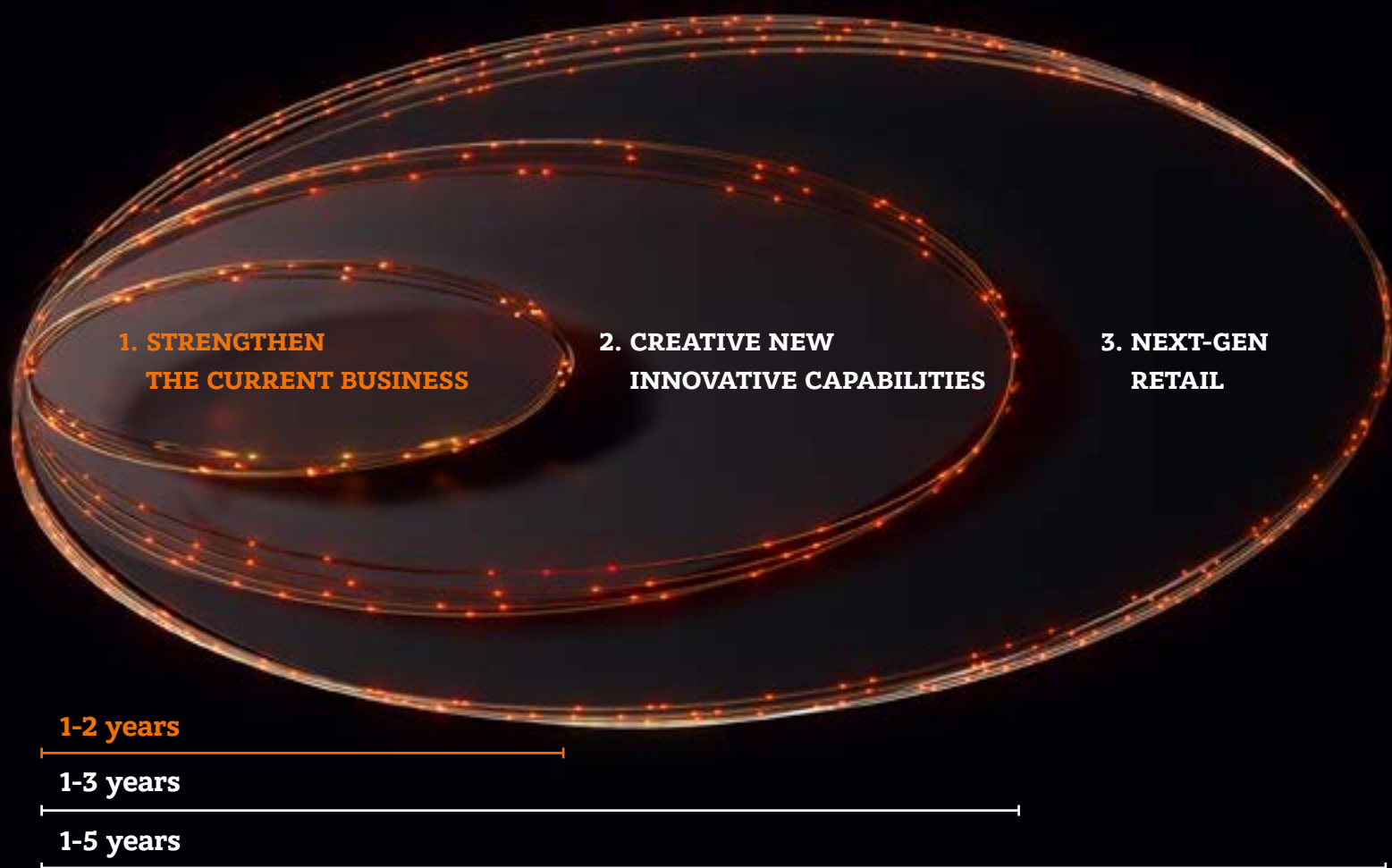


Our strategy in action

While X5 further secured its position as the leader in the Russian food retail industry in 2018, we are fully aware of the need to continuously evolve and to be prepared for potential disruption in our market as consumer expectations change and technology opens up ever more channels for retailers to reach customers. We have adapted our strategy to reflect the changing market landscape, taking into account factors ranging from persistent macroeconomic challenges and growing competition to emerging technologies and potential disruptive innovations.

Our strategy is evolving



With this in mind, we have three core streams of activity: short-term measures to strengthen the current business, medium-term initiatives to create new innovative capabilities, and our long-term goal of transforming X5 into Russia's leading next-gen retailer.

