

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*The following discussion and analysis of financial condition and results of operations should be read in conjunction with the unaudited consolidated interim condensed financial information for the six months ended June 30, 2020. This consolidated interim condensed financial information is prepared in accordance with International Accounting Standard 34 Interim Financial Reporting. The consolidated interim condensed financial information for the six months ended June 30, 2020 should be read in conjunction with the consolidated financial statements for the year ended December 31, 2019 prepared in accordance with International Financial Reporting Standards.*

### OVERVIEW

We are one of the world's largest gas and oil companies in terms of volume of reserves, production of gas and market capitalisation. Our sales are primarily derived from sales of natural gas, crude oil and other hydrocarbon products to countries of Western and Central Europe, the Russian Federation and other Former Soviet Union countries.

We are involved in the following activities:

- exploration and production of gas;
- transportation of gas;
- sales of gas within the Russian Federation and abroad;
- gas storage;
- production of crude oil and gas condensate;
- processing of oil, gas condensate and other hydrocarbons and sales of refined products;
- electric and heat energy generation and sales.

Other activities include production of other goods, other works and rendering of other services.

The official Russian Ruble ("RUB") to US Dollar foreign exchange rate as determined by the Central Bank of the Russian Federation was as follows:

- as of June 30, 2020 – 69.9513 (as of June 30, 2019 – 63.0756);
- as of December 31, 2019 – 61.9057 (as of December 31, 2018 – 69.4706).

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

- as of June 30, 2020 – 78.6812 (as of June 30, 2019 – 71.8179);
- as of December 31, 2019 – 69.3406 (as of December 31, 2018 – 79.4605).

The average exchange rates of RUB for the six months ended June 30, 2020 and for the six months ended June 30, 2019 were:

- to US Dollar – 69.3714 and 65.3384, respectively;
- to Euro – 76.4417 and 73.8389, respectively.

## RESULTS OF OPERATION

(in RUB million)

	Three months ended		Six months ended	
	June 30,		June 30,	
	2020	2019	2020	2019
Sales	1,163,316	1,784,930	2,903,148	4,076,751
Net gain (loss) from trading activity	4,043	(26,020)	14,438	(32,615)
Operating expenses	(1,253,556)	(1,414,471)	(2,693,257)	(3,196,687)
Impairment loss on financial assets	<u>(17,277)</u>	<u>(22,323)</u>	<u>(34,344)</u>	<u>(66,571)</u>
<b>Operating profit (loss)</b>	<b>(103,474)</b>	<b>322,116</b>	<b>189,985</b>	<b>780,878</b>
Finance income	324,386	95,415	459,352	353,638
Finance expense	(58,014)	(55,502)	(740,984)	(124,493)
Share of profit of associates and joint ventures	<u>29,016</u>	<u>51,323</u>	<u>74,841</u>	<u>115,255</u>
<b>(Loss) profit before profit tax</b>	<b>191,914</b>	<b>413,352</b>	<b>(16,806)</b>	<b>1,125,278</b>
Current profit tax expense	(9,884)	(77,230)	(37,788)	(197,494)
Deferred profit tax income (expense)	<u>(28,488)</u>	<u>(16,991)</u>	<u>100,054</u>	<u>(49,140)</u>
Profit tax	(38,372)	(94,221)	62,266	(246,634)
<b>Profit for the period</b>	<b>153,542</b>	<b>319,131</b>	<b>45,460</b>	<b>878,644</b>
<b>Other comprehensive income (loss):</b>				
Items that will not be reclassified to profit or loss:				
(Loss) gain arising from changes in fair value of financial assets measured at fair value through other comprehensive income, net of tax	34,820	70,666	(71,273)	47,499
Remeasurement of provision for post-employment benefits	<u>(40,290)</u>	<u>(53,739)</u>	<u>(35,091)</u>	<u>(77,852)</u>
<b>Total other comprehensive (loss) income that will not be reclassified to profit or loss</b>	<b>(5,470)</b>	<b>16,927</b>	<b>(106,364)</b>	<b>(30,353)</b>
Items that may be reclassified subsequently to profit or loss:				
Share of other comprehensive loss of associates and joint ventures	(1,450)	(2,433)	(34,535)	(4,329)
Translation differences	(154,043)	(24,663)	172,076	(140,628)
(Loss) gain from hedging operations, net of tax	<u>(54)</u>	<u>4,668</u>	<u>(11,999)</u>	<u>10,024</u>
<b>Total other comprehensive income (loss) that may be reclassified subsequently to profit or loss</b>	<b>(155,547)</b>	<b>(22,428)</b>	<b>125,542</b>	<b>(134,933)</b>
<b>Total other comprehensive income (loss) for the period, net of tax</b>	<b><u>(161,017)</u></b>	<b><u>(5,501)</u></b>	<b><u>19,178</u></b>	<b><u>(165,286)</u></b>
<b>Comprehensive income (loss) for the period</b>	<b>(7,475)</b>	<b>313,630</b>	<b>64,638</b>	<b>713,358</b>
<b>Profit for the period attributable to:</b>				
Owners of PJSC Gazprom	149,168	300,589	32,919	836,497
Non-controlling interest	<u>4,374</u>	<u>18,542</u>	<u>12,541</u>	<u>42,147</u>
	<b>153,542</b>	<b>319,131</b>	<b>45,460</b>	<b>878,644</b>
<b>Comprehensive income (loss) for the period attributable to:</b>				
Owners of PJSC Gazprom	(1,371)	296,378	40,666	679,588
Non-controlling interest	<u>(6,104)</u>	<u>17,252</u>	<u>23,972</u>	<u>33,770</u>
	<b>(7,475)</b>	<b>313,630</b>	<b>64,638</b>	<b>713,358</b>

