

**MANAGEMENT REPORT  
PJSC GAZPROM  
FOR 2017**

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Note:

This Management Report determines some operating and economic parameters in accordance with the International Financial Reporting Standards (IFRS) principles for the Group's entities included in the IFRS consolidated financial statements of PJSC Gazprom for the year ended 31 December 2017. Therefore, they may differ from similar parameters in reports of PJSC Gazprom prepared under Russian statutory requirements.

Moreover, some operating parameters of PJSC Gazprom and its subsidiaries are determined in accordance with the principles underlying management reporting.

Analysis of financial results should be read in conjunction with the audited consolidated financial statements of PJSC Gazprom for the year ended 31 December 2017 prepared in accordance with IFRS.

Among other things, the Management Report discloses information on the future production and economic activities of Gazprom Group, based on the management's forecasts and estimates considering the current situation. Actual results may differ from the said forecasts and estimates due to the effect of various objective factors.

PJSC Gazprom and its subsidiaries (“Gazprom Group”, “Gazprom”, or the “Group”) is one of the world’s largest vertically integrated energy companies.

## THE GROUP’S POSITION IN THE GLOBAL ENERGY INDUSTRY

Gazprom remains a global leader in terms of natural gas reserves (ca. 17% of global gas reserves) and gas production (ca. 12% of global gas production). Gazprom’s share in total Russian production stands at 68% for gas and 11% for oil and gas condensate (including the Group’s share in production volumes of entities in which Gazprom has investments classified as joint operations).

The Unified Gas Supply System (UGSS) of Russia is a centrally operated system of natural gas treatment, transportation and storage. The UGSS incorporates the world’s longest network of high-pressure trunk pipelines covering European Russia and Western Siberia. As at the end of 2017, the combined length of trunk pipelines and connections operated by the Group’s gas transportation subsidiaries in Russia totalled 172.05 thousand km.

In Russia, Gazprom Group accounts for a half of all natural and associated petroleum gas processing and 18% of oil and stable gas condensate refining.

Gazprom is the dominant supplier of gas to consumers in Russia and countries of the former Soviet Union (FSU). In addition, the Group is Europe’s major supplier of natural gas. The share of PJSC Gazprom’s gas sales under contracts signed by LLC Gazprom export and under direct contracts with GAZPROM Schweiz AG in the total gas consumption in European far abroad countries is 34.2%.

The Group also owns electricity generating assets, which provide approximately 15% of all the electrical power generated in Russia. Gazprom is the largest Russian heat producer.

Gazprom Group’s key operational and financial indicators for 2017 and 2016 are presented in the tables below:

	As at and for the year ended 31 December		Change, %
	2017	2016	
<b>Reserves of hydrocarbons under PRMS standards<sup>(1)</sup></b>			
Proved and probable gas reserves, bcm	24,146.57	23,855.11	1.2
Proved and probable gas condensate reserves, mm tonnes	1,105.68	1,018.94	8.5
Proved and probable crude oil reserves, mm tonnes	1,360.02	1,378.72	-1.4
Total proved and probable hydrocarbon reserves <sup>(2)</sup> , bboe	175.72	173.26	1.4
<b>Operating indicators</b>			
Natural and associated petroleum gas production <sup>(1)</sup> , bcm	472.1	420.1	12.4
Crude oil production <sup>(1)</sup> , mm tonnes	48.6	47.2	3.0
Unstable gas condensate production <sup>(1)</sup> , mm tonnes	15.9	15.9	–
Total hydrocarbon production <sup>(1),(2)</sup> , mm boe	3,550.2	3,202.5	10.9
Natural and associated petroleum gas processing, bcm	30.8	31.0	-0.6
Liquid hydrocarbons refining, mm tonnes	64.1	65.9	-2.7
Electricity generation, billion kWh	156.55	157.51	-0.6

	As at and for the year ended 31 December		Change, %
	2017	2016	
<b>Key financial results, RUB mm</b>			
Sales revenue	6,546,143	6,111,051	7.1
Operating profit	870,623	725,580	20.0
Profit for the year attributable to the owners of PJSC Gazprom	714,302	951,637	-24.9
Adjusted EBITDA	1,466,910	1,322,199	10.9
<b>Balance Sheet highlights, RUB mm</b>			
Cash and cash equivalents	869,007	896,728	-3.1
Total debt	3,266,518	2,829,623	15.4
Net debt	2,397,511	1,932,895	24.0
Total assets	18,238,770	16,918,938	7.8
Total equity (including non-controlling interest)	12,015,481	11,441,839	5.0
<b>Ratios</b>			
Earnings per share for profit attributable to the owners of PJSC Gazprom, RUB	32.32	42.19	-23.4
Total debt to equity ratio (including non-controlling interest)	0.27	0.25	8.0
Adjusted EBITDA margin, %	22.4	21.6	3.7
Profit margin for the year attributable to the owners of PJSC Gazprom, %	10.9	15.6	-30.1

Note:

- (1) Including the Group's share in the reserves and production volumes of entities in which Gazprom has investments classified as joint operations.
- (2) For management accounting purposes, Gazprom Group measures hydrocarbon reserves and production in metric units. In this Management Report, gas reserves and production are converted from metric units to barrels of oil equivalent at a ratio of 1,000 cubic metres to 6.49 boe.

## OPERATING RESULTS

### Reserves and Development of Hydrocarbons

The table below shows assets and capital expenditures in the Production of gas and Production of oil and gas condensate segments:

	As at 31 December	
	2017	2016
<b>Production of gas</b>		
Assets, RUB million	2,677,231	2,636,296
Share in the Group's total assets, %	15.2	15.7
<b>Production of oil and gas condensate</b>		
Assets, RUB million	2,516,019	2,310,960
Share in the Group's total assets, %	14.3	13.8
<b>For the year ended 31 December</b>		
<b>2017</b>		
<b>2016</b>		
<b>Production of gas</b>		
Capital expenditures, RUB million	216,450	235,161
Share in the Group's total capital expenditures, %	14.4	17.3
<b>Production of oil and gas condensate</b>		
Capital expenditures, RUB million	330,424	326,366
Share in the Group's total capital expenditures, %	22.0	24.0

## Reserves

According to an audit of Gazprom Group's hydrocarbon reserves under PRMS standards performed by DeGolyer and MacNaughton, as at 31 December 2017 proved and probable hydrocarbon reserves of Gazprom Group (including the share in the reserves of entities in which Gazprom has investments classified as joint operations) are estimated at 175.72 bboe. The audit covered 94.1% of gas reserves, 92.7% of condensate reserves, and 93.5% of oil reserves in A, B<sub>1</sub>, and C<sub>1</sub> reserve categories.

The table below shows proved and probable reserves of Gazprom Group (including the share in the reserves of entities in which Gazprom has investments classified as joint operations) under PRMS standards:

		<b>As at 31 December</b>	
		<b>2017</b>	<b>2016</b>
<b>Gas</b>			
Share of A+B <sub>1</sub> +C <sub>1</sub> reserves covered by the audit under PRMS standards <sup>(1)</sup> , %		94.1	95.4
Proved			
	bcm	18,253.39	18,596.47
	bboe	118.46	120.69
Probable			
	bcm	5,893.18	5,258.64
	bboe	38.25	34.13
Proved and probable			
	bcm	24,146.57	23,855.11
	bboe	156.71	154.82
<b>Gas condensate</b>			
Share of A+B <sub>1</sub> +C <sub>1</sub> reserves covered by the audit under PRMS standards <sup>(1)</sup> , %		92.7	93.5
Proved			
	mm tonnes	797.75	759.23
	bboe	6.52	6.21
Probable			
	mm tonnes	307.93	259.71
	bboe	2.52	2.12
Proved and probable			
	mm tonnes	1,105.68	1,018.94
	bboe	9.04	8.33
<b>Oil</b>			
Share of A+B <sub>1</sub> +C <sub>1</sub> reserves covered by the audit under PRMS standards <sup>(1)</sup> , %		93.5	93.3
Proved			
	mm tonnes	736.80	789.56
	bboe	5.40	5.79
Probable			
	mm tonnes	623.22	589.16
	bboe	4.57	4.32
Proved and probable			
	mm tonnes	1,360.02	1,378.72
	bboe	9.97	10.11

	<b>As at 31 December</b>	
	<b>2017</b>	<b>2016</b>
<b>Total</b>		
Share of A+B <sub>1</sub> +C <sub>1</sub> reserves covered by the audit under PRMS standards <sup>(1)</sup> , %	94.0	95.2
Proved, bboe <sup>(2)</sup>	130.38	132.69
Probable, bboe <sup>(2)</sup>	45.34	40.57
Proved and probable, bboe <sup>(2)</sup>	175.72	173.26

Notes:

- <sup>(1)</sup> The A+B<sub>1</sub>+C<sub>1</sub> reserve classification accepted in Russia is based on geological data analysis and estimates the actual hydrocarbon reserves contained in geological formations. Under the new Classification of Reserves and Resources of Oil and Flammable Gases, approved by the Ministry of Natural Resources and Environment of the Russian Federation (Decree No. 477 dated 1 November 2013) and effective from 1 January 2016, A+B<sub>1</sub>+C<sub>1</sub> categories comprise explored reserves of high geological certainty and correspond to the previously used A+B+C<sub>1</sub> categories. PRMS standards take into account not only the probability of hydrocarbon presence in geological formations but also the economic feasibility of extracting reserves, which is determined based on exploration and drilling costs, operating expenses for production and transportation, taxes, current hydrocarbon prices, and other factors.
- <sup>(2)</sup> For management accounting purposes, Gazprom Group measures hydrocarbon reserves and production in metric units. In this Management Report, gas reserves are converted from metric units to barrels of oil equivalent at a ratio of 1,000 cubic metres to 6.49 boe.

Gazprom Group's PRMS proved and probable hydrocarbon reserves increased by 2.46 bboe from the previous estimate as at 31 December 2016. In addition to the annual production from the fields operated by Gazprom, the key factors behind the changes in reserve estimates under international standards included an audit of the Yuzhno-Lunskoye, Zemlyanskoye, Novosamarskoye, Severo-Samburgskoye, and Kamennomyskoye (onshore) fields, as well as re-estimation of reserves contained in the Malyginskoye field, Achimov deposits of the Urengoykoye field, and Cenomanian deposits of the Yamburgskoye field.

The bulk of the Group's hydrocarbon reserves is concentrated within its licence areas in Russia. International reserves of the Group are seen as insignificant.

As at 31 December 2017, Gazprom Group held 265 subsoil licences for conducting geological surveys, prospecting, exploration, and production of hydrocarbons in the Russian Federation. These licence blocks aggregately cover the area of 547.5 thousand square km. In addition, entities in which Gazprom has investments classified as joint operations held a total 36 licences covering a total area of 23.1 thousand square km.

As at 31 December 2017, Gazprom Group's A+B<sub>1</sub>+C<sub>1</sub> hydrocarbon reserves in Russia were 35,355.4 bcm of natural gas, 1,595.6 mm tonnes of gas condensate, and 2,045.3 mm tonnes of oil, including the share in the reserves of entities in which Gazprom Group has investments classified as joint operations – 24.3 bcm of gas, 2.8 mm tonnes of gas condensate, and 183.2 mm tonnes of oil.

The Group's share in A+B<sub>1</sub>+C<sub>1</sub> hydrocarbon reserves of associates and joint ventures as at 31 December 2017 was 1,003.8 bcm of natural and associated gas, 100.8 mm tonnes of gas condensate, and 578.3 mm tonnes of oil.

The table below shows changes to A+B<sub>1</sub>+C<sub>1</sub> reserves of natural gas, gas condensate, and oil (including the share in the reserves of entities in which Gazprom Group has investments classified as joint operations) contained within the licenced areas of Gazprom Group in Russia in 2017:

	Natural gas, bcm	Gas condensate, mm tonnes	Oil, mm tonn es	Total, mm boe
<b>Reserves as at 31 December 2016</b>	<b>36,443.9</b>	<b>1,534.9</b>	<b>2,078.5</b>	<b>264,311.8</b>
<b>including non-controlling interests<sup>(1)</sup></b>	<b>622.3</b>	<b>4.2</b>	<b>68.6</b>	<b>4,575.9</b>
Exploration-based additions to reserves	852.9	95.6	3.3	6,341.5
Transfer of reserves discovered in 2017 to the Russian open acreage <sup>(2)</sup> , to the books of other companies; acquisition from other companies	-46.4	-	1.2	-292.3
Obtaining of licences	12.8	1.9	-	98.6
Licence returns	-0.1	-	-	-0.6
Acquisition of assets	-	-	-	-
Disposal of assets	-	-	-9.4	-68.9
Re-estimation	-1,437.8	-24.8	19.8	-9,389.1
Production (including losses)	-469.9 <sup>(3)</sup>	-12.0 <sup>(4)</sup>	-48.1	-3,500.4
<b>Reserves as at 31 December 2017</b>	<b>35,355.4</b>	<b>1,595.6</b>	<b>2,045.3</b>	<b>257,500.6</b>
<b>including non-controlling interests<sup>(1)</sup></b>	<b>517.9</b>	<b>4.2</b>	<b>71.2</b>	<b>3,917.4</b>

Notes:

- (1) Non-controlling interest as at the end of the year is calculated based on Gazprom Group's effective interest in the share capital of the relevant subsidiary which is a subsoil use licence holder.
- (2) Under the Russian laws, a subsoil user does not have any vested right to develop reserves it discovers within the areas covered by its exploration licences or beyond the licenced areas. Such reserves are to be transferred to the open acreage of the Russian Federation, with the subsoil user granted the pre-emptive right to subsequently obtain a licence for developing the relevant discovery.
- (3) Excluding dissolved gas.
- (4) Any production-driven changes in gas condensate reserves are recognized following conversion into stable gas condensate (C<sub>5+</sub>). In 2017, Gazprom Group produced 15.9 mm tons of unstable gas condensate.

### Re-estimation of reserves

Accounting for reserves under the new Russian Classification of Reserves and Resources of Oil and Flammable Gases using gas recovery factors (GRFs) since January 2016 was a major factor behind the changes in A+B<sub>1</sub>+C<sub>1</sub> natural gas reserves vs the estimate as at 31 December 2016. As at 31 December 2017, Gazprom completed the GRF estimation for fields containing 19% of Gazprom Group's A+B<sub>1</sub>+C<sub>1</sub> reserves (Kirinskoye, Bovanenkovskoye, Yen-Yakhinskoye, Yamburgskoye (Cenomanian), Yuzhno-Russkoye (Cenomanian and Turonian), and Chayandinskoye). Following the GRF re-estimation, the reported recoverable reserves of natural gas decreased by 1,281.6 bcm.

## Exploration

The table below shows summary information on the exploration activities completed in 2017 across Gazprom Group's licenced areas in Russia and within the foreign projects implemented with the Group's participation:

**For the year ended 31 December 2017**

	<b>In Russia</b>	<b>Abroad<sup>(1)</sup></b>
Exploration drilling, thousand m	85.9	18.4
Completed exploration wells, units	36	8
including successful wells	31	5
2D seismic surveys, thousand km	–	–
3D seismic surveys, thousand square km	18.7	1.2
Financing for exploration (including VAT), RUB billion	82.6	4.1

Note.

<sup>(1)</sup> The consolidated data reflecting the physical metrics of the exploration activities carried out by Gazprom Group in foreign countries include the data for projects in which the Group's subsidiaries act as operators.

In addition, for entities in which Gazprom has investments classified as joint operations, exploration drilling stood at 12.8 thousand m, with four exploration wells completed and flowing, and 3D seismic was acquired on 0.2 thousand square km.

In 2017, exploration-driven additions to Gazprom Group's A+B<sub>1</sub>+C<sub>1</sub> hydrocarbon reserves in Russia totalled 852.9 bcm of natural gas, 95.6 mm tonnes of gas condensate, and 3.3 mm tonnes of oil. The bulk of this growth in gas reserves was concentrated at the Tambeyskoye (395.5 bcm) and Malyginskoye (201.1 bcm) fields on the Yamal Peninsula, and in the Achimov deposits of the Urengoykoye field in the Yamal-Nenets Autonomous Area (194.9 bcm). In 2017, reserves were estimated at 48.9 bcm of gas for the Yuzhno-Lunskoye field within the Kirinsky prospect on the Sea of Okhotsk continental shelf.

C<sub>1</sub>+C<sub>2</sub> reserves grew during the reporting year at the Tambey cluster fields (Tambeyskoye and Malyginskoye) from 2.6 tcm as at 31 December 2016 to 7.7 tcm as at 31 December 2017 (including 7.4 tcm within PJSC Gazprom's licence blocks). Gazprom's surveys found that the Severo-Tambeyskoye, Zapadno-Tambeyskoye, and Tasiyskoye fields, previously considered to be separate fields, are in fact one and the same Tambeyskoye field.

The Group discovered four fields during 2017 – Yuzhno-Lunskoye (the Sea of Okhotsk continental shelf), Salairskoye (the Krasnoyarsk Territory), Alexander Zhagrin (the Khanty-Mansi Autonomous Area – Yugra), and Novozarinskoye (the Orenburg Region), and 47 new deposits at previously discovered fields in the Yamal-Nenets Autonomous Area, Khanty-Mansi Autonomous Area – Yugra, and in the Tomsk, Irkutsk, and Orenburg Regions. In addition, entities in which Gazprom has investments classified as joint operations discovered the Melimovskoye field in the Tomsk Region, as well as five deposits in the Khanty-Mansi Autonomous Area – Yugra, and in the Tomsk Region.

Gazprom completed the construction of a 2,700 m exploration well within the Ayashsky licence block on the Russian Sea of Okhotsk continental shelf (Sakhalin-3 project) during the reporting year. When tested, the well produced commercial oil flow, and reserves will be estimated in 2018.

The reserve replacement ratio for the Group's assets in Russia was 1.82 for natural gas, and 1.64 for gas condensate and oil.

During 2017, Gazprom Group carried out a number of geological and geophysical (G&G) surveys under the relevant contracts in FSU countries, Europe, Southeast Asia, Africa, the Middle East, and South America.



Exploration campaigns conducted by Gazprom Group on the Group-operated projects included drilling in Serbia and Romania and Iraq, as well as 3D seismic surveys in Serbia. The exploration programmes discovered three fields in Serbia, and one field in Romania.

Exploration campaigns across projects not operated by Gazprom Group resulted in the discovery of Winchelsea field in 2017.

