

Report of the Supervisory Board

The Supervisory Board is responsible for supervising and advising the Management Board and overseeing the Company's general course of affairs, strategy and operational performance. In performing its duties, the Supervisory Board acts in accordance with the interests of the Company and

its affiliated businesses, taking into consideration the overall good of the Company and the relevant interests of all its stakeholders. In X5's two-tier corporate structure under Dutch law, the Supervisory Board is a separate body operating fully independently of the Management Board.

Composition and profile of the Supervisory Board

X5's Supervisory Board currently consists of eight members, with a majority of five independent members. On an ongoing basis, the Supervisory Board reviews the profile of its size and (future) composition, as well as its rotation schedule, taking into account the evolving nature of X5's business and activities and the desired expertise and background of the members of the Supervisory Board. The Supervisory Board profile is published on X5's corporate website.

The composition of the Supervisory Board changed substantially in 2018. Christian Couvreur stepped down from the Supervisory Board at the 2018 Annual General Meeting of Shareholders, having served two terms in office since 2010. In June, Pawel Musial resigned as a member of the Supervisory Board, having served in this capacity for nearly five years. The Supervisory Board expresses its profound gratitude for the significant contribution of both Christian and Pawel to the development of X5 during an important time of transformation, when the Company regained market leadership by making customers, stores and growth its key priorities.

In order to fill these vacancies, and mindful of the profile of the Supervisory Board, the Supervisory Board nominated Karl-Heinz Holland and Nadia Shouraboura as independent members of the Supervisory Board. Both of the new members were nominated based on their extensive experience as leading retail industry professionals. As former CEO of Lidl Group, Karl Heinz Holland has wide-ranging expertise in European retail and a track record of establishing Lidl as a powerhouse in European food retail,

while Nadia Shouraboura's nine years at Amazon provided her with extensive experience in the development of innovative concepts for modern retail as well as technology- and data-driven solutions for consumers. Both nominees were appointed by the General Meeting of Shareholders on 30 August 2018.

Upon the appointment of Karl-Heinz Holland and Nadia Shouraboura, the Supervisory Board continued to reflect on the need to strengthen its expertise in the area of technical and commercial innovation. This resulted in the nomination of Alexander Torbakhov on 25 January 2019 in view of his extensive experience in digital transformation processes, most recently as Deputy Chairman of the Executive Board of Sberbank. Subject to his appointment by the 2019 Annual General Meeting of Shareholders, X5's Supervisory Board will consist of nine members, with a majority of six independent members.

In accordance with the retirement and reappointment schedule of the Supervisory Board, the terms of Stephan DuCharme, Geoff King, Petr Demchenkov and Michael Kuchment will expire in 2019. All four Board members are eligible for reappointment.

Finally, in line with governance best practice, the Supervisory Board approved the appointment of Peter Demchenkov as Vice-Chairman of the Supervisory Board as of March 2019.

An overview of the current composition of the Supervisory Board and a short biography of each member is presented in the Corporate Governance Report on pages 212-213.

Composition of the committees

While retaining overall responsibility, the Supervisory Board assigns certain tasks to four committees: the Audit and Risk Committee, the Nomination and Remuneration Committee, a newly created Innovation and Technology Committee and the Related-Party Committee.

Upon the appointment of Nadia Shouraboura and Karl-Heinz Holland in August, the latter became a member of the Audit and Risk Committee and the Nomination and Remuneration Committee, while the former took over Michael Kuchment's position as a member of the Related-Party Committee.

In 2018, the Supervisory Board resolved to rename the Audit Committee the Audit and Risk Committee in order to reflect the significant element of the Committee's risk oversight.

The Innovation and Technology Committee was established in January 2019 to strengthen the focus of the Supervisory Board on technical and commercial innovation and to address the disruption that increasingly characterises retail across many geographies. The members of the committee are Nadia Shouraboura, Michael Kuchment and, subject to his appointment by the 2019 Annual General Meeting of Shareholders, Alexander Torbakhov, who was nominated by the Supervisory Board in January 2019.

An overview of the current composition of the committees is presented in the Corporate Governance Report.