## Sales

The following table sets out volumes and sales prices:

(in RUB million unless indicated otherwise)

	Three months ended June 30,		Six months ended June 30,	
	2020	2019	2020	2019
<b>Sales of gas</b>				
<i>Europe and other countries</i>				
Gross sales <sup>(1)</sup>	372,028	742,550	930,480	1,806,757
Customs duties	(73,239)	(132,829)	(161,648)	(340,625)
Excise tax	(1,994)	(13,526)	(12,553)	(32,541)
Net sales	296,795	596,195	756,279	1,433,591
Volumes in bcm	46.6	55.5	98.2	117.9
Average price, US Dollar per mcm <sup>(2)</sup> (including excise tax and customs duties) <sup>(3)</sup>	110.1	207.5	136.0	235.3
Average price, RUB per mcm <sup>(2)</sup> (including excise tax and customs duties)	7,975.2	13,392.1	9,475.4	15,331.0
<i>Former Soviet Union countries</i>				
Gross sales <sup>(1)</sup>	55,300	68,687	146,186	202,637
Customs duties	(3,136)	(6,446)	(6,903)	(22,899)
Net sales	52,164	62,241	139,283	179,738
Volumes in bcm	5.6	6.9	14.9	19.1
Average price, US Dollar per mcm <sup>(2)</sup> (including customs duties) <sup>(3)</sup>	136.8	154.5	140.7	163.2
Average price, RUB per mcm <sup>(2)</sup> (including customs duties)	9,911.3	9,969.1	9,803.5	10,637.1
<i>Russian Federation</i>				
Gross sales (net of VAT)	165,938	169,326	488,703	518,256
Net sales	165,938	169,326	488,703	518,256
Volumes in bcm	40.4	42.1	117.6	126.4
Average price, RUB per mcm <sup>(2)</sup> (net of VAT)	4,111.1	4,020.3	4 156.8	4,100.8
<i>Total gas sales</i>				
Gross sales (net of VAT)	593,266	980,563	1,565,369	2,527,650
Customs duties	(76,375)	(139,275)	(168,551)	(363,524)
Excise tax	(1,994)	(13,526)	(12,553)	(32,541)
Retroactive gas price adjustments	6,086	8,009	2,324	8,009
Net sales	520,983	835,771	1,386,589	2,139,594
Volumes in bcm	92.6	104.5	230.7	263.4
Net sales of refined products (net of excise tax, VAT and customs duties)	347,894	536,462	820,853	1,043,371
Net sales of crude oil and gas condensate (net of VAT and customs duties)	91,189	192,558	212,050	382,947
Electric and heat energy net sales (net of VAT)	94,157	104,482	252,240	277,895
Gas transportation net sales (net of VAT)	53,203	54,653	109,290	110,154
Other sales (net of VAT)	55,890	61,004	122,126	122,790
<b>Total sales (net of excise tax, VAT and customs duties)</b>	<b>1,163,316</b>	<b>1,784,930</b>	<b>2,903,148</b>	<b>4,076,751</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> One mcm is equivalent to 35,316 cubic feet.

