Our Financial Condition and Financial Reporting Changes in the exchange rate of the ruble against the U.S. dollar and in interest rates may materially adversely affect our business, financial condition and results of operations. Russia is also one of the world's largest producers and exporters of metal products and its economy is vulnerable to fluctuations in world commodity prices and the imposition of international sanctions, tariffs and/or antidumping measures by any of its principal export markets.

As many of the factors that affect the Russian and global economies affect our business and the business of many of our domestic and international customers, our business could be materially adversely affected by a downturn in the Russian economy or the global economy. In addition to a reduction in demand for our products, we may experience increases in overdue accounts receivable from our customers, some of whom may face liquidity problems and potential bankruptcy. Our suppliers may raise their prices, eliminate or reduce trade financing or reduce their output. A decline in product demand, a decrease in collectibility of accounts receivable or substantial changes in the terms of our suppliers' pricing policies or financing terms, or the potential bankruptcy of our customers or contract counterparties may have a material adverse effect on our business, financial condition, results of operations and prospects.

In June 2016, a majority of voters in the United Kingdom elected to withdraw from the E.U. in a national referendum. In early February 2017, the parliament of the United Kingdom voted in favor of advancing legislation that would give the Prime Minister the authority to initiate the formal process of leaving the E.U. On March 29, 2017, the Prime Minister of the United Kingdom signed the letter that gives an official notice to European Council in accordance with Article 50 of the Treaty on European Union of the United Kingdom's intention to withdraw from the European Union, beginning a legal process of leaving the E.U. As a result, there remains significant uncertainty about the future relationship between the United Kingdom and the E.U. In addition, the recent U.S. presidential election, as a result of which the Republican party nominee, Donald Trump, became the next president of the United States, may impact the financial markets and lead to greater uncertainty on the status of trade relations between the U.S. and some of its largest trade partners, including the U.S.'s existing trade agreements. These developments, or the perception that any of them could occur, have had and may continue to have a material adverse effect on global economic conditions and the stability of global financial markets, and may significantly reduce global market liquidity and restrict the ability of key market participants to fund their capital and liquidity requirements and operate in certain financial markets. Any of these factors could depress economic activity, commodities markets and restrict access to capital, which could result in the global economic conditions deterioration.

In addition, a deterioration in macroeconomic conditions could require us to reassess the value of goodwill on certain of our assets, recorded as the difference between the fair value of the net assets of business acquired and its purchase price. This goodwill is subject to impairment tests on an annual basis. The weakening macroeconomic conditions in the countries in which we operate and/or a significant difference between the performance of an acquired company

and the business case assumed at the time of acquisition could require us to write down the value of the goodwill or portion of such value. See note 18 to the consolidated financial statements.

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***Political and social risks***

*Political and governmental instability could materially adversely affect our business, financial condition, results of operations and prospects and the value of our shares and ADSs.*

Tensions in Russia's relations with other countries and world bodies or conflicts between the government and powerful business groups or among such business groups, as well as the continuation of and the development of international sanctions imposed on Russian institutions, organizations and individuals could disrupt or reverse political, economic and regulatory reforms and also lead to restrictions on our business and a negative impact on Russia's economy and investment climate. Any disruption or reversal of reform policies or economic downturn could lead to social, political or governmental instability or the occurrence of conflicts between various groups, which could have a material adverse effect on our business, financial condition, results of operations and prospects and the value of our shares and ADSs and impede our efforts to restructure our indebtedness, especially in relation to international lenders.

*Corruption and negative publicity could negatively impact our business and the value of our shares and ADSs.*

The local press and international press have reported high levels of corruption in Russia, including unlawful demands by government officials and the bribery of government officials for the purpose of initiating investigations by government agencies. Press reports have also described instances in which government officials engaged in selective investigations and prosecutions to further the commercial interests of certain government officials or certain companies or individuals. In addition, there are reports of the Russian media publishing disparaging articles in return for payment. From time to time, we are the subject of press reports that we believe contain false information about our business and financial condition as well as our largest shareholder. If we or our managers, largest shareholder or counterparties are accused of involvement in government corruption or are otherwise the subject of libelous reports in the press, the resulting negative publicity could disrupt our ability to conduct our business and impair our relationships with customers, suppliers, creditors and other parties, which could have a material adverse effect on our business, financial condition and results of operations and the value of our shares and ADSs and impede our efforts to restructure our indebtedness.

*Shortage of skilled Russian labor could materially adversely affect our business, financial condition, results of operations and prospects.*

Currently the Russian labor market suffers from a general shortage of skilled and trained workers, and we compete with other Russian companies to hire and retain such workers. In Russia, the working age population has declined due to a relatively low birth rate at the end of the 1980s and through the early 1990s. As of January 1, 2017, Rosstat estimated Russia's population at 146.8 million, a decline of 1.7 million from 1992. In recent years, declines in population levels slowed down as a result of an increase in migration and a reduction in the natural decline of the population; in 2014-2016, the population level in fact increased. However, the birth rate remains relatively low, which together with the aging and high mortality of the population, is the main problem of Russia's demographic development. Russia's working age population is estimated to decline by 10-13 million by 2025. A shortage of skilled Russian labor combined with restrictive immigration policies could materially adversely affect our business, financial condition, results of operations and prospects.

***Legal risks and uncertainties***

*Deficiencies in the legal framework relating to subsoil licensing subject our licenses to the risk of governmental challenges and, if our licenses are suspended or terminated, we may be unable to realize our reserves, which could materially adversely affect our business, financial condition, results of operations and prospects.*

Most of the existing subsoil licenses in Russia date from the Soviet era. The Russian government enacted the Procedure for Subsoil Use Licensing on July 15, 1992, which came into effect on August 20, 1992 (the **Licensing Regulation** ). As was common with legislation of this time, the Licensing Regulation was passed

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without adequate consideration of transition provisions and contained numerous gaps. In an effort to address the problems in the Licensing Regulation, the Ministry of Natural Resources (the **MNR**) issued ministerial acts and instructions that attempted to clarify and, in some cases, modify the Licensing Regulation. Many of these acts contradicted the law and were beyond the scope of the MNR's authority, but subsoil licensees had no option but to deal with the MNR in relation to subsoil issues and comply with its ministerial acts and instructions. Thus, it is possible that licenses applied for and/or issued in reliance on the MNR's acts and instructions could be challenged by the prosecutor general's office as being invalid. In particular, deficiencies of this nature subject subsoil licensees to selective and arbitrary governmental claims.

Legislation on subsoil rights still remains internally inconsistent and vague, and the regulator's acts and instructions are often arguably inconsistent with legislation. Subsoil licensees thus continue to face the situation where both failing to comply with the regulator's acts and instructions and choosing to comply with them places them at the risk of being subject to arbitrary governmental claims, whether by the regulator or the prosecutor general's office. Our competitors may also seek to deny our rights to develop certain natural resource deposits by challenging our compliance with tender rules and procedures or compliance with license terms.

An existing provision of the law that a license may be suspended or terminated if the licensee does not comply with the significant or material terms of a license is an example of such a deficiency in the legislation. The MNR (including its successor agency since May 13, 2008, the Ministry of Natural Resources and Ecology) has not issued any interpretive guidance on the meaning of these terms. Similarly, under Russia's civil law system, court decisions interpreting these terms do not have any precedential value for future cases and, in any event, court decisions in this regard have been inconsistent. These deficiencies result in the regulatory authorities, prosecutors and courts having significant discretion over enforcement and interpretation of the law, which may be used to challenge our subsoil rights selectively and arbitrarily.