Within each of these core streams, there are specific goals and targets:

- To strengthen the current business over the next year or two, we will focus on smart and balanced expansion, further enhancing operational efficiency, as well as continuing to adapt our formats' CVPs.
- Over the next three years, we aim to create new innovative capabilities by developing technology-based solutions and further leveraging the possibilities of big-data-enabled tools to bolster the effectiveness and efficiency of our business.
- While next-gen retail has a five-year horizon, we are already actively working towards this goal, with omnichannel business models like Perekrestok Online in its second year of operations, Karusel due to launch a click-and-collect service in 2019, and Pyaterochka preparing to pilot new initiatives in the year ahead.

We believe that this three-pronged strategy aimed at addressing the short-term and long-term needs of our business is the best way to build a company that will create value for all its stakeholders while delivering good returns to shareholders.

We have updated our core strategic goals in response to the changing market landscape. While we remain focused on smart growth, adaptation of our CVP and operational excellence, X5 has elevated the importance of developing its omnichannel business and implementing innovative solutions throughout our operations. At the same time, efficiency and cost optimisation remain top priorities as we deal with the challenging macro-environment and face increasing competition, including from newcomers to the market.

The Supervisory Board believes that these strategic priorities are what X5 Retail Group needs to further secure its leadership position in the medium term, while evolving into a next-gen retailer in the longer term.

Strategic progress

1. Strengthen the current business

Strategic goals

Smart and balanced expansion

- Focus on return on invested capital (ROIC) as the key criteria for expansion, selecting the most attractive locations with the best opportunities for sustainable, profitable operations
- Decelerate openings to balance expansion with profitability and return on investment
- Continued enhancement of technological solutions that inform and accelerate the decision-making process for the selection of new sites
- Continued acquisition of smaller players
- Strengthened position in the most lucrative markets

Further adaptation of CVP

- Focus on NPS as a key metric to drive customer orientation as one of our core values
- Adapt value proposition of each format to evolving consumer needs and expectations, including localisation of store assortment to adjacent demographics and customer shopping mission profiles
- Continue to enhance regional store models to reflect differing income levels, population densities as well as local customer needs
- Improve quality of perishables, increase service levels, and continue driving assortment differentiation
- Enhance in-store execution, including improvement of on-shelf availability
- Tie top-to-bottom personnel motivation to service quality and NPS

Operational efficiency

- Maintain focus on reducing costs in an environment of challenging macroeconomic conditions and growing competition

What we did in 2018

- Opened landmark 14,000th store, ending the year with 14,431 stores
 - Added 2,310 stores in 2018 compared to 2,934 stores in 2017 (a 21.3% decrease year-on-year)
 - Increased food retail market share from 9.5% in 2017 to 10.7% in 2018
 - The number of cities and towns where X5's stores operate grew by 17% year-on-year
 - Continued to improve the geo-information system used to evaluate the attractiveness of new sites
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- Increased Pyaterochka Helps (Vyruchai-Karta) loyalty programme penetration in sales to 64%. This is the only proximity format loyalty programme in Russia to provide personalised offers for its customers
 - Piloted assortment and pricing clusterisation across the Pyaterochka network to make stores better-adapted to adjacent-area customer needs
 - Reached an 86% completion of the Perekrestok format renovation programme by the end of 2018
 - Continued to refurbish Karusel hypermarkets in line with the new concept
 - Improved quality in perishable categories and continued updating the ready-to-eat offering at Perekrestok
 - Enhanced the Karusel hypermarkets assortment, expanding healthy, bio, organic and craft offerings
 - Further expanded assortment of private-label and exclusive brands
 - Created cross-format import division to implement direct import strategy
 - Further focused personnel motivation schemes on NPS as a KPI in all formats down to the store director level
 - Enhanced employee engagement with a new incentive programme and specific steps to upgrade working conditions
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- Launched initiatives aimed at reducing shrinkage, optimising inventories, improving effectiveness of promo planning and control, and enhancing end-to-end cold chain consistency and quality control
 - Pyaterochka achieved a positive trend in shrinkage reduction since the new team took over in the middle of 2018
 - Reduced rent costs by renegotiating terms with landlords with a focus on revenue-lined rents and rent indexation aligned with food inflation
 - Continued development of a multi-echelon logistics system and implementation of a warehouse management system (WMS)
 - Over the past three years, we have opened 21 distribution centres and purchased over 3,000 new trucks
 - Since 2014, improvements in logistics efficiency have led to an improvement in the warehouse-to-selling space ratio by 32%

Long-term goals

- Deliver top-line growth above the market and competition while maintaining margins and returns
- Focus on both organic expansion and acquisition of smaller players
- Continue optimising costs, including shrinkage, logistics costs and other operating expenses
- Continue to refine data-driven strategy in response to market developments
- Enhance customer-centric decision-making based on data analytics
- Support a self-regulation strategy for Russian retail
- Increase the share of direct imports up to 10% by the end of 2020
- Increase the share of private label