<sup>(3)</sup> Calculated on the basis of average exchange rate between the RUB and US Dollar.

Total sales (net of excise tax, VAT and customs duties) decreased by RUB 1,173,603 million, or 29 %, to RUB 2,903,148 million for the six months ended June 30, 2020 compared to the same period of the prior year.

Net sales of gas accounted for 48 % of total net sales for the six months ended June 30, 2020 (52 % for the same period of the prior year).

Net sales of gas decreased by RUB 753,005 million, or 35 %, from RUB 2,139,594 million for the six months ended June 30, 2019 to RUB 1,386,589 million for the six months ended June 30, 2020.

Net sales of gas to Europe and other countries decreased by RUB 677,312 million, or 47 %, to RUB 756,279 million for the six months ended June 30, 2020 compared to the same period of the prior year. The change was due to the decrease in average prices (including excise tax and customs duties) denominated in the Russian Ruble by 38 % and the decrease in volumes of gas sold by 17 % for the six months ended June 30, 2020 compared to the same period of the prior year. At the same time average prices denominated in US Dollar decreased by 42 % compared to the same period of the prior year.

Net sales of gas to Former Soviet Union countries decreased by RUB 40,455 million or 23 %, to RUB 139,283 million for the six months ended June 30, 2020 compared to the same period of the prior year. The change was due to the decrease in volumes of gas sold by 22 % and the decrease in average prices (including customs duties) denominated in the Russian Ruble by 8 % for the six months ended June 30, 2020 compared to the same period of the prior year. At the same time average prices denominated in US Dollar decreased by 14 % compared to the same period of the prior year.

Net sales of gas in the Russian Federation decreased by RUB 29,553 million, or 6 %, to RUB 488,703 million for the six months ended June 30, 2020 compared to the same period of the prior year. This change was explained by the decrease in volumes of gas sold by 7 %, which was partially compensated by the increase in average prices in the Russian Ruble (net of VAT) by 1 %.

Net sales of refined products (net of excise tax, VAT and customs duties) decreased by RUB 222,518 million, or 21 %, to RUB 820,853 million for the six months ended June 30, 2020 compared to the same period of the prior year. The decrease in net sales of refined products was mainly due to a decrease in average prices denominated in the Russian Ruble in all geographic segments.

Net sales of crude oil and gas condensate (net of VAT and customs duties) decreased by RUB 170,897 million, or 45 %, to RUB 212,050 million for the six months ended June 30, 2020 compared to the same period of the prior year. The change was mainly due to a decrease in net sales of crude oil primarily caused by a decrease in average prices of crude oil.

## Operating expenses

Operating expenses decreased by RUB 503,430 million, or 16 %, to RUB 2,693,257 million for the six months ended June 30, 2020 compared to RUB 3,196,687 million for the same period of the prior year. Operating expenses as a percentage of sales increased from 78 % for the six months ended June 30, 2019 to 93 % for the six months ended June 30, 2020. The table below presents a breakdown of operating expenses in each period:

