

Press Conference
Gazprom's Power Generation Strategy
May 16, 2018

MODERATOR: Good afternoon. We continue the series of Press Conferences in the lead-up to the annual General Shareholders Meeting of Gazprom. Today, we will review Gazprom's Power Generation Strategy.

This Press Conference is attended by Denis Fyodorov, Head of Directorate at Gazprom and Director General of Gazprom Energoholding.

I give the floor to Mr. Fyodorov, and then we will move on to your questions.

DENIS FYODOROV: Good afternoon, dear colleagues. I will try to be brief in my presentation and then answer all of your questions.

I would like to begin by emphasizing that 2017 was an anniversary year for us. It was exactly 10 years ago that Gazprom obtained its first power assets. The Gazprom Board of Directors approved the power generation development strategy. By now, it has been fully implemented and completed, and we are ready to put forward a new 10-year strategy for approval very soon.

The projects implemented by Gazprom made it possible to create the country's largest power holding company: controlling stakes were acquired in Mosenergo and TGC-1, in OGK-2 and OGK-6, which are now consolidated in a single company, as well as in MOEK. Today, we account for 16 per cent of all electricity produced in Russia and hold the lead in the national heat supply market. Our most remarkable success of recent years is MOEK's transformation into a company with positive operating results. We already know that some banking organizations are showing interest in its bond issues, which means that the company has finally managed to show a consistently positive trend after several years of financial instability. We are proud of this important achievement.

We have successfully completed our CSA (capacity supply agreement) program within 10 years. The only remaining project we are involved in now is the construction of the Grozny Thermal Power Plant. There were a lot of questions about the TPP from the media. At present, the Siemens-made turbines, having already departed from St. Petersburg, are being transported by rivers to the destination point. We plan to put the first and second power units of the Grozny TPP onstream by the year's end and in the middle of next year, respectively, thereby fully completing our investment program.

Last year, Mosenergo celebrated its 130th anniversary, and I extend my congratulations to the company's staff on this occasion. Mosenergo is one of the oldest power producers in Russia and probably one of the oldest Russian companies as well. In addition to being a stable and sustainable business, it is a leader in the domestic power industry.

As I have already said, in the near future we will review Gazprom's power generation strategy for the next 10-year period.

Now let's turn to the presentation.

(Slide 1) The first slide depicts our highlights for 2017.

About operating activities: our electricity and heat production has decreased. In the case of heat, the obvious reason is the weather factor. Electricity production dipped due to the ongoing load optimization at our power plants, as we are only using cost-efficient operating modes. Besides, there are certain decisions of the System Operator (System Operator of the Unified Energy System) that we have to abide by.

As for financial results, our revenues increased by 4.9 per cent and EBITDA – by 30.9 per cent according to the Russian Accounting Standards (RAS), and IFRS-based financial data are not available yet.

As for investments, as I have already mentioned, the investment program is almost completed: 8.6 GW

of new capacities have been built. In 2017, the Central CHPP (TGC-1, St. Petersburg) with two 50 MW turbines was put into operation. We continue to execute the Grozny TPP project.

Speaking of major events, which are also indicated in the slide, I would, first of all, highlight a rather significant growth of EBITDA that was primarily caused by higher CSA payments. Besides, we decommissioned about 100 MW of obsolete and inefficient equipment. Arguably, the capitalization of our companies has grown significantly. However, we are well aware that currently the Russian stock market a) does not reflect the intrinsic value of companies and b) is experiencing strong fluctuations driven by external rather than internal factors.

(Slide 2) Here you can see the main performance data broken down by companies. As I've said earlier, we observe a general downturn in electricity and heat output for all companies except TGC-1. The fall in heat output was a result of higher ambient temperatures compared to the previous period.

(Slide 3) The financial results were also compiled according to the Russian Accounting Standards. I've already commented on them, but they are presented in more detail for each company here. EBITDA generated by new CSA projects in 2017 stands at RUB 67 billion, which is more than half of the total EBITDA made by Gazprom Energoholding.

(Slide 4) The debt burden. We are doing well in this segment, too. As you see, in 2012–2015 we were building up our debt to begin paying it down in 2016–2017, and we really stepped up our payments in 2017. We consider the debt to EBITDA ratio to be one of the key indicators of a company's financial stability. To this date, the ratio for Gazprom Energoholding is 1.1, which seems to be a good result, and everyone seems to agree with us. Naturally, we try to take the lead from the parent company when targeting the debt to EBITDA ratio.