### Production

The table below shows information on the volumes of natural gas and liquid hydrocarbons produced by Gazprom Group, its associates and joint ventures in Russia:

	Natural and associated gas, bcm	Unstable gas condensate, mm tonnes	Oil, mm ton nes	Total, mm boe
<b>For the year ended 31 December 2017</b>				
Production of Gazprom Group, including the share in production volumes of entities in which Gazprom has investments classified as joint operations	472.1	15.9	48.6	3,550.2
Gazprom Group's share in production volumes of associates and joint ventures	27.0	5.0	10.9	296.0
<b>For the year ended 31 December 2016</b>				
Production of Gazprom Group, including the share in production volumes of entities in which Gazprom has investments classified as joint operations	420.1	15.9	47.2	3,202.5
Gazprom Group's share in the production volumes of associates and joint ventures	27.2	5.2	9.9	291.6

In 2017, Gazprom Group produced 472.1 bcm of natural and associated gas in Russia, up 12.4% year-on-year, including the share in production volumes of entities in which Gazprom has investments classified as joint operations (1.1 bcm of natural and associated gas).

Gazprom Group produced 48.6 mm tonnes of oil, including the share in production volumes of entities in which Gazprom has investments classified as joint operations (7.6 mm tonnes). The production increase was driven by higher oil production from the Novoportovskoye and Prirazlomnoye fields following the drilling of production wells with a total production of 8.6 mm tonnes.

Gazprom Group produced 15.9 mm tonnes of gas condensate in 2017.

In 2017, associates and joint ventures produced 27.0 bcm of natural and associated gas, 5.0 mm tonnes of gas condensate, and 10.9 mm tonnes of oil (share attributable to Gazprom Group). Oil production increased due to higher production from JSC Messoyakhneftegaz-operated Vostochno-Messoyakhskoye field, put into commercial development in 2H 2016. The company is owned by PJSC Gazprom Neft and PJSC Rosneft as equal shareholders.

Naftna Industrija Srbije (NIS), a Serbian subsidiary of Gazprom Neft Group, produced 1.0 mm tonnes of oil and 0.5 bcm of natural and associated gas in 2017.

The table below shows information on the number of Gazprom Group's field developments and production well stock (excluding entities in which Gazprom has investments classified as joint operations):

	<b>As at 31 December 2017</b>	
	<b>In Russia</b>	<b>Abroad</b>
Fields in commercial development	136	46
Fields in pilot development	18	2
Gas production wells (active)	7,438	81
Oil production wells (active)	7,358	737

In addition, as at 31 December 2017, entities in which Gazprom has investments classified as joint operations had 35 fields in commercial development, and six fields under pilot development.

Gazprom Group also has stakes in a number of oil and gas projects at the production stage in a number of foreign countries.

In terms of natural gas and gas condensate production, the largest of them include the following projects:

- projects within licence blocks 05–2 and 05–3 in the Vietnamese section of the South China Sea bed (49% held by Gazprom Group). Total gas production in 2017 from the Moc Tinh and Hai Thach fields was 2.0 bcm of gas.
- Ipati and Aquio licence blocks in Bolivia (20% held by Gazprom Group). Total gas production in 2017 from the Incahuasi field was 2.5 bcm of gas.

The Badra field development project in Iraq (30% held by Gazprom Group) is the largest asset by production of oil and associated petroleum gas among the foreign projects implemented with the Group's participation. In 2017, a total 3.8 mm tonnes of oil were produced from the Badra field, and gas supplies were started to Az-Zubaidiya power station supplying electric power to several provinces across Iraq and the capital city of Baghdad.

Wintershall Noordzee B.V. joint venture (50% held by the Group) produced 0.8 bcm of gas in 2017. The company also started the commercial development of the Ravn oil field in the Danish North Sea.

In Lybia, the Group's associate Wintershall AG (50% owned by the Group) operates nine fields on oil concessions C96 and C97, with production interruptions due to the unstable political situation in the country. A total 1.5 mm tonnes of oil and 0.2 bcm of associated petroleum gas were produced in 2017.

#### Major capex projects

The bulk of gas production capex was spent on field construction to develop the Chayandinskoye OGCF, the Cenomanian-Aptian deposits at the Bovanenkovskoye OGCF, and the Achimov deposits in the Urengoy OGCF while oil and gas condensate production capex was mostly directed toward field construction to develop the oil rim in the Botuobinsky horizon of the Chayandinskoye OGCF, and the implementation of Gazprom Neft Group's projects, including construction and production drilling at the Novoportovskoye and Prirazlomnoye fields, as well as capex projects for conventional assets.

As part of its gas production capex projects, Gazprom commissioned in 2017 two booster compressor stations at the Zapolyarnoye OGCF (Phase 1) and the Bovanenkovskoye OGCF (Phase 2, Stage 1) with combined capacity of 176 MW, and added new, 16 MW gas pumping unit to the booster compressor station (Phase 2) at the Zapadno-Tarkosalinskoye OGCF.

As part of oil production initiatives, the following facilities were commissioned to improve APG utilisation rates:

- a gas compressor station at the Shinginskoye field with an annual capacity of 150 mmcm and two vacuum compressor stations at the Shinginskoye and Luginetskoye groups of fields

- a gas pipeline to bring gas from the Orenburgskoye OGCF's Eastern block to the Orenburg GPP
- a CGTU with an annual capacity of 3.6 bcm at the Novoportovskoye field, to support APG treatment and utilisation through re-injection into a reservoir to maintain formation pressure.

Apart from that, new production wells were commissioned in Russia: 37 gas wells, and 666 oil wells. Production drilling totalled 240.8 thousand m for gas, and 2,559.5 thousand m for oil.

Outside Russia, a CGTU (Phase 1) and an export gas pipeline were commissioned as part of the Badra field development project in Iraq.

#### Oil and gas condensate sales

In 2017, Gazprom Group sold 27.6 mm tonnes of crude oil and stable gas condensate, up by 2.9 mm tonnes, or 11.7%, year-on-year, with total net sales revenue (net of VAT and customs duties) reaching RUB 540.0 bn, up by RUB 128.0 bn, or 31.1% year-on-year, a significant increase over 2016 driven mostly by increased revenue from sales to Europe and other countries due to higher prices and sales volumes.

The table below shows the volumes of oil and gas condensate sales by Gazprom Group in the domestic and foreign markets:

(Mm tonnes)	For the year ended 31 December		Change, %
	2017 <sup>(1)</sup>	2016 <sup>(1)</sup>	
Russia	4.3	5.9	-27.1
including Gazprom Neft Group	2.8	4.4	-36.4
FSU countries	1.7	1.7	–
including Gazprom Neft Group	1.7	1.7	–
Europe and other countries	21.6	17.1	26.3
including Gazprom Neft Group	19.3	13.6	41.9
<b>Total</b>	<b>27.6</b>	<b>24.7</b>	<b>11.7</b>

Note.

<sup>(1)</sup> The volumes of oil and gas condensate sales do not include intra-group sales.

Higher sales to Europe and other countries in 2017 were attributable to increased oil production from the Novoportovskoye and Prirazlomnoye fields, and start-up of production from the Vostochno-Messoyakhskoye field in Russia, as well as oil production growth in Iraq, and decline in oil refining volumes. Lower sales in the domestic market were due to lower cost-efficiency of oil trading operations.

Gazprom Group's performance is affected by the global and domestic oil prices. According to PLATTS, the average price of Urals crude (average quotes of Urals Mediterranean and Urals Rotterdam) was USD 53.06 per barrel in 2017, up by 26% year-on-year.

Crude oil benchmark	January	February	March	April	May	June
USD per barrel						
Brent <sup>(1)</sup>	54.67	55.11	51.56	52.53	50.43	46.52
Urals <sup>(2)</sup>	53.30	53.68	49.92	51.30	49.33	45.88
Urals–Brent spread	1.37	1.43	1.65	1.23	1.10	0.64

Crude oil benchmark	July	August	September	October	November	December
USD per barrel						
Brent <sup>(1)</sup>	48.56	51.64	56.05	57.36	62.62	64.19
Urals <sup>(2)</sup>	47.90	50.89	53.84	56.34	61.78	63.45
Urals–Brent spread	0.66	0.75	2.20	1.02	0.84	0.74

Notes:

<sup>(1)</sup> Based on daily average Brent quotes calculated as the average between the highest and lowest intraday prices.

<sup>(2)</sup> Based on daily average quotes of Urals Mediterranean and Urals Rotterdam calculated as the average between the highest and lowest intraday prices.

### Events in the reporting year

A framework was established in 2017 to expand Russian-Iranian cooperation. During 2017, Gazprom and Iranian companies signed a number of agreements for cooperation in exploration, production, transportation, processing, and marketing of hydrocarbons. The documents provide a framework to further expand bilateral partnerships across the entire value chain from production to marketing.

### Outlook for the Production of gas and Production of crude oil and gas condensate segments

Gas reserves contained in the conventional hydrocarbon fields operated by Gazprom Group represent over 70 years of supply to the domestic and foreign markets at the current production rate of 471 bcm of gas per year (excluding the share in production volumes of entities in which Gazprom has investments classified as joint operations).

One of Gazprom's key production objectives is to achieve target production rates for the existing fields, bring online new fields in the Nadym-Pur-Taz region, further explore the deposits in deep-lying Achimov and Jurassic sediments and above the Cenomanian sediments in fields under development in the Yamal-Nenets Autonomous Area, and launch production at unique, large fields in the Yamal Peninsula and on the continental shelf in Russian northern seas to sustain and increase hydrocarbon production levels. Gazprom consistently adds production capacity within the Nadym-Pur-Taz region and the Bovankenkovskoye field in the Yamal Peninsula.

Strategic priority gas production regions over the longer term include the Yamal Peninsula (Cenomanian-Aptian deposits of the Kharasaveyskoye field, Neocomian-Jurassic deposits of the Bovankenkovskoye and Kharasaveyskoye fields, and the Kruzenshternskoye field), and Russian northern seas (fields in the Ob and Taz Bays, primarily the Severo-Kamennomysskoye and Kamennomysskoye-Sea fields, and the offshore Shtokman field in the Barents Sea).

Gazprom is making consistent progress in building gas production hubs in Russia's Eastern regions, with the Chayandinskoye oil and gas condensate field being the core field for the Yakutsk gas production hub, and the Irkutsk gas production hub being formed around the Kovyktinskoye gas and condensate field. These fields will comprise the resource base for the Power of Siberia trunk pipeline. The priority developments to add production capacity at the Sakhalin gas production hub include Sakhalin-3 fields – the Kirinskoye gas and condensate field put into commercial development in 2014, and the Yuzhno-Kirinskoye gas and condensate field, one of Gazprom's priority projects in gas production over the longer term.

Gazprom Neft Group aims to increase its annual hydrocarbon production to 100 mm tonnes of oil equivalent by 2020 and sustain this rate through 2025, maintaining a proved reserve life of at least 15 years. To achieve these targets, Gazprom Neft Group intends to maximise the profitability of the remaining resource extraction at its active production sites through the roll-out of best development optimisation practices, the reduction of the cost of tested production technologies, and the adoption and commercial introduction of new technologies. The company contemplates a new production hub in the northern part of the Yamal-Nenets Autonomous Area. Gazprom Neft Group treats unconventional reserves as a growth opportunity and will expand this asset class as an important component of its portfolio.

## Transportation

The table below shows information on the assets and capital expenditures in the Transportation segment:

	As at 31 December	
	2017	2016
Assets, RUB million	6,721,549	6,596,937
Share in the Group's total assets, %	38.1	39.3

  

	For the year ended 31 December	
	2017	2016
Capital expenditures, RUB million	498,550	406,828
Share in the Group's total capital expenditures, %	33.1	30.0

### Gas transportation system

The Unified Gas Supply System (UGSS) of Russia is a centrally operated system of natural gas treatment, transportation and storage. The UGSS incorporates the world's longest network of high-pressure trunk pipelines covering European Russia and Western Siberia. In addition, the Group owns trunk pipelines in the Russian Far East: Sakhalin – Khabarovsk – Vladivostok, and Sobolevo – Petropavlosk-Kamchatsky pipelines.

As at the end of 2017, the combined length of trunk pipelines and connections operated by the Group's gas transportation subsidiaries in Russia totalled 172.05 thousand km (taking into account technological jumpers). The gas transportation system (GTS) comprises 254 compressor stations, equipped with a total 3,844 gas pumping units with a combined capacity of 46,700 MW.

The table below shows age breakdown of Gazprom Group's gas transport subsidiaries' trunk gas pipelines in Russia:

Age of trunk gas pipelines	As at 31 December 2017	
	Length, thousand km	Share, %
10 years or less	17.31	10.1
11 to 20 years	16.22	9.4
21 to 30 years	40.85	23.8
31 to 40 years	55.13	32.0
41 to 50 years	24.81	14.4
Over 50 years	17.73	10.3
<b>Total</b>	<b>172.05</b>	<b>100.0</b>

During 2017, a total 672.1 bcm of gas were supplied into Gazprom's GTS in Russia, up 8% year-on-year. The growth was driven by higher demand and subsequent increase in gas supplies by Gazprom and non-Group companies. In 2017, the amount of natural gas consumed for the GTS' own operational needs was 37.3 bcm.

As the owner of the Russian section of the GTS, PJSC Gazprom leases out free pipeline capacity (subject to its availability) to independent companies outside Gazprom Group provided they have a gas production licence and a supply contract with the buyer of the supplied gas. Such third-party gas also needs to meet relevant technical standards.

In 2017, the volume of gas transported via Gazprom Group's GTS in Russia by companies outside Gazprom Group was 137.9 bcm (129.0 bcm in 2016).

All overhauls of the gas transportation system facilities scheduled for the reporting year under the relevant targeted comprehensive repair programmes were completed in full.

Gazprom Group subsidiaries own the gas transportation systems in Belarus, Armenia, and Kyrgyzstan. OJSC Gazprom transgaz Belarus is the Group's core gas transportation asset abroad, supplying natural gas to consumers in Belarus, and carrying transit supplies of gas to Europe and

Russia's Kaliningrad Region. Daily requests by PJSC Gazprom to transport Russian natural gas through Belarus were satisfied in full.

The table below shows the volumes of gas injected into the gas transportation systems in Belarus:

(bcm)	For the year ended 31 December	
	2017	2016
Belarus (OJSC Gazprom transgaz Belarus and the Yamal – Europe trunk gas pipeline) including gas in transit	61.2 42.2	60.3 41.7

Gas transportation services in foreign countries are provided to the Group by a number of entities in which Gazprom has a non-controlling interest. Nord Stream and Blue Stream, offshore cross-border pipeline systems constructed with the Group's involvement, secure gas supplies to consumers in Northwest and Central Europe, as well as in Turkey. The key drivers of gas pipeline capacity utilisation include demand from European consumers and regulatory restrictions by supervisory authorities on access to pipeline capacity for transit supplies.

Offshore cross-border pipeline systems constructed with the Group's involvement secured gas supplies to consumers in Northwest and Central Europe (Nord Stream, 51.0 bcm of gas in 2017, up 16.0% year-on-year) and Turkey (Blue Stream, 15.9 bcm in 2017, up 21% year-on-year). The increase in gas volumes transported through Nord Stream in 2017 followed the resolution of issues related to the use of the OPAL pipeline capacity for transit supplies while gas volumes carried via Blue Stream increased in response to higher demand from Turkish consumers.

#### Major capex projects

Most capex was spent to finance the construction of the Power of Siberia and the Ukhta – Torzhok 2 trunk gas pipelines, and the UGSS expansion project for the Gryazovets to Ust-Luga section in the North-West region.

A total 640.2 km of new trunk gas pipelines and connections were commissioned in Russia in 2017.

Gazprom made investments in upgrades to its gas transportation infrastructure, commissioning in 2017 three gas pumping units with a total capacity of 40 MW, 100.2 km of linear section trunk pipelines and connections, and six gas distribution stations.

#### Events in the reporting year

In April and June 2017, financing agreements were signed with ENGIE, OMV, Shell, Uniper, and Wintershall for the Nord Stream 2 offshore pipeline project. The European energy companies committed to provide long-term financing for 50% of the total cost of the project.

Construction of the TurkStream gas pipeline commenced in May 2017.

#### Outlook for the Transportation segment

Expansion of PJSC Gazprom's gas transportation capacity is done in tandem and close coordination with the development of gas production and storage, and also takes into account the degree of readiness to receive gas shown by new consumers, as well as export projects.

Timelines for commissioning new and upgrading existing gas transportation facilities are scheduled with a long-term perspective and depend on their effective utilisation periods and the need to maintain optimal throughput of the existing GTS. This approach helps prevent introducing excess capacity, ensure efficient and flexible use of PJSC Gazprom's investments, and optimise gas transportation costs.

Apart from greenfield gas transmission projects, Gazprom also upgrades and retrofits its existing gas transportation facilities.

Gazprom is decommissioning excess capacity of the Central Gas Transmission Corridor to improve operational efficiency of its gas transmission capacity taking into account the diversification of its

gas export routes. Excess capacity is slated for retirement taking into account the need to have required back-up capacity available to maintain the reliability of the transportation network in the future.

To ensure gas supplies to the domestic market and meet its obligations under export contracts, PJSC Gazprom is implementing a number of gas transmission projects.

The Bovanenkovo – Ukhta and Ukhta – Torzhok trunk gas pipeline systems are intended to carry gas from the Yamal fields.

To diversify export routes for Russian pipeline gas supplies to PJSC Gazprom's traditional European market, Gazprom continued to implement its Nord Stream 2 project. The new pipeline, to be laid from Russia to Germany across the Baltic Sea will comprise two offshore strings with a capacity of 27.5 bcm each. Western and Central European countries are the project's target markets. Pipeline capacity additions are planned along the Gryazovets – Volkhov – Russian Baltic Sea Coast route to support gas supplies via Nord Stream 2. The Nord Stream 2 project is proceeding on schedule, with both strings expected to be commissioned in Q4 2019.

In the reporting year, PJSC Gazprom continued to focus on the TurkStream project to supply Russia's natural gas across the Black Sea to Turkey, and further to its neighbouring countries.

As part of its consistent efforts to ensure geographic diversification of routes for Russian gas exports, Gazprom pays particular attention to pipeline gas supplies from Russia to China.

Gazprom has been constructing the Power of Siberia trunk gas pipeline project since 2014 to transmit gas from Yakutsk and Irkutsk gas production hubs to consumers in Russia's Far East and in China. According to a schedule set out in the EPC-contract, construction of an underwater crossing of the Amur River commenced from the Chinese side in September 2017, and from the Russian side in April 2017. Construction of the pipeline's tunnel crossing line 1 was completed in November 2017.