Induction and ongoing education

Induction and ongoing education are key elements of good governance. Following their appointment, new Supervisory Board members go through X5's strategic, financial, legal and reporting affairs with senior Company executives. In addition, prior to their appointment, they are invited to meetings of the Supervisory Board and its committees. On an ongoing basis, and together with members of senior management, members of the Supervisory Board visit stores and distribution centres to expand their knowledge of local operations, opportunities and challenges.

As part of the follow-up measures to the 2017 Supervisory Board assessment, the Board critically reviewed and improved

the induction process for its new members, also in view of the changes made to the composition of the Supervisory Board in 2018. In addition, the Supervisory Board launched a tailored peer group networking programme for its Chairman and committee Chairs to create a targeted network of experienced non-executive directors as a source of best practice and informal learning. As an additional source of informal learning, guest speakers with expert knowledge of topics that are of particular relevance to the Company and the Board were invited to plenary Board meetings as a matter of standard practice going forward. The Supervisory Board remains committed to the ongoing education of its members in order to comply with the highest standards of excellence and governance.

Meetings of the Supervisory Board

In 2018, the Supervisory Board held four regular meetings and one meeting by conference call. In addition, resolutions in writing were taken when necessary during the year. For each of the four meetings in 2018, the Supervisory Board meeting was preceded by meetings of the Audit and Risk Committee and the Nomination and Remuneration Committee. The Related-Party Committee convened throughout the year if and when necessary.

The plenary Supervisory Board meetings in June, September and December included a half-day strategy session, thus ensuring sufficient time for meetings and discussions on specific topics, such as operational performance, strategy and management development. The CEO attended all meetings, and the CFO and other members of senior management were regularly invited to present. In 2018, the Supervisory Board held regular private sessions without members of the Management Board present to independently discuss matters related to the

performance, functioning and development of members of the Executive Board. The external auditor attended the meeting in March at which the 2017 Annual Report and financial statements were recommended for adoption by the Annual General Meeting of Shareholders. In between the Supervisory Board meetings, several informal meetings and telephone calls took place among Supervisory Board members and members of the Management Board and other Company management to consult with each other on various topics and to ensure that the Supervisory Board remains well informed about the running of the Company's operations.

The Supervisory Board confirms that all Supervisory Board members have adequate time available to give sufficient attention to the concerns of the Company. In 2018, the attendance rate was 100% for both the Supervisory Board and the committee meetings.

Activities in 2018

In 2018, the Supervisory Board reviewed various matters related to all significant aspects of the Company, its activities and operational results, strategy going forward and the management team and its development.

Throughout the year, the Board continued to monitor the implementation of X5's corporate strategy, with a focus on long-term value creation through operational excellence and X5's capacity to adjust to changing customer needs. Against the background of an increasingly competitive environment and challenging macroeconomic conditions as well as technological disruption, the Supervisory Board particularly focused on measures to strengthen X5's current businesses, with specific attention paid to operational efficiencies and improving customer experience through the use of technology and innovation.

As part of its strategic cycle, the Supervisory Board reviewed a progress update of X5's "Strategic Vision 2020" and X5's current and future capability and requirements in terms of organisation, leadership and corporate culture to ensure sustainable growth in the rapidly transforming global retail landscape driven by innovative business concepts and omnichannel retailing.

The Supervisory Board paid specific attention to succession planning and management development in the context of a number of senior executives leaving the Company during the first half of the year. In response, the Supervisory Board, assisted by its Nomination and Remuneration Committee, ensured continuity in X5's leadership team, while simultaneously strengthening the group's executive retention programme. The Supervisory Board is pleased with the important weight of internal promotions as part of the Company's systematic succession planning. The Supervisory Board also reviewed human resource policy at store level, alongside measures to improve staff engagement, recognising that the quality and commitment of staff, supported by simple and efficient end-to-end processes, are key factors in a customer-centric business approach.

As part of the ongoing performance review of the Company's various functions and business divisions, the main topics reviewed and discussed by the Supervisory Board included:

- the leadership strategy for the Pyaterochka retail format, with renewed focus on the assortment and value proposition, human resources, quality of service, operational efficiencies and cost discipline, as well as organisational structure in view of the format's size and geographic span;

- the leadership strategy for the Perekrestok retail format, with ongoing focus on the value proposition and performance of regional stores versus cosmopolitan stores, as well as the growth strategy for the format’s online business;
- the growth strategy for the hypermarket format Karusel, driven by innovative pilot projects to strengthen the format as a distinct brand within X5’s multi-format strategy;
- the private-label strategy and implementation programme for each of the formats.