(Slide 5) The next slide shows the dividends of the Gazprom Energoholding Group. They are rising, and the rise will be reflected in the 2017 results. The debt to EBITDA ratio for each of the generating companies is as follows: 0.5 in Mosenergo, 1.1 in TGC-1, and 2.1 in OGK-2. In response to the question of how we determine the size of dividend payouts, I can say that we are looking at the debt and the long-term outlook of our financial performance. Our mission is to preserve the financial stability of the company.

(Slide 6) We continue to pursue cost reduction programs. Amid the uncertainties associated with the approval of the CSA Prime program, we consider it necessary to actively pursue cost optimization efforts in order to ensure operational effectiveness of our companies. And no regulatory actions have been taken in this respect as yet. Therefore, we optimize our expenses, divest non-core assets, and strive to provide import substitution in our projects whenever possible.

(Slide 7) Our key development priorities. As I've already stated, Gazprom's power generation strategy will be updated. We will select potential construction projects for new generating capacities based on their economic viability, optimizing operating and investment expenditures. It is planned to phase out about 2 GW of loss-making capacities until 2022.

We engage in international projects, such as the Pancevo Thermal Power Plant, which has been ratified and launched in Serbia. The advance payment for the TPP has been made, and all is set for construction.

We intend to continue paying out dividends and raise their amount.

That's it for 2017. Let us now turn to your questions.

QUESTION: Marina Kotsubinskaya, RIA Novosti. Could you please tell us about the company's forecast profit and EBITDA for 2018?

DENIS FYODOROV: The planned net profit for 2018 is RUB 32.5 billion for Gazprom Energoholding, RUB 13.2 billion for Mosenergo, RUB 4.2 billion for TGC-1, RUB 7.4 billion for OGK-2, and RUB 7.6 billion for MOEK. These are conservative estimates, and we will probably revise them in the middle of the year, because we see that some of our companies have exceeded the financial targets already in the first quarter of the year.

QUESTION: Alexey Kirichenko, Kommersant newspaper. Gazprom Energoholding was going to

build electric vehicle (EV) charging stations in St. Petersburg and Moscow, as well as wind power plants. Are these projects still on the table? If so, could you describe how they will be carried out?

DENIS FYODOROV: We are implementing a project for 150 EV charging stations for Mosenergo, the proposals to that end have been submitted to the Moscow Government. Meanwhile, we are reviewing proposals for another 200 EV charging stations.

The Board of Directors of TGC-1 tasked the company's management with preparing an EV charging stations program for St. Petersburg and the Leningrad Region.

As for wind power plants, TGC-1 will compete for a 50 MW power plant project.

ALEXEY KIRICHENKO: Who is holding the tender?

DENIS FYODOROV: The Market Council (Nonprofit Partnership Council for Organizing Efficient System of Trading at Wholesale and Retail Electricity and Capacity Market) is the organizer. This is standard practice. We will submit a bid in late May this year.

QUESTION: Anton Khlyshchenko, Interfax – Severo-Zapad agency. According to the Director of the Kazakhstan privatization fund, Samruk-Kazyna will offer 100 per cent of Samruk-Energo to Russian investors at the St. Petersburg International Economic Forum. Could this asset be of interest to Gazprom Energoholding and on what terms?

DENIS FYODOROV: No, we are not interested in this asset at the moment. We are still looking forward to the presentation at the Forum. But for now, this project is of no interest to us.

MODERATOR: We are receiving questions online, too. Nikolai Khrenkov from the Federal News Agency is asking: "Power businesses have long had disagreements with coal suppliers over fuel prices. Today, global coal prices are on the rise again. Are you reaching any compromises? Have you developed a price regulation formula that suits both parties?"

DENIS FYODOROV: This is a highly complicated and sensitive issue both for us and for coal suppliers. You know about severe disputes that we have had with coal supplying companies time and again. We often seek support from the Russian Ministry of Energy and governors of the regions where we run our business. The last well-known example is the Novochoerkassk SDPP (OGK-2, Rostov Region), which was close to falling below the level of total required fuel reserve last winter. By now, the situation with coal supplies has stabilized there, but we are following it closely. We even considered building a gas pipeline to provide the power plant with gas instead of coal.

CHPP-22 of Mosenergo is also using export grade coal. This is why we have decided that we will switch the station exclusively to natural gas and abandon coal and coal-fired infrastructure. This will primarily have a positive effect on Moscow's natural environment. Besides, the financial state of the plant is unfavorable. Given the current prices of export coal, it is much more profitable for us to use natural gas.