The project is pursued to meet Russia's obligations under the 2014 agreement for Russian pipeline gas supplies to China via the eastern route. The sales and purchase agreement provides for exports of 38 bcm of gas per year over 30 years, and came into full force in May 2015. In July 2017, PJSC Gazprom and China National Petroleum Corporation (CNPC) signed a supplementary agreement to the contract, providing for the delivery of natural gas supplies into China's gas transportation system to commence before or on 20 December 2019.

In May 2015, PJSC Gazprom and CNPC signed the Heads of Agreement for pipeline gas supplies to China via the Power of Siberia 2 gas pipeline.

In addition, PJSC Gazprom and CNPC signed in December 2017 the Heads of Agreement for natural gas supplies from Russia's Far East to China. The document outlines the basic parameters of future supplies, namely the volumes, the term of the contract, the starting date of supplies, the ramp-up period, and the cross-border point location.

## Underground Gas Storage

The table below shows information on the assets and capital expenditures in the Gas storage segment:

	As at 31 December	
	2017	2016
Assets, RUB million	347,929	393,482
Share in the Group's total assets, %	2.0	2.3

  

	For the year ended 31 December	
	2017	2016
Capital expenditures, RUB million	37,694	35,542
Share in the Group's total capital expenditures, %	2.5	2.6

A network of underground gas storage facilities (UGSFs) is an integral part of the country's Unified Gas Supply System (UGSS). Storage facilities offset any fluctuations in demand, whether seasonal, weekly or daily, accounting for 20% to 40% of Gazprom's total supplies during the heating season. Peak and base load gas storage facilities improve reliability of the UGSS infrastructure, and optimise technical parameters and capital intensity of gas transportation systems.

In Russia, Gazprom operates 22 UGSFs in 26 geological structures: 17 facilities in depleted gas deposits, eight in aquifers, and one in a salt cavern. The storage facilities are located in 19 regions. Their operation is supported by 19 compressor stations with an aggregate capacity of 948.5 MW, and the operating well stock of 2,694 units.

As at 31 December 2017, the Group's UGSFs in Russia had an aggregate total gas storage capacity of 74.9 bcm. During 2017, withdrawal and injection amounts for Russian UGSFs totalled 45.5 bcm and 44.2 bcm of gas, respectively.

The maximum aggregate daily deliverability was registered on 8 February 2017 at 590.5 mmcm. By the start of the 2017/2018 withdrawal season, the potential maximum daily deliverability was increased to 805.3 mmcm of gas, an increase of 4 mmcm from the previous year. By the 2017/2018 withdrawal season, operating gas reserves in Russian UGSFs increased by 0.086 bcm from the previous season to 72.2 bcm.

The improved performance in 2017 was driven by a recovery in target well productivity, and by renovations of the existing Punginskoye, Sovkhoznoye, Severo-Stavropolskoye, and Kaliningradskoye UGSFs.

As a means to build strategic natural gas inventories, underground gas storage facilities are indispensable for addressing transit risks inherent to exports.

In the FSU countries, Gazprom operates UGSFs in Belarus (Pribugskoye, Osipovichskoye, and Mozyrskoye), and Armenia (Abovianskaya underground gas storage station), and also has access to Inčukalns UGSF's capacity in Latvia. As at 31 December 2017, the operating gas reserves in FSU-based UGSFs totalled 3.0 bcm, with a daily deliverability of 55.6 mmcm.

To secure reliable and flexible gas supplies, Gazprom's export projects make extensive use of gas storage facilities located abroad: in Austria (Haidach), Germany (Jemgum, Rehden, Katarina, and Etzel), Serbia (Banatski Dvor), the Netherlands (Bergermeer), and the Czech Republic (Dambořice).

In 2017, Gazprom's own gas storage capacity in far abroad European countries totalled 5.03 bcm, with an aggregate daily deliverability of 83.3 mmcm of gas. In 2017, a total of 8.6 bcm of gas were pumped into UGSFs in far abroad European countries, with a total gas withdrawal of 4.3 bcm.

The Group's gas storage facilities are marketed mostly through a standalone business in the European market, operated by astora GmbH & Co. KG, part of Gazprom Germania Group. As at 31 December 2017, astora GmbH & Co. KG leased out 0.8 bcm of working gas capacity at Jemgum and Haidach UGSFs to companies outside Gazprom Group, which makes up ca. 12% of available gas storage capacity.



### Major capex projects

The bulk of capital expenditures for underground gas storage in Russia was used towards salt cavern construction at the Kaliningradskoye and Volgogradskoye UGSFs, renovation of the Sovkhoznoye UGSF and the existing capacity to transmit gas from the Severo-Stavropolskoye UGSFs, as well as production drilling at underground gas storage facilities. New capacity was commissioned at the Punginskoye, Kaliningradskoye, and Sovkhoznoye UGSFs in 2017, increasing the aggregate total gas storage capacity by 1.3 bcm, with a 32.0 MW compressor station launched at the Punginskoye UGSF, 24 wells connected, and renovation of gas production facilities and the gas treatment unit completed at the Krasnodarskoye UGSF.

### Outlook for the Gas storage segment

Gazprom's forward-looking plans provide for further expansion of its UGSF network with a focus on the following areas:

- Sustaining the capacity levels achieved for the UGSF network through renovation and replacement of worn-out and obsolete fixed assets, as well as de-bottlenecking of UGSFs and the GTS
- Improving the flexibility of Russia's UGSF system by constructing small, peak load balancing gas storage facilities in salt caverns to maintain deliverability rates during increased gas withdrawal periods through to 1 February (the date of the calculated indicator of the maximum seasonal lowering of the ambient air temperature)
- Providing underground gas storage capacity to the regions where such capacity is in short supply (new UGSFs are planned for construction in the Northwestern, Siberian, and Far Eastern Federal Districts of the Russian Federation)

A total of 47 UGSF capex projects are planned in Russia (including well workovers and drilling, expansion and upgrades of the GTS connections), of which 36 projects aim to sustain the achieved capacity through upgrades and retrofits, four to expand existing capacity, and seven to construct new gas storage facilities (peak load balancing facilities and facilities in the regions with a shortage of storage capacity).

Plans until 2030 include commissioning total gas storage capacity of 4.77 bcm and 11 compressor plants with an aggregate capacity of 228 MW, and connecting 130 wells.

A major focus of the Group's investment programmes is on expanding its underground gas storage system to ensure uninterrupted gas supply to European consumers during autumn/winter peak demand periods and during repairs at GTS, as well to boost gas sales from foreign-based underground gas storage facilities. In terms of international underground gas storage expansion, the challenge is to expand Gazprom Group's UGSFs in foreign countries to an aggregate working gas capacity equal to at least 5% of annual export volumes by 2030, with a focus on constructing own storage capacity. Gazprom is planning to further expand aggregate working gas capacity by adding new capacity to the Katarina UGSF in Germany and Dambořice UGSF in the Czech Republic based on their respective expansion schedules.

## Distribution of Gas

The table below shows information on the assets and capital expenditures in the Distribution of gas segment:

	As at 31 December	
	2017	2016
Assets, RUB million	1,669,202	1,557,089
Share in the Group's total assets, %	9.5	9.3

	For the year ended 31 December	
	2017	2016
Capital expenditures, RUB million	51,675	41,785
Share in the Group's total capital expenditures, %	3.4	3.1

The table below shows Gazprom Group's natural gas sales volumes by geographic segment:

(bcm)	For the year ended 31 December		Change, %
	2017	2016	
Russia	229.9	214.9	7.0
FSU countries <sup>(1)</sup>	35.0	33.2	5.4
Europe and other countries <sup>(1)</sup>	242.0	228.3	6.0
<b>Total</b>	<b>506.9</b>	<b>476.4</b>	<b>6.4</b>

Note:

- <sup>(1)</sup> Sales to FSU countries, and to Europe and other countries include both gas exports from the Russian Federation, and sales of gas purchased by the Group outside Russia.

In 2017, Gazprom Group sold 242.0 bcm of natural gas to Europe and other countries, up by 13.7 bcm, or 6.0%, year-on-year. Net sales revenue (net of excise tax and customs duties) was RUB 2,221.2 bn, up 3.8% year-on-year.

The natural gas sold to Europe and other countries in 2017 accounted for 48% of Gazprom Group's total gas sales (48% in 2016) and 66% of total revenue from gas sales (65% in 2016).

PJSC Gazprom is a major supplier of natural gas to the European market.

PJSC Gazprom's gas supplies in 2017 to European far abroad countries under the contracts with LLC Gazprom export and direct contracts with GAZPROM Schweiz AG totalled 194.4 bcm, up by 15.1 bcm, or 8.4%, year-on-year. The share of PJSC Gazprom's gas sales under contracts with LLC Gazprom export and direct contracts with GAZPROM Schweiz AG in the total gas consumption in European far abroad countries was 34.2% for 2017.

The Group's exports are diversified by markets, the largest consumers being Germany, Turkey, and Italy.

The significant increase in supplies was mainly driven by higher natural gas consumption in Europe (above all, in electricity generation), with domestic gas production in the region growing only marginally year-on-year. The increase was also supported by PJSC Gazprom's competitive gas prices.

Gas withdrawals demonstrated a significant growth in Germany and Turkey, while in Italy gas withdrawals dropped due to increased alternative supplies.

LNG sales from Gazprom Group's trading portfolio totalled 3.34 mm tonnes, or 4.46 bcm, in 2017. Another country, Spain, was added to the list of destination markets for LNG supplies out of the Group's trading portfolio.

Corporates in Asia Pacific, in particular in Japan (36%) and China (19%), were the key buyers of LNG from Gazprom Group's trading portfolio in 2017, just like in previous years.

Gazprom is the largest natural gas supplier on the Russian market. In 2017, gas consumption in Russia totalled 468.0 bcm, up by 2.5% year-on-year. This growth was mostly driven by lower temperatures in 2H 2017.

In 2017, Gazprom Group sold 229.9 bcm of gas to consumers in the Russian Federation, with net sales revenue (excluding VAT) at RUB 875.7 bn, up by 6.8% year-on-year. Natural gas sold to Russian consumers in 2017 accounted for 45% (45% in 2016) of Gazprom Group's total gas sales and ca. 26% of total revenue from gas sales (25% in 2016).

Major consumers of natural gas in Russia include electricity and heat generating companies, households, oil industry, utilities, and steel-makers.

Gazprom Group covers a significant portion of natural gas demand in FSU countries.

In 2017, Gazprom Group sold 35.0 bcm of gas to the FSU countries, with net sales revenue (net of customs duties) at RUB 292.8 bn, down by 5.4% year-on-year.

Natural gas sold to the FSU countries in 2017 and 2016 accounted for 7% of Gazprom Group's total gas sales, and 9% of gas sales revenue.

The increase in gas supplies to FSU countries in 2017 resulted from higher demand and gas withdrawals in Belarus and the Baltic states, and the resumption of gas supplies to Azerbaijan.

#### Domestic natural gas prices

The table below shows the average prices of natural gas sold by Gazprom Group in the domestic market:

	<b>For the year ended 31 December</b>	
	<b>2017</b>	<b>2016</b>
	<b>(net of VAT)</b>	
RUB per mcm	3,808.3	3,815.5

In accordance with applicable Russian laws, end consumers buy gas at regulated prices which are differentiated between consumer groups (households vs industrial consumers), as well as by price zone, based on the relative distance from the gas production region to the consumer. In 2017, wholesale gas prices for subsequent resale to household consumers were 5% lower than wholesale gas prices for industrial consumers.

In Russia, gas is sold and purchased using two different pricing approaches, which results in the existence of two gas sales sectors – with prices fixed by the Government or unregulated prices.

Gas produced by PJSC Gazprom subsidiaries is sold mostly at prices fixed by the Government. In accordance with applicable Russian laws, wholesale prices of gas produced by PJSC Gazprom and its associates are subject to regulation. These prices are differentiated between consumer groups (prices of gas purchased for resale to households vs industrial consumers), as well as by price zone, based on the relative distance from the gas production region to the consumer.

The Forecast of Russia's Socio-economic Development drafted by the Russian Ministry of Economic Development and approved by the Government in September 2017 assumes increases in domestic regulated wholesale gas prices by 3.4% from 1 July 2018, by 3.1% from 1 July 2019, and by 3.0% from 1 July 2020.

The table below shows changes in the average regulated wholesale gas prices for industrial and household consumers as per the Forecast of the Ministry of Economic Development of the Russian Federation between 2018 and 2020, annual average increase vs the previous year:

	<b>2018</b>	<b>2019</b>	<b>2020</b>
Change in the average regulated wholesale prices for all Russian consumer groups, %	3.4	3.1	3.0
Change in the average regulated wholesale prices for all consumers excluding households, %	3.4	3.1	3.0
Change in the average regulated wholesale prices for households, %	3.4	3.1	3.0

To promote market-driven pricing principles, PJSC Gazprom is actively in exchange-based gas trade at the Saint Petersburg International Mercantile Exchange (SPIMEX). In 2017,

PJSC Gazprom sold 17.5 bcm of gas through the exchange-based trading channel, the maximum allowed it is allowed to sell in this channel.

#### Natural gas prices in FSU, Europe and other countries

The table below shows the average prices of natural gas sold by Gazprom Group to FSU, Europe and other countries:

	<b>For the year ended 31 December</b>	
	<b>2017</b>	<b>2016</b>
	<b>(including excise tax and customs duties)</b>	
Natural gas sales to Europe and other countries <sup>(1)</sup>		
USD per mcm <sup>(2)</sup>	200.2	176.0
RUB per mcm	11,670.5	11,763.3
Natural gas sales to FSU countries <sup>(1)</sup>		
USD per mcm <sup>(2)</sup>	158.4	153.6
RUB per mcm	9,237.0	10,263.1

Notes:

- (1) (1) VAT is not charged on sales to Europe and other countries, as well as to FSU countries.  
(2) Calculated based on the year-average RUB/USD exchange rate.

#### Major capex projects

In 2017, Gazprom Group continued the construction of an LNG production, storage, and shipping complex with an annual production capacity of 1.5 mm tonnes near the Portovaya compressor station in the Leningrad Region. LNG will be marketed as an off-mains solution and as an NGV and bunker fuel, or supplied as necessary to an LNG regasification terminal in the Kaliningrad Region.

The Group's investments in gas infrastructure expansion in Russia account for the bulk of capital expenditures for the Distribution of gas segment. As part of the Programme for Expansion of Gas Infrastructure in Russian Regions, the Group completed the construction of 121 inter-community gas pipelines in 2017, spanning a total of 1,848 km across 32 Russian regions and supplying gas to 207 locations. 51.8 thousand households and 173 boiler houses, with a total annual gas consumption of 0.4 bcm, will be ready to receive gas as soon as regional administrations fully meet their commitments.

#### Events in the reporting year

In 2017, the starting date was finalised for natural gas supplies to China via the eastern route: in July 2017, PJSC Gazprom and China National Petroleum Corporation (CNPC) signed a supplementary agreement to the the gas sales and purchase agreement, providing for the delivery of the first gas via the eastern route into China's gas transmission system before or on 20 December 2019.

PJSC Gazprom and Shell continued their joint Baltic LNG project: in June 2017, the two companies signed the Joint Study Framework Agreement for the Baltic LNG project and the Heads of Agreement to set up a joint venture which will construct and operate the planned LNG plant in the Leningrad Region.

Also during the year, positive opinions were obtained from Russia's Main Directorate of State Expert Review (GlavgosExpertiza) for the Sakhalin-2 T3 project, including for design documents developed to Russian standards for the expansion of the project's gas transportation system and LNG plant, and construction of a LNG loading berth.

## Refining

The table below shows information on the assets and capital expenditures in the Refining segment:

	As at 31 December	
	2017	2016
Assets, RUB million	1,715,485	1,361,161
Share in the Group's total assets, %	9.7	8.1
	<b>For the year ended 31 December</b>	
	<b>2017</b>	<b>2016</b>
Capital expenditures, RUB million	225,240	193,243
Share in the Group's total capital expenditures, %	15.0	14.2

### Processing of hydrocarbons and production of refined products

The table below shows the volumes of Gazprom Group's hydrocarbon processing:

	For the year ended 31 December	
	2017 <sup>(1)</sup>	2016 <sup>(1)</sup>
Natural and associated gas, bcm	30.8	31.0
Liquid hydrocarbon feedstocks, mm tonnes	64.1	65.9

Note:

<sup>(1)</sup> Excluding tolling arrangements.

In 2017, Gazprom Group (including its equity share of the APG processing volumes of LLC Yuzhno-Priobskiy GPZ, classified as joint operations) processed 30.8 bcm of natural and associated gas (almost flat year-on-year), excluding tolling arrangements. Processing of liquid hydrocarbon feedstocks (crude oil, gas condensate, and fuel oil) was down by 2.7% to 64.1 mm tonnes mainly due to lower processing volumes at Gazprom Neft Group's facilities due to renovation projects and scheduled overhauls.

The table below shows production volumes of major refined products of Gazprom Group:

	For the year ended 31 December			
	2017 <sup>(1)</sup>		2016 <sup>(1)</sup>	
	Total	including abroad	Total	including abroad
Dry gas, bcm	23.6	–	24.0	–
Liquefied petroleum gases, mm tonnes	3.5	0.1	3.5	0.1
including Gazprom Neft Group	0.7	0.1	0.9	0.1
Natural gas liquids, mm tonnes	1.3	–	1.8	–
Stable gas condensate and crude oil, mm tonnes	8.7	–	8.2	–
Oil products, mm tonnes	49.4	3.4	50.2	3.1
including Gazprom Neft Group	38.4	3.4	38.8	3.1
including Gazprom neftekhim Salavat Group	5.2	–	5.5	–
Helium, mmcm	5.1	–	5.1	–
Sulphur, mm tonnes	5.0	0.0 <sup>(2)</sup>	4.9	0.0 <sup>(2)</sup>
including Gazprom Neft Group	0.1	0.0 <sup>(2)</sup>	0.2	0.0 <sup>(2)</sup>

Notes:

<sup>(1)</sup> Excluding tolling arrangements.

<sup>(2)</sup> Less than 0.05.

