Shorthand record of speech by Famil Sadygov, Deputy Chairman of Gazprom Management Committee, at Gazprom's Investor Day

Let us consider the financial and economic performance of the Gazprom Group.

As noted by my colleagues, 2020 saw a "perfect storm" in the global energy commodity markets. It peaked in the period from April through June, for reasons that are well-known.

Firstly, it was caused by lockdowns and other restrictions imposed due to the COVID-19 pandemic, which led to lower demand for natural gas and oil. Sometimes, the demand was abnormally low.

Secondly, the pandemic was further aggravated by discrepancies between the participants in the OPEC+ agreement as to how the deal could be extended. In late March 2020, after the previous terms of the agreement expired, oil production went up. Hence, the global energy commodity prices dropped to record lows.

Thirdly, the winter of 2019–2020 was abnormally warm. The average ambient temperature in Europe was 3 degrees above the average figures for the last half-century. Understandably, this constrained the demand for gas in Europe. In turn, lower demand resulted in overstretched gas storage capacities: in March 2020, Europe's underground gas storage facilities were 60 per cent full. In the last five years, the average numbers for March never exceeded 38 per cent.

Fourthly, LNG producers had to continue with their supplies, even incurring significant losses. This exacerbated the oversupply of gas in the European market.

As a result, European gas hub prices plummeted in the first half of 2020. In May, they were at their lowest since 1995. The minimum price stood at less than USD 1 per MBTU, i.e. less than USD 30 per 1,000 cubic meters. This price was more than four times lower than that at the start of 2020.

These extraordinary circumstances became an extremely challenging stress test for Gazprom's financial position. We can now say that we passed this stress test admirably thanks to, first and foremost, our conservative financial policy. I would like to remind you that Gazprom's budget for 2020 was shaped so as to include a significant reserve fund of almost RUB 700 billion. This liquidity cushion allowed us to finance all of the Company's liabilities without any additional measures to adjust the budget.

However, we understood how acute the situation was. Throughout the year, we analyzed our income and expenditures on a monthly basis line by line, and we updated the budget not only for the head company but also for the subholding companies, in particular Gazprom Neft, Gazprom Energoholding, and Gazprom Mezhregiongaz. The budgets of all our subsidiaries underwent regular control with a strict focus on cost optimization. This approach has brought specific positive results in the crisis environment and laid the foundation to improve the efficiency of our budgeting process in the long term.

In 2020, Gazprom continued to centralize its cash flows and liquidity. As of the end of 2020, the single cash pooling system included as many as 583 companies of the Group. The total consolidated liquidity exceeded RUB 720 billion. The unified settlement center and the single cash pooling system of the Gazprom Group allowed us to distribute the cash flows efficiently and reduce the external borrowings of subsidiaries. This was achieved thanks to intra-Group financing. In 2020, its volume went up nearly five times and reached more than RUB 48 billion.

Another effective instrument in our work has been the banking support for the Group's contracts. The full-fledged implementation of this instrument has allowed us to efficiently control the expenses under the Gazprom Group's contracts with external counterparties.

While all these actions and instruments were important, our primary response to the external challenges was a major reduction in operating and capital expenditures. I am going to elaborate on that.

The Gazprom Group's operating expenses in 2019 totaled USD 99 billion. In 2020, they went down to USD 79 billion. The difference is 20 per cent.

In the course of cutting costs, it was important for us to prevent disruptions in our production plans and to maintain the reliability of gas supplies to our consumers. We made substantial savings by optimizing oil and gas procurements. We reduced the costs for geological exploration, heat supplies, and a wide range of administrative and managerial cost items. The scope of the cost optimization program did not include the protected expense groups: taxes, payroll, social payments, insurance, and pandemic-related expenses.

In addition, the free cash flow was supported to a great degree by the optimization of capital expenditures. Across the Gazprom Group, they went down by 27 per cent: from USD 27 billion in 2019 to USD 20 billion in 2020. The biggest reduction was achieved in the gas business – over USD 4 billion. We reduced the capital expenditures across a broad spectrum of projects. This optimization, however, did not affect the timelines of the key projects.

Currently, we are aiming for the so-called "cautious recovery scenario." We continue optimizing operating and capital expenditures. When shaping the budget for 2021, we set the limits based on the cost savings achieved last year.

Even with the cost-saving measures in place, the extraordinary drop in gas prices in the first half of the year had predictably negative outcomes: the Group's EBITDA went down, taking the net debt/EBITDA ratio out of the comfort zone. At the end of 2020, the ratio stood at 2.6. Throughout the year, there was a real threat of the net debt/EBITDA ratio growing well over 3. We took a number of preventive measures to curb that threat.

We managed to minimize the reduction of our EBITDA. To achieve that, firstly, we systematically cut costs, as I have already explained. Secondly, we increased our gas exports in the improved pricing environment of the second half of 2020. While EBITDA went down for every company in the oil and gas industry, our losses were 17 p.p. lower than the industry average.