In addition, throughout the year, the Supervisory Board discussed and/or approved the following (regular) topics:

- the financial reporting process and in particular the approval of the 2017 Annual Report and review of the 2018 half-yearly and quarterly financial reports;
- the agenda and explanatory notes for the Annual General Meeting of Shareholders to be held in May 2018, including the dividend proposal;
- reports by the internal and external auditors;
- impact of the new IFRS 16 accounting standards for lease accounting to be implemented as of 2019;
- the assessment of cooperation with the external auditor, based on a report from the Audit and Risk Committee;
- the regular assessment of the members of the Executive Board, including talent management and succession planning;
- a review of the profile and composition of the Supervisory Board, particularly in the context of the in-depth board evaluation performed by an external evaluator during the autumn of 2017 and the changing composition of the Board in 2018;
- X5’s Group Leadership Diversity Policy, codifying the Company’s commitment to supporting and valuing inclusiveness and diversity, and setting diversity targets in terms of age, skills, background and gender;
- the amendment of the Supervisory Board’s rules of procedure, in line with new Board practices and the revised Dutch Corporate Governance Code that entered into force on 1 January 2017;
- the corporate social responsibility strategy and initiatives;
- updates to X5’s risk landscape and risk appetite, as well as risk mitigation measures and internal controls;
- The annual budget for 2019.

Board evaluation

X5 undertakes an annual review of its Supervisory Board, its committees and its individual members. The evaluation operates on a three-year cycle, with one externally led evaluation followed by two subsequent years of internal evaluations.

Throughout the year, the Supervisory Board reflected on the recommendations from the Board assessment performed by an external party in 2017, with, as key points of attention, enhanced focus on the profile and composition of the Board, making sure that the Board remains “fit for tomorrow”, further emphasis on the induction and development of new and current Board members, and improving the effectiveness of discussions

in the boardroom. With the appointment and nomination of new Supervisory Board members in 2018 and January 2019, and enhanced Board induction and development initiatives as described in this report, the Supervisory Board ensured that it made good progress in its continuous development as a team, that it has a balanced composition that suits the Company in its current life stage, and that it works well together in an open and constructive atmosphere.

The Supervisory Board attaches great value to these evaluations. They ensure continuous focus on the quality of the activities, composition and functioning of the Supervisory Board and its committees and its relationship with the Executive Board.

Meetings of the committees

Audit and Risk Committee

The role of the Audit and Risk Committee is described in its charter, which is available on the Company's website. On 31 December 2018, the Audit and Risk Committee consisted of Geoff King (Chairman), Andrei Elinson and Karl-Heinz Holland. In 2018, the Committee held four meetings in person. Additional meetings were held by conference call when necessary, for instance to review the publication of the half-yearly results. As a rule, all meetings were attended by the CFO, the external auditor and the internal audit director, while the Chairman and CEO were invited to attend all meetings. Other members of the Supervisory Board and senior management were invited when necessary or appropriate. The Committee met once with the external auditor without the presence of management.

In 2018, the Committee focused on, among other things, overseeing the integrity and quality of X5's financial reporting and the effectiveness of the internal risk and control systems. The Committee reviewed the Company's annual and interim financial statements, including non-financial information, the quarterly results and related press releases, as well as the outcomes of the year-end audit. The Committee discussed relevant and new accounting standards, with increased focus on the impact of lease accounting under IFRS 16. Throughout the year, the Committee reviewed the level of financial provisions, key movements in the balance sheet and any contingent liability movements. As part of this review, the Committee paid specific attention to controls and initiatives in the area of working capital management.

Furthermore, the Committee reviewed and approved the audit plans of the internal and external auditors, with a focus on scoping, materiality and key risks. The Committee monitored the progress of the internal and external audit activities, including a review of observations identified as a result of the internal audit activities during the quarter, quarterly procedures performed by the external auditor and the audit performed at year end by the external auditor. The Committee oversaw follow-up by management to the recommendations made in internal and external management letters.