### Sales of refined products

The table below shows sales of refined and petrochemical products by Gazprom Group:

(mm tonnes)	For the year ended 31 December		Change, %
	2017 <sup>(1), (2)</sup>	2016 <sup>(1), (2)</sup>	
Russia	41.0	41.2	-0.5
including Gazprom Neft Group	28.0	27.8	0.7
FSU countries	3.6	3.6	-
including Gazprom Neft Group	2.5	2.5	-
Europe and other countries	21.5	23.3	-7.7
including Gazprom Neft Group	13.0	14.4	-9.7
<b>Total</b>	<b>66.1</b>	<b>68.1</b>	<b>-2.9</b>

Notes:

(1) Excluding intra-group sales. Sales of own products and products purchased from third parties.

(2) Excluding helium.

In 2017, Gazprom Group's sales of oil and gas refined products were 66.1 mm tonnes, down by 2.0 mm tons, or 2.9% year-on-year.

Total sales of refined oil and gas products by Gazprom Group declined in 2017 due to a lower output of refined products resulting from scheduled overhauls at Gazprom Neft Group's refineries.

### Major capex projects

Gazprom Group's capital expenditures for the Refining segment were directed towards the following projects in 2017:

- projects to enable liquid hydrocarbon transportation from the Nadym-Pur-Taz region: construction of the Urengoy – Surgut gas condensate pipeline (Line 2), and the 107 km – 288 km section; construction of a stabilisation unit for Achimov deposit condensate from the Nadym-Pur-Taz region; construction of the Urengoy – Purpe oil and condensate pipeline, and the Urengoy oil pumping station;
- construction of the Amur GPP;
- renovation of Phase 1 and Phase 2 of the Astrakhan Gas Processing Plant into an integrated operation;
- construction and upgrade of oil refining and petrochemical facilities at Gazprom neftekhim Salavat Group, including the construction of a hydrogen unit with a pressure swing adsorption (PSA) facility; a pentane-hexane fraction isomerisation plant, a catalytic cracking complex, a sulphide and alkaline waste neutralisation unit, a propane-propylene processing unit, and an elemental sulphur production unit;
- construction and upgrades of production facilities at Moscow Refinery (comprehensive upgrade of a catalytic cracking unit, and the construction of Euro+ combined refining unit), and at Omsk Refinery (construction of a primary refining unit).

### Outlook for the Refining segment

To process the projected volumes of liquid hydrocarbons extracted through natural gas production at gas and condensate fields in Western Siberia, Gazprom implementing a number of projects, including a capacity expansion and upgrade project at the Urengoy Condensate Pre-Transportation Preparation Plant to ramp it up to design capacity; construction of Achimov deposit condensate and oil treatment and transport facilities, completion of the construction of uncompleted sections of the Urengoy – Surgut gas condensate pipeline, and upgrades and retrofits of the Surgut Condensate Stabilisation Plant.

PJSC Gazprom continues to implement a project to construct a gas chemical complex near Novy Urengoy, with gases recovered from de-ethanized gas condensate in the Nadym-Pur-Taz region to be used as a key feedstock.

Upgrade of the motor fuel production facilities is planned at the Astrakhan GPP to increase their output while ensuring compliance with Class 5 standards of the Technical Regulations.

Construction commenced in August 2017 for the core production facilities of a gas processing and helium complex of the Amur GPP near Svobodny in the Amur Region, to be supplied via the Power of Siberia gas pipeline with gas from the Yakutia and Irkutsk gas production hubs currently developed by PJSC Gazprom under the Eastern Gas Programme. When online, the Amur Gas Processing Plant will become Russia's No. 1 and the world's No. 2 gas processing facility by production capacity (42 bcm per year), and also the global leader in helium production (up to 60 mmcm per year). The plant will be an essential part of the process chain of natural gas supply to China via the Power of Siberia gas pipeline.

Implementing refinery upgrade programmes and improvements to operational performance remain to be Gazprom Neft Group's strategic priority in the development of its Russian oil refinery business. The company completed Phase 1 of a major refinery upgrade programme, improving the quality of its refined products, with all motor fuels produced by Gazprom Neft Group now meeting Euro 5 standards. The company continues the implementation of its key projects to increase the refining depth and yields for light products. Operational excellence initiatives and projects to reduce environmental footprint have been continued. The target scale of Gazprom Neft Groups's distribution business should ensure marketing of 100% of the oil products produced by own refineries via controlled sales channels to maximise the coverage of the entire value chain in the oil business.

## Power Generation

The table below shows information on the assets and capital expenditures in the Electric and heat energy generation and sales segment:

	<b>As at 31 December</b>	
	<b>2017</b>	<b>2016</b>
Assets, RUB million	868,933	990,120
Share in the Group's total assets, %	4.9	5.9
	<b>For the year ended 31 December</b>	
	<b>2017</b>	<b>2016</b>
Capital expenditures, RUB million	58,110	63,485
Share in the Group's total capital expenditures, %	3.9	4.7

Gazprom Group is Russia's largest owner of generating assets. Power stations operated by Gazprom energoholding Group, in which Gazprom Group's key generating assets (PJSC Mosenergo, PJSC TGC-1, PJSC MIPC, and PJSC WGC-2) are consolidated, account for ca. 16% (ca. 39 GW) of the total installed capacity of Russia's Unified Energy System (UES).

Outside Russia, the Group owns Unit 5 at the Hrazdan TPP through its subsidiary CJSC Gazprom Armenia.

The table below shows information on Gazprom Group's key generating assets:

	<b>As at 31 December 2017</b>	
	<b>Installed electrical capacity, GW</b>	<b>Installed heat capacity, thousand Gcal/h</b>
Gazprom energoholding Group including	38.82	67.81
PJSC Mosenergo	12.87	42.76
PJSC MIPC	–	4.28
PJSC WGC-2	19.00	4.16
PJSC TGC-1	6.95	13.65
LLC TSK Novaya Moskva and LLC TSK Mosenergo	–	2.96
Other generating assets in Russia and abroad	1.38	2.22
<b>Total</b>	<b>40.20</b>	<b>70.03</b>

The table below shows the volumes of Gazprom Group's electricity generation:

(billion kWh)	<b>For the year ended 31 December</b>	
	<b>2017</b>	<b>2016</b>
Gazprom energoholding Group including	150.81	153.83
PJSC Mosenergo	57.87	59.07
PJSC MIPC	–	–
PJSC WGC-2	63.43	67.09
PJSC TGC-1	29.51	27.67
Other generating assets in Russia and abroad	5.74	3.68
<b>Total</b>	<b>156.55</b>	<b>157.51</b>

Note. The table shows power generation, i.e. the amount of power generated by power stations.

The table below shows the volumes of Gazprom Group's heat generation:

(million Gcal)	<b>For the year ended 31 December</b>	
	<b>2017</b>	<b>2016</b>
Gazprom energoholding Group <sup>(1)</sup> including	120.77	123.36
PJSC Mosenergo	79.45	81.83
PJSC MIPC	5.79	6.09
PJSC WGC-2	6.76	6.90
PJSC TGC-1	24.71	24.44
LLC TSK Novaya Moskva and LLC TSK Mosenergo	4.06	4.10
Other generating assets in Russia and abroad	6.57	6.12
<b>Total</b>	<b>127.34</b>	<b>129.48</b>

<sup>(1)</sup> Starting from 2017, heat generation figures include PJSC MIPC's subsidiaries LLC TSK Novaya Moskva and LLC TSK Mosenergo. For data comparability, the figures for 2016 take into account the volumes of these entities.

Note. The table shows heat supply from TPPs, i.e. the amount of heat supplied by a power station to consumers at the asset ownership / interface boundary points.

During 2017, the Group generated 155.46 billion kWh of electricity (in 2016 – 156.73 billion kWh of electricity) and 127.34 million Gcal of heat (in 2016 – 129.48 million Gcal of heat) at its generating assets in Russia. The decline in electricity generation by the Group by 0.8% was due to the load factors of generating assets requested by the UES System Operator and its optimised operation modes. Heat generation decrease by 1.7% year-on-year was due to warmer temperatures during the heating season.

Electricity produced by the Group's Russian generating companies is sold in Russia, with a small portion exported to Norway and Finland.



Outside Russia, Gazprom Group generated 1.09 billion kWh of electricity, up by 39.7% year-on-year (0.78 billion kWh in 2016), mostly due to increased power output from Unit 5 at Hrazdan TPP due to the actual operation of the power system in Armenia and the extension of the repair of the Armenian nuclear power station.

Gazprom Group, acting via Gazprom Marketing & Trading, supplies electricity to end consumers.

#### Major capex projects

Gazprom Group's investment programme is one of the biggest in the Russian power industry. The launch of the Grozny TPP in 2019 will complete the implementation of LLC Gazprom energoholding's ambitious investment programme to build new generating capacity in line with its obligations under capacity supply agreements (CSAs). The CSA investment programme implemented by the Group companies is expected to add 8.9 GW of new capacity in Russia between 2007 and 2019, with total investments under the programme for the same period exceeding RUB 450 bn (inclusive of VAT).

The bulk of this capex was spent in 2017 on the construction of the second start-up complex facilities at the Troitskaya GRES and two new GTU-180 power unit projects at the Grozny TTP, capacity expansion upgrade to the PSU-420 power unit at PJSC WGC-2-operated Cherepovetskaya GRES, and equipment upgrade of Power Unit 9 at CHPP-22 operated by PJSC Mosenergo.

Outside Russia, PJSC Centerenergyholding, part of Gazprom energoholding Group, is constructing through a joint project with NIS (a Serbian subsidiary of Gazprom Neft Group) a power station with an installed capacity of approximately 200 MW in Pančevo, Serbia. The project aims to meet the power and heat needs of Pančevo Refinery, and sell power and heat in the Serbian electricity market and via European energy exchanges. The project is currently in the FEED stage, with custom specifications approved for core equipment. The contract provides for the construction to be completed in 2020.

#### Outlook for the Electric and heat energy generation and sales segment

Power generation sector is a strategic line of business for Gazprom Group. Enhanced presence in the power generation sector facilitates the entire Group's business sustainability over the longer term and provides additional revenue streams. Gazprom Group's Power Generation Strategy was adopted in 2007.

Strategic objectives in the power generation business include:

- optimisation of the generation capacity mix
- business diversification for the Group's generating companies
- diversification of tariff regulation risks
- fuel mix diversification
- operational excellence and cost optimisation.

Gazprom Group is developing its long-term power generation strategy until 2027; this effort includes analyses of the following:

- the results of the implementation of the Group's strategy adopted in 2007
- the Group's operational and capex performance and improvement potential
- opportunities to develop the power generation business.

Gazprom Group's new, long-term power generation strategy is expected to be approved in mid-2018.

## **INNOVATION-DRIVEN DEVELOPMENT**

In its evolution as a global energy company and a reliable energy supplier, Gazprom focuses on research and application of new knowledge and technology, as well as on continuous improvement of its innovation capabilities and acceleration of innovation to address a number of strategic, technological, and economic challenges that such leadership involves.

Gazprom's track record of achievement has been driven to a large extent by R&D carried out for the Group by in-house R&D centres, research organisations in related industries, subdivisions of the Russian Academy of Sciences, and higher education institutions.

PJSC Gazprom's Innovative Development Programme until 2025 was approved by Resolution of PJSC Gazprom's Board of Directors No. 2762 dated 21 June 2016 and is a fundamental instrument for long-term planning and management of innovations, embedded into Gazprom's strategic development planning, and containing nine priority technology targets. Once delivered, the overall potential economic effect from the priority technology targets will exceed RUB 450 bn. The Programme covers the gas, oil, and power generation businesses of Gazprom Group and is an efficient tool for innovation through optimising and concentrating the Group's diverse resources and putting in place such innovative development mechanisms as research and development (R&D) programmes, intellectual property management, joint R&D initiatives and partnerships, training and career enhancement programmes, and innovative project portfolio management.

Technological priorities (key areas of technological development) set by PJSC Gazprom's Innovative Development Programme:

- hydrocarbon field exploration and appraisal, including development of unconventional resources
- brownfield enhancement technologies
- offshore hydrocarbon development technologies
- greenfield development technologies
- efficiency enhancement of trunk gas pipelines, and diversification of gas distribution methods
- enhancement of gas storage
- enhancement of gas and gas condensate processing
- LNG production technologies
- gas marketing and utilisation technologies.

Gazprom's advanced projects for production and transportation of gas and liquid hydrocarbons are unrivalled in terms of technical sophistication. The harsh climatic conditions and geology of field developments in the Yamal Peninsula, northern seas, and Eastern Siberia require the development and use of fundamentally new technologies, equipment, and operating principles to ensure that hydrocarbon production in these regions is viable.

Gazprom has in place an extensive innovation management framework consistently improved by the Group. A new R&D planning framework has been put in place to improve performance of R&D investments and cut project leadtimes.

In the reporting year, PJSC Gazprom also approved and put in place the Corporate Framework for Management of Innovations at Subsidiaries of PJSC Gazprom to promote company-wide principles for managing innovations at PJSC Gazprom's subsidiaries.

Gazprom successfully maintains an intellectual property management framework which is essentially intended to determine company-wide principles governing the creation, legal protection, registration, commercialisation, and monitoring of the use of intellectual property across Gazprom Group, as well as to provide incentive schemes encouraging employees of Gazprom Group companies to create intellectual property.

A strong focus is placed on R&D and pre-investment studies. The Group allocates significant amounts for its annual R&D budgets, and R&D results are applied in its priority projects.

In 2017, RUB 8.2 bn worth of R&D was carried under R&D projects commissioned by Gazprom Group entities (RUB 6.3 bn in 2016).

In 2017, Gazprom implemented over 325 R&D results across its facilities, with an expected economic effect totalling over RUB 310 bn.

## PERSONNEL

Governed by the standards of the International Labour Organisation, Gazprom Group respects the fundamental rights and principles set forth in ILO conventions and recommendations, covering in particular:

- freedom of association and the effective recognition of the right to collective bargaining
- elimination of all forms of forced or compulsory labour
- effective abolition of child labour
- elimination of discrimination in respect of employment and occupation.

Gazprom also adheres to international standards on hours and conditions of work, occupational safety, remuneration for work, social security, and holidays with pay.

As at 31 December 2017, the total headcount of the Group was 469.6 thousand employees (467.4 thousand in 2016). The headcount grew by 2.2 thousand people in 2017 as Gazprom ramped up its production operations.

The table below shows the gender balance of Gazprom Group's workforce:

	<b>As at 31 December 2017</b>
Women	29.3
Men	70.7

The table below shows the age balance of Gazprom Group's workforce:

	<b>As at 31 December 2017</b>
Under 30 years	15.3
30 to 40 years	31.3
40 to 50 years	28.6
50 years and older	24.8

Gazprom has in place a corporate Continuous Vocational Education and Training System designed to upgrade employee skills to meet the ever growing operational and performance requirements and support deployment of new technologies and expansion of the Group's regional footprint. Training is mostly provided in educational organisations of the Group, in training and production centres of Gazprom subsidiaries, and at Russia's leading universities. Focused and consistent succession management is a key priority in talent pool management.

In 2017, 342.9 thousand employees of Gazprom Group were trained under career enhancement and retraining programmes.

The Remuneration Management Policy for Employees of PJSC Gazprom's Entities sets out unified corporate remuneration standards for Gazprom Group's employees. Its purpose is to provide a framework for attracting and retaining people with required skills, and motivate employees to perform as expected.

Current remuneration schemes link fixed salaries and pay rates to qualifications and business skills, and also provide for monthly performance bonuses, premiums and additional allowances for work scope and conditions, as well as ad hoc and annual bonuses.

Gazprom's social policy provides it with a competitive advantage, raises its profile in the employment market, and seeks to attract and retain best talent over the long term.

The key principle that underlies the implementation of PJSC Gazprom's social policy is the use of social partnership mechanism, i.e. a constructive dialogue between employees and employers on the matters related to the regulation of social and labour relations. Gazprom Interregional Trade Union, which is part of the Russian Oil, Gas and Construction Workers' Union, represents the interests of Gazprom Group's employees.

The key aspects of employees' social security are set out in the General Collective Bargaining Agreement of PJSC Gazprom and in the collective bargaining agreements of Gazprom's subsidiaries, and provide for a set of employee social support measures, including social benefits, personal insurance, and healthcare benefits.

## **OCCUPATIONAL SAFETY**

Gazprom puts the health and safety of its employees at the top of its agenda. The Group companies have in place a top-level framework to ensure workplace safety. Gazprom's Unified Occupational Health and Safety Management System was successfully recertified in 2017 to OHSAS 18001:2007 standards.

The key objectives of PJSC Gazprom's Occupational Health, Industrial and Fire Safety Policy are to:

- create safe working conditions and protect the health and safety of employees
- reduce the risks of accidents and incidents at hazardous industrial facilities
- ensure fire safety.

These objectives are achieved through prevention of injuries, occupational diseases, accidents, incidents, fires, and fire outbreaks through:

- hazard identification
- occupational risk assessments and management
- awareness raising among employees and employee representatives, and their involvement in the occupational health and safety management system.

Gazprom also seeks to improve employee safety during off hours.

The Unified Occupational Health and Safety Management System is part of PJSC Gazprom's integrated management system developed and introduced to manage OHS risks and meet PJSC Gazprom's objectives and commitments under its occupational Health, Industrial and Fire Safety Policy. The scope of the Unified Occupational Health and Safety Management System covers PJSC Gazprom, its gas exploration, production, processing, transportation, and underground storage, and energy subsidiaries, as well as subsidiaries supporting the operation of the Russian UGSS, with a total headcount of around 325 thousand employees.

Gazprom Group is compliant with the occupational safety laws of the Russian Federation, Gazprom's internal regulations, and the international standards adopted by Gazprom, including requirements applicable to management systems.

Compliance with PJSC Gazprom's OHS standards and regulations by suppliers and contractors operating at the facilities of PJSC Gazprom and its subsidiaries is an essential requirement of occupational safety. In its activities, Gazprom engages suppliers and contractors who share the principles set out in Gazprom's Occupational Health, Industrial and Fire Safety Policy.

Since 2014, the Unified Occupational Health and Safety Management System has been regularly audited for compliance to OHSAS 18001:2007 by the Russian Register Certification Association (a member of the International Certification Bodies Association – IQNet). The scope of this certification exercise includes PJSC Gazprom and its 26 subsidiaries engaged in gas production, transportation, and underground storage, as well as in gas, gas condensate and oil processing/refining. Gazprom successfully passed a recertification audit in 2017.

Gazprom annually expands the certification scope by including new entities. By the end of 2017, the number of subsidiaries certified to OHSAS 18001:2007 reached 51 entities, with their total headcount over 300 thousand people.

PJSC Gazprom makes consistent efforts to reduce injuries, accidents, and fires. The Group is currently implementing a range of programmes and plans to ensure accident-free operation of hazardous facilities, improve working conditions, and prevent accidents and fires, resulting in steadily declining accident rates.