(in RUB million)	Three months ended June 30,		Six months ended June 30,	
	2020	2019	2020	2019
Taxes other than on profit	271,643	357,204	617,679	733,509
Purchased gas and oil	162,406	325,917	441,522	729,779
Staff costs	207,530	194,315	414,587	381,134
Depreciation	197,327	175,223	396,891	347,875
Transit of gas, oil and refined products	158,519	167,351	312,423	336,053
Materials	53,424	83,550	110,350	147,393
Goods for resale, including refined products	33,940	69,780	85,046	125,846
Electricity and heating	24,788	23,948	56,283	57,144
Repairs and maintenance	30,633	35,294	49,016	53,361
Insurance	8,514	7,955	17,200	15,477
Social expenses	8,840	9,522	16,106	16,315
Impairment loss (reversal of impairment loss) on non-financial assets	149	(351)	14,200	1,802
Transportation expenses	6,547	3,446	14,024	9,714
Processing services	4,611	5,129	10,341	10,496
Research and development	4,360	4,152	9,301	9,367
Lease	4,574	5,581	8,548	12,884
Derivatives (gain) loss	(1,344)	2,987	(1,798)	10,051
Foreign exchange differences on operating items	52,125	4,139	(63,459)	51,390
Other	79,290	80,605	170,463	219,217
	<b>1,307,876</b>	<b>1,555,747</b>	<b>2,678,723</b>	<b>3,268,807</b>
Change in balances of finished goods, work in progress and other effects	<u>(54,320)</u>	<u>(141,276)</u>	<u>14,534</u>	<u>(72,120)</u>
<b>Total operating expenses</b>	<b>1,253,556</b>	<b>1,414,471</b>	<b>2,693,257</b>	<b>3,196,687</b>

### Taxes other than on profit

Taxes other than on profit consist of:

(in RUB million)	Three months ended June 30,		Six months ended June 30,	
	2020	2019	2020	2019
Mineral extraction tax	152,804	289,795	389,444	589,467
Excise tax	74,388	19,443	130,676	53,850
Property tax	39,235	37,681	78,810	74,749
Other taxes	5,216	10,285	18,749	15,443
<b>Total taxes other than on profit</b>	<b>271,643</b>	<b>357,204</b>	<b>617,679</b>	<b>733,509</b>

Expenses for taxes other than on profit decreased by RUB 115,830 million, or 16 %, to RUB 617,679 million for the six months ended June 30, 2020 compared to RUB 733,509 million for the same period of the prior year. The change was mainly due to a decrease in the mineral extraction tax expenses that was partially compensated by an increase in the excise tax expenses.

Mineral extraction tax (MET) expenses decreased by RUB 200,023 million or 34 % to RUB 389,444 million for the six months ended June 30, 2020 compared to RUB 589,467 million for the same period of the prior year. MET expenses decreased mainly due to a decrease in oil prices and a decrease in volumes of gas production for the six months ended June 30, 2020 compared to the same period of the prior year.

Excise tax expenses increased by RUB 76,826 million, or 143 %, to RUB 130,676 million for the six months ended June 30, 2020 compared to RUB 53,850 million for the same period of the prior year. Excise taxes expenses increased mainly due to the impact of the dampfer component, resulting from the reduction in export-parity prices for automobile gasoline and diesel fuel on the external market, arising from the lower oil price and the worsening epidemiological situation.

### Purchased gas and oil

Cost of purchased gas and oil decreased by RUB 288,257 million, or 39 %, to RUB 441,522 million for the six months ended June 30, 2020 compared to RUB 729,779 million for the same period of the prior year.

Cost of purchased gas included in the cost of purchased gas and oil decreased by RUB 163,899 million, or 34 %, to RUB 323,839 million for the six months ended June 30, 2020 compared to RUB 487,738 million for the same period of the prior year. The change was mainly due to a decrease in average prices and a decrease in volumes of purchased gas.

Cost of purchased oil included in the cost of purchased gas and oil decreased by RUB 124,358 million, or 51 %, to RUB 117,683 million for the six months ended June 30, 2020 compared to RUB 242,041 million for the same period of the prior year. The change was mainly due to a decrease in prices of oil and volumes of purchased oil.

#### *Depreciation*

Depreciation increased by RUB 49,016 million, or 14 %, to RUB 396,891 million for the six months ended June 30, 2020 compared to RUB 347,875 million for the same period of the prior year. The increase was mainly due to an increase in the fixed asset base.