Moreover, during the tumultuous period of the transformation of the Russian planned economy into a free market economy in the 1990s, documentation relating to subsoil licenses was not properly maintained in accordance with administrative requirements and, in many cases, was lost or destroyed. Thus, in many cases, although it may be clearly evident that a particular enterprise has mined a licensed subsoil area for decades, the historical documentation relating to its subsoil licenses may be incomplete. If, through governmental or other challenges, our licenses are suspended or terminated we would be unable to realize our reserves, which could materially adversely affect our business, financial condition, results of operations and prospects.

*Weaknesses relating to the Russian legal system and legislation create an uncertain investment climate.*

Russia is still developing the legal framework required to support a market economy. The following weaknesses relating to the Russian legal system create an uncertain investment climate and result in risks with respect to our legal and business decisions:

inconsistencies between and among the Constitution, federal laws, presidential decrees and governmental, ministerial and local orders, decisions, resolutions and other acts;

conflicting local, regional and federal rules and regulations;

rapid enactment of many laws and regulations resulting in their ambiguities and inconsistencies;

large-scale continuing reforms in almost all legal matters;

the lack of fully developed corporate and securities laws, significant changes in the regulatory framework;

substantial gaps in the regulatory structure due to the delay or absence of implementing legislation;

changes in the Russian court system, in particular, the merger of the Supreme Arbitrazh Court with the Russian Supreme Court;

the relative inexperience of judges in interpreting legislation and contradictory judicial interpretations of the law;

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the lack of full independence of the judicial system from commercial, political and nationalistic influences;

difficulty in enforcing court orders;

a high degree of discretion or arbitrariness on the part of governmental authorities; and

still-developing bankruptcy procedures that are subject to abuse. See **Risks Relating to Our Financial Condition and Financial Reporting** We may become subject to bankruptcy procedures, which may result in the inability of holders of our shares and ADSs to recover any of their investments.

All of these weaknesses could affect our ability to protect our rights under our licenses and under our contracts, or to defend ourselves against claims by others. We make no assurances that regulators, judicial authorities or third parties will not challenge our compliance with applicable laws, decrees and regulations.

*One or more of our subsidiaries could be forced into liquidation on the basis of formal non-compliance with certain requirements of Russian law, which could materially adversely affect our business, financial condition, results of operations and prospects.*

Certain provisions of Russian law may allow a court to order liquidation of a Russian legal entity on the basis of its formal non-compliance with certain requirements during formation, reorganization or during its operation. There have been cases in the past in which formal deficiencies in the establishment process of a Russian legal entity or non-compliance with provisions of Russian law have been used by Russian courts as a basis for liquidation of a legal entity. For example, under Russian corporate law, if a Russian company's net assets calculated on the basis of Russian accounting standards at the end of its third or any subsequent financial year, fall below its share capital, the company must decrease its share capital to the level of its net assets value or initiate a voluntary liquidation. In addition, if a Russian company's net assets calculated on the basis of Russian accounting standards at the end of its second or any subsequent financial year, fall below the minimum share capital required by law, the company must initiate voluntary liquidation not later than six months after the end of such financial year. If the company fails to comply with either of the requirements stated above within the prescribed time limits, the company's creditors may accelerate their claims and demand reimbursement of applicable damages, and governmental authorities may seek involuntary liquidation of the company. Certain Russian companies have negative net assets mainly due to very low historical asset values reflected on their balance sheets prepared in accordance with Russian accounting standards; however, their solvency, i.e., their ability to pay debts as they become due, is not otherwise adversely affected by such negative net assets. Currently, we have the following subsidiaries with total liabilities greater than total assets: Mechel Garant, Mechel-Steel Management, Mechel Trading House, Mecheltrans, Mechel Energo, Kaslinsky Architectural Art Casting Plant, Port Kambarka, VtorResource, Mechel Materials, Yakutugol, Metallurgshakhtspetsstroy, Southern Kuzbass Coal Company, Shakhtspetsstroy, Romantika, Port Mechel Vanino, Sky-Extra, Mechel-Remservice, Maritime Cargo Shipping, Mecheltrans Management, MecheltransVostok, Izhstal, Mecheltrans Auto and Mechel Vtormet.

If involuntary liquidation were to occur, then we may be forced to reorganize the operations we currently conduct through the affected subsidiaries. Any such liquidation could lead to additional costs, which could materially adversely affect our business, financial condition, results of operations and prospects.

*Selective government action could have a material adverse effect on the investment climate in Russia and on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.*



Governmental authorities in Russia have a high degree of discretion. Press reports have cited instances of Russian companies and their major shareholders being subjected to government pressure through prosecutions of violations of regulations and legislation which are either politically motivated or triggered by competing business groups.

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In mid-2008, Mechel came under public criticism by the Russian government. Repeated statements were made accusing Mechel of using tax avoidance schemes and other improprieties. Ultimately the allegations regarding tax avoidance were not confirmed by the tax authorities, but the antimonopoly investigation resulted in imposition of a fine and issuance of a FAS directive regarding our business practices. See [Risks Relating to Our Business and Industry](#) Antimonopoly regulation could lead to sanctions with respect to the subsidiaries we have acquired or established or our prices, sales volumes and business practices.

Selective government action, if directed at us or our largest shareholder, could have a material adverse effect on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.

*Due to still-developing law and practice related to minority shareholder protection in Russia, the ability of holders of our shares and ADSs to bring, or recover in, an action against us may be limited.*

In general, minority shareholder protection under Russian law derives from supermajority shareholder approval requirements for certain corporate actions, as well as from the ability of a shareholder to demand that the company purchase the shares held by that shareholder if that shareholder voted against or did not participate in voting on certain types of actions. Russian law does not expressly require obtaining prior consent for interested party transactions, unless persons specified by the law do not require it. See [Item 10. Additional Information](#) Description of Capital Stock Rights attaching to common shares. Disclosure and reporting requirements have also been enacted in Russia. Concepts similar to the fiduciary duties of directors and officers to their companies and shareholders are also expected to be further developed in Russian legislation; for example, amendments to the Russian Code of Administrative Offenses imposing administrative liability on members of a company's board of directors or management board for violations committed in the maintenance of shareholder registers and the convening of general shareholders' meetings. While these protections are similar to the types of protections available to minority shareholders in U.S. corporations, in practice, the enforcement of these and other protections has not been effective.

The supermajority shareholder approval requirement is met by a vote of 75% of all voting shares that are present at a general shareholders' meeting. Thus, controlling shareholders owning less than 75% of the outstanding shares of a company may hold 75% or more of the voting power if enough minority shareholders are not present at the meeting. In situations where controlling shareholders effectively have 75% or more of the voting power at a general shareholders' meeting, they are in a position to approve amendments to a company's charter, reorganizations, significant sales of assets and other major transactions, which could be prejudicial to the interests of minority shareholders. See [Risks Relating to Our Business and Industry](#) The concentration of our shares with our largest shareholders will limit your ability to influence corporate matters and transactions with largest shareholders may present conflicts of interest, potentially resulting in the conclusion of transactions on less favorable terms than could be obtained in arm's length transactions.

*Shareholder liability under Russian legislation could cause us to become liable for the obligations of our subsidiaries.*

The Civil Code and the Joint-Stock Companies Law generally provide that shareholders in a Russian joint-stock company are not liable for the obligations of the joint-stock company and bear only the risk of loss of their investment. This may not be the case, however, when one entity is capable of determining decisions made by another entity. The entity capable of determining such decisions is deemed an effective parent. The entity whose decisions are capable of being so determined is deemed an effective subsidiary. Under the Joint-Stock Companies Law, an effective parent bears joint and several responsibility for transactions concluded by the effective subsidiary in carrying out these decisions if:

this decision-making capability is provided for in the charter of the effective subsidiary or in a contract between such entities; and

the effective parent gives obligatory directions to the effective subsidiary based on the above-mentioned decision-making capability.