The 2017 targets for occupational health, industrial and fire safety were mostly met.

The number of injuries was reduced by 41% between 2015 and 2017 – from 103 to 61. During 2017, accidents mainly included traffic accidents and same-level falls. The number of accidents and incidents at hazardous facilities decreased by 53% in 2017 versus 2015 – from 55 to 26.

Gazprom Neft Group benefits from a vertically integrated industrial safety management system compliant with ISO 14001, ISO 9001, and OHSAS 18001 international standards.

Gazprom Neft Group's operations are aligned with the corporate policy on industrial, fire and transport safety, environmental protection, health and workplace safety, and civil protection, and are coordinated at the Corporate Centre level by the Occupational Safety Department. Gazprom Neft Group's occupational health and safety (OHS) management system has been integrated with its operations management system (OMS). The Joint Committee for OMS and OHS was launched at PJSC Gazprom Neft in 2017, comprising members of the company's Management Committee and heads of operations. OHS committees have also been established in individual business segments and PJSC Gazprom Neft's subsidiaries.

At Gazprom energoholding Group and its subsidiaries, occupational health and safety issues are addressed in line with the requirements of Russian laws and applicable statutory regulations. CEOs of generating companies are responsible for compliance with these requirements, while relevant activities are coordinated by Chief Engineers of subsidiaries and branches (power plants).

## **ENVIRONMENTAL PROTECTION**

Gazprom prioritises care for the environment in everything it does – both in major projects and day-to-day tasks. The Group employs technical solutions that keep environmental impact from its operations to a minimum.

PJSC Gazprom also puts care for the environment at the top of its agenda when implementing projects both in Russia and abroad. Sustainable use of natural resources and environmental protection are the core principles that underpin PJSC Gazprom's operations as a socially and environmentally responsible energy company.

Gazprom Group's subsidiaries operating abroad are also committed to minimising their environmental footprint in strict compliance with the local regulations and provisions of PJSC Gazprom's Environmental Policy.

The Environmental Policy is the primary document governing the PJSC Gazprom's environmental activities. It is updated on an ongoing basis to comply with changing legislation and address new environmental challenges. The updated version of the Environmental Policy approved by resolution of the PJSC Gazprom's Management Committee in 2015 reflects key trends in environmental protection, energy efficiency, and greenhouse gas (GHG) reduction. The Environmental Policy sets out additional commitments to environmental safety that Gazprom undertakes in developing hydrocarbon fields on the Russian continental shelf and in the Russian Arctic and in minimising the risks of negative impact on the environment, including on particularly vulnerable natural sites and areas, and features of high conservation value.

The Environmental Management System (EMS) is a key tool to implement PJSC Gazprom's Environmental Policy. PJSC Gazprom's EMS underwent a recertification audit in December 2017, receiving a certificate of compliance with ISO 14001:2015, valid until December 2020.

PJSC Gazprom's EMS covers 34 wholly-owned subsidiaries which are engaged in the core activities of exploration, production, transportation, storage and processing of gas and gas condensate or are managing capital projects.

Corporate Environmental Targets are set within PJSC Gazprom's EMS based on the annually updated list of significant environmental aspects, and environmental activities are grouped into programmes for focused implementation.

Five out of the six set targets set for 2017–2019 were met in 2017:

No.	Corporate Environmental Target	Entities within the EMS scope	Progress against the target (vs the 2014 baseline)
1.	Reduction of methane emissions	All subsidiaries engaged in natural gas transportation	Down 5.03%
2.	Reduction of specific emissions of nitrogen oxides	All subsidiaries engaged in natural gas transportation	Down 4.06%
3.	Reduction of waste and effluent water discharge into surface water bodies	All subsidiaries	Down 18.02%
4.	Reduction of landfill share	All subsidiaries	Down 5.71%
5.	Reduction of above-limit impact charges	All subsidiaries	Up 6.58%
6.	Reduction of specific fuel & energy consumption for own operational needs (at comparable transportation volumes)	All subsidiaries engaged in natural gas transportation	Down 0.62%

Those Gazprom Group companies that are not covered by PJSC Gazprom's EMS also have in place their own effective, business-specific environmental management systems.

The table below shows key metrics for the environmental impact from Gazprom Group's operations in the Russian Federation:

Key metrics	For the year ended 31 December	
	2017	2016
Air pollutant emissions, thousand tonnes	2,795.9	2,868.5
Waste water discharge into surface water bodies, mmcm	3,905.3	3,855.5
Waste generation, thousand tonnes	4,130.3	4,289.8
Area of land disturbed during the year, thousand ha	42.2	27.0
Area of land rehabilitated, thousand ha	19.6	42.5

The Group companies disturbed 42.2 ha of land in 2017, up by 56% year-on-year. During 2017, 87.3 ha of land were contaminated due to pipeline ruptures at Gazprom Group facilities. The land was disturbed as a result of construction, maintenance, and exploration operations. Substantial stretches of land were affected by the construction of the Power of Siberia trunk gas pipeline.

Presented below is information on the environmental protection costs related to Gazprom Group's operations in the Russian Federation:

(RUB bn)

	<b>For the year ended 31 December</b>	
	<b>2017</b>	<b>2016</b>
Total current environmental protection costs	34.47	34.10
Capital expenditures for environmental protection and sustainable use of natural resources	35.58	22.54
Negative environmental impact charges	0.77	0.82
<b>Total</b>	<b>70.82</b>	<b>57.46</b>

In 2017, Gazprom Group's total environmental protection costs increased by 23%, driven mostly by higher capital expenditures for environmental protection and sustainable use of natural resources.

Gazprom Group's capital expenditures for environmental protection and sustainable use of natural resources were up 58% in 2017, and spent under Gazprom's major capex construction projects.

The Group paid RUB 11.41 mm of fines in 2017, including RUB 3.42 mm paid for breaches identified by audits in previous years. A total of RUB 91.13 mm were paid by the Group in compensation for environmental damage including for previous years.

#### *Corporate Climate Policy*

The implementation of PJSC Gazprom's programmes for expansion of regional gas infrastructure and promotion of transportation conversion to natural gas contributes to lower national GHG emissions and decarbonisation of natural gas importing countries.

Taking into account the Plan for Ratification of the Paris Climate Agreement approved by the Government of the Russian Federation, PJSC Gazprom assessed the potential for cutting emissions by the Group's key business segments as part of developing a roadmap for corporate GHG reduction, which helped PJSC Gazprom decide on further actions to reduce its carbon footprint.

PJSC Gazprom uses secondary, alternative, and renewable sources of energy (subject to their viability) to generate energy for own operational needs and for marketing to external customers to reduce GHG emissions.

Independent auditors confirmed that PJSC Gazprom employs a highly mature corporate system for GHG monitoring, reporting, and management, which is compliant with the requirements of international GHG reporting standards and provides all stakeholders with unbiased information on GHG emissions.

PJSC Gazprom was for the sixth time ranked as Russia's best energy sector company in the climate change list of the Carbon Disclosure Project (CDP).

In 2017, GHG emissions from Gazprom Group's facilities totalled 233.9 mm tonnes of CO<sub>2</sub> equivalent, up 2.5% year-on-year. The growth was due to increased production across all production operations segments and a higher number of subsidiaries covered by the reporting.

In 2017, major steps were taken to enhance data objectivity for assessments of the carbon footprint of the Russian natural gas exports to far abroad countries. Germany's Federal Environment Agency (UBA) approved the carbon footprint profile submitted by PJSC Gazprom for Russian supplies of natural gas to Central Europe (which average 12.2 kg of CO<sub>2</sub> equivalent / GJ, and 9.3 kg of CO<sub>2</sub> equivalent / GJ for supplies via Nord Stream), which will improve the accuracy of data inputs used for regulation of the energy sector and development of forecasts for Germany's low-carbon development.

## **MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION**

The official Russian Ruble (“RUB”) to US Dollar foreign exchange rates as determined by the Central Bank of the Russian Federation were as follows:

- as of December 31, 2017 – 57.6002;
- as of December 31, 2016 – 60.6569.

The official RUB to Euro foreign exchange rates as determined by the Central Bank of the Russian Federation were as follows:

- as of December 31, 2017 – 68.8668;
- as of December 31, 2016 – 63.8111.

The average exchange rates of RUB for the year ended December 31, 2017 and for the year ended December 31, 2016 were:

- to US Dollar – 58.3529 and 67.0349, respectively;
- to Euro – 65.9014 and 74.2310, respectively.



## Results of Operation

(RUB million)	Year ended December 31,	
	2017	2016
Sales	6,546,143	6,111,051
Net (loss) gain from trading activity	(16,352)	3,382
Operating expenses	(5,714,090)	(5,244,983)
Change in impairment and other provisions	<u>54,922</u>	<u>(143,870)</u>
<b>Operating profit</b>	<b>870,623</b>	<b>725,580</b>
Finance income	426,705	1,018,997
Finance expense	(407,044)	(543,370)
Share of net income of associates and joint ventures	126,940	82,872
Gain on disposal of available-for-sale financial assets	<u>782</u>	<u>1,059</u>
<b>Profit before profit tax</b>	<b>1,018,006</b>	<b>1,285,138</b>
Current profit tax expense	(241,817)	(218,113)
Deferred profit tax expense	<u>(9,310)</u>	<u>(69,921)</u>
Profit tax	(251,127)	(288,034)
<b>Profit for the year</b>	<b>766,879</b>	<b>997,104</b>
<b>Other comprehensive income (loss):</b>		
Items that will not be reclassified to profit or loss:		
Remeasurements of post-employment benefit obligations	<u>(5,064)</u>	<u>33,118</u>
<b>Total items that will not be reclassified to profit or loss</b>	<b>(5,064)</b>	<b>33,118</b>
Items that will be reclassified subsequently to profit or loss:		
(Loss) gain arising from change in fair value of available-for-sale financial assets, net of tax	(30,404)	62,133
Share of other comprehensive income (loss) of associates and joint ventures	2,967	(6,397)
Translation differences	23,290	(297,703)
Gain from cash flow hedges, net of tax	<u>13,601</u>	<u>49,196</u>
<b>Total items that may be reclassified subsequently to profit or loss</b>	<b>9,454</b>	<b>(192,771)</b>
<b>Other comprehensive income (loss) for the year, net of tax</b>	<b>4,390</b>	<b>(159,653)</b>
<b>Total comprehensive income for the year</b>	<b>771,269</b>	<b>837,451</b>
<b>Profit for the year attributable to:</b>		
Owners of PJSC Gazprom	714,302	951,637
Non-controlling interest	<u>52,577</u>	<u>45,467</u>
	<b>766,879</b>	<b>997,104</b>
<b>Total comprehensive income for the year attributable to:</b>		
Owners of PJSC Gazprom	710,840	806,903
Non-controlling interest	<u>60,429</u>	<u>30,548</u>
	<b>771,269</b>	<b>837,451</b>

## Sales

The following table sets out volumes and realized prices:

(RUB million unless indicated otherwise)	<b>Year ended</b>	
	<b>December 31,</b>	<b>2016</b>
	<b>2017</b>	<b>2016</b>
<b>Sales of gas</b>		
<i>Europe and Other countries</i>		
Gross sales <sup>(1)</sup>	2,823,939	2,685,551
Customs duties	(550,849)	(506,266)
Excise tax	(51,873)	(39,258)
Net sales	2,221,217	2,140,027
Volumes in bcm	242.0	228.3
Average price, US Dollar per mcm (including excise tax and customs duties) <sup>(2)</sup>	200.2	176.0
Average price, RUB per mcm (including excise tax and customs duties)	11,670.5	11,763.3
<i>Former Soviet Union countries</i>		
Gross sales <sup>(1)</sup>	323,037	340,437
Customs duties	(30,260)	(30,793)
Net sales	292,777	309,644
Volumes in bcm	35.0	33.2
Average price, US Dollar per mcm (including customs duties) <sup>(2)</sup>	158.4	153.6
Average price, RUB per mcm (including customs duties)	9,237.0	10,263.1
<i>Russian Federation</i>		
Gross sales (net of VAT)	875,685	819,924
Net sales	875,685	819,924
Volumes in bcm	229.9	214.9
Average price, RUB per mcm (net of VAT)	3,808.3	3,815.5
<i>Total sales of gas</i>		
Gross sales (net of VAT)	4,022,661	3,845,912
Customs duties	(581,109)	(537,059)
Excise tax	(51,873)	(39,258)
Retroactive gas price adjustments	(49,092)	33,175
Net sales	3,340,587	3,302,770
Volumes in bcm	506.9	476.4
Net sales of refined products (net of excise tax, VAT and customs duties)	1,687,090	1,497,562
Net sales of crude oil and gas condensate (net of VAT and customs duties)	539,958	411,958
Electric and heat energy net sales (net of VAT)	503,819	481,716
Gas transportation net sales (net of VAT)	235,061	198,971
Other revenues (net of VAT)	<u>239,628</u>	<u>218,074</u>
<b>Total sales (net of excise tax, VAT and customs duties)</b>	<b><u>6,546,143</u></b>	<b><u>6,111,051</u></b>

Notes:

<sup>(1)</sup> VAT is not charged on sales to Europe and Other countries as well as Former Soviet Union countries.

<sup>(2)</sup> Calculated on the basis of average exchange rate between RUB and US Dollar.

Total sales (net of excise tax, VAT and customs duties) increased by RUB 435,092 million, or 7%, to RUB 6,546,143 million for the year ended December 31, 2017 compared to the prior year. The increase in sales was mainly driven by an increase in sales of refined products and crude oil.

Net sales of gas accounted for 51% of total net sales for the year ended December 31, 2017 (54% for the prior year).

Net sales of gas increased by RUB 37,817 million, or 1%, from RUB 3,302,770 million for the year ended December 31, 2016 to RUB 3,340,587 million for the year ended December 31, 2017.

Net sales of gas to Europe and Other countries increased by RUB 81,190 million, or 4%, to RUB 2,221,217 million for the year ended December 31, 2017 compared to the prior year. The change was driven by the increase in volumes of gas sold by 6% that was partially compensated by the 1% decrease in average Russian Ruble prices (including excise tax and customs duties) for the year ended December 31, 2017 compared to the prior year. At the same time the average US Dollar prices increased by 14% compared to the prior year.

Net sales of gas to Former Soviet Union countries decreased by RUB 16,867 million, or 5%, to RUB 292,777 million for the year ended December 31, 2017 compared to the prior year. The change was due to the decrease in average Russian Ruble prices (including customs duties) by 10% that was partially compensated by the increase in volumes of gas sold by 5% for the year ended December 31, 2017.

Net sales of gas in the Russian Federation increased by RUB 55,761 million, or 7%, to RUB 875,685 million for the year ended December 31, 2017 compared to the prior year. This change is mainly explained by the 7% increase in volumes of gas sold.

Net sales of refined products (net of excise tax, VAT and customs duties) increased by RUB 189,528 million, or 13%, to RUB 1,687,090 million for the year ended December 31, 2017 compared to the prior year. The increase in sales of refined products was due to an increase in average prices.

Net sales of crude oil and gas condensate (net of VAT and customs duties) increased by RUB 128,000 million, or 31%, to RUB 539,958 million for the year ended December 31, 2017 compared to the prior year. The increase in sales of crude oil was mainly due to an increase in volumes of crude oil sold by Gazprom Neft Group to customers in Europe and Other countries, which was due to crude oil production growth at Novoport, East-Messoyakhskoye and Prirazlomnoye fields and reduction of crude oil delivery to refineries and also due to an increase in average prices in all geographic segments.

## Operating expenses

Operating expenses increased by RUB 469,107 million, or 9% for the year ended December 31, 2017 to RUB 5,714,090 million compared to RUB 5,244,983 million for the prior year. Operating expenses as a percentage of sales increased from 86% for the year ended December 31, 2016 to 87% for the year ended December 31, 2017. The table below presents a breakdown of operating expenses in each period:

(RUB million)	Year ended December 31,	
	2017	2016
Taxes other than on income	1,246,059	900,397
Purchased gas and oil	1,236,201	1,157,585
Staff costs	682,060	641,036
Depreciation	613,160	571,564
Transit of gas, oil and refined products	593,327	610,275
Materials	261,642	288,497
Cost of goods for resale, including refined products	207,689	185,441
Repairs and maintenance	154,785	147,608
Electricity and heating expenses	109,485	98,992
Rental expenses	37,723	30,152
Social expenses	34,461	35,516
Insurance expenses	30,491	29,967
Transportation services	27,253	28,923
Processing services	16,261	15,568
Research and development expenses	16,175	28,990
Foreign exchange rate differences on operating items	(14,487)	52,880
Derivatives (gain) loss	(18,344)	9,863
Other	610,787	414,638
	<b>5,844,728</b>	<b>5,247,892</b>
Change in finished goods, work in progress and other effects	(130,638)	(2,909)
<b>Total operating expenses</b>	<b>5,714,090</b>	<b>5,244,983</b>

### *Taxes other than on income*

Taxes other than on income consist of:

(RUB million)	Year ended December 31,	
	2017	2016
Mineral extraction tax (MET)	915,228	613,662
Excise tax	162,140	144,648
Property tax	154,639	127,053
Other taxes	14,052	15,034
<b>Taxes other than on income</b>	<b>1,246,059</b>	<b>900,397</b>

Mineral extraction tax increased by RUB 301,566 million or 49% to RUB 915,228 million for the year ended December 31, 2017 compared to RUB 613,662 million for the prior year, mainly as a result of changes in the elements of the natural gas and crude oil MET formulas introduced with effect from January 1, 2017.

Property tax increased by RUB 27,586 million, or 22%, to RUB 154,639 million for the year ended December 31, 2017 compared to RUB 127,053 million for the prior year. The change was mainly due to the revaluation of fixed assets as of December 31, 2016 used for the purposes of calculating the tax base for property tax as well as an increase in the tax rate on trunk pipelines, power transmission lines and their integral technological part facilities from 1.3% in 2016 to 1.6% in 2017.

### *Purchased gas and oil*

Cost of purchased gas and oil increased by RUB 78,616 million, or 7%, to RUB 1,236,201 million for the year ended December 31, 2017 compared to RUB 1,157,585 million for the prior year.

Cost of purchased gas increased by RUB 974 million to RUB 873,866 million for the year ended December 31, 2017 compared to RUB 872,892 million for the prior year. The change was due to an increase in volumes of gas purchased from external suppliers that was compensated by a decrease in cost of gas purchased by GAZPROM Germania Group in Russian Ruble terms.

