

# CONTRIBUTION TO ECONOMIC DEVELOPMENT

In 2018, we approved a new Development Strategy for 2018–2028. The strategy defines the target state of the Company in the medium term as a stable company with an acceptable level of debt and a strict leverage management system.

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### **Financial stability improvement**

In 2018 we managed to cover losses and significantly improve our financial performance. In 2018, the KMG external debt was reduced, limits on investments were set and the regulations were adopted for project deadlines. We were also able to bring non-core activities into the market environment, which allowed us to reduce duplicate functions.

# Contribution to Economic Development

## LOW-CARBON DEVELOPMENT

GRI 102-15, 103-1, 103-2, 103-3, 201-2, 302-1, OG3

In our long-term KMG Development Strategy, we have identified the following priority areas on climate aspects:

- management of greenhouse gas emissions;
- reduction of regular flaring of associated petroleum gas;
- improvement in emission rates per production volume and energy efficiency.

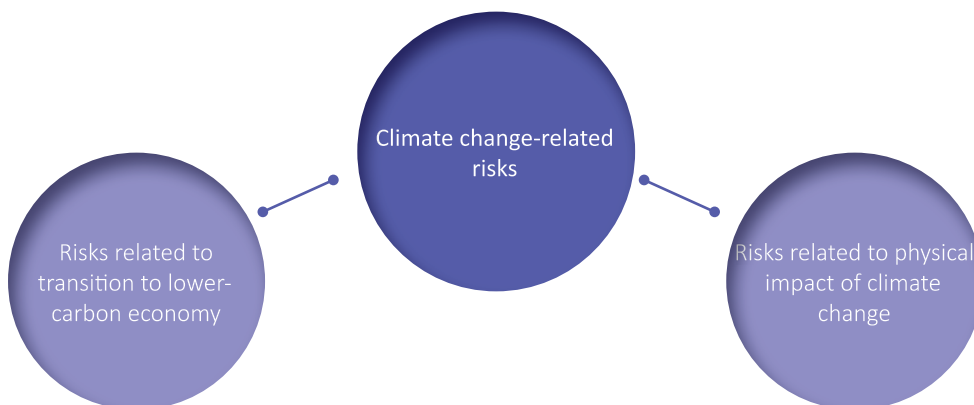
In 2018, KMG developed an emission management policy consisting of eight key principles, six of which are directly related to climate change:

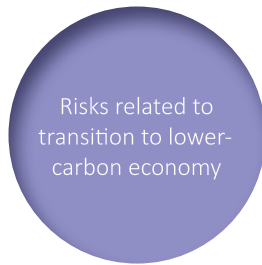
- compliance with the volume of established quotas for greenhouse gas emissions;
- regular accounting, inventory and monitoring of emissions, including indirect greenhouse gas emissions;
- cessation of regular flaring of raw gas while extraction of hydrocarbons;
- implementation of measures to reduce emissions and reduce the carbon footprint;

- carbon asset management;
- continuous improvement of emission management activities (e.g. forecasting, prevention and mitigation of climate change-related damage).

Climate change issues require the identification of risks and the adoption of measures to reduce burden on the environment.

The corporate risk management system is a key component of the corporate governance system and is aimed at timely identification, assessment, monitoring and reduction of potential risk events that may adversely affect the achievement of strategic and operational goals. We identify and report quarterly to the Board of Directors on the HSE risks, as well as include the risks related to climate change in the corporate risk matrix:





**Political and regulatory risks** (e.g., implementation of mechanisms for establishment/enhancement of carbon prices for reducing greenhouse gas emissions; transition of the state to distribution of quotas only through the use of specific emission factors as a result, some enterprises may have a shortage of quotas; reduction of energy consumption to reduce emissions; adoption of energy-saving solutions; strengthening of measures to improve water use efficiency and promoting more sustainable land use practices).

**Market risk** (a risk of changes in supply and demand for certain climate-related goods, products and services).

**Technological risk** (development and use of new technologies such as renewable energy sources (RES), energy-saving technologies, best available technologies (BAT), carbon capture and storage technologies, etc.).