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In addition, an effective parent is secondarily liable for an effective subsidiary's debts if an effective subsidiary becomes insolvent or bankrupt due to the fault of an effective parent resulting from its action or inaction. This is the case no matter how the effective parent's ability to determine decisions of the effective subsidiary arises. For example, this liability could arise through ownership of voting securities or by contract. Other shareholders of the effective subsidiary may claim compensation for the effective subsidiary's losses from the effective parent which caused the effective subsidiary to take action or fail to take action knowing that such action or failure to take action would result in losses. Accordingly, we could be liable in some cases for the debts of our subsidiaries. This liability could have a material adverse effect on our business, financial condition, results of operations and prospects.

*Shareholder rights provisions under Russian law could result in significant additional obligations on us.*

As a general rule, Russian law provides that shareholders that vote against or do not participate in voting on certain matters have the right to request that the company redeem their shares at value determined in accordance with Russian law. The decisions of a general shareholders' meeting that trigger this right include:

decisions with respect to a reorganization;

consent or subsequent approval by shareholders of a major transaction, which involves property in excess of 50% of the balance sheet value of the company's assets calculated according to Russian accounting standards, regardless of whether the transaction is actually consummated (including those which are simultaneously interested party transactions), except for transactions undertaken in the ordinary course of business;

the amendment of the company's charter or approval of a new version of the company's charter that limits shareholder rights; and

the amendment of the public company's charter which eliminates indication that the company is public, simultaneously with the decision on applying to the CBR on release from obligation to disclose information under the laws of the Russian Federation on securities and the decision on applying for delisting of shares and securities convertible into shares.

Our and our Russian subsidiaries' obligation to purchase shares in these circumstances, which is limited to 10% of our or the subsidiary's net assets, respectively, calculated in accordance with Russian accounting standards at the time the matter at issue is voted upon, could have a material adverse effect on our business, financial condition, results of operations and prospects due to the need to expend cash on such obligatory share purchases.

*The lack of a central and rigorously regulated share registration system in Russia may result in improper record ownership of our shares and ADSs.*

Ownership of Russian joint-stock company shares (or, if the shares are held through a nominee or custodian, then the holding of such nominee or custodian) is determined by entries in a share register and is evidenced by extracts from that register. Currently, there is no single central registration system in Russia. Share registers can be maintained only by licensed registrars located throughout Russia. Regulations have been adopted regarding the licensing conditions for such registrars, as well as the procedures to be followed by licensed registrars when performing the functions of registrar. In practice, however, these regulations have not been strictly enforced, and registrars generally have

relatively low levels of capitalization and inadequate insurance coverage. Moreover, registrars are not necessarily subject to effective governmental supervision. Due to the lack of a central and rigorously regulated share registration system in Russia, transactions in respect of a company's shares could be improperly or inaccurately recorded, and share registration could be lost through fraud, negligence or oversight by registrars incapable of compensating shareholders for their misconduct. This creates risks of loss not normally associated with investments in other securities markets. Furthermore, the depositary, under the terms of the deposit agreements governing record keeping and custody of our ADSs, is not liable for the unavailability of

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shares or for the failure to make any distribution of cash or property with respect thereto due to the unavailability of the shares. See Item 10. Additional Information Description of Capital Stock Registration and transfer of shares.

*Characteristics of and changes in the Russian tax system could materially adversely affect our business, financial condition, results of operations and prospects and the value of our shares and ADSs.*

Generally, Russian companies are subject to numerous taxes. These taxes include, among others:

a profit tax;

a value-added tax ( **VAT** );

a mineral extraction tax; and

property and land taxes.

Laws related to these taxes have been in force for a short period relative to tax laws in more developed market economies and few precedents with regard to the interpretation of these laws have been established. Global tax reforms commenced in 1999 with the introduction of Part One of the Tax Code of the Russian Federation, as amended (the **Russian Tax Code** ), which sets general taxation guidelines. Since then, Russia has been in the process of replacing legislation regulating the application of major taxes such as the corporate profit tax, VAT and property tax with new chapters of the Russian Tax Code.

In practice, the Russian tax authorities generally interpret the tax laws in ways that rarely favor taxpayers, who often have to resort to court proceedings to defend their position against the tax authorities. Events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretations of the legislation and assessments. Contradictory interpretations of tax regulations exist within government ministries and organizations at the federal, regional and local levels, creating uncertainties and inconsistent enforcement. Tax declarations and documentation such as customs declarations, are subject to review and investigation by relevant authorities, which may impose severe fines, penalties and interest charges. Generally, in a tax audit, taxpayers are subject to inspection with respect to the three calendar years which immediately preceded the year in which the audit is carried out. Previous audits do not completely exclude subsequent claims relating to the audited period because Russian tax law authorizes upper-level tax inspectorates to re-audit taxpayers which were audited by subordinate tax inspectorates. In addition, on July 14, 2005, the Russian Constitutional Court issued a decision that allows the statute of limitations for tax liabilities to be extended beyond the three-year term set forth in the tax laws if a court determines that a taxpayer has obstructed or hindered a tax audit. As a result of the fact that none of the relevant terms are defined, tax authorities may have broad discretion to argue that a taxpayer has obstructed or hindered a tax audit and ultimately seek back taxes and penalties beyond the three year term. In some instances, new tax regulations have been given retroactive effect.

Since May 2009, in connection with the proposal expressed by the Russian President in his Budget Message regarding the budget policy for 2010-2012, an overhaul of the anti-avoidance mechanism of double tax treaties has begun. In November 2014, Russian legislation was significantly revised in order to prevent unlawful use of low-tax jurisdictions for tax evasion in the Russian Federation. The amendments in the legislation set out the rules for the taxation of

income of a foreign organization that is deemed to be a controlled foreign company. A foreign organization is recognized as a controlled foreign company if it is not a tax resident of the Russian Federation and the participation interest of the controlling legal entities or individuals in the organization is more than 25%. The transition period provides for a gradual reduction in the size of non-taxable profit, in particular, 50 million rubles, 30 million rubles and 10 million rubles for 2015, 2016 and 2017 and thereafter, respectively. Starting from 2015, these changes in tax regulations could increase the tax burden on companies which are recognized to be controlling of foreign companies. In addition, Russian companies are required to disclose information about controlled foreign companies to the Russian tax authorities. All of these measures are intended

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to ensure the transparency of economic transactions, including foreign trade transactions. Disclosure of beneficial ownership, beneficial recipients of income and tax residence of legal entities at their actual place of business is, according to the new legislation, a prerequisite for the application of tax preferences, including reduced tax rates under international double tax treaties. In July 2015, the Convention on Mutual Administrative Assistance in Tax Matters became effective. The Convention provides for the potential exchange of tax information, including simultaneous tax inspections with Member States of the Council of Europe and member countries of the Organization for Economic Co-operation and Development (OECD), which signed the convention, as well as for assistance in the collection of taxes on their territories. Furthermore, starting from June 30, 2014, the Federal Law No. 173-FZ entered into force, which regulates the procedure of interaction of financial market entities with foreign tax authorities, primarily within the bounds of the U.S. law Foreign Account Tax Compliance Act (FATCA).