Cost of purchased oil included in the purchased gas and oil increased by RUB 77,642 million, or 27%, to RUB 362,335 million for the year ended December 31, 2017 compared to RUB 284,693 million for the prior year. This change was mainly related to an increase in prices of oil.

### *Depreciation*

Depreciation increased by RUB 41,596 million, or 7%, to RUB 613,160 million for the year ended December 31, 2017 compared to RUB 571,564 million for the prior year. The increase was primarily due to the growth in the fixed assets base.

### *Transit of gas, oil and refined products*

Transit of gas, oil and refined products expenses decreased by RUB 16,948 million, or 3% to RUB 593,327 million for the year ended December 31, 2017 compared to RUB 610,275 million for the prior year. This decrease was mainly due to a decrease in transit of gas expenses in Russian Ruble terms.

### *Cost of goods for resale, including refined products*

Cost of goods for resale, including refined products increased by RUB 22,248 million, or 12%, to RUB 207,689 million for the year ended December 31, 2017 compared to RUB 185,441 million for the prior year. The increase was mainly due to an increase in volumes of petroleum products purchases in Gazprom Neft Group connected with a refining decline caused by scheduled maintenance in own refineries.

### *Foreign exchange rate differences on operating items*

Foreign exchange rate gain on operating items amounted to RUB 14,487 million for the year ended December 31, 2017 compared to a net loss of RUB 52,880 million for the prior year. This change was mainly explained by the depreciation of US Dollar against the Russian Ruble by 5% and by the appreciation of Euro against the Russian Ruble by 8% for the year ended December 31, 2017 compared to the depreciation of US Dollar and Euro against the Russian Ruble by 17% and 20%, respectively, for the prior year.

### *Other operating expenses*

Other operating expenses increased by RUB 196,149 million, or 47%, to RUB 610,787 million for the year ended December 31, 2017 compared to RUB 414,638 million for the prior year. Expenses related to the recognition of liabilities in accordance with the court decisions for NJSC Naftogaz Ukraine were included in other expenses for the year ended December 31, 2017. Other expenses include gas and gas condensate production expense, services from gas distribution companies, bank charges, security services, legal and consulting services, charity and financial aid, and advertising.

### *Change in finished goods, work in progress and other effects*

The line item Change in finished goods, work in progress and other effects decreased by RUB 127,729 million to the negative amount of RUB 130,638 million for the year ended December 31, 2017 compared to the negative amount of RUB 2,209 million for the prior year. The change in this line item is explained by an increase in the balances of finished goods for the year ended December 31, 2017 compared to the prior year.

### **Change in impairment and other provisions**

The line item Change in impairment and other provisions decreased by RUB 198,792 million, or 138%, to the negative amount of RUB 54,922 million for the year ended December 31, 2017 compared to the positive amount of RUB 143,870 million for the prior year. This change was mainly caused by reverse of impairment allowance for doubtful accounts receivable of NJSC Naftogaz Ukraine for the year ended December 31, 2017.

### **Operating profit**

As a result of the factors discussed above, operating profit increased by RUB 145,043 million, or 20%, to RUB 870,623 million for the year ended December 31, 2017 compared to RUB 725,580 million for the prior year. The operating profit margin increased from 12% for the year ended December 31, 2016 to 13% for the year ended December 31, 2017.

### **Net finance income**

(RUB million)	Year ended December 31,	
	2017	2016
Foreign exchange gain	342,984	925,503
Foreign exchange loss	<u>(353,712)</u>	<u>(471,814)</u>
Net exchange (loss) gain	(10,728)	453,689
Interest income	83,721	93,494
Interest expense	<u>(53,332)</u>	<u>(71,556)</u>
<b>Net finance income</b>	<b>19,661</b>	<b>475,627</b>

The net foreign exchange loss of RUB 10,728 million for the year ended December 31, 2017 compared to the net foreign exchange gain of RUB 453,689 million for the prior year were explained by the depreciation of US Dollar against the Russian Ruble by 5% and by the appreciation of Euro against the Russian Ruble by 8% for the year ended December 31, 2017 compared to the depreciation of US Dollar and Euro against the Russian Ruble by 17% and 20%, respectively, for the prior year.

Interest income decreased by RUB 9,773 million, or 10%, to RUB 83,721 million for the year ended December 31, 2017 compared to RUB 93,494 million for the prior year.

Interest expense decreased by RUB 18,224 million, or 25%, to RUB 53,332 million for the year ended December 31, 2017 compared to RUB 71,556 million for the prior year.

### **Share of net income of associates and joint ventures**

Share of net income of associates and joint ventures increased by RUB 44,068 million, or 53%, to RUB 126,940 million for the year ended December 31, 2017 compared to RUB 82,872 million for the prior year. This change was mainly caused by an increase in the share of net income of Sakhalin Energy Investment Company Ltd and JSC Messoyakhaneftegaz.

### **Profit tax**

Total profit tax decreased by RUB 36,907 million, or 13%, to RUB 251,127 million for the year ended December 31, 2017 compared to RUB 288,034 million for the prior year. The effective profit tax rate was 24.7% and 22.4% for the years ended December 31, 2017 and 2016, respectively.

The change in the effective profit tax rate was mainly driven by an increase in non-deductible expenses for tax purposes for the year ended December 31, 2017 compared to the prior year.

### **Profit for the year attributable to owners of PJSC Gazprom**

As a result of the factors discussed above, profit for the year attributable to owners of PJSC Gazprom decreased by RUB 237,335 million, or 25%, from RUB 951,637 million for the year ended December 31, 2016 to RUB 714,302 million for the year ended December 31, 2017.

### **Profit for the year attributable to non-controlling interest**

Profit for the year attributable to non-controlling interest increased by RUB 7,110 million, or 16%, to RUB 52,577 million for the year ended December 31, 2017 compared to RUB 45,467 million for the prior year.

### **Liquidity and capital resources**

The following table summarises the cash flows for the year ended December 31, 2017 and 2016:

(RUB million)	Year ended December 31,	
	2017	2016
Net cash from operating activities	1,187,022	1,571,323
Net cash used in investing activities	(1,368,131)	(1,445,965)
Net cash from (used in) financing activities	149,944	(460,479)

#### *Net cash from operating activities*

Net cash from operating activities decreased by RUB 384,301 million, or 24%, to RUB 1,187,022 million for the year ended December 31, 2017 compared to RUB 1,571,323 million for the prior year. This change was mainly driven by a replace of cash on short-term deposits included within other current assets and increase in profit tax paid.

#### *Net cash used in investing activities*

Net cash used in investing activities decreased by RUB 77,834 million, or 5%, to RUB 1,368,131 million for the year ended December 31, 2017 compared to RUB 1,445,965 million for the prior year. The change was mainly due to the cash received from closed long-term bank deposits for the year ended December 31, 2017 compared to the placement of cash on long-term bank deposits for the prior year that was partially compensated by an increase in investments in associates and joint ventures.

#### *Net cash from (used in) financing activities*

Net cash from financing activities amounted to RUB 149,944 million for the year ended December 31, 2017 compared to net cash used in financing activities amounted to RUB 460,479 million for the prior year. This change was mainly due to an increase in proceeds from borrowings.

### **Working Capital**

The working capital surplus (current assets less current liabilities) was RUB 879,750 million as of December 31, 2017 and RUB 1,312,538 million as of December 31, 2016. The decrease in the working capital by RUB 432,788 million in the year ended December 31, 2017 was primarily due to an increase in the current portion of long-term borrowings.

Management believes that the working capital is sufficient to meet the requirements of the Group for at least next twelve months. However, we are dependent on the short-term credit markets to finance our working capital.

## Capital expenditures

Total capital expenditures (excluding the effect of acquisitions of subsidiaries) by segments for the years ended December 31, 2017 and 2016 in Russian Ruble terms, amounted to the following:

(RUB million)	Year ended	
	December 31,	
	2017	2016
Transportation	498,550	406,828
Production of crude oil and gas condensate	330,424	326,366
Refining	225,240	193,243
Production of gas	216,450	235,161
Electric and heat energy generation and sales	58,110	63,485
Distribution of gas	51,675	41,785
Gas storage	37,694	35,542
All other segments	86,457	54,926
<b>Total</b>	<b>1,504,600</b>	<b>1,357,336</b>

Total capital expenditures increased by RUB 147,264 million, or 11%, from RUB 1,357,336 million for the year ended December 31, 2016 to RUB 1,504,600 million for the year ended December 31, 2017.

## Debts

Net debt balance (defined as the sum of short-term borrowings, current portion of long-term borrowings, short-term promissory notes payable, long-term borrowings, long-term promissory notes payable, net of cash and cash equivalents and balances of cash and cash equivalents restricted as to withdrawal under the terms of certain borrowings and other contractual obligations) increased by RUB 464,616 million, or 24%, from RUB 1,932,895 million as of December 31, 2016 to RUB 2,397,511 million as of December 31, 2017. This increase was due to an increase in long-term borrowings.



The following table shows borrowings and promissory notes as of December 31, 2017 and December 31, 2016:

(RUB million unless indicated otherwise)

	<b>As of December 31,</b>	
	<b>2017</b>	<b>2016</b>
<b>Long-term borrowings</b>		
Fixed interest rate borrowings	2,355,672	2,086,181
Weighted average interest rates for fixed rate borrowings	6.26%	6.34%
Variable interest rate borrowings	824,665	682,810
Weighted average interest rates for variable rate borrowings	<u>3.54%</u>	<u>4.11%</u>
<b>Total long-term borrowings</b>	<b>3,180,337</b>	<b>2,768,991</b>
Russian Ruble denominated borrowings	558,509	427,014
Foreign currency denominated borrowings	<u>2,621,828</u>	<u>2,341,977</u>
<b>Total long-term borrowings</b>	<b>3,180,337</b>	<b>2,768,991</b>
Less: current portion of long-term borrowings	<u>(788,624)</u>	<u>(386,448)</u>
<b>Total long-term debt obligations</b>	<b>2,391,713</b>	<b>2,382,543</b>
<b>Short-term borrowings</b>		
Fixed interest rate borrowings	47,789	39,037
Weighted average interest rates for fixed rate borrowings	8.49%	9.75%
Variable interest rate borrowings	38,392	21,595
Weighted average interest rates for variable rate borrowings	<u>8.19%</u>	<u>6.67%</u>
<b>Total short-term borrowings</b>	<b>86,181</b>	<b>60,632</b>
Russian Ruble denominated borrowings	74,374	44,352
Foreign currency denominated borrowings	<u>11,807</u>	<u>16,280</u>
<b>Total short-term borrowings</b>	<b>86,181</b>	<b>60,632</b>
Add: current portion of long-term borrowings	<u>788,624</u>	<u>386,448</u>
<b>Total short-term debt obligations</b>	<b>874,805</b>	<b>447,080</b>
<b>Total borrowings</b>	<b>3,266,518</b>	<b>2,829,623</b>

The following table shows the breakdown by currency of foreign currency denominated long-term borrowings as of December 31, 2017 and December 31, 2016 as well as the same balances expressed in Russian rubles:

	<b>As of December 31,</b>	
	<b>2017</b>	<b>2016</b>
U.S. dollar denominated (expressed in millions of U.S. dollars)	20,544	21,291
Euro denominated (expressed in millions of U.S. dollars) <sup>(1)</sup>	20,953	15,212
Other currencies denominated (expressed in millions of U.S. dollars)	<u>4,021</u>	<u>2,107</u>
<b>Total long-term foreign currency denominated borrowings expressed in millions of U.S. dollars</b>	<b>45,518</b>	<b>38,610</b>
<b>Total long-term foreign currency denominated borrowings expressed in millions of Russian Rubles<sup>(2)</sup></b>	<b>2,621,828</b>	<b>2,341,977</b>

Notes:

(1) Converted at euro to U.S. dollar exchange rates of 1.20 and 1.05 as of December 31, 2017 and as of December 31, 2016, respectively.

(2) Converted at the exchange rate as of period-end.

The following table shows the schedule of repayments of long-term borrowings as of December 31, 2017 and December 31, 2016:

(RUB million)

	<b>As of December 31,</b>	
	<b>2017</b>	<b>2016</b>
Between one and two years	481,070	708,355
Between two and five years	1,087,239	956,731
After five years	<u>823,404</u>	<u>717,457</u>
<b>Total</b>	<b>2,391,713</b>	<b>2,382,543</b>

## SHAREHOLDING STRUCTURE AND STOCK MARKET OF PJSC GAZPROM

PJSC Gazprom's charter capital is RUB 118,367,564,500 divided into 23,673,512,900 ordinary shares with a par value of RUB 5 each. PJSC Gazprom has no preferred shares.

As a major shareholder of PJSC Gazprom, the Russian Government holds a more than 50% controlling stake (including direct and indirect ownership) in PJSC Gazprom. The Russian Federation does not have a special right to manage PJSC Gazprom's affairs (a "golden share").

The following table summarises quotations for PJSC Gazprom shares and ADRs:

(%)	As at 31 January	
	2017	2016
The Russian Federation represented by the Federal Agency for State Property Management	38.37	38.37
JSC ROSNEFTEGAZ <sup>(1)</sup>	10.97	10.97
JSC Rosgazifikatsiya <sup>(1)</sup>	0.89	0.89
ADR holders <sup>(2)</sup>	25.20	26.86
Other registered holders	24.57	22.91

Notes:

- <sup>(1)</sup> As at 31 December 2016 and 31 December 2017, the cumulative share in PJSC Gazprom directly or indirectly controlled by the Russian Federation and calculated by direct addition totals 50.23% and is owned through the full ownership of JSC ROSNEFTEGAZ which also holds a 74.55% stake in JSC Rosgazifikatsiya.
- <sup>(2)</sup> The Bank of New York Mellon issued ADRs on PJSC Gazprom's shares.

As at 31 December 2017, the holders of American depositary receipts (ADRs) on the PJSC Gazprom's shares accounted for about 25.2% of PJSC Gazprom's charter capital.

As at 31 December 2017, there were no PJSC Gazprom shares the title to which was transferred to PJSC Gazprom. At the same time, as at the said date, PJSC Gazprom's subsidiaries held 1,573 million ordinary shares of PJSC Gazprom, or 6.6% of the total number of ordinary shares of PJSC Gazprom.

PJSC Gazprom shares are included in the first (top) level quotation list of the Moscow Exchange and PJSC Saint Petersburg Exchange.

ADRs on PJSC Gazprom shares are traded on the London, Berlin, and Frankfurt exchanges, the Moscow Exchange, the US OTC market, and on the Singapore OTC market among qualified institutional buyers (QIBs). The London Stock Exchange (LSE) accounts for the bulk of trade in PJSC Gazprom ADRs.

The following table summarises quotations for PJSC Gazprom shares and ADRs:

	As at 31 December		Change, %
	2017	2016	
<b>Moscow Exchange</b>			
Share closing price, RUB			
at year-end	130.50	154.55	-15.6
minimum	115.35	124.60	-7.4
maximum	157.97	168.47	-6.2
Average daily trading volume, mm	28.87	29.91	-3.5
Average daily trading volume, RUB bn	3.72	4.31	-13.7
<b>LSE</b>			
ADR closing price, USD			
at year-end	4.41	5.05	-12.7
minimum	3.85	3.02	27.5
maximum	5.27	5.27	-
Average daily trading volume, mm	11.96	15.89	-24.7
Average daily trading volume, USD mm	53.11	68.56	-22.5

In 2017, PJSC Gazprom's market capitalisation decreased by 15.6% year-on-year; as at 31 December 2017, its capitalisation stood at RUB 3.1 tn.

As at 31 December 2017, dividend payouts in 2017 based on PJSC Gazprom's performance results for 2016 were as follows:

	Accrued, RUB thousand	Paid, RUB thousand	Unpaid, RUB thousand <sup>(1)</sup>	Unpaid to accrued, %
<b>Total</b>	<b>190,327,942</b>	<b>189,948,536</b>	<b>379,406</b>	<b>0.20</b>
including dividends on shares:				
held by the Russian Federation represented by the Federal Agency for State Property Management	73,035,261	73,035,261	-	-
held by individuals and corporate entities whose rights to shares are accounted for in the register	27,108,579	26,910,213	198,366	0.73
held by individuals and corporate entities whose rights to shares are accounted for by the depository maintaining a nominee holder account in the issuer's register <sup>(2)</sup>	90,183,954	90,003,062	180,892	0.20
held by unidentified persons	148	-	148	100.00

Notes:

- (1) No dividend payouts were made to individuals or corporate entities who had failed to provide clear payout details as per clauses 8 and 9 of Article 42 of Federal Law No. 208-FZ On Joint Stock Companies dated 26 December 1995. Dividends accrued on shares held by unidentified persons are paid out as soon as the title to securities is established.
- (2) PJSC Gazprom paid out RUB 90,183,954 thousand in dividends to nominee holders on 3 August 2017 in execution of the Annual General Shareholders Meeting resolutions on dividend payouts based on PJSC Gazprom's 2016 results, which was held on 30 June 2017. As at 31 December 2017, the amount of dividends nominee holders failed to transfer as prescribed by the securities laws of the Russian Federation for reasons beyond their control (clause 8 and clause 9, Article 42 of Federal Law No. 208-FZ dated 26 December 1995) totalled RUB 180,892 thousand.

## CORPORATE GOVERNANCE

The rights of PJSC Gazprom's shareholders and the regulatory framework for PJSC Gazprom's management bodies are determined and exercised in accordance with Russian laws and may differ from the regulatory practice applicable to UK companies.

Key documents of PJSC Gazprom ensuring protection of shareholder rights:

- Articles of Association of Public Joint Stock Company Gazprom
- Code of Corporate Governance of PJSC Gazprom
- Code of Corporate Ethics of PJSC Gazprom
- Regulations on the General Shareholders Meeting of PJSC Gazprom
- Regulations on the Board of Directors of PJSC Gazprom
- Regulations on the Board of Directors' Audit Committee of JSC Gazprom
- Regulations on the Board of Directors' Nomination and Remuneration Committee of PJSC Gazprom
- Regulations on the Management Committee of PJSC Gazprom
- Regulations on the Chairman of the Management Committee of PJSC Gazprom
- Regulations on the Audit Commission of JSC Gazprom, new version
- Regulations on the Internal Control System of PJSC Gazprom
- External Audit Policy for PJSC Gazprom, its subsidiaries and entities
- Procedures for Documenting of Proposals and Requests of Shareholders Related to the Convocation of the General Shareholders Meeting of PJSC Gazprom
- Dividend Policy of Joint Stock Company Gazprom
- Regulations on the Information Disclosure of PJSC Gazprom
- Procedure for Providing Information about PJSC Gazprom to Shareholders
- JSC Gazprom's Regulation on Control of Compliance with the Laws on Countering the Unlawful Use of Insider Information and Market Manipulation
- Anti-Corruption Policy of PJSC Gazprom
- Regulations on the Hotline for Fighting Fraud, Corruption, and Embezzlement at Gazprom Group

These documents are available on PJSC Gazprom's website (<http://www.gazprom.ru/investors/documents/>).

