

Press Conference Background

GAZPROM'S POWER GENERATION STRATEGY

(May 13, 2015)

The year of 2014 saw a paramount step in the development of Gazprom Group's power generation business. Gazprom took a number of measures to increase the profitability of operating activities and boost the production efficiency, including the management improvement at affiliates and production facilities, cost saving, optimization of equipment loads and fuel balance, and reduction of the lifetime of inefficient equipment. The Company intensified the cooperation with Russian power equipment manufacturers and R&D centers, and streamlined the corporate maintenance & repair business.

The Group's major generating companies are consolidated in Gazprom Energoholding, Gazprom's wholly-owned subsidiary, which has a majority stake in Mosenergo, MOEK, TGC-1 and OGK-2. In the meantime, 2014 is the first year of MOEK being a full-fledged member of the Group.

In 2014 the main companies of the Group produced a total of 152.2 billion kWh of electricity (4.63 per cent down compared to 2013) and 120 million Gcal of heat (two per cent down). Lower power generation rates are conditioned by optimizing the load on inefficient power units as well as a slump in electricity demand throughout Group's business activity regions. A four per cent increase in heat supply by Mosenergo-owned power plants and reduction of the respective indicator by 20.4 per cent in MOEK followed the changes in the Moscow heat supply network introduced by the Group: placing MOEK's heat generating facilities under the Mosenergo management and the load shifting to the Mosenergo CHPPs. The transfer of heat loads to more efficient facilities provided for saving 203 million cubic meters of natural gas in 2014.

The total proceeds (Mosenergo, TGC-1, OGK-2 and MOEK under RAS, excluding Murmansk CHPP, a subsidiary of MOEK) amounted to RUB 448.8 billion (0.9 per cent up versus 2013) and net profit – RUB 3.8 billion (50 per cent down) in 2014. The MOEK losses dropped to RUB 6.8 billion (from 8.8 billion – by 14.4 per cent), and all generating companies of the Group (Mosenergo, TGC-1 and OGK-2) closed 2014 with the total profit of RUB 10.6 billion.

An action plan for cost optimization is currently being implemented in MOEK, which expects to save over RUB 9 billion at 2015 year-end.

Thus, in 2014 Mosenergo, TGC-1 and OGK-2 went on executing the 'Lean Production' and 'Efficiency' programs and some other initiatives aimed at improving the financial & economic performance.

The following activities yielded the maximum monetary profit in 2014:

- Balance of Plant enhancement (OGK-2) – RUB 1,145.2 billion;
- carrying out fuel supply activities (OGK-2) – RUB 900 million;
- optimizing the procurement procedures (OGK-2) – RUB 334 million;
- reducing burnouts (OGK-2) – RUB 305.9 million;
- optimizing taxes (Mosenergo) – RUB 343 million;

- improving the investment program (Mosenergo) – RUB 131 million;
- selling non-core assets (TGC-1) – RUB 220 million;
- increasing water use efficiency (TGC-1) – RUB 198 million;
- enhancing power generation efficiency (TGC-1) – RUB 171 million.

Ural Turbine Works started the pilot project for retrofitting power unit No. 9 at CHPP-22 in Moscow in 2014 (Ural Turbine Works had manufactured the main equipment in early 1970s). The project will represent an important step in developing Russia's power engineering sector. Together with Lomonosov Moscow State University, a research center for studying heat insulating materials was set up and a plant for their production was constructed.

In addition, in 2014 Mosenergo, TGC-1 and OGK-2 continued executing a large-scale investment program under capacity supply agreements (CSA).

In 2014 the Group commissioned 905 MW of new generating capacities in Russia:

- 420 MW combined-cycle gas turbine unit at the Cherepovets SDPP (OGK-2);
- 420 MW combined-cycle gas turbine unit at CHPP-16 (Mosenergo);
- 65 MW gas turbine unit at CHPP-9 (Mosenergo).

Thus, starting from 2007, the year of Gazprom Group's entry into the power industry, till 2014 the Group has already commissioned about 6 GW of new capacity under CSAs. The overall program budget equals some RUB 410 billion and it has been 87 per cent financed as of late 2014.

In addition, 428 MW of inefficient power equipment were decommissioned in 2014:

- three turbine generators with the aggregate capacity of 150 MW and two boiler units at the Serov SDPP (OGK-2);
- 278 MW power at the Troitsk SDPP (OGK-2).

The company borrowed funds to implement the CSA projects; the amount of debt will be decreasing in parallel with the facilities construction. Nevertheless, in 2014 the joint debt of Gazprom Energoholding companies (excluding the Murmansk CHPP) grew by 65.8 per cent – up to RUB 148.9 billion, mostly due to the inclusion of MOEK's debt (RUB 26.7 billion up).

That is why when pursuing its dividend policy, Gazprom Energoholding is governed by the reasonable necessity of maintaining a balance between the debt servicing and the amount of dividend payout. An increase in dividend amount is expected after the completion of the CSA projects. At 2015 year-end the Group's companies are expected to generate 162.1 billion kWh (6.5 per cent up) of electricity, and 122.9 million Gcal (2.4 per cent up) of heat. Total revenues under RAS are forecast to grow by 6.4 per cent (to RUB 477.6 billion), net profit – 2.2 times (to RUB 8.4 billion) and net losses of MOEK will drop by another 32 per cent (to RUB 4.6 billion).