On November 16, 2011, the Russian President signed the Law on Amendment of Part One and Part Two of the Tax Code of the Russian Federation in Connection with the Formation of a Consolidated Group of Taxpayers. The main provisions of the law came into force on January 1, 2012. The law provides for formation of a consolidated group of taxpayers for the purposes of profit tax calculation and payment on the basis of the combined business performance of the members of such group. However, the law sets forth a number of requirements for the formation of a consolidated group of taxpayers. Starting from 2013, 16 companies of our group have formed a consolidated group of taxpayers, with Mechel being a responsible party. The formation of the consolidated group of taxpayers allowed us to determine the taxable income with profit and loss offset of all the companies included in the consolidated group of taxpayers and to pay profit tax from total aggregate income under the consolidated group of taxpayers, starting from January 1, 2013. In 2014, there have been some changes in the composition of the consolidated group of taxpayers as a result the number of members has increased to 20 companies. Due to changes in Russian tax legislation, starting in 2015 the consolidated tax base does not include any profit received from controlled foreign companies by a member of the consolidated group of taxpayers (such member being the controlling entity of such controlled foreign companies and the responsible party for paying profit tax in respect of the profits of controlled foreign companies irrespective of the profit tax of the consolidated group of taxpayers).

However, regardless of being a member of the consolidated group of taxpayers or not, Mechel and our Russian subsidiaries pay Russian taxes on dividends they receive from other companies in our group. The tax rate on dividend income amounts to 0% or 13% (depending on whether the recipient of dividends qualifies for Russian participation exemption rules) if being distributed to Russian companies, and 15% (or lower, subject to benefits provided by relevant double tax treaties) if being distributed to foreign companies which are not controlled foreign companies. Dividends from foreign companies to Russian companies are subject to a tax of 13%. Taxes paid in foreign countries by Russian companies may be offset against payment of these taxes in the Russian Federation up to the maximum amount of the Russian tax liability. In order to apply the offset, the company is required to confirm the payment of taxes in the foreign country. The confirmations must be authorized by the tax authority of the foreign country if taxes were paid by the company itself, and the confirmation must be authorized by the tax agent if taxes were withheld by the tax agent under foreign tax law or an international tax agreement.

In 2017, due to changes in the Russian tax legislation, the order of set-off of tax loss accumulated by Russian companies, including companies within the consolidated group of taxpayers significantly changed. Such changes may lead to an increase in the Mechel's tax burden. During the period from 2017 to 2020, the amount of recognized loss for previous tax periods cannot exceed 50% of the tax base of the current period. Since 2021, this limitation will cease to apply and the recognition of accumulated losses in full will be possible again. At the same time, the current 10-year limit on the transfer of losses is canceled.

The limitation in the amount of recognized loss is also applied to the members of the consolidated group of taxpayers with respect to current year loss of its members. Such limitation equals to 50% of the consolidated tax base of the



consolidated group of taxpayers for the current reporting (tax) period. The limitation in the amount of

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not more than 50% of the consolidated tax base for the current reporting (tax) period is also set on the amounts of loss, which were formed prior to January 1, 2017. This change in accounting the loss of the consolidated group of taxpayers in combination with a limited duration of the agreement for the consolidated group of taxpayers increase the tax burden on companies included in the consolidated group of taxpayers.

In addition, application of current Russian thin capitalization rules and the developing negative court practice on such disputes, especially at the level of the Presidium of the Supreme Arbitrazh Court of the Russian Federation and the Supreme Court of the Russian Federation, may require us to withhold dividend taxes in Russia upon payment of interest on loans. In particular, taking into account the requirements of Russian law and negative court practice on thin capitalization, part of the interest on borrowings of our subsidiaries which are either received from Mechel or received from independent banks and guaranteed by Mechel may be classified as dividends and may not be treated as expenses for tax purposes under certain conditions provided by thin capitalization rules. In February 2016, a law which significantly changes the current approach to thin capitalization rules application was adopted. We believe that thin capitalization rules are not applicable to Mechel's loans starting from May 2016. However, we cannot guarantee that in case of change of the existing thin capitalization rules and the applicable practice we will not be subject to the risks specified above.

In accordance with amendments to the Russian Tax Code which entered into force on November 30, 2016, the tax authorities are entitled to seek in court payment of taxes by the company's dependent persons, including dependent individuals, for example, the owners, founders or shareholders of such company, if these persons received cash or property from the company which has outstanding tax amounts within the amounts received by them.

The foregoing conditions create tax risks in Russia that are more significant than typically found in countries with more developed tax systems, imposing additional burdens and costs on our operations, including management resources. In addition to our tax burden, these risks and uncertainties complicate our tax planning and related business decisions, potentially exposing us to significant fines and penalties and enforcement measures despite our best efforts at compliance. See also Risks Relating to the Russian Federation Legal risks and uncertainties Selective government action could have a material adverse effect on the investment climate in Russia and on our business, financial condition, results of operations and prospects and the value of our shares and ADSs.

*Established practice in applying Russian transfer pricing rules only starts to develop and a small number of decisions pronounced in favor of taxpayers exposes our business to the risk of significant additional liabilities.*

The Russian transfer pricing rules entered into force on January 1, 2012 require taxpayers to notify the tax authorities on controlled transactions that are performed from January 1, 2012. Controlled transactions mean any transactions between related parties both domestic and cross-border as well as certain transactions between unrelated parties. The rules introduce specific pricing methods, and documentation requirements for proving market prices. Currently established practice in applying the rules only starts to develop and in some cases decisions are being pronounced not in favor of taxpayers, therefore we cannot predict what effect the transfer pricing rules will have on our business. If the tax authorities impose significant additional tax assessments as a result of changes in transfer pricing regulation and we are unable to successfully challenge them in court or make symmetrical adjustments provided by these rules, it could have a material adverse effect on our business, financial condition, results of operations and prospects.

*Expansion of limitations on foreign investment in strategic sectors could affect our ability to attract and/or retain foreign investments.*

On April 29, 2008, the Federal Law On the Procedure for Foreign Investment in Companies with Strategic Impact on the National Defense and Security of the Russian Federation was adopted. See Item 4. Information on the Company

Regulatory Matters The Strategic Industries Law.

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As our subsidiary Southern Urals Nickel Plant holds the subsoil license on land plots with nickel and cobalt ore deposits which are included in the official list of subsoil plots of federal importance published on March 5, 2009 in the Russian official newspaper *Rossiyskaya Gazeta* as amended (the **Strategic Subsoil List**), it qualifies as a Strategic Company and is subject to special regulation. Our subsidiaries Urals Stampings Plant and Port Posiet are included in the register of natural monopolies, and therefore are also Strategic Companies. Furthermore, entities producing and distributing industrial explosives are deemed to be Strategic Companies. Thus, our subsidiaries Yakutugol, Vzryvprom and Korshunov Mining Plant also qualify as Strategic Companies, as they hold licenses to carry out activities related to the handling of industrial explosives.

Therefore, any transfer, directly or indirectly, to a foreign investor or its group of entities (except for the transfer to a foreign investor controlled by the Russian Federation, the constituent entity of the Russian Federation and/or Russian nationals provided such Russian nationals are Russian tax residents and do not have other nationality) of a stake or certain rights in or fixed assets (equal to 25% or more of the balance sheet value of the relevant entity) of Southern Urals Nickel Plant, Yakutugol, Vzryvprom, Korshunov Mining Plant, Urals Stampings Plant and Port Posiet, which, according to the Strategic Industries Law, is deemed to transfer control, as described in Item 4. Information on the Company Regulatory Matters The Strategic Industries Law, will be subject to prior approval from the state authorities. Likewise, a sale to a foreign investor or its group of entities of a stake in Mechel which provides control (as defined in the Strategic Industries Law) over Southern Urals Nickel Plant, Yakutugol, Vzryvprom, Korshunov Mining Plant, Urals Stampings Plant and Port Posiet, will also be subject to prior approval in accordance with the Strategic Industries Law.