In 2018, the Audit and Risk Committee, together with management, conducted its periodic assessment of the functioning and independence of the external auditor, in line with the Company's Rules on External Auditor Independence and Selection. The results were shared with the current auditors, and actions to further improve optimising the auditor relationship were agreed. The main conclusions of this assessment, including

the proposed external audit fees for the next three-year period, were shared with the Supervisory Board for the purpose of submitting the reappointment of the external auditor to the General Meeting of Shareholders.

Throughout the year, the Committee closely monitored risk management and the risk management process, including the timely follow-up to high-priority actions and risk mitigation measures based on quarterly progress updates. In the context of periodic ethics and compliance updates, the Committee reviewed whistle-blower reports, and dedicated specific attention to economic and political sanctions and their impact on X5's operations. Furthermore, the Committee reviewed activities and initiatives related to detection and prevention of misconduct and irregularities, and risk-mitigating measures to protect the Company in these areas.

The Committee extensively discussed the effectiveness of the internal control framework. Each quarter, the agenda includes a discussion of current control topics, including internal audit findings and the external auditor's reflections on the control framework. These discussions guided management and Internal Audit to focus on the right priorities throughout the year, to mitigate any significant risks or weaknesses and to build a relevant internal audit plan for 2019.

Throughout the year, the Committee continued to review the operational control framework, paying particular attention to stock and fixed assets. Management processes concerning stock-holding and loss levels were examined across all formats. The Committee also closely monitored the effectiveness of the capital investment process, the appraisal methodology and the safeguarding of core assets. Twice during the year, the Committee reviewed an assessment of the level of returns from recent investments, as well as management actions addressing underperforming stores and assets whose carrying value were impaired.

The Audit Committee also discussed other issues, including:

- the external auditor's report with respect to accounting and audit issues and internal control recommendations in respect of their audit of the 2017 consolidated financial statements;
- quarterly interim financial reports and trading updates;
- X5's financing strategy;
- X5's dividend policy;
- tax matters;
- IT infrastructure and data security;
- material legal cases;
- regulatory compliance and changes in legislation, with

ongoing attention to Russian trade law and its proposed amendments on the return of unsold goods to suppliers, effective as of 1 January 2019;

- the effectiveness of the internal audit function and its plans to develop in the coming years;
- non-audit fee payments to the incumbent external auditor, ensuring that the level of expenditure does not exceed the internal Company guideline of 70% of the annual audit fee in any given year.

With respect to the external auditor's management letter about the 2018 financial year, the Audit and Risk Committee confirms that the management letter contained no significant items that need to be mentioned in this report.

Nomination and Remuneration Committee

The role of the Nomination and Remuneration Committee is described in its charter, which is available on the Company's website. On 31 December 2018, the Nomination and Remuneration Committee consisted of Peter Demchenkov (Chairman), Stephan DuCharme, Andrei Elinson and Karl-Heinz Holland. The Nomination and Remuneration Committee held six meetings in 2018, including two meetings held by conference call. The CEO was invited to attend every meeting, and other members of the Supervisory Board and senior management were invited when necessary or appropriate.

In 2018, the Committee's main areas of focus were succession planning for the Supervisory Board and overall succession and management development processes, with specific attention paid to new executive succession planning following changes in the management team during the first half of the year. Also, as part of an in-depth analysis of corporate culture, the Committee reviewed measures to increase employee engagement, recognising that the quality and commitment of staff, supported by simple and efficient end-to-end processes, are key factors in a customer-centric business approach. In this context, the Committee also discussed the Company's approach to the level and structure of compensation for personnel other than members of the Executive Board, with a focus on operational and store personnel.

The Committee was also involved in organisational and governance matters in relation to the Company's multi-format operating model and strategic objectives. In this context, the Committee reflected on headcount and cost discipline at the central level, aiming to strike the right balance between the Group's decentralised operating model and the role and size of the Group's Corporate Centre as a platform for performing unique functions in support of the three formats. The Committee also reviewed and made recommendations in respect of the Group's central leadership and direct reports structure.