### Enhancement of corporate governance at PJSC Gazprom in 2017

In 2017, PJSC Gazprom continued to improve its standards.

In particular, the resolution of PJSC Gazprom's Annual General Shareholders Meeting dated 30 June 2017 (Minutes No. 1) updated a number of key documents: the Articles of Association, Regulations on the Board of Directors of PJSC Gazprom, Regulations on the Management Committee of PJSC Gazprom, and Regulations on the Chairman of the Management Committee of PJSC Gazprom were amended and a new version of PJSC Gazprom's Corporate Governance Code was approved.

PJSC Gazprom developed the new version of its Corporate Governance Code in line with recommendations of the Russian Corporate Governance Code, recommended by the Bank of Russia, applicable Russian laws, Articles of Association of PJSC Gazprom, Regulations on the Board of Directors of PJSC Gazprom, and other internal documents of PJSC Gazprom.

In addition, the Board of Directors of PJSC Gazprom approved a new version of the Regulations on the Information Disclosure of PJSC Gazprom by Resolution No. 2921 dated 29 March 2017 and incorporating, inter alia, recommendations of the Russian Corporate Governance Code.

In 2017, PJSC Gazprom conducted a scheduled independent audit of its corporate governance practice, involving an independent assessment of the performance of Gazprom's Board of Directors, the Audit Committee of PJSC Gazprom's Board of Directors, and the Nomination and Remuneration Committee of the Board of Directors of PJSC Gazprom.

Auditors' approaches to the corporate governance practice and, accordingly, the performance of the Board of Directors and its committees are based on Russian and international best practices and meet, inter alia, recommendations of the Russian Corporate Governance Code, rules of Russian stock exchanges, guidelines of Russian federal executive authorities (the Ministry of Economic Development and Federal Agency for State Property Management), and national risk management and social responsibility standards.

#### Corporate governance model

The corporate governance model in place at PJSC Gazprom relies on Russian laws, the requirements of Russian stock exchanges applicable to issuers whose shares have been included in the first (top) level quotation list. Key principles underlying PJSC Gazprom's corporate governance are set forth in the Code of Corporate Governance of PJSC Gazprom, the new version of which was approved by the General Shareholders Meeting of PJSC Gazprom on 30 June 2017.

PJSC Gazprom's corporate governance pillars include management and supervisory bodies: General Shareholders Meeting, Board of Directors, Management Committee, Chairman of the Management Committee, and Audit Commission. The Department of the Management Committee Administration responsible for internal audit performs fair assessment of the internal control performance and develops recommendations for improvement. PJSC Gazprom's financial and business performance is independently reviewed by an external auditor.

To preview most important matters of PJSC Gazprom's business reserved to the Board of Directors, the Board set up the Audit Committee and the Nomination and Remuneration Committee of the Board of Directors of PJSC Gazprom.

The Board of Directors established the Commission on Strengthening Financial Discipline for Domestic Gas Supplies in 2017.

PJSC Gazprom has in place the role of the Corporate Secretary whose responsibilities are distributed, to the extent recommended by the Russian Corporate Governance Code, among the following business units of PJSC Gazprom, in line with the regulations governing their functions:

- Department of the Management Committee Administration (Yury Nosov)
- Secretariat of the Management Committee Administration (Nikolai Kruglikov)
- Department Directorate (Alexey Finikov)
- Department Directorate Division (Maksim Babich).

In order to maintain a transparent and constructive dialogue with the investment community, PJSC Gazprom has in place the Coordinating Committee for Shareholder and Investor Relations led by Andrey Kruglov, Deputy Chairman of the Management Committee. The Committee also includes heads of business units responsible for development and implementation of the relevant strategy.

To monitor the compliance of PJSC Gazprom and its employees with the laws on countering the misuse of insider information and market manipulation and the compliance with insider laws and regulations applicable, PJSC Gazprom set up a business unit responsible for insider information, which reports to PJSC Gazprom's Board of Directors.

## Membership of the Board of Directors and the Management Committee

As at 31 December 2017, the membership of PJSC Gazprom's Board of Directors was as follows:

<b>Name</b>	<b>Year of birth</b>	<b>Position</b>
Viktor A. Zubkov	1941	Chairman of PJSC Gazprom's Board of Directors; Special Presidential Representative for Cooperation with the Gas Exporting Countries Forum Deputy chairman of the board of directors of LLC Gazprom gazomotornoe toplivo
Alexey B. Miller	1962	Deputy Chairman of PJSC Gazprom's Board of Directors Chairman of PJSC Gazprom's Management Committee
Andrey I. Akimov	1953	Chairman of the management board at Gazprombank (Joint-stock Company)
Timur A. Kulibaev	1966	Chairman of the Kazakhstan Association of Oil, Gas and Energy Sector Organisations (KAZENERGY) Chairman of the Presidium of the National Chamber of Entrepreneurs of the Republic of Kazakhstan (Atameken)
Denis V. Manturov	1969	Minister of Industry and Trade of the Russian Federation
Vitaly A. Markelov	1963	Deputy Chairman of PJSC Gazprom's Management Committee
Viktor G. Martynov	1953	Rector of I.M. Gubkin Russian State Oil and Gas University (a federal state budget-funded educational institution of higher professional education, national research university)
Vladimir A. Mau	1959	Rector of the Russian Presidential Academy of National Economy and Public Administration (a federal state budget-funded institution of higher education)
Alexander V. Novak	1971	Minister of Energy of the Russian Federation
Dmitry N. Patrushev	1977	Member of the supervisory board of JSC Rosselkhozbank, chairman of the management board of JSC Rosselkhozbank
Mikhail L. Sereda	1970	Deputy Chairman of the Management Committee – Head of PJSC Gazprom's Management Committee Administration

Changes to the Board of Directors in 2017 were as follows:

<b>Name</b>	<b>Change</b>
Denis V. Manturov	Member of PJSC Gazprom's Board of Directors since 30 June 2017

In 2017, the Board held a total of 59 meetings, including 12 meetings held in person and 47 meetings held in absentia. At these meetings, 180 resolutions were passed, including 49 resolutions in person and 131 resolutions in absentia.

In 2017, the Audit Committee of PJSC Gazprom's Board of Directors continued its work. The Audit Committee reports to PJSC Gazprom's Board of Directors. As at 31 December 2017, the Board of Directors' Audit Committee had three members of PJSC Gazprom's Board of Directors: Viktor Martynov, Mikhail Sereda, and Vladimir Mau. Viktor Martynov was the Chairman of the

Committee. During the year, the Committee held 8 meetings, including 3 meetings held in person. The most important matters discussed by the Committee in 2017 included LLC FBK's information on critical audit issues at PJSC Gazprom and its subsidiaries, along with the external auditor's reports on ensuring independence and on the effectiveness of external audit.

The Audit Committee maintained close contact with the external auditor LLC FBK, the Audit Commission, and PJSC Gazprom's Department responsible for internal audit.

PJSC Gazprom's Nomination and Remuneration Committee of the Board of Directors started to operate under its action plan in January 2017. As at 31 December 2017, the Board of Directors' Nomination and Remuneration Committee had three members of PJSC Gazprom's Board of Directors: Mikhail Sereda, Vladimir Mau, and Viktor Martynov. Mikhail Sereda was the Chairman of the Committee.

In 2017, the Committee held 10 meetings, including one meeting held in person. The Committee reviewed the following matters: election of members of PJSC Gazprom's Management Committee; approval of the PJSC Gazprom's actual 2016 KPI values for the purposes of the annual bonus scheme for the management of PJSC Gazprom as well as target (planned), threshold, and maximum KPI values for 2017; remuneration of members of PJSC Gazprom's Board of Directors and Audit Commission; assessment of Directors' performance, etc.

Members of PJSC Gazprom's Management Committee as at 31 December 2017:

<b>Name</b>	<b>Year of birth</b>	<b>Position</b>
Alexey B. Miller	1962	Chairman of PJSC Gazprom's Management Committee
Elena A. Vasilieva	1959	Deputy Chairwoman of PJSC Gazprom's Management Committee – Chief Accountant of PJSC Gazprom
Valery A. Golubev	1952	Deputy Chairman of PJSC Gazprom's Management Committee
Andrey V. Kruglov	1969	Deputy Chairman of PJSC Gazprom's Management Committee
Vitaly A. Markelov	1963	Deputy Chairman of PJSC Gazprom's Management Committee
Alexander I. Medvedev	1955	Deputy Chairman of PJSC Gazprom's Management Committee
Sergey F. Khomyakov	1953	Deputy Chairman of PJSC Gazprom's Management Committee, Director General of PJSC Gazprom's Corporate Security Service Branch
Oleg E. Aksyutin	1967	Head of Department (prospective development)
Igor Y. Fyodorov	1965	Head of Department (legal support)
Vladimir K. Markov	1955	Head of Department (relations with the Russian Federation authorities)
Elena V. Mikhailova	1977	Head of Department (asset management and corporate relations), Deputy Director General for Corporate Relations and Asset Management at LLC Gazprom mezhhregiongaz
Vyacheslav A. Mikhaleenko	1965	Head of Department (gas transportation and underground storage)

Sergey F. Prozorov	1958	Head of Department (managing construction of production facilities)
Kirill G. Seleznev	1974	Head of Department (marketing; gas and liquid hydrocarbons processing; developing electric power and heat generation), Director General of LLC Gazprom mezhregiongaz
Vsevolod V. Cherepanov	1966	Head of Department (hydrocarbon exploration and production)

Changes to the Management Committee in 2017 were as follows:

<b>Name</b>	<b>Change</b>
Nikolai N. Dubik	The powers of a Management Committee member terminated by Resolution of PJSC Gazprom's Board of Directors No. 2955 dated 19 May 2017.
Alexander N. Kozlov	The powers of a Management Committee member terminated by Resolution of PJSC Gazprom's Board of Directors No. 3062 dated 26 December 2017.

#### Remuneration of key executives

The General Shareholders Meeting has the authority to resolve on payment, and determine amounts of, remuneration to members of the Board of Directors during their time in office. Members of the Board of Directors holding public or civil office in the Russian Federation receive no remuneration from the PJSC Gazprom.

Remuneration of members of executive bodies (Chairman and members of the Management Committee) and other executives of PJSC Gazprom is determined by their employment agreements. Short-term remuneration of PJSC Gazprom's key executives (members of the Board of Directors and Management Committee), including salaries, bonuses, and remuneration for their service on management bodies of PJSC Gazprom's entities amounted to ca. RUB 4,537 mm and RUB 4,685 mm for the years ended on 31 December 2017 and 31 December 2016, respectively.

#### Liability insurance of directors, officers, and PJSC Gazprom

PJSC Gazprom insures the liability of its directors (excluding directors holding public office), officers, and PJSC Gazprom. The terms of the 2017 liability insurance programme for directors, officers, and PJSC Gazprom are as follows:

- insurance coverage: USD 100 mm
- insurance premium: USD 900 thousand.

Persons insured:

- members of the Board of Directors (excluding directors who hold public office)
- PJSC Gazprom's Management Committee members
- heads of PJSC Gazprom's Departments who are not members of PJSC Gazprom's Management Committee.

Risks insured:

- risk of third-party claims against the insured for losses arising from unintentional errors made by the insured in their management roles
- risk of third-party claims against PJSC Gazprom for losses arising from unintentional errors made by the insured in their management roles: claims related to PJSC Gazprom's securities; claims initially made against the insured.



The insurance coverage under the current liability insurance policy is in line with PJSC Gazprom's needs and Russian and international insurance standards in terms of risk coverage and indemnity limits.

#### PJSC Gazprom shares held by members of the Board of Directors and Management Committee

As at 31 December 2017, members of the Board of Directors, Management Committee, and the Chairman of the Management Committee had a shareholding of 0.012454% in PJSC Gazprom's equity.

#### Internal control system and audit

PJSC Gazprom's internal controls is a system of internal control bodies and methods, rules of conduct, and actions of employees aimed at achieving PJSC Gazprom's goals.

Goals, objectives, internal controls, their operation, and PJSC Gazprom's management bodies and persons responsible for internal control are set forth in the Regulations on the Internal Control System of PJSC Gazprom (approved by Resolution of the Board of Directors No. 2315 dated 25 February 2014, as amended by Resolution of the Board of Directors No. 2848 dated 15 November 2016).

The internal control system is designed to provide reasonable assurance that PJSC Gazprom:

- performs efficiently
- ensures the completeness, timeliness, and fairness of all types of accounting and reporting at PJSC Gazprom
- complies with applicable laws
- prevents and counters corruption
- protects its assets (including data assets).

Internal control is exercised by PJSC Gazprom's Board of Directors, Audit Committee of PJSC Gazprom's Board of Directors, PJSC Gazprom's Audit Commission, executive bodies (the Management Committee and Chairman of the Management Committee), heads of business units, and other employees of PJSC Gazprom.

#### *Audit Commission*

The Audit Commission's authority is set forth in the Federal Law On Joint-Stock Companies and PJSC Gazprom's Articles of Association. The Audit Commission operates under the Regulations on the Audit Commission of JSC Gazprom approved by the Resolution of JSC Gazprom's Annual General Shareholders Meeting (Minutes No. 1 dated 28 June 2013).

Key roles of the Audit Commission:

- monitor the fairness of presentation of PJSC Gazprom's financial and accounting statements and other information on PJSC Gazprom's financial and business operations and condition of its assets
- supervise statutory compliance of PJSC Gazprom's accounting practices and of submission of its financial statements and information to relevant authorities and shareholders
- prepare proposals on enhancing PJSC Gazprom's asset management and other financial and business operations of PJSC Gazprom, mitigate financial and operating risks, and improve internal controls.

The Audit Commission is accountable to the General Shareholders Meeting and coordinates its activities with the Audit Committee of the Board of Directors.

Following an audit of PJSC Gazprom's financial and business operations, the Audit Commission presented its opinion confirming the fairness of data in PJSC Gazprom's statements and other financial documents.

The Audit Commission of nine members is elected by the General Shareholders Meeting.

#### *Internal Audit*

Internal audit assists in achieving the PJSC Gazprom's goals through applying a holistic consistent approach to assessment and improvement of risk management, internal control, and corporate governance processes.

To improve the internal audit function and in accordance with Directive of the Russian Government for persons representing interests of the Russian Federation No. 3984p-P13 dated 24 June 2015, PJSC Gazprom developed and approved the Regulations on Internal Audit of PJSC Gazprom in 2015 (Resolution of the Board of Directors No. 2621 dated 6 November 2015).

These Regulations determine the goals, objectives, status, powers, and liability of the Department responsible for internal audits at PJSC Gazprom, as well as the scope of internal audit.

Pursuant to the Regulations, the internal audit in PJSC Gazprom is organised by the relevant Department, a business unit of PJSC Gazprom, and by internal audit units – in PJSC Gazprom's subsidiaries.

The key priority of the Department is to provide the Board of Directors (through the Audit Committee of the Board of Directors) and management of PJSC Gazprom with independent and unbiased assurances and advice as to the improvement of PJSC Gazprom's operations.

The Department is administratively accountable to the Chairman of PJSC Gazprom's Management Committee within the Management Committee Administration and functionally accountable to the Board of Directors (through the Board of Directors' Audit Committee). The Head of the Department is appointed and removed from office by the Chairman of PJSC Gazprom's Management Committee upon recommendation of the Deputy Chairman of the Management Committee – Head of the Administration of PJSC Gazprom's Management Committee, as approved by the Board of Directors (through the Board of Directors' Audit Committee).

#### *External Auditor*

PJSC Gazprom selects its auditor annually by a public tender in accordance with applicable Russian laws.

A public tender for the service contract to audit PJSC Gazprom's accounting (financial) statements, Gazprom Group's consolidated accounting statements, and Gazprom Group's consolidated IFRS financial statements for 2017 was announced on 20 February 2017.

LLC FBK won the public tender among audit firms to conduct statutory annual audit of PJSC Gazprom and was approved as auditor by the Annual General Shareholders Meeting of PJSC Gazprom on 30 June 2017. The contract price offered by the winner was RUB 208,000,000 (exclusive of VAT) and was approved by Resolution of the Board of Directors No. 2951 dated 19 May 2017.

In 2017, LLC FBK provided other audit-related services to PJSC Gazprom outside its audit contract. In 2017, a fee of RUB 20,917,045.11 (inclusive of VAT) was paid for other audit-related services.

#### Anti-corruption efforts

PJSC Gazprom has procedures in place to ensure compliance with anti-corruption laws.

PJSC Gazprom's management is consistently focused on improving its procedures for preventing and revealing corrupt practices in Gazprom Group. PJSC Gazprom's Board of Directors reviews preventing and countering corruption on an annual basis.

PJSC Gazprom has adopted its Code of Corporate Ethics developed with due account for Russian and international corporate governance best practices. The PJSC Gazprom's Code of Corporate Ethics provides for corporate values and determines the fundamental rules of business conduct stemming from such values, which rule out any conflicts of interest or corrupt practices, as well as

cases of nepotism, with relatives directly or indirectly reporting to each other. Most of PJSC Gazprom's subsidiaries have developed and adopted similar documents based on the Code.

The Code specifies the procedure to be followed by PJSC Gazprom's employees in the event of a conflict of interest, declares zero tolerance for corrupt conduct, affirms environmental responsibility and non-discriminatory principles, establishes implementation and supervision practices on compliance with corporate ethics standards.

The Code's provisions are mandatory for PJSC Gazprom's employees (including all members of the Management Committee and the Board of Directors who are PJSC Gazprom's employees) and the Group-controlled corporate entities. The Code's provisions are not mandatory for employees of PJSC Gazprom's affiliates which are not under the Group's control, and employees of PJSC Gazprom's counterparties.

PJSC Gazprom's management, including members of the Management Committee and the Board of Directors, who are PJSC Gazprom's employees, signed up to the Code of Corporate Ethics of PJSC Gazprom.

The permanent Corporate Ethics Commission of PJSC Gazprom is responsible for supervising compliance with the Code's requirements and provisions.