In addition, in case a foreign investor or its group of entities which is a holder of securities of Southern Urals Nickel Plant, Yakutugol, Vzryvprom, Korshunov Mining Plant, Urals Stampings Plant and Port Posiet, becomes a holder of voting shares in amount which is considered to give them direct or indirect control over these companies in accordance with the Strategic Industries Law due to the allocation of voting shares as a result of certain corporate procedures provided by Russian law (e.g., as a result of a buy-back by the relevant company of its shares, conversion of preferred shares into common shares, or holders of preferred shares becoming entitled to vote at a general shareholders meeting in cases provided under Russian law), such shareholders will have to apply for approval within three months after they acquired such control.

In this connection, there is a risk that the requirement to receive prior or subsequent approvals and the risk of not being granted such approvals might affect our ability to attract foreign investments, create joint ventures with foreign partners with respect to our companies that qualify as Strategic Companies or effect restructuring of our group which might, in turn, materially adversely affect our business, financial condition, results of operations and prospects.

*Land use rights regulation in Russia is subject to uncertainty and contradiction.*

The main law governing the title to land is the Land Code of the Russian Federation introduced by the Federal Law On Introduction of the Land Code, dated October 25, 2001, as amended (the **Land Code**), which establishes the principles of land legislation and determines relations governed by land legislation.

In March 2015, the Land Code was significantly amended in part concerning the procedure for allotment of land plots by public authorities to citizens and legal entities. Law enforcement practice, taking into account changes in the applicable legislation, is currently under development; therefore, risks associated with uncertainty of regulatory aspects of the allotment of land plots by public authorities exist.

In addition, there is a general risk of seizure of land plots for state needs for the implementation of governmental programs and projects, which means creation and construction of complexes within the framework of such federal

programs. Moreover, if the land plots owned or leased by us are found not to be in compliance with all applicable approvals, consents, registrations or other regulations, we may lose the use of such land plots.

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The ambiguous interpretation of land law and/or a potential seizure of our land plots for state needs or for other reasons may have a material adverse effect on our business, financial condition, results of operations and prospects.

### ***Item 4. Information on the Company***

#### **Overview**

We are a vertically integrated group with revenues of RUB 276,009 million in 2016, RUB 253,141 million in 2015 and RUB 243,992 million in 2014, with operations organized into three industrial segments: mining, steel and power, each of which has a management company that performs the functions of respective executive management bodies of the companies within the segment, as described below.

Our group includes a number of logistical and marketing companies that help us to deliver and market our products. We have freight seaports in Russia on the Sea of Japan (Port Posiet) and on the Sea of Azov (Port Temryuk) and a freight river port on the Kama River, a tributary of the Volga River in central Russia (Port Kambarka). We have a fleet of freight railcars, locomotives and long-haul trucks, and operate a rail line to our Elga coal deposit in the Sakha Republic.

We have a network of overseas subsidiaries, branches, warehouses, service centers and agents to market our products internationally, and we have a Russian domestic steel retail and service subsidiary with regional offices in 43 cities throughout Russia.

Mechel PAO is a public joint-stock company incorporated under the laws of the Russian Federation. From the date of our incorporation on March 19, 2003 until July 19, 2005, our corporate name was Mechel Steel Group OAO. We conduct our business through a number of subsidiaries. We are registered with the Federal Tax Service of the Russian Federation under main state registration number (OGRN) 1037703012896. Our principal executive offices are located at Krasnoarmeyskaya Street, 1, Moscow 125167, Russian Federation. Our telephone number is +7 495 221 8888. Our Internet addresses are [www.mechel.com](http://www.mechel.com) and [www.mechel.ru](http://www.mechel.ru). Information posted on our website is not a part of this document. We have appointed CT Corporation System, located at 111 Eighth Avenue, New York, New York 10011, as our authorized agent upon which process may be served for any suit or proceeding arising out of or relating to our shares, ADSs or the deposit agreements.

#### ***Mining Segment***

Our mining segment produces metallurgical coal (coking coal, PCI and anthracite), steam coal, iron ore and iron ore concentrate and coke.

The segment primarily consists of our coal, iron ore and coke production facilities in Russia. It also includes certain transportation and logistics facilities and engineering operations.

Our subsidiary Southern Kuzbass Coal Company and its subsidiaries operate coal mines located in the Kuznetsky basin, near Mezhdurechensk in Western Siberia. These mines include four open pit mines and three underground mines. Another of our subsidiaries, Yakutugol, operates coal mines located in the Sakha Republic in Eastern Siberia, consisting of three open pit mines. Yakutugol also holds subsoil licenses for three iron ore deposits, located in close proximity to its coal mining operations. In August 2013, we established Elgaugol which holds the subsoil license for the Elga coal deposit, located in the Sakha Republic in Eastern Siberia. Our mining segment also provides coal washing services to our coal mining subsidiaries.

Korshunov Mining Plant operates two open pit iron ore mines and a washing plant located near Zheleznogorsk-Ilimsky, a town in the Irkutsk region in Eastern Siberia.

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The mining segment also produces significant amounts of coke, both for use by our subsidiaries in the steel segment and for sales to third parties. We have the flexibility to supply our own steel mills with our mining products or to sell such mining products to third parties, depending on price differentials between local suppliers and foreign and domestic customers.

In April 2008, we established Mechel Mining, a wholly-owned subsidiary, in which we consolidated coal, iron ore and coke assets of our mining segment (Southern Kuzbass Coal Company, Korshunov Mining Plant, Yakutugol, Moscow Coke and Gas Plant and Mechel Coke and certain other companies).

Mechel Mining Management, a wholly-owned subsidiary of Mechel Mining, acts as the sole executive body of our subsidiaries in the mining segment.

### ***Steel Segment***

Our steel segment produces and sells semi-finished steel products, long products of a wide range of steel grades, carbon and stainless flat steel products and high value-added metal products, including wire products, stampings and forgings.

Our steel production facilities in Russia include one integrated steel mill, one steel-making mill, a wire products plant and forgings and stampings mill in the southern Ural Mountains and a wire products plant in northwestern Russia near the border with Finland. We also have a wire products plant in Lithuania.

In 2014, to further optimize the structure of our group, we transferred our ferrosilicon producing subsidiary Bratsk Ferroalloy Plant to the steel segment.

Mechel-Steel Management, a wholly-owned subsidiary of Mechel, acts as the sole executive body of our main subsidiaries in the steel segment.

Our steel segment also includes our distribution network in Russia and abroad, which consists of Mechel Service Global and its subsidiaries in Russia, the CIS and Europe.

### ***Power Segment***

The power segment was formed in April 2007, when we acquired a controlling interest in Southern Kuzbass Power Plant located in Kaltan in the Kemerovo region, which sells electricity and capacity to the wholesale market. In June 2007, we acquired a controlling interest in Kuzbass Power Sales Company, the largest power distribution company in the Kemerovo region. Our power segment enables us to market high value-added products, such as electricity and heat energy, and to increase the power self-sufficiency of our mining and steel segments. Mechel Energo acts as the sole executive body of Southern Kuzbass Power Plant in our power segment.



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**Competitive Strengths**

Our main competitive strengths are the following:

***Leading mining and metals group by production volume with strong positions in key businesses***

*We are the second largest coking coal producer and exporter by volume in Russia.*

In 2016, we were the second largest coking coal producer in Russia, with an approximately 18.5% share of total coking coal production by volume, according to the Central Dispatching Department of Fuel and Energy Complex ( **Central Dispatching Department** ), a Russian information agency reporting on the fuel and energy industry. In 2016, our export sales of coking coal concentrate were the second largest by volume among Russian companies, according to Metals & Mining Intelligence ( **MMI** ), a private information and research company.