**Reputational risks** associated with changing the perception of the Company by stakeholders in terms of its contribution to the transition to a low-carbon economy, or evasion of this transition.



**Short-term risks** caused by extreme weather events such as cyclones, hurricanes, floods.

**Systematic (chronic) risks** caused by long-term changes in climate models (e.g., long periods of abnormally high air temperatures, sea level rise and inundation of onshore wells).

**SUSTAINABLE DEVELOPMENT GOALS**



**Principle 7**

Businesses should support a precautionary approach to environmental challenges.



**Principle 8**

Undertake initiatives to promote greater environmental responsibility.

**Principle 9**

Encourage the development and diffusion of environmentally friendly technologies.

**Principle 10**

Businesses should work against corruption in all its forms, including extortion and bribery.



In order to mitigate these risks, we are actively involved as part of the Working Groups under the Ministry of Energy of Kazakhstan in improving the regulatory framework of Kazakhstan in the field of state regulation of greenhouse gas emissions.

Every year the Company builds new recycling facilities, reconstructs the existing production facilities, invests in the construction of pipelines and infrastructure, for example, the construction of integrated gas processing at the Prorvinskaya group of fields, the construction of the Saryarka gas pipeline. In 2019, it is planned to put the gas treatment plant-40 into full-scale operation at the Kozhasay field in Aktobe region. These measures contribute to the increase of APG utilization level and, accordingly, lead to the reduction of direct carbon dioxide emissions.

At the same time, the role of natural gas will grow in connection with the desire of electricity-generating companies to transit to fuels that would reduce emissions into the atmosphere. It is expected that in about ten years gas will become one of the main fuels for electricity generation.

As part of modernization in 2019–2021, it is planned to introduce at the Kazakhstan refineries an automated system of technical energy accounting to be implemented on the basis of microprocessor-based computing facilities and control systems, which is an information and computer system with centralized control and distributed measurement function. Implementation of this project will lead to:

- reduction of energy costs by optimizing the operating mode and quality control of electricity consumption;
- automation of the process of collecting and processing data on electricity consumption in the context of large consumers, units, assemblies;

- management of power consumption modes, increasing the efficient electricity use in the technological processes of the refineries;
- predictive analysis, real-time monitoring;
- creation of a common environment for monitoring and analysis of electricity consumption of subsidiaries and affiliates of KMG Oil Refining;
- development of a statistical database on electricity consumption in the context of time and facilities;
- identification of emergency situations and development of solutions;
- implementation of one of the main steps in establishment of a digital enterprise.

Also, research of the current level of development of the Kazakhstan refineries is in progress as compared with the world's best refineries under the HSB Solomon Associates LLC methodology (hereinafter – Solomon). The purpose of Solomon's research is: determination of the main indicators – “Solomon indices” – refineries in a comparable basis, i.e. how effectively the available capacity is used. Performance indicators are designed to compare refineries that are similar in size and configuration, and are better used for operational comparisons that allow comparison of refinery performance (both production and economic) with the performance of other refineries in different groups.

In 2019, it is planned to install solar panels with a total capacity of 10 kW to power the lighting network of the industrial site of “Amangeldy Gas” LLP.

Renewable energy sources (hereinafter – RES) implemented in KTG subsidiaries and affiliates in previous years operate effectively: waterkotte geothermal heat pumps; monocrystalline solar panels (batteries); thermoelectric generators (Closed cycle vapor turbogenerator).

*The total amount of generated (produced) renewable energy by sources for 2018 was:*

Output of geothermal (thermal) energy by heat pumps is  
**678.53 Gcal**

Output of electric power generation solar panels is  
**103,572 kW\*hour**

Output of electric power generation by thermal power generators (TPG – Rankine cycle) is  
**240,900 kW\*hour**

## ECONOMIC PERFORMANCE

(GRI) 102-7, 103-1, 103-2, 103-3, 201-1, 201-4

The Company makes a significant contribution to development of the Kazakhstan regions, increase of socio-economic capacity and improvement of welfare of the population of the regions.

The economic performance of the Company allows assessing this contribution to the country's economy, revenues, liabilities and taxes paid.

KMG does not receive financial assistance from the state.