We try to find middle ground in every situation. You know the story with the Cherepovets SDPP (OGK-2, Vologda Region). The town of Inta (Inta coal deposit, Komi Republic) will face quite a difficult situation if we phase out the old part of the Cherepovets SDPP. We consume 60–65 per cent of the coal extracted in Inta.

The situation in Novochoerkassk (Novochoerkassk SDPP) is rather complex. Our company is the main buyer of coal from the so-called Eastern Donbass surface mine (Rostov part of the Donetsk coal basin), accounting for about 65–70 per cent of their coal sales. Considering that the power plant is operating at a loss, we know that refusal to buy coal has dire social implications for the Rostov Region.

To this end, we initiated meetings at the Ministry of Energy – not just one or two, but quite a lot of meetings – at which we argued that the prices for coal-fired power capacities are significantly lower in the European part of the country than in the second price zone, which is rather puzzling. It could also be seen as an incentive for us to decommission these capacities – if so, that's what we will do. But then, the Russian Government and the Ministry of Energy should assess all of the potential social and economic consequences for these regions.

To this date, we have developed a common understanding with Alexander Novak, Russian Minister of Energy, as to the necessity to raise the capacity price for the Novochoerkassk SDPP. However, the appropriate decision has not been made yet despite the acceptance of said official agreement made at the meeting of all federal executive authorities hosted by the Ministry of Energy. Many federal executive bodies are attempting to prevent us from doing this, which is not acceptable for us. Once the new cabinet of the Russian Government is formed, we will get in touch with the relevant ministries and ask them to remedy the situation.

MODERATOR: Another question from Nikolai Khrenkov: “The President has approved the program for the upgrade of generating capacities. Which power plants have been picked by Gazprom Energoholding for the upgrade?”

DENIS FYODOROV: This is a comprehensive issue that has not been legally regulated yet. We are aware that it is being actively discussed and that trial bidding was held within the so-called CSA Prime project. But today it is not more than just a project.

Regarding specific companies, we have outlined the following priorities to meet our internal needs: replacement of T-250 turbines at Mosenergo, power plant renovation projects for OGK-2 in relation to the Krasnoyarsk, Surgut and Stavropol SDPPs, and new steam power units for OGK-2 and TGC-1.

I would like to add more details about OGK-2. It will be very difficult to carry out the upgrade projects, as they have to meet localization requirements, i.e. to have high content of domestically-manufactured equipment that will be used in the upgrade process, which I consider reasonable and justified. Nevertheless, it doesn't seem practical to me to upgrade condensing blocks by replacing one steam turbine with another steam turbine operating in condensing cycle and producing only electric power. The only result that we will obtain this way is a 3–4 per cent increase in efficiency. They need to be upgraded by being converted to the combined cycle.

Concerning the claims that the content of domestic equipment should be raised to 100 or 80 per cent: it is impossible to find a large-sized gas turbine manufactured in Russia. We have repeatedly mentioned it before. And the local content of turbines produced by SGTT (Siemens Gas Turbine Technologies) in St. Petersburg does not exceed 50–55 per cent. Testing of the well-known Saturn gas turbine (UEC-Saturn) ended in nothing, as has been said many times before. Hence, it is very important to understand whether we will completely eliminate wholesale generation companies and all condensing power plants from the upgrading process or we will find the right solutions.

QUESTION: Anna Artemova, TASS – Petersburg agency. Regarding the construction of a TPP in China: when will you arrive at the final decision, and will you have a partner or build it on your own?

Are you interested in working in Syria and Iran?

DENIS FYODOROV: In response to the second question, I can say that if we get any instructions, we will work it out, but so far we have no willingness to take it up.

As regards China, we are currently studying two or three offers. I don't want to give you the details as our Chinese partners are quite difficult to negotiate with. It's not even a provisional arrangement but some kind of rough outlines on these projects. Among the projects, the one which I think we have had the most progress with is a 900 MW electric power plant. Naturally, Gazprom will not be even the controlling shareholder there, we are considering to join the project with a 24–25 per cent participating interest. But again, it is a matter of distant future. We haven't advanced beyond preliminary plans and non-binding memorandums yet.

ANTON KHLyshCHENKO: What amount of dividends is Gazprom Energoholding planning to pay out for 2018? And how may these payments be affected by the upgrade of electric power assets?