*We have a large coal reserve base and a broad-range offering of high-quality metallurgical coals, as well as steam coals of various grades.*

Our total coal reserves amounted to 3,029.9 million tonnes as of December 31, 2016, as accounted pursuant to SEC Industry Guide 7.

Our coal reserves allow us to supply steel producers and coke makers globally with a wide range of coal grades to make quality metallurgical coke or to use in PCI-assisted and sintering-assisted steel manufacturing. In addition to metallurgical coals, we supply steam coals of various grades. In particular, Southern Kuzbass Coal Company produces semi-hard and semi-soft coking coal, PCI, anthracite and steam coal. Most of the coking coal grades of Southern Kuzbass Coal Company are sold in Russia, while PCI, steam coal and anthracite are generally exported. Yakutugol produces low-volatile hard coking coal used by customers both in the Asia-Pacific region and in Russia, as well as steam coal which is sold domestically to local municipal services and for export. Elgaugol produces high-quality hard coking coal of high-volatile content and steam coal which are primarily supplied for export. The ability to serve our customers with a broad range of metallurgical and steam coal grades gives us a competitive advantage in entering the new markets and establishing long-term relationships with the customers.

*By production volume we are Russia's second largest producer of long steel products and Russia's largest producer of wire products.*

According to Metal Expert, a source for global steel and raw materials market news and analytics, in 2016 by production volume we were Russia's second largest producer of long steel products (excluding square billets), second largest producer of reinforcement bars (rebar) and largest producer of wire rod. Our long steel products business has particularly benefited from the increased infrastructure and construction activity in Russia. Our share of Russia's total production volume of rebar in 2016 was approximately 19.2%, according to Metal Expert. According to Metal Expert and Chermets, a Russian ferrous metals industry association ( **Chermets** ), we are Russia's third largest producer of special steel by production volume, accounting for 11.8% of Russia's total special steel output in 2016. Our product range in special steel is broader and more comprehensive than other Russian producers, giving us an added advantage in our markets. According to Metal Expert, we are Russia's largest producer of wire products by production volume, accounting for 35.9% of Russia's total wire products output in 2016.

***High degree of vertical integration***

*Our steel segment is able to source most of its raw materials from our group companies, which provides a hedge against supply interruptions and market volatility.*

We believe that our internal supplies of coke, iron ore concentrate and ferrosilicon give us advantages over other steel producers, such as higher stability of operations, better quality control of end products, reduced production costs, improved flexibility and planning latitude in the production of our steel and value-added steel

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products and the ability to respond quickly to market demands and cycles. In 2016, we were fully self-sufficient with respect to coke and ferrosilicon; we were approximately 72% self-sufficient with respect to iron ore concentrate; and we satisfied approximately 26% of our electricity needs internally. We believe that the level of our self-sufficiency in raw materials gives our steel business a competitive advantage.

We view our ability to source most of our inputs internally not only as a hedge against potential supply interruptions, but as a hedge against market volatility. From an operational perspective, since our mining and power assets produce the same type of inputs that our manufacturing facilities use, we are less dependent on third party vendors and less susceptible to supply bottlenecks. From a financial perspective, this also means that if the market prices of our steel segment's inputs rise, putting pressure on steel segment margins, the margins of our mining segment will tend to increase. Similarly, while decreases in commodity prices tend to reduce revenues in our mining segment, they also create an opportunity for increased margins in our steel business.

Furthermore, we work on improving the quality of our steel products and reducing the costs for raw materials. Depending on prevailing market conditions, we evaluate the efficiency of use of our own raw materials and the raw materials purchased from third parties to be able to generate additional income.

The ability to internally source our materials also gives us better market insight when we negotiate with our outside suppliers, and improves our ability to manage our raw materials costs.

*Our logistics capability allows us to better manage infrastructure bottlenecks, to market our products to a broader range of customers and to reduce our reliance on trade intermediaries.*

We are committed to maximum efficiency in delivering goods to consumers and have been actively developing our own logistics network. Using our own transportation capacity enables us to save costs as we are less exposed to market fluctuations in transportation prices and are able to establish flexible delivery schedules that are convenient for our customers. Our logistics capacities are currently comprised of two seaports (Port Posiet and Port Temryuk) and a river port (Port Kambarka), as well as freight forwarding companies (Mecheltrans, MecheltransVostok and Mecheltrans Auto) which manage rail and motor transportation of our products and carry out the overall coordination of our sea, rail and motor transportation logistics. These companies not only transport our products but also provide transportation services to third parties.

We own two seaports and a river port and we have our own rail rolling stock. Port Posiet in the Russian Far East, on the Sea of Japan, gives us easy access to the Asia-Pacific seaborne market and provides a delivery terminal for the coal mined by our subsidiaries Yakutugol and Elgaugol in Yakutia. We are in the process of the Port Posiet's modernization, which enabled us to expand the cargo-handling capacity of the port up to 7.0 million tonnes per annum. Port Temryuk on the Sea of Azov, an inlet of the Black Sea basin, is primarily used for coal and metal transshipment and provides us access to the emerging market economies of the Black Sea and Mediterranean basins. Port Kambarka on the Kama River in the Republic of Udmurtia (a Russian administrative region also known as Udmurtia) is connected to the Volga River basin and the Caspian Sea, by canal to the Don River and the Sea of Azov, as well as by the Volga-Baltic Route to the Baltic Sea. As of December 31, 2016, our subsidiaries Mecheltrans and Mecheltrans Auto owned and leased 11,478 freight transportation units, including 11,433 railcars and 45 long-haul trucks that we use to ship our products.

In June 2008, pursuant to the terms of our subsoil license for the Elga coal deposit we began construction of a private rail line, which we own and control subject to applicable regulation. In December 2011, we finished laying track for the rail line in accordance with the terms of the license. The 321 kilometer-long rail line is now in operation and we are able to use it for transportation of coal currently produced at the Elga deposit. The rail line connects the Elga coal

deposit with the Baikal-Amur Mainline (at the Ulak railway station), which, in turn, provides access to the Russian rail network, in general, and Pacific Ocean ports, in particular. We will further develop the rail line to increase its capacity in line with our coal production plans. We anticipate that the Elga rail line will not only provide an avenue for delivery of coal produced at the Elga coal deposit, but will eventually serve as the transport route for coal, iron ore and other raw materials mined in the adjacent deposits.

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**Table of Contents*****One of the lowest-cost metallurgical coal producers***

According to CRU International Limited ( **CRU** ), our hard coking coal operations are in the first quartile of the global business cost curve (CFR basis). In 2016, approximately 93% of our coking coal production was mined from open pit mines, which we believe is one of the highest rates among our Russian competitors. Open pit coal mining is generally considered safer, cheaper and faster than the underground method of mining. Most of our mines and processing facilities have long and established operating histories. We view strict cost management and increases in productivity as fundamental aspects of our day-to-day operations, and continually reassess and improve the efficiency of our mining operations.

***Strategically positioned to supply key growth markets***

*Our mining and logistical assets are well-positioned to expand sales to the Asia-Pacific seaborne market.*

Eastern Siberian coal mines of Yakutugol and Elga coal deposit, which are part of our mining segment, are strategically located and will enable us to expand exports of our products to key Asian markets. Yakutugol and Elgaugol are located within the shortest distance among Russian coking coal producers to Port Posiet and Port Vanino in the Russian Far East. We view the proximity of these mining and logistical assets to the Asian economies as one of the key competitive advantages which allow us to diversify our sales, provides us with additional growth opportunities and acts as a hedge in the event of a decrease in demand from customers in Russia. Moreover, due to our integration, experience and location in Russia, which has some of the largest deposits of coal and iron ore in the world, we are better positioned than many of our international peers to secure future production growth.