We reduced traditional loans and borrowings by RUB 129 billion as compared to our original plans.

In October 2020, Gazprom became the first company in the CIS to place perpetual Eurobonds. Please be reminded that, according to IFRS rules, funds attracted with this instrument do not increase the Company's debt burden but are counted as equity to the full extent. We issued USD 1.4 billion and EUR 1 billion worth of perpetual Eurobonds. This is one-third of the total amount envisaged by the head company's Borrowing Program.

In March 2021, the Bank of Russia registered an issue of perpetual ruble bonds in the amount of up to RUB 150 billion. Their purpose is to finance the Gas Infrastructure Expansion Program. The issuance of such bonds is supported by the government through coupon payments.

Efforts for attracting project financing were intensified. In August 2020, we closed a project financing deal for the second phase of development of the Yuzhno-Russkoye field in the amount of RUB 40 billion.

In the future, we plan to use this form of financing in developing both our own fields and the fields where we have strategic partners: Semakovskoye with RusGazDobycha, Layavozhskoye and Vaneyvisskoye with LUKOIL, and Urengoyskoye with Wintershall Dea. In 2022, we plan to attract project financing for the gas processing complex in Ust-Luga.

The diversification of financing sources allows us to reduce the burden on the Company's balance sheet. Based on this, we expect that in 2021 the net debt/EBITDA ratio will drop to a comfortable level below 2 points.

The measures taken by Gazprom amid the "perfect storm" in the natural gas market proved to be effective. This is borne out by the stability of our credit ratings and positive reviews from stock market analysts. Throughout 2020, all international and Russian rating agencies either confirmed Gazprom's credit rating or left it unchanged.

As a point of comparison with the general situation in the oil and gas market: last year, 36 per cent of the world's oil and gas companies saw their credit ratings go down, and another 27 per cent of companies had their outlooks revised downward. This shows that rating agencies gave a positive assessment of Gazprom's financial stability even in the crisis period.

The equity market was equally positive: Gazprom's shares remained attractive in 2020. Over 75 per cent of investment analysts recommend to buy Gazprom's shares. In late 2019, similar recommendations stood at 58 per cent. Please note that there are no recommendations to sell Gazprom's shares at the moment.

Finally, it should be said that Gazprom consistently holds leading positions among the 22 companies listed in the MSCI Index. The Company has a relative weight of some 17.5 per cent in the index.

In 2019, the Gazprom Board of Directors approved a new Dividend Policy. The Policy aims to raise the income of our shareholders and gradually increase the dividend payouts to the level of 50 per cent of the net profit under IFRS.

We have already discussed the macroeconomic and pricing environment of 2020. I would like to add that in the current circumstances some 60 per cent of international oil and gas majors have announced that they are reducing or completely cancelling their dividend payouts. About 90 per cent of these companies cancelled or reduced their buyback programs.

The aggregate amount of shareholder payouts among international oil and gas companies has dropped by 25 per cent.

With this in mind, Gazprom's management decided not to adjust the net profit downward in 2020 and instead to allocate 30 per cent of the total net profit for the dividend payout. This translates into about 36 per cent of the adjusted net profit received in 2019. As a result, we paid out RUB 361 billion in dividends in 2020, thereby fulfilling and even exceeding our commitments under the announced Dividend Policy. Gazprom became a leader in dividend payments among Russian public companies.

The measures we took to improve our financial performance and the positive dynamics of Gazprom's operational indicators were consonant with the recovery in the pricing environment of gas and oil markets in the second half of 2020. Thus, in the second half of the year we managed to offset the losses incurred due to price drops in the beginning of the year and, crucially, to go back to the pre-crisis levels in terms of export volumes.

Our final results for 2020 turned out to be better than the main parameters of the adjusted budget and the expectations of most analysts. Our revenue stood at USD 88 billion and EBITDA at USD 20.4 billion. These results allowed us to finance all of our planned projects. We also managed to maintain a comfortable liquidity position: the total amount of deposits and cash at year's end was USD 14.2 billion. This exceeds the planned amount of our debt payments for the coming year by 1.5 times.

The largest contribution to the Group's results was made by the gas business, which brought USD 53 billion in revenue and USD 10.1 billion in EBITDA. The second most important segment of the Gazprom Group – the oil business – generated USD 5.8 billion in EBITDA.

In last year's highly volatile conditions, the power generation segment of our business played a major role as well, providing for stable EBITDA of USD 1.5 billion and a positive free cash flow of more than USD 400 million.

Clearly, it was impossible to avoid a decline in key financial indicators in 2020. It should be noted, however, that the rates of decline in Gazprom's revenue and EBITDA were more moderate than the average rates for oil and gas majors. This dynamic was brought on by the strong competitive advantages of Gazprom, the timely measures to improve the financials, and the well-balanced structure of the Group's business.