#### *Goods for resale, including refined products*

Cost of goods for resale, including refined products decreased by RUB 40,800 million, or 32 %, to RUB 85,046 million for the six months ended June 30, 2020 compared to RUB 125,846 million for the same period of the prior year. The decrease in cost was mainly due to a decrease in prices and volumes of refined products purchases in domestic and international markets.

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

The foreign exchange gain on operating items amounted to RUB 63,459 million for the six months ended June 30, 2020 compared to the foreign exchange loss in the amount of RUB 51,390 million for the same period of the prior year. This change was mainly due to the revaluation of accounts receivable from foreign customers and loans issued, which was caused by the appreciation of the US Dollar and the Euro against the Russian Ruble by 13 % for the six months ended June 30, 2020 compared to the depreciation of the US Dollar and the Euro against the Russian Ruble by 9 % and 10 %, respectively, for the same period of the prior year.

#### *Other operating expenses*

Other operating expenses decreased by RUB 48,754 million, or 22 %, to RUB 170,463 million for the six months ended June 30, 2020 compared to RUB 219,217 million for the same period of the prior year. Other expenses include gas and gas condensate production expenses, services from gas distribution companies, bank charges, security services, legal and consulting services, charity and financial aid and advertising.

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

The positive amount on the line item Change in balances of finished goods, work in progress and other effects amounted to RUB 14,534 million for the six months ended June 30, 2020 compared to the negative amount of RUB 72,120 million for the same period of the prior year. The change in this line item was mainly due to a decrease in the balances of finished goods for the six months ended June 30, 2020 compared to an increase in the balances of finished goods for the same period of the prior year.

#### **Impairment loss on financial assets**

Impairment loss on financial assets decreased by RUB 32,227 million, or 48 %, to RUB 34,344 million for the six months ended June 30, 2020 compared to RUB 66,571 million for the same period of the prior year. The decrease was mainly due to the termination of the accrual of the allowance for expected credit losses on accounts receivable due from NJSC Naftogaz of Ukraine as a result of the settlement of mutual debts in accordance with the agreement between NJSC Naftogaz of Ukraine and PJSC Gazprom.

#### **Operating profit**

As a result of the factors discussed above, operating profit decreased by RUB 590,893 million, or 76 %, to RUB 189,985 million for the six months ended June 30, 2020 compared to RUB 780,878 million for the same period of the prior year. The operating profit margin decreased from 19 % for the six months ended June 30, 2019 to 7 % for the six months ended June 30, 2020.

## Net finance (expense) income

(in RUB million)	Three months ended June 30,		Six months ended June 30,	
	2020	2019	2020	2019
Foreign exchange gain	307,175	70,848	421,799	305,451
Foreign exchange loss	(40,887)	(36,346)	(706,907)	(86,964)
Net foreign exchange (loss) gain	266,288	34,502	(285,108)	218,487
Interest income	17,211	24,567	37,553	48,187
Interest expense	(17,127)	(19,156)	(34,077)	(37,529)
<b>Net finance (expense) income</b>	<b>266,372</b>	<b>39,913</b>	<b>(281,632)</b>	<b>229,145</b>

The net foreign exchange loss amounted to RUB 285,108 million for the six months ended June 30, 2020 compared to the net foreign exchange gain of RUB 218,487 million for the same period of the prior year. The change was explained by the appreciation of US Dollar and Euro against the Russian Ruble by 13 % for the six months ended June 30, 2020 and the depreciation of US Dollar and Euro against the Russian Ruble by 9 % and 10 % respectively for the same period of the prior year. The loss and the gain were mainly related to the revaluation of loans and borrowings denominated in foreign currencies.

Interest income decreased by RUB 10,634 million, or 22 %, to RUB 37,553 million for the six months ended June 30, 2020 compared to RUB 48,187 million for the same period of the prior year.

Interest expense decreased by RUB 3,452 million, or 9 %, to RUB 34,077 million for the six months ended June 30, 2020 compared to RUB 37,529 million for the same period of the prior year.