*Our steel mills are well-positioned to supply Russian infrastructure projects.*

Russia is our core steel market and we have significant domestic market shares in main types of carbon and special steel long products. We believe we have established a strong reputation and brand image for Mechel within Russia, just as we have with our international customers. The location of a number of our core steel segment assets in the southern Urals positions us advantageously, from a geographical and logistical perspective, to serve the areas in the west of the Urals as this region is a large consumer of long steel products in Russia, according to Metal Expert. The construction industry has been a major source of our revenue and we have captured a large portion of the market. According to Metal Expert, our share of Russia's total production volume of rebar in 2016 was approximately 19.2%.

***Established distribution and sales platform***

We have a non-retail sales and distribution network represented by our Swiss subsidiaries Mechel Trading and Mechel Carbon with representative offices in various countries. This network facilitated sales constituting 23.9% of our total sales in 2016.

We also have Mechel Service Global's distribution network which conducts sales of our steel products in Russia, the CIS and Europe. Through our distribution network in Russia and the CIS we sell a whole range of steel products manufactured by our plants. In case of sales to the European Union, we focus on sales of high value-added products, primarily high-quality rolled steel products and forgings produced by our Urals plants, through Mechel Service Belgium. Our companies in Germany, Austria and the Czech Republic provide customers with a wide range of services for metal processing. Mechel Service Global sales accounted for 50.7% of our steel segment sales and 29.7% of our total sales in 2016. Approximately 91.2% of Mechel Service Global sales were sold domestically. Sales to companies within our group accounted for 1.6% of total sales of Mechel Service Global (including intra-group sales) in 2016.

Our direct access to end customers allows us to obtain real-time market intelligence and improve production planning at our steel facilities, which in turn allows us to improve the efficiency of our existing operations through the optimization of our sales structure.

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### ***Strong and focused management team***

Our current management team has significant experience in all aspects of our businesses. Mr. Zyuzin, one of the founders of our group and our Chairman and largest shareholder, has led our successful transformation from a small coal trading operation to a large integrated mining and metals group. Mr. Zyuzin has over 30 years of experience in the coal mining industry and holds a Ph.D. in technical sciences in the coal mining field. Our divisional management also has long-tenured experience in the mining and metals industry. See Item 6. Directors, Senior Management and Employees Directors and Executive Officers.

### **Business Strategy**

Our goal is to become one of the largest producers of metallurgical coal and steel products by realizing potential of the vertical integration and maximizing synergies between our performing assets underlying our business model.

Our strategy aimed at extracting the maximum value from our mining and steel assets. We intend to concentrate on efficiency improvements and modernization of the business lines, which we expect will increase the business overall profitability.

In the mining segment, we will continue to develop our existing coal reserves, particularly in order to sell more high-quality metallurgical coal and coal products to third parties. We intend to prioritize the development of the Elga coal deposit, one of the largest global metallurgical coal reserves. Our coking coal and iron ore production form a solid platform for our steel business. Steam coal can be used to feed our power generating business which enables us to market high value-added products, such as electricity and heat energy, and to increase the power self-sufficiency of our mining and steel segments. However, even as we develop our internal sourcing capability, we intend to adhere to our long-standing approach of purchasing inputs from third party suppliers and selling products, including raw materials, to domestic and international customers in a way that we believe creates the most advantageous profit opportunities for our group.

In the steel segment, we plan to focus on the Russian rail, engineering and construction markets. The launch of the universal rail and structural rolling mill at Chelyabinsk Metallurgical Plant allowed us to widen our portfolio of high value-added products such as structural shapes and rails, as well as significantly improve our competitive advantage as a full product range supplier to the construction sector and as an important supplier to Russian Railways. In 2015, we successfully went through the certification of rail products resulting in obtainment of three certificates of conformity of the Customs Union. The increase in sales volume of the universal rolling mill products will occur along with the development and certification of new types of products and will enable us to realize the import substitution strategy. We intend to increase our group's output and improve the quality of high value-added steel products in order to preserve our leadership in special and stainless steels and wire products in Russia. For some of these products, we hold a unique market niche, which serves as the basis for further improvement of our market share and growth of our customer base.

Our distribution network provides us with a strong platform for further development of our sales. In the current economic situation, we are capable to quickly respond to changing market conditions and if necessary redirect deliveries of our products not only in Russia but abroad, thereby allowing us to obtain additional profit.

Another strategic priority is development of our logistics capabilities. Our own railcar fleet is to ensure the balance between transportation security and cost efficiency. Development of the cargo-handling capacity of Port Posiet is crucial for continuous shipments of our coal products in the Asia-Pacific region. Growing production of export-oriented coal in our mining segment will require further expansion of port capacities on our main export routes.



With focus on efficiency improvements of our main businesses, we may also consider selective disposal of assets in order to minimize possible costs, as well as attract financial or strategic investors to our key assets in order to reduce the debt burden and contribute to business development.

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**Table of Contents****Our History and Development**

We trace our beginnings to a small coal trading operation in Mezhdurechensk in the southwestern part of Siberia in the early 1990s. See Item 5. Operating and Financial Review and Prospects History of Incorporation. Since that time, through strategic acquisitions in Russia and abroad, Mechel has developed into one of the world's leading mining and metals companies, comprising producers of coal, iron ore, coke, steel, rolled products, ferrosilicon, heat energy and electricity, with operations and assets in Russia, the CIS and Europe. We intend to retain a controlling voting interest in each of our subsidiary holding companies as we continue to build upon our business model of vertical integration among our assets.

**Mining Segment**

Our mining segment produces coking coal and other types of metallurgical coal (anthracite and coal for pulverized, or finely crushed, coal injection (PCI)), steam coal, middlings, coking coal and steam coal concentrates, as well as coke and chemical products, iron ore and iron ore concentrate. Our mining segment also includes certain transportation and logistics facilities and engineering operations. Our coal operations consist of Southern Kuzbass Coal Company, Yakutugol and Elgaugol, which together produced 14.2 million tonnes of raw coking coal, 6.1 million tonnes of raw steam coal and 2.4 million tonnes of raw anthracite in 2016. Our coke operations consist of Moscow Coke and Gas Plant and Mechel Coke, which together produced 3.0 million tonnes of coke in 2016. Our iron ore operations consist of Korshunov Mining Plant which produced 8.2 million tonnes of iron ore and 2.7 million tonnes of iron ore concentrate in 2016.

***Description of key products***

*Coking coal and metallurgical coal.* Southern Kuzbass Coal Company produces high-quality bituminous coal, which is washed to reduce the ash content. The premier product is a high-quality, low phosphorous, low sulfur semi-soft to semi-hard coking coal used to produce coke for the iron and steel industry. Other products produced by Southern Kuzbass Coal Company include PCI and anthracite. Yakutugol produces hard coking coal of low-volatile content. Elgaugol produces high-quality hard coking coal of high-volatile content.

*Steam coal.* Southern Kuzbass Coal Company, Yakutugol and Elgaugol produce high-energy steam coal as part of their product mix. Steam coal is primarily used for the generation of electricity in coal-fired power stations.

*Coke.* Coke is used in the blast furnace as a main source of heat, a reducing agent for iron and a raising agent for charging material in the smelting process. It is a product prepared by pyrolysis (heating in the absence of oxygen) of low-ash, low-phosphorus and low-sulfur coal charging material. We offer customers coke from our Moscow Coke and Gas Plant and Mechel Coke.