DENIS FYODOROV: It's too early to make forecasts for 2018 in this regard. After all, the amount of dividends is determined by our parent company – we come up with a proposal and then we begin to coordinate it with the relevant departments of Gazprom. But we are definitely planning to pay at least 26 per cent of the net profit under RAS and to continue reducing the debt. That is my first point.

My second point is that the upgrade models we are developing now for the CSA Prime projects don't

suggest that the level of dividends will be affected in any way by the implementation of such projects if they are executed. According to the provisional data of financial planning models, we will be able to secure a payout level of at least 26 per cent and provide financing for the investment program.

MODERATOR: We also have a question about the dividend policy from VTB Capital: “Is Gazprom Energoholding going to somehow adjust the dividend policy for its subsidiaries and affiliated companies rather than outline the frameworks of possible payouts as a percentage of net profit?”

DENIS FYODOROV: Do you mean to ask whether we want to set it in monetary terms? It seems a rather complicated question to me. It depends on the company’s financial results for the year. They can be subject to internal and external factors. Therefore, we will finally determine the payouts after summing up the annual results.

Today, we not only monitor the interest rate paid by us annually, but also try to control the amount that we pay out per one share. And we strive to ensure the annual growth of the dividend payouts per share. However, the non-adoption of the CSA Prime model, should it happen, will inevitably have an adverse impact on our financial performance.

In Mosenergo, three power units will be excluded from CSA projects this year. They will be transferred from the CSAs to CCO (competitive capacity outtake). The financial result will decline accordingly. Of course, the forecasts are different for each company. The matter is that Mosenergo was one of the first companies, if not the first, to promptly deliver major construction projects for combined-cycle power plants and to receive cash income. But the following year, a decline in net profit occurred, which may lead to lower dividend payouts per share in 2019 based on the results of 2018.

But we are not discussing this yet, because, as I’ve said earlier, the first quarter was much better than expected, so there is a chance of payouts per share not going down. We will look at the results of each company separately and make sure that our minority shareholders, to say nothing of our parent company Gazprom, receive enough monetary funds.

ANTON KHLyshCHENKO: There are persistent rumors in the media that Viktor Vekselberg proposed that Gazprom Energoholding acquire T Plus as a way of assisting Renova under the sanctions regime. Mr. Fyodorov, are you aware of this proposal? Can you confirm or deny this information? And could you formulate your opinion if you do confirm it?

DENIS FYODOROV: The only thing I can say is that it is a very complicated issue. For all I know, there are a lot of legal nuances that could harm all the companies. So I will not comment.

ANTON KHLyshCHENKO: What can you say about the possible sale of St. Petersburg Heating Grid to the city authorities?

DENIS FYODOROV: This is no big secret: we tried to come to an agreement with the vice governors for four or five years and to bring the issue to the highest level. It didn’t work out. I have been talking about it a lot and in great detail.

Then we decided to take a different approach and to hold talks with Igor Fyodorov, Director General of St. Petersburg Fuel and Energy Complex (TEK SPB). We proposed to exchange boiler houses for heat supply networks. By now, TGC-1 and TEK SPB have almost finalized the negotiations, and we have found common ground, deciding that Mr. Fyodorov and I will discuss issues with our respective management bodies. We will try to resolve the matter using a bottom-up approach and we believe that this is possible. We don’t have any serious differences with TEK SPB, and this solution is a fruitful one as it will give St. Petersburg a unified heat supply company.

Our achievements in Moscow are demonstrated by the financial results of MOEK. When we transferred all the boiler houses to Mosenergo, and Mosenergo transferred its heat supply networks to MOEK, a clear comprehensible pricing scheme for transmission services and thermal energy production was established in the city. Besides, it generated strong synergies in terms of saving gas and improving efficiency of Mosenergo power plants. We gradually close boiler houses, selling some of them, and we do it very carefully. We have agreed with Moscow that the boiler houses will be put on standby for two or three winter seasons just in case, so that we can assess whether the heat supply

process remains effective without these supplying facilities. And then we will just put them out of service.

We believe that it is a very good scheme, as it has proven its effectiveness in Moscow, the largest city in Russia, where the world's most extensive heat supply system is located. Our careful and step-by-step actions have produced positive results, both technologically and economically. I think that any large city with a heating system should adopt the best practices. St. Petersburg can easily follow this route and launch a project for setting up a unified heating grid company.