## Share of profit of associates and joint ventures

Share of profit of associates and joint ventures decreased by RUB 40,414 million, or 35 %, to RUB 74,841 million for the six months ended June 30, 2020 compared to RUB 115,255 million for the same period of the prior year. This change was mainly explained by a share of loss of PJSC NGK Slavneft and its subsidiaries for the six months ended 30 June 2020, as well as a decrease in a share of profit of JSC Messoyakhaneftegaz, Sakhalin Energy Investment Company Ltd. and JSC Arcticgas compared to a share of profit for the same period of the prior year.

## Profit for the period attributable to the owners of PJSC Gazprom

As a result of the factors discussed above, profit attributable to the owners of PJSC Gazprom amounted to RUB 32,919 million for the six months ended June 30, 2020.

## Liquidity and capital resources

The following table summarises the cash flows for the six months ended June 30, 2020 and for the six months ended June 30, 2019:

(in RUB million)	Six months ended June 30,	
	2020	2019
Net cash from operating activities	759,651	1,256,653
Net cash used in investing activities	(858,971)	(958,604)
Net cash from financing activities	86,404	71,326

### *Net cash from operating activities*

Net cash from operating activities decreased by RUB 497,002 million, or 40 %, to RUB 759,651 million for the six months ended June 30, 2020 compared to RUB 1,256,653 million for the same period of the prior year. This change was mainly driven by a decrease in cash flow from operating activities before working capital changes for the six months ended June 30, 2020 compared to the same period of the prior year.

### *Net cash used in investing activities*

Net cash used in investing activities decreased by RUB 99,633 million, or 10 %, to RUB 858,971 million for the six months ended June 30, 2020 compared to RUB 958,604 million for the same period of the prior year. The change was mainly due to a decrease in loans issued for the six months ended June 30, 2020 compared to the same period of the prior year.

### *Net cash from financing activities*

Net cash from financing activities increased by RUB 15,078 million, or 21 %, to RUB 86,404 million for the six months ended June 30, 2020 compared to RUB 71,326 million for the same period of the prior year. This change was mainly due to an increase in proceeds from long-term borrowings compared to the same period of the prior year.

### **Capital expenditures**

Total capital expenditures (excluding the effect of acquisitions of subsidiaries) by segments for the six months ended June 30, 2020 and for the six months ended June 30, 2019 denominated in the Russian Ruble are presented in the following table:

(in RUB million)	Six months ended June 30,	
	2020	2019
Production of crude oil and gas condensate	176,482	118,150
Refining	147,517	147,831
Production of gas	89,293	97,292
Transportation of gas	81,927	191,304
Electric and heat energy generation and sales	40,201	26,144
Distribution of gas	5,313	8,233
Gas storage	3,072	5,655
All other segments	<u>32,085</u>	<u>62,573</u>
<b>Total</b>	<b>575,890</b>	<b>657,182</b>

Total capital expenditures decreased by RUB 81,292 million, or 12 %, from RUB 657,182 million for the six months ended June 30, 2019 to RUB 575,890 million for the six months ended June 30, 2020.

The largest portion of capital expenditures refers to the Production of crude oil and gas condensate segment. The amount of capital expenditures of the Production of crude oil and gas condensate segment increased by RUB 58,332 million, or 49 %, to RUB 176,482 million for the six months ended June 30, 2020, mainly due to the investment programme implementation at new oil fields by Gazprom Neft Group entities.

The amount of capital expenditures of the Transportation of gas segment decreased by RUB 109,377 million, or 57 %, to RUB 81,927 million for the six months ended June 30, 2020, mainly due to the completion of most part of works on the construction of the TurkStream and Nord Stream 2 gas pipelines as well as putting the Power of Siberia gas pipeline into operation in the end of 2019.

### **Debts obligation**

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) increased by RUB 516,317 million, or 16 %, from RUB 3,167,847 million as of December 31, 2019 to RUB 3,684,164 million as of June 30, 2020. This change was mainly due to an increase in the amount of long-term borrowings denominated in the Russian Ruble caused by the appreciation of US Dollar and Euro against the Russian Ruble.