*Chemical products.* Chemical products are hydrocarbon products obtained as a by-product of the production of coke. We produce chemical products in our subsidiaries Moscow Coke and Gas Plant and Mechel Coke. We offer our customers coal tar, naphthalene and other compounds. Worldwide, coal tar is used in diverse applications, including in the production of electrode pitch, pitch coke, coal-tar oils, naphthalene, as well as boiler fuel. Naphthalene, a product of the distillation of coal tar, is used by the chemical industry to produce chemical compounds used in synthetic dyes, solvents, plasticizers and other products.

*Iron ore concentrate.* From our Korshunov Mining Plant we offer iron ore concentrate with a standard iron content of 62%. Yakutugol holds subsoil licenses for three iron ore deposits located in Yakutia. These deposits contain high-quality iron ore, which will allow to produce iron ore concentrate with 65% iron content.

***Mining process***

*Coal.* At our Russian mines, coal is mined using open pit or underground mining methods. Following a drilling and blasting stage, a combination of shovels and draglines is used for moving coal and waste at our open

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pit mines. Production at the underground mines is predominantly from longwall mining, a form of underground coal mining where a long wall of coal in a seam is mined in a single slice. After mining, depending upon the amount of impurities in the coal, the coal is processed in a washing plant, where it is crushed and impurities are removed by gravity methods. Coking coal concentrate is then transported to coking plants for conversion to coke for use in pig iron smelting at steel plants. Steam coal is shipped to power utilities which use it in furnaces for steam generation to produce electricity. Among the advantages of our mining business are the high quality of our coking coal and the low level of volatile matter in our steam coal.

*Iron ore.* At our Korshunov Mining Plant, ore is mined using the open pit mining method. Following a drilling and blasting stage, ore is hauled by dump trucks and dumping cars to the washing plant. At the washing plant, the ore is crushed and ground to a fine particle size, then separated into an iron ore concentrate slurry and a waste stream using wet magnetic separators. The iron ore is upgraded to a concentrate that contains about 62% elemental iron. Tailings are pumped to a tailings dam facility located adjacent to the washing plant. The concentrate is sent to disk vacuum filters which remove the water from the concentrate to reduce the moisture level, enabling shipment to customers by rail during warmer months; in colder periods the concentrate must be dried further to prevent freezing in railcars. Korshunov Mining Plant operates its own drying facility with a dry concentrate production capacity of up to 16,000 tonnes per day. In 2011-2012, Yakutugol obtained subsoil licenses for the Pionerskoye iron ore deposit, the Sutamskaya iron ore area and the Sivaglinskoye iron ore deposit in Yakutia. We plan to develop all new iron ore deposits with the open pit mining method, using excavators and dump trucks.

***Coal production***

Our coal production consists of the following mines in Russia:

<b>Subsidiary (Location)</b>	<b>Surface</b>	<b>Underground</b>
Yakutugol (Sakha Republic, Russia)	Neryungrinsky Open Pit Kangalassky Open Pit Dzhebariki-Khaya Open Pit	
Elgaugol (Sakha Republic, Russia)	Elga Open Pit	
Southern Kuzbass Coal Company (Kuzbass, Russia)	Sibirginsky Open Pit  Tomusinsky Open Pit  Olzherassky Open Pit  Krasnogorsky Open Pit	V.I. Lenina Underground Sibirginskaya Underground Olzherasskaya- Novaya Underground

Our coal mines are primarily located in the Kuznetsky basin, a major Russian coal-producing region, and in the Sakha Republic in Eastern Siberia.

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The table below summarizes our run-of-mine (ROM) coal production by type of coal and location of mines for the periods indicated.

	2016		2015		2014	
	Tonnes	% of Production	Tonnes	% of Production	Tonnes	% of Production
	(In millions of tonnes) <sup>(1)</sup>					
<b>Coking Coal</b>						
Yakutugol	8.9		7.8		8.9	
Elgaugol	2.8		2.6		0.7	
Southern Kuzbass Coal Company	2.5		3.4		4.3	
Bluestone <sup>(2)</sup>					0	
<b>Total Coking Coal</b>	<b>14.2</b>	<b>62.7%</b>	<b>13.8</b>	<b>59.5%</b>	<b>13.9</b>	<b>61.5%</b>
<b>Steam Coal</b>						
Yakutugol	1.0		1.4		0.5	
Elgaugol	0.9		1.3		0.5	
Southern Kuzbass Coal Company	4.2		4.2		5.4	
Bluestone <sup>(2)</sup>					0	
<b>Total Steam Coal</b>	<b>6.1</b>	<b>26.8%</b>	<b>6.9</b>	<b>29.7%</b>	<b>6.4</b>	<b>28.3%</b>
<b>Anthracite</b>						
Yakutugol						
Elgaugol						
Southern Kuzbass Coal Company	2.4		2.5		2.3	
Bluestone <sup>(2)</sup>						
<b>Total Anthracite</b>	<b>2.4</b>	<b>10.5%</b>	<b>2.5</b>	<b>10.8%</b>	<b>2.3</b>	<b>10.2%</b>
<b>Total Coal</b>	<b>22.7</b>	<b>100%</b>	<b>23.2</b>	<b>100%</b>	<b>22.6</b>	<b>100%</b>

(1) Volumes are reported on a wet basis.

(2) In January-February 2014, we temporarily suspended works at our Bluestone mines due to adverse market conditions. In February 2015, we disposed of Bluestone mining business.

The coking coal produced by our Russian mines is predominately low-sulfur (0.3%) bituminous coal. Heating values for coking coal range from 6,861 to 8,488 kcal/kg on a moisture- and ash-free basis. Heating values for steam coal range from 6,627 to 8,286 kcal/kg on a moisture- and ash-free basis.

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The table below summarizes our saleable coal production by type of coal and location of mines for the periods indicated.

	2016		2015		2014	
	Tonnes	% of Production	Tonnes	% of Production	Tonnes	% of Production
	(In millions of tonnes)					
<b>Coking Coal</b>						
Yakutugol	5.9	30%	5.1	25%	5.7	26%
Elgaugol	1.6	8%	1.6	8%	0.2	1%
Southern Kuzbass Coal Company	3.1	16%	2.7	13%	4.0	19%
Bluestone <sup>(1)</sup>					0	0%
<b>Total Coking Coal</b>	<b>10.6</b>	<b>54%</b>	<b>9.4</b>	<b>46%</b>	<b>9.9</b>	<b>46%</b>
<b>PCI</b>						
Yakutugol						
Elgaugol						
Southern Kuzbass Coal Company	1.4	7%	2.0	9%	2.6	12%
Bluestone <sup>(1)</sup>						
<b>Total PCI</b>	<b>1.4</b>	<b>7%</b>	<b>2.0</b>	<b>9%</b>	<b>2.6</b>	<b>12%</b>
<b>Anthracite</b>						
Yakutugol						
Elgaugol						
Southern Kuzbass Coal Company	1.8	9%	2.1	10%	1.5	7%
Bluestone <sup>(1)</sup>						
<b>Total Anthracite</b>	<b>1.8</b>	<b>9%</b>	<b>2.1</b>	<b>10%</b>	<b>1.5</b>	<b>7%</b>
<b>Steam Coal</b>						
Yakutugol	3.2	17%	3.5	17%	2.9	14%
Elgaugol	1.3	7%	1.6	8%	0.5	2%
Southern Kuzbass Coal Company	1.2	6%	2.0	10%	4.2	19%
Bluestone <sup>(1)</sup>					0	0%
<b>Total Steam Coal</b>	<b>5.7</b>	<b>30%</b>	<b>7.1</b>	<b>35%</b>	<b>7.6</b>	<b>35%</b>
<b>Total Coal</b>	<b>19.5</b>	<b>100%</b>	<b>20.6</b>	<b>100%</b>	<b>21.6</b>	<b>100%</b>

(1) In January-February