In terms of remuneration, the Committee reviewed adjustments within the total remuneration package of the members of the Executive Board based on a base salary benchmarking analysis, in combination with the introduction of a new long-term incentive plan designed to create greater balance between short- and long-term compensation.

The Nomination and Remuneration Committee further reviewed and prepared the following items for recommendation or report to the full Supervisory Board, as part of its ongoing responsibilities:

- the annual assessment of the Management Board and Executive Board and its individual members;
- performance measures, targets and remuneration of individual members of the Executive Board;
- changes in the composition of the Executive Board, including the appointment of Sergey Goncharov as General Director of Pyaterochka and Vladislav Kurbatov as General Director of Perekrestok;
- the profile and composition of the Supervisory Board, including the nominations of Karl-Heinz Holland and Nadia Shouraboura, who were appointed as new Board members by the General Meeting of Shareholders in August;
- the new long-term incentive programme 2018-2020 as approved by the 2018 Annual General Meeting of Shareholders.

 For information on the remuneration policy, see "Remuneration" on pages 221-225.

Details of actual remuneration in 2018 can be found in notes 27 and 28 to the consolidated financial statements.

Related-Party Committee

The role of the Related-Party Committee is described in its charter, which is available on the Company's website. On 31 December 2018, the Related-Party Committee consisted of Geoff King (Chairman) and Nadia Shouraboura. In 2018, the Related-Party Committee convened once in person to discuss, in particular, safeguards to make sure that pre-approved related-party transactions are periodically tested to ensure ongoing competitiveness. Resolutions in writing were taken when necessary during the year. Under the Company's Related-Party Transactions Policy, the Related-Party Committee reviews transactions of a recurring nature that are pre-approved by the Supervisory Board; transactions with a materiality threshold for either the Company or members of the Supervisory Board, Management Board and Executive Board; and transactions that qualify as significant related-party transactions as defined in the policy. Pursuant to this policy, the Related-Party Committee specifically reviewed the following transactions in 2018:

- service agreements with Alfa Services Limited;
- the supply agreement with Alidi following its acquisition of Central Distribution Company;

- a joint venture agreement with Sovcom Bank for distribution of online orders through a network of parcel lockers in Pyaterochka and Perekrestok stores;
- an agreement with Sovcombank on the use of the Halva instalments card in stores;
- agreements with Vimpelcom related to the supply of hardware for stores and mobile application support for store personnel;
- the sublease of storage space in Tyumen to Hoff;
- an agreement with Alfabank on Perekrestok "Mobile Wallet" loyalty cards.

These transactions were discussed and approved by the Related-Party Committee and/or the Supervisory Board with due observance of best practice provisions 2.7.3 and/or 2.7.5 of the Corporate Governance Code, as well as the rules set forth in Article 10 (Conflicts of Interest) of the rules of procedure of the Supervisory Board, which are available on the Company's website. The Supervisory Board determined that, to the extent that any of the listed transactions constituted a conflict of interest for certain members of the Supervisory Board, such conflict did not undermine the independent judgement of these Supervisory Board members while performing their duties for X5.

Remuneration

The General Meeting of Shareholders determines the remuneration of the members of the Supervisory Board. The detailed amounts are stated in notes 27 and 28 to the consolidated financial statements.

Financial Statements

This Annual Report and the 2018 consolidated financial statements, audited by Ernst & Young Accountants LLP, were presented to the Supervisory Board in the presence of the Management Board and the external auditor. Ernst & Young's report can be found on pages 293-301.

The Supervisory Board recommends that shareholders adopt these financial statements and, as proposed by the Management Board, appropriate RUB 25,000 million for dividend payments. The underlying principle of the dividend policy is that at least 25% of the consolidated net profit for the full year has to be placed at the disposal of holders of global depositary receipts

for distribution as dividends. The proposed dividend amounts to RUB 92.06 per GDR with a nominal value of EUR 0.25.

The Supervisory Board furthermore requests that the Annual General Meeting of Shareholders grant discharge to the members of the Management Board for their management and to the members of the Supervisory Board for their supervision in 2018.

The Supervisory Board wishes to express its sincere appreciation for the results achieved and would like to thank the Executive Board and all X5 employees for their continued dedication and efforts in 2018.

The Supervisory Board

19 March 2019