### Direct economic value generated and distributed\*

Indicator	Units	2016	2017	2018
<b>Direct economic value generated (gross revenue)</b>	<b>KZT billion</b>	<b>4,035</b>	<b>5,451</b>	<b>7,905</b>
<b>Economic value distributed ( gross expenses)</b>	<b>KZT billion</b>	<b>3,675</b>	<b>4,926</b>	<b>7,211</b>
<b>Economic value retained (profit)</b>	<b>KZT billion</b>	<b>360</b>	<b>525</b>	<b>694</b>

Indicator	Units	2016	2017	2018
<b>Other taxes and payments (without CIT)</b>	<b>KZT billion</b>	<b>781</b>	<b>914</b>	<b>1,258</b>
<b>Income tax paid</b>	<b>KZT billion</b>	<b>106</b>	<b>113</b>	<b>186</b>
<b>Payments to providers of capital</b>	<b>KZT billion</b>	<b>294</b>	<b>275</b>	<b>291</b>

\* Data are taken from the KMG Audited Financial Statements for 2018, prepared in accordance with the international financial reporting standards (IFRS). Economic performance indicators are presented in accordance with GRI Standards (201-1).



(GRI) 201-3

## Social Benefits and Pension Contributions

In accordance with the national legislation, pension savings of citizens are in the Unified Pension Savings Fund. Pension savings consist of: the minimum pension rate guaranteed by the state, the individual pension savings (monthly contribution of 10% of salary) and additional regional allowances.

In addition to the state social security and pension program, the KMG Group implements a pension program for non-working pensioners, according to which employees, after

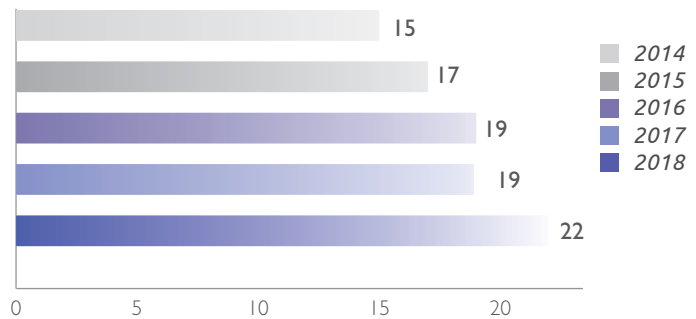
going on a well-deserved rest, can receive some material support.

In some oilfield service organizations of KMG Group of Companies, such as "Oil Transport Corporation" LLP, "Oil Construction Company" LLP, "Oil Services Company" LLP, a project is implemented on provision of the pre-retirement age employees with early retirement with compensation to be paid upon termination of labor relations by agreement of the parties with employees who have reached retirement

age, with compensation being paid upon termination of labor relations.

In 2018, expenses for social support of KMG Group employees amounted to KZT 22 billion (in 2017 – KZT 18.9 billion), including social assistance to non-working pensioners.

Social support of KMG Group employees, KZT billion



Indicator	Units	2016	2017	2018
Social benefits and pension contributions paid	KZT billion	43	52	52

## Indirect Economic Impacts

### Capital expenditures for 2016–2018

GRI 203-1, 203-2

Indicator	Units	2016	2017	2018
Capital expenditures	KZT billion	554	669	628

As part of the region gasification program, KazTransGas continues the gasification and modernization of settlements in Kazakhstan. A road map has been developed for implementation of Five Social Initiatives of the President of Kazakhstan in terms of the Project “Construction of Gas Distribution Networks to Connect to Saryarka Pipeline”. The project will create the necessary conditions for development of production capacities of the existing enterprises and the establishment of new plants, stable gas supplies to Nur-Sultan and Central Kazakhstan, improving the environmental situation, improving the quality of life of the population, attracting and increasing employment of the local population by creating additional jobs at the stage of construction and operation of the main gas pipeline and infrastructure facilities of the main gas pipeline, as well as

stable socio-economic development of Nur-Sultan and central regions.