2. Create new innovation capabilities

Technology-based solutions and innovations

Strategic goals

- Leverage technology to improve operations and efficiency
- Actively seek out, test and implement new technologies that will ensure that X5 is at the forefront of the emerging next generation in food retail

Big data

- Use data-driven tools to enhance our ability to meet customer demand

3. Next-gen retail

Omnichannel business model

Strategic goals

- Enhance CVPs and customer offerings of existing retail formats by piloting and developing omnichannel capabilities



What we did in 2018

- Piloted 37 projects at X5 stores in 2018 (including video monitoring of shelves, smart shelves, facial recognition and Wi-Fi recognition, customer queue video and AI-based monitoring)
- Launched an X5 lab store in Moscow in October 2018 for testing and fine-tuning new technologies
- Created a Corporate Centre-based Big Data Department (headed by Anton Mironenkov) with over 100 professionals coming from some of Russia's leading tech companies
- Implemented big data solutions for demand forecasting, assortment adaption, pricing optimisation and customer personalisation

Long-term goals

- Disrupt our business before new technologies introduced by smaller start-ups do so
- Ensure that innovation is not done for its own sake but to improve the sustainability of our business and our competitive market position
- Remain at the forefront of technological innovation in retail

What we did in 2018

- Expanded Perekrestok Online into St Petersburg and parts of the Moscow region, increasing the number of dark stores from one to three
- Installed a network of parcel lockers at X5 stores to enable customers to pick up third-party online non-food purchases
- Prepared a click-and-collect pilot launch at several Karusel hypermarkets

Long-term goals

- Evolve X5 into a next-gen retailer by creating a consumer-centric ecosystem by expanding into food and non-food adjacencies

What we did in 2018

Our investors

Governance

- Listing on Moscow Exchange, allowing X5 to expand its investor base and improve share liquidity for sustainable growth in the interests of shareholders, customers and partners
- Strengthened the Supervisory Board in the area of technical and commercial innovation, and enhanced Supervisory Board practice in terms of induction and ongoing education
- Filled vacancies at senior executive level with internal promotions, as part of the Company's systemic succession planning

Risk management

- Impact of key risks was quantified in addition to qualitative assessment
- Reorganised Forensic, Compliance, Internal Control and Risk Assessment functions and started to design X5's Assurance Map
- Revised approach of Internal Control development
- X5 Internal Audit Department successfully completed an independent and external professional evaluation by KPMG

Our people

Corporate culture

- Integration of X5's common values into all HR processes
- Customer focus as the main feature of the Company's corporate culture
- Making the X5 brand more attractive as an employer

Training and professional development

- Established an approach to the systematic, long-term development of X5 managers
- Launched training programme for X5's top managers
- Developed basic managerial and professional skills for employees

Occupational health and safety

- Continued implementation of health and safety standards and ensuring safe working conditions across all operations
- Company-wide occupational health and safety policy and training courses for all blue-collar professions at X5

Our world

Environmental management

- Implemented remote monitoring and management systems to optimise in-store electricity use
- Continued installation of energy-efficient LED lighting at Karusel format
- Continued recycling of own waste and piloted programme to let consumers recycle PET bottles at Pyaterochka stores
- Operated and maintained modern transport fleet that adheres to strict environmental standards

Community commitment

- Introduced new format for Basket of Kindness: citywide food marathons
- Expanded cooperation with Life Line Foundation to assist children in need
- Continued to support pensioners by offering discounts during off-peak hours
- Supported volunteer activities by employees to support socially beneficial projects

Long-term goals

- Continuously refine X5's governance in support of the Company's long-term value creation for the benefit of all stakeholders
- Maintain constructive dialogue with investors, analysts, regulators and other market stakeholders

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- Emphasis on cost-benefit of risk mitigation activities and controls
 - Prediction of known and new risks and integration into strategic planning
 - Efficient and transparent interaction – a three-tier model to establish and maintain internal control
 - Continuous improvement of risk management and internal control culture and practices at all levels of X5 with the participation of all stakeholders

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- Systematically communicating the Company's updated goals and strategies at all levels
 - Breaking goals down into cross-cutting key performance indicators

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- Retain talented employees by cross-cutting/cross-format training programmes and expanding opportunities for career growth at X5

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- Involvement of all X5 Retail Group employees in ensuring a safe working environment

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- Continue to implement measures that limit our impact on the environment, benefit local communities, and improve the efficiency of our business.

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- Continue to implement activities that support the communities where we operate, in line with our policies and guidelines