In the third and fourth quarters of 2020, the market environment improved substantially. Nonetheless, we maintained a conservative approach to budgeting for 2021 and continued putting strict limits on operating and capital expenditures.

The Company's budget for the current year is based on conservative assumptions. They appear quite modest against the current export prices. Even with these assumptions, we expect significant growth in our financial indicators:

- the Group's revenue growing by 16 per cent;
- EBITDA growing by 9 per cent;
- the free cash flow going back to positive levels;
- the liquidity cushion growing and the debt burden decreasing.

The head company's investment program for 2021 remains at the relatively low level of RUB 902 billion. The Group's overall capital investments will be slightly higher than in 2020, standing at about RUB 1.5 trillion. This increase is related to the enhanced scope of gas infrastructure expansion programs performed by Gazprom Mezhregiongaz in Russian regions.

The first three months of 2021 showed a marked improvement in the oil and gas markets. We conducted a thorough analysis of our budget implementation in these three months and updated our forecasts for the full year accordingly.

Based on the current market situation, we expect the Gazprom Group's financials to grow significantly and go back to the pre-crisis levels, namely:

- the growth in EBITDA against 2020 may exceed 50 per cent as compared to the conservative estimate of 9 per cent;
- the growth in net profit will, naturally, cause the dividend base to increase;
- control of the capital investments will ensure that the free cash flow will go back to positive levels. The free cash flow can be expected to cover the dividend payments based on the results of 2020;
- control of the debt burden will bring the net debt/EBITDA ratio back to a comfortable level below 2 points. The long-term baseline for us is the range from 1 to 2 points;
- growing income will allow us to reduce our borrowings by over RUB 100 billion compared to the 2021 budget.

The positive forecast of free cash flows for 2021 allowed the Management Committee to recommend that the dividend payout make up as much as 50 per cent of the adjusted net profit based on the results of 2020. Therefore, we are one year ahead of schedule in achieving the targets set in the Dividend Policy. This once again proves that the growth in dividend yield is a priority for Gazprom's management.

The decrease in net profit in 2020 was largely driven by non-monetary factors such as foreign exchange losses on financial items in the amount of RUB 605 billion. Under the Dividend Policy, net profit is adjusted with regard to non-monetary items. As a result, the dividend base for 2020 was considerably bigger than the amount of net profit, totaling RUB 595 billion. Half of that amount – RUB 297 billion – will be paid as dividends. The final recommendation on the amount of dividends for 2020 will be made by the Board of Directors in May.

Starting the following year based on the results of 2021, the 50 per cent level is going to be the minimum threshold for us. We also intend to have the dividend payments fully covered by the free cash flow.

It is important to note that Gazprom is committed to sustainable development principles. Among our priorities are environmental care and safety working conditions. These priorities are already well-integrated into our corporate governance system. For instance, we have medium-term and short-term goals to reduce emissions, which we successfully achieve every year thanks to the planned measures we undertake. The carbon footprint of gas production at Gazprom is among the lowest in the oil and gas industry.

Our efforts to preserve the climate are reflected in ESG ratings. Gazprom is the leader in the Russian fuel and energy complex according to the highly respected CDP rating.

In order to achieve the strategic goals in the area of sustainable development, we have devised the eponymous Policy, which will soon be submitted for approval to the Board of Directors. We have also launched a project to draft scenarios of low-carbon development through to 2050.

Our next steps include establishing a Sustainable Development Committee under the Board of Directors and appointing a senior independent director.

As noted by my colleagues today, the European gas market has recovered after the shocks it experienced in the first half of 2020. This is clearly demonstrated by the gas price charts for the last nine months.

Given the visible improvement in the market environment, many investment analysts note that Gazprom's share prices have significant upside potential. We firmly believe that, as the external markets improve, the investment attractiveness of Gazprom will be reflected in its market capitalization.

To conclude my presentation, I would like to once again stress that growth in shareholder value is an absolute priority for the Company's management. We expect Gazprom's shares to fulfill their growth potential. Our optimism stems from objective circumstances.

Firstly, Gazprom has strong and fundamental competitive advantages, which we fully demonstrated in the crisis year of 2020.

Secondly, improved environment in the oil and gas markets coupled with expected growth in the Gazprom Group's income have not been fully reflected in the Company's share prices as of yet.

Thirdly, Gazprom's activities are underpinned by sustainable development principles. Every year, we intensify our efforts for environmental protection, industrial safety, social responsibility, and quality of corporate governance.

Fourthly, our long-term strategy provides for well-balanced business development based on our key competencies.

And fifthly, we strive to ensure that our shareholder return keeps growing while maintaining financial stability by generating a positive free cash flow.

Thank you for your attention.