In 2018, the following investment projects were successfully completed:

1. Increase in Capacity of Kazakhstan – China Pipeline (Line C). With the commissioning of the third line of the gas pipeline (Line C), the capacity of Kazakhstan – China Pipeline was increased to 55 billion m<sup>3</sup> per year.
2. Expansion of Gasification of Kostanay Region Settlements. 7 settlements have been gasified (Kachar settlement in Rudny, Oktyabrsky settlement in Lisakovsk, Toguzak village in Karabalyk district, Antonovka, Alchanovka in Denisovsk district, Auliyekol in Auliyekol district – a supply pipeline has been commissioned, continued gasification in Rudny). In total, the Project plans to connect about 7 thousand new

- subscribers, including 6.7 thousand houses and apartments, 184 small municipal enterprises, 12 industrial enterprises (with a total consumption of 28 million m<sup>3</sup> of gas).
- As part of the gasification of the Northern and Central regions of the Republic of Kazakhstan, the Saryarka Pipeline construction DED was developed in 2018.

In 2018, the following new investment projects were launched:

- Construction of three compressor stations at Beyneu – Bozoy – Shymkent Pipeline.
- Work has begun on development of a Feasibility Study “Increase in Capacity of Kazakhstan – China Pipeline (Lines A and B) to 40 billion m<sup>3</sup> per year.
- Work has begun on development of a Technical and Economic Assessment to expand the capacity of Beyneu – Bozoy – Shymkent to 15 billion m<sup>3</sup> per year.
- Gasification of Almaty, modernization, reconstruction of gas distribution systems of Almaty. The Project contributes to improvement of the environmental situation in the city, will connect about 4.1 thousand new subscribers to the gas supply with an average annual consumption of 15.8 million m<sup>3</sup> of gas.
- “MunaiTas” LLP launched the Kenkiyak – Atyrau oil pipeline reverse project. The project is aimed at ensuring the transportation of West Kazakhstan oil in the amount of up to 6 million tons per year to PPCP and PKOP.

## Investments for Production Upgrading

GRI 203-1

**It is planned to continue work in the framework of investment projects for modernization of gas distribution networks:**

- Modernization of the gas distribution system in Taraz. From 2012 to 2018, 862 km of new gas pipelines were built and 29 thousand subscribers were re-connected to the new gas supply system. In 2019, the construction of about 38 km of gas pipelines is planned, the completion of the project is planned.
- Modernization, reconstruction and new construction of gas distribution system of the Mangistau region settlements. Since 2015, 1,323 km of gas pipelines have been built and modernized, 6 sets of automatic gas distribution stations, 34 gas distribution cabinet points, 41 gas distribution block points have been installed. 5 settlements have been gasified.
- Gasification of Almaty, modernization, reconstruction of gas distribution systems of Almaty. The project envisages the construction of 288 km of gas pipelines, the reconstruction of 101 km of gas pipelines and 34 cabinet gas control points.

As part of modernization of the Kazakhstan refineries, the following investments were made:

- Complex of deep oil refining within the framework of Atyrau refinery modernization: assimilation of CAPEX for 2018 is KZT 54,172.8 million (without VAT)
- Modernization and reconstruction of Shymkent refinery is KZT 260,730 million (without VAT)
- Modernization of Pavlodar Oil Chemistry Refinery was completed in December 2017.

Modernization of the refineries will ensure the production of K4, K5 motor fuels, as well as significantly reduce emissions of harmful and polluting substances. As a result of the reconstruction and modernization of the capacity of oil refineries will be 17.5 million tons per year, and one of its main results is a significant increase in output of light oil products (including gasoline, diesel fuel), which ensured the elimination of their deficit in the country.

Other capital expenditures in 2018 amounted to KZT 16.7 billion, which also included the construction of the Martial Arts Palace in Nur-Sultan.



## PROCUREMENT PRACTICES

**(GRI) 103-1, 103-2, 103-3, 102-9, 204-1**

One of the principles of procurement in Company is to provide all potential suppliers with equal opportunities to participate in the procurement process.

At the same time, the current system of procurement of goods provides for an open tender or procurement through a request for price offers only among producers of goods purchased, which are members of the Register of producers of “Samruk-Kazyna” JSC, and also only among organizations of persons with disabilities producing purchased goods, which are members of the Register of