Of course, some areas are operated by other heat suppliers. Nevertheless, TEK SPB will become a truly unified heating grid company. It will allow both the city authorities and TEK SPB to analyze their investment program at large in order to improve the technical condition of the heating networks in St. Petersburg, which, unfortunately, causes serious concerns today.

MODERATOR: Bloomberg wants to clarify whether the profit forecast for Mosenergo and TGC-1 is based on RAS or IFRS.

DENIS FYODOROV: The profit forecast is for the year 2018 and is based on the Russian Accounting Standards. All of our statements for 2017–2018 are prepared according to the RAS.

MARINA KOTSUBINSKAYA: The presentation outlines the acquisition of core assets as a key priority and highlights the ongoing monitoring related to the company's horizontal expansion. Could you expand on the topic?

In January, you said that bitcoin mining companies were approaching Gazprom Energoholding with cooperation proposals. What about that?

DENIS FYODOROV: We are having a lot of negotiations with bitcoin mining companies. Each month, two or three companies turn up with various proposals. We have not implemented any big mining projects so far. But I think that the options and proposals that we present to our colleagues are quite favorable. Perhaps we will soon be able to talk about a number of projects carried out in this area.

As regards the acquisition of core assets, this is a fairly standard wording for all of our presentations. I guess that any company that follows the current market situation analyzes offers for the acquisition of certain assets and makes decisions based on its own needs and economic feasibility. We carry out monitoring with regard to assets acquisition, but we have no projects close to completion now.

OLGA KVASHINA: CSA Prime is important for the Krasnoyarsk SDPP-2. Could you inform us, from what you know, when we should expect the adoption of federal laws for the CSA Prime projects?

DENIS FYODOROV: The first CSA Prime program was developed back when the previous Government was in office, with Sergey Shmatko as Minister of Energy. It was even submitted to the federal executive authorities, but that was the end of it.

Today, we have an instruction from the Russian President. As far as I know, the Government of the Russian Federation reported on it and forwarded to the Presidential Administration the documents describing the Ministry of Energy's vision with regard to the implementation of CSA Prime. We could certainly propose some amendments, but we have always believed that perfect is the enemy of good. Besides, we have been dragging the program out for more than seven or eight years, although its importance is quite obvious to all industry professionals. And now we are very close to getting it done. As soon as the new Government is formed, the regulatory framework can be developed for the program within three or four months, and then the first competitive tenders can take place.

The Krasnoyarsk SDPP-2 is undoubtedly among our priorities in terms of upgrades.

ALEXEY KIRICHENKO: A clarifying question about the asset swap with St. Petersburg Fuel and Energy Complex: will you get all of their boiler houses as a result of this transaction?

DENIS FYODOROV: Yes, we will get all of them.

ALEXEY KIRICHENKO: Have you already come to an agreement with Igor Fyodorov on this?

DENIS FYODOROV: We are currently at a rather unsettled stage. There are certain tensions, but I don't think that they play an important part in the negotiating processes.

ALEXEY KIRICHENKO: Will the Governor or Vice Governor of St. Petersburg approve this transaction?

DENIS FYODOROV: We have already attempted to contact all vice governors with regard to this issue and have not been able to achieve anything; we have been trying to solve this issue for many years. This is why we believe that it needs to be settled at the next Interdepartmental Council concerning the Cooperation Agreement between St. Petersburg and Gazprom or at a meeting between the St. Petersburg Governor and the Chairman of the Gazprom Management Committee. In any case, our companies, TGC-1 and Gazprom Energoholding, are ready to sign this deal.

MODERATOR: We are receiving some rather popular questions online: "Are you planning an IPO for Gazprom Energoholding? Are you planning to transition to a unified share?"

DENIS FYODOROV: We are not planning such a transition. Let's see what we have: we hold 53 per cent in Mosenergo and 51 per cent in TGC-1. What expenses will we have to incur in order to redeem shares from minority shareholders and make proposals that will seem appealing to them?! And it is quite obvious that the minority shareholders are not interested in the market right now. Because, as I've said earlier, it does not reflect the intrinsic value of companies. Therefore, I do not consider it worthwhile to take the heavy financial load.

The same is also true for the IPO. Until the exchange stabilizes and stock prices reach the values we consider adequate, we will not go for it.

ANNA ARTEMOVA: What is the amount of debt that you are going to pay off in 2018?

DENIS FYODOROV: RUB 19 billion.

MODERATOR: Thank you. The Press Conference is over.