The Commission reviews reports on an ongoing basis as required by applicable laws of the Russian Federation. In some cases, reports so received are forwarded to PJSC Gazprom's subsidiaries to be reviewed on the merits by the respective subsidiary's corporate ethics commission. The results of such reviews are communicated to Commission members. In 2017, the Commission received no reports on any conflict of interest of members of the Board of Directors of PJSC Gazprom, members of the Management Committee of PJSC Gazprom, and/or the Chairman of PJSC Gazprom's Management Committee.

The Commission's performance is reported to the Chairman of PJSC Gazprom's Management Committee on an annual basis.

PJSC Gazprom and its subsidiaries organise awareness days to communicate to their employees the effective rules of business, including anti-corruption corporate ethics. Subsidiaries gather and consolidate information on efforts made to comply with requirements and restrictions established by codes of corporate ethics with respect to entertainment expenses, business gift expenses, charity, and other activities involving corporate risk exposure.

## **RISK MANAGEMENT**

PJSC Gazprom's risk management system is defined as an aggregate of the organisational structure, internal regulations, corporate culture standards, guidelines, and procedures aimed at providing adequate assurances that PJSC Gazprom's goals will be achieved, and supporting the management and employees of PJSC Gazprom's business units and subsidiaries in decision making in an uncertain environment. As an integral part of PJSC Gazprom's corporate governance framework, it covers all management levels and business lines across PJSC Gazprom.

PJSC Gazprom's risk management system complies with the principles set forth in the Russian Code of Corporate Governance.

PJSC Gazprom's business units and subsidiaries are charged with risk identification and assessment, development and implementation of risk management activities, monitoring of risks and activities.

### **Strategic and country risks**

#### Risks related to the global economy

An unfavourable economic environment can lead to a slowdown in energy demand and drive the cost of borrowed capital.

### *Risk management / mitigation*

To ensure growth of revenue from energy sales PJSC Gazprom diversifies its markets and sales channels and expands the uses of natural gas. To maintain its financial stability, PJSC Gazprom optimises leverage.

#### European gas market risks

The European Union pursues a policy of diversifying its gas supply sources and increasing the share of natural gas exchange trade, which affects PJSC Gazprom as one of the main suppliers of natural gas to the EU countries.

### *Risk management / mitigation*

PJSC Gazprom ensures reliable and flexible gas supplies through long-term contracts. Additionally, to minimise the risk of lower supply levels a set of initiatives continues to be implemented to both build new infrastructure and bolster demand for natural gas, as well as strengthen PJSC Gazprom's position in the sectors with a potential for extra supplies.

#### Political risk

Starting from 2014, Russia is under sanctions imposed by the EU, the United States, and other countries.

### *Risk management / mitigation*

PJSC Gazprom pursues a policy of ensuring technological independence and import substitution to reduce the impact the economic restrictions against Russia have on PJSC Gazprom.

#### Natural gas transit risks

Gas transmission via third countries is associated with the risk of the counterparties defaulting on their transit obligations, which exposes Gazprom Group to the risk of improper performance of its obligations under gas supply contracts.

### *Risk management / mitigation*

A number of measures are taken to reduce the reliance on transit countries, including diversification of export routes, expanding access to UGSFs abroad, and development of LNG trade.

#### Russian regulatory risks for the gas industry

PJSC Gazprom's operations as a natural monopoly are regulated by Federal Law No. 147-FZ On Natural Monopolies dated 17 August 1995. The Government holds an interest of over 50% in the equity of PJSC Gazprom.

### *Risk management / mitigation*

PJSC Gazprom is consistently engaged in intensive dialogue with government authorities to improve the pricing policy and taxation of companies in the gas industry; objective supporting cases are prepared to inform decision making by PJSC Gazprom's Board of Directors.

#### Unconventional gas development risks

Unconventional gas production has been growing since mid-2000's, primarily from shale deposits in the US. Shale gas appeals mostly to countries with limited conventional gas reserves and resources; however, the risk that these countries will reduce gas imports in the mid-term is still assessed as insignificant.

### *Risk management / mitigation*

PJSC Gazprom continuously monitors the evolution of the shale gas industry and developments in other unconventional hydrocarbons industries around the world. The monitoring results, including the economics of unconventional gas production and its potential as a competition to PJSC Gazprom in its existing or prospective markets, are reviewed by PJSC Gazprom's management bodies on a regular basis, which enables PJSC Gazprom to build an effective region-specific marketing policy.

#### Renewable energy risks

Renewable energy output can be expected to grow in some countries, which may squeeze gas consumption in these markets.

### *Risk management / mitigation*

The use of natural gas, inter alia, for power generation offers consumers economic, technological, and environmental benefits, which, PJSC Gazprom believes, will support natural gas as the most common energy source. In most cases, renewable power generation supplements power generation from other sources and may entail certain risks for the natural gas market if aggressive policies of subsidising renewable energy are maintained at national and/or supranational levels.

### **Customs, currency, and tax regulation risks**

#### Risk of changes in the Russian currency regulation and tax legislation

Currency regulation and tax legislation risks persist, along with the risk of a heavier tax burden on companies operating in the fuel and energy sector. Changes in the Russian currency regulation and tax legislation, as well as tax legislation changes in the countries in which Gazprom Group has a presence may affect the operations of PJSC Gazprom and Gazprom Group's entities.

### *Risk management / mitigation*

Changes in currency and tax laws are consistently monitored, and relevant requirements are strictly complied with.

PJSC Gazprom liaises with government authorities to ensure timely adjustment of its operations in line with changes in Russian and international laws.

#### Risks related to changes in Russian rules on customs control and duties

Customs authorities may introduce additional customs requirements if the rules of customs control and export duty payment are amended.

### *Risk management / mitigation*

PJSC Gazprom complies with the requirements of customs laws, tracking proposed amendments to regulations at the earlier drafting stages, and submits its proposals while communicating with government authorities.

### **Financial risks**

#### Foreign exchange and interest rate risks

High exchange rate volatility coupled with income and expenses denominated in different currencies affect PJSC Gazprom's performance.

### *Risk management / mitigation*

To minimise losses from exchange rate volatility, PJSC Gazprom hedges its foreign exchange and interest rate risks. In addition, PJSC Gazprom complies with the Bank of Russia's instructions on

the ratio assets and liabilities denominated in foreign currency and accounts for the foreign exchange risk using earnings at risk (EaR) assessment.

#### Credit and liquidity risks

Delayed or incomplete discharge of contractual obligations by some counterparties entails risks for PJSC Gazprom's operations.

#### *Risk management / mitigation*

Relations with credit institutions are subject to credit risk limits revised on a regular basis and reflecting, inter alia, the credit rating calculated by PJSC Gazprom, subsidiaries, and entities. Performance of contractual obligations is monitored.

#### **Market risks**

If oil prices and gas exchange quotations drop, resulting risks may lead to a decline in revenues. There are also volume risks associated with a certain flexibility that buyers have in terms of gas offtake.

#### *Risk management / mitigation*

These risks are managed by adjusting contract terms and conditions, determining approved types of transactions and financial instruments and counterparties to enter into such transactions.

#### **PJSC Gazprom's operating risks**

##### Risks of early termination and suspension of subsoil licences

Non-compliance with the licence agreements exposes PJSC Gazprom to risks of early termination or suspension of subsoil licences for the survey, exploration, and production of hydrocarbons.

#### *Risk management / mitigation*

Regular monitoring, control of compliance with licence requirements, and timely amendment of licence agreements minimise the likelihood of licence revocation and suspension.

##### Risks related to occupational health and industrial safety

PJSC Gazprom's performance on the efficiency of its occupational health and industrial safety practices.

#### *Risk management / mitigation*

PJSC Gazprom has in place and operates a Unified Occupational Health and Safety Management System integrated into its management system.

#### Cost risks

Increased prices for equipment, technical devices, spare parts, as well as works and services, which form the actual cost of capital construction projects, constitute one of the most significant investment risks.

#### *Risk management / mitigation*

Competitive procurement, whereby the suppliers offering goods of adequate quality and submitting the lowest price bids are selected, helps cut the costs of procurement and sourcing of feedstock, materials, spare parts, works, and services.

To control the cost of procurement from a sole supplier (contractor, service provider), Gazprom Group's Central Procurement Office and PJSC Gazprom's Budget Committee review the pricing procedure and fairness of prices of contracts (with changes and amendments) to be signed by

Gazprom Group based on customer estimates, optimise such prices, establish price limits (additional agreements), match the prices of the signed contracts (additional agreements) against the set prices.

#### Facilities risks

The key operations, including hydrocarbon production, transportation, processing/refining, and storage, carry process and engineering, natural and climatic risks, as well as risks of adverse actions by personnel or third parties.

#### *Risk management / mitigation*

The Unified Gas Supply System (UGSS) ensures reliable gas supplies. Stable operation of the system is achieved by implementing advanced and innovative diagnostic methods, carrying out timely overhaul and maintenance, revamping and upgrading existing facilities. Insurance coverage is provided to protect subsidiaries' property interests, which includes property insurance (including offshore facilities), business interruption insurance for GPPs, and liability insurance for construction, repair, and operation of production facilities.

#### Hydrocarbon reserve estimation risks

PJSC Gazprom's strategic and financial goals depend on hydrocarbon reserves and the accuracy of reserve estimates.

#### *Risk management / mitigation*

Independent reserve estimation procedures have been developed and are implemented in accordance with the Petroleum Resources Management System (PRMS) standards. Gazprom's reserves estimated under Russian reserves classification standards are recorded in its books only after the annual review and approval by the State Reserves Commission of the Russian Ministry of Natural Resources.

#### Environmental risks

The key operations, including hydrocarbon production, transportation, refining/processing, and storage, carry environmental risks (risks of environmental pollution, non-compliance with environmental regulations) that may lead to legal, financial, and reputational implications.

#### *Risk management / mitigation*

PJSC Gazprom implements a unified Environmental Policy, programmes, and initiatives to reduce its environmental footprint, takes out voluntary environmental liability insurance, introduces best available innovative technology for mitigating the environmental impact.

PJSC Gazprom has developed and operates an efficient environmental management system combining environmental controls of both the parent company and subsidiaries. PJSC Gazprom's EMS successfully passed a recertification audit in December 2017 for ISO 14001:2015.

Efforts taken by PJSC Gazprom help maintain high levels of environmental risk manageability.

## **BRANCHES AND REPRESENTATIVE OFFICES OF PJSC GAZPROM**

The list of branches and representative offices of PJSC Gazprom as at 31 December 2017:

<b>Name</b>	<b>Location</b>
Branch Avtopredpriyatie of PJSC Gazprom	Saint Petersburg
Branch Corporate Premises Management of PJSC Gazprom	Saint Petersburg
Branch Bogorodskoye Reception House	Moscow
Branch Souyz Holiday Hotel	Moscow Region
Branch Morozovka Holiday Hotel	Moscow Region
Branch Corporate Security Services of PJSC Gazprom	Saint Petersburg
Branch Central Interregional Security Division of PJSC Gazprom	Moscow Region
Branch Main Security Division of PJSC Gazprom in Saint Petersburg	Saint Petersburg
Branch Southern Interregional Security Division of PJSC Gazprom	Krasnodar
Branch Volga Interregional Security Division of PJSC Gazprom	Samara
Branch North Urals Interregional Security Division of PJSC Gazprom	Novy Urengoy
Branch South Urals Interregional Security Division of PJSC Gazprom	Yekaterinburg
Branch Siberian Interregional Security Division of PJSC Gazprom	Tomsk
Branch Far Eastern Interregional Security Division of PJSC Gazprom	Khabarovsk
Branch Office 333 of PJSC Gazprom in Saint Petersburg	Saint Petersburg
Representative office in Ukraine	Kiev
Representative office in the People's Democratic Republic of Algeria	Algiers
Representative office in the Islamic Republic of Iran	Tehran
Representative office in the Republic of Turkey	Ankara
Representative office in the People's Republic of China	Beijing
Representative office in the Republic of India	New Delhi
Representative office in Turkmenistan	Ashgabat
Representative office in the Republic of Kazakhstan	Astana
Representative office in the Republic of Latvia	Riga
Representative office in the Federative Republic of Brazil	Rio de Janeiro
Representative office in the Republic of Moldova	Chişinău
Representative office in the State of Qatar	Doha
Representative office in the Kingdom of Belgium	Brussels
Representative office in Japan	Tokyo



**CONVERSION TABLE**

<b>Metric measure</b>	<b>U.S. measure</b>
1 bcm of natural gas	6.49 barrels of oil equivalent (boe)
1 tonne of oil	7.33 barrels of oil equivalent (boe)
1 tonne of gas condensate	8.18 barrels of oil equivalent (boe)
1 kilometre	Approximately 0.62 miles

## GLOSSARY OF KEY TERMS AND ABBREVIATIONS

Terms and abbreviations	Description
A+B <sub>1</sub> +C <sub>1</sub> hydrocarbon reserves	Explored reserves estimated under the Russian Classification of Reserves and Resources with high geological certainty and corresponding to the previously used A+B+C <sub>1</sub> reserves. Recovery factors for oil, gas, and gas condensate reserves are determined based on field geology with account for existing technologies
Adjusted EBITDA	Earnings before interest, taxes, depreciation, and amortization adjusted by changes in impairment provisions and other provisions
ADR of PJSC Gazprom	American Depositary Receipt issued for PJSC Gazprom shares
APG	Associated petroleum gas
Associate	Entity over which the Group has significant influence and that are neither a subsidiary nor an interest in a joint arrangement. Significant influence occurs when the Group has the power to participate in the financial and operating policy decisions of an entity but has no control or joint control over those policies
boe	Barrel of oil equivalent
Brent	Benchmark brand of crude oil produced in the North sea
CCO	Competitive Capacity Outtake
CHPP	Combined heat and power plant
CSA	Capacity Supply Agreement
cubic m	A cubic metre of natural gas measured at 1 Pa pressure and 20°C.
EMS	Environmental Management System
Europe and other countries	Foreign countries other than FSU countries
European far abroad countries	25 EU countries (excluding Latvia, Lithuania, and Estonia), such non-EU countries as Turkey, Norway, and Switzerland, and the Balkan states of Bosnia, Bosnia and Herzegovina, Macedonia, and Serbia
FSU	Former Soviet Union republics, except for the Russian Federation
Gazprom Group, the Group, Gazprom	An aggregate of entities which includes PJSC Gazprom (parent company) and its subsidiaries
Gazprom energoholding Group	An aggregate of entities which includes LLC Gazprom energoholding (parent company) and its subsidiaries. Gazprom Group controls Gazprom energoholding Group
Gazprom neftekhim Salavat Group	An aggregate of entities which includes LLC Gazprom neftekhim Salavat (parent company) and its subsidiaries Gazprom Group controls Gazprom neftekhim Salavat Group
Gazprom Neft Group	An aggregate of entities which includes PJSC Gazprom Neft (parent company) and its subsidiaries. Gazprom Group controls Gazprom Neft Group
GHG	Greenhouse gases
GPP, GPZ	Gas and/or condensate processing plant
GRES	State district power station
GTS	Gas Transportation System
GW	Gigawatt
ha	Hectare
IFRS	International Financial Reporting Standards
ISO 14001	International Organization for Standardization, the international environmental

	management standard
ISO 9001	International Organization for Standardization, the international quality management standard
Joint operation	Joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligation for the liabilities, relating to the arrangement. Where the Group acts as a joint operator, the Group recognises in relation to its interest in a joint operation: its assets, including its share of any assets held jointly; its liabilities, including its share of any liabilities incurred jointly; its revenue from the sale of its share of the output arising from the joint operation; its share of the revenue from the sale of the output by the joint operation; and its expenses, including its share of any expenses incurred jointly
Joint venture	Joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement. With regards to joint arrangements, where the Group acts as a joint venture, the Group recognises its interest in a joint venture as an investment and accounts for that investment using the equity method
km	Kilometre
kWh	Kilowatt hour
LNG	Liquefied natural gas
LSE	London Stock Exchange
m	Metre
MW	Megawatt
Net debt	The sum of short-term borrowings, current portion of long-term borrowings, short-term promissory notes payable, long-term borrowings, long-term promissory notes payable, net of cash and cash equivalents and balances of cash and cash equivalents restricted as to withdrawal under the terms of certain borrowings and other contractual obligations
OGCF	Oil and gas condensate field
OHSAS 18001	Occupational Health and Safety Management Systems, the international standard for occupational health and safety management systems
PRMS standards	International classification and assessment of hydrocarbon reserves under PRMS (Petroleum Resources Management System).
R&D	Research and Development
RUB	Russian rouble
sq km	Square kilometre
tonne	Metric ton
Total debt	The sum of short-term borrowings, current portion of long-term borrowings, short-term promissory notes payable, long-term borrowings, long-term promissory notes payable
TPP	Thermal power plant
Urals	Russian brand of export crude oil mixture
UGSF	Underground gas storage facility
UGSS	Unified Gas Supply System of Russia
USA	United States of America
USD	United States (US) dollars
VAT	Value Added Tax

## CONTACTS

### Full name

Public Joint Stock Company Gazprom

### Abbreviated name

PJSC Gazprom

### Location

Moscow, Russian Federation

Address: 16 Nametkina str., GSP-7, Moscow, 117997, Russian Federation

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### Website

[www.gazprom.ru](http://www.gazprom.ru) (in Russian)

[www.gazprom.com](http://www.gazprom.com) (in English)

### E-mail

[gazprom@gazprom.ru](mailto:gazprom@gazprom.ru)

### Certificate of entry into the Unified State Register of Legal Entities

by the Moscow Department of the Ministry of Taxation dated 2 August, 2002, OGRN 1027700070518

### Taxpayer Personal Identification Number (INN)

7736050003

### Contact for shareholders

Shareholders Relations

Phone: +7 812 609 7657 (for shareholders of PJSC Gazprom)

**Contact for investors**

Investors Relations

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**Auditor**

Limited Liability Company Financial and Accounting Consultants (LLC FBK).

LLC FBK is a member of the self-regulated organisation of auditors Auditor Association Sodruzhestvo

Location and postal address: 44/1 Myasnitskaya str., bld. 2 AB, Moscow, 101990, Russian Federation

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Website: [www.fbk.ru](http://www.fbk.ru).

**Registrar**

Joint Stock Company Specialised Registrar – Register Keeper for Gas Industry Shareholders (JSC DRAGa)

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**Depository bank (PJSC Gazprom ADRs)**

Bank of New York Mellon

Website: [www.bnymellon.com](http://www.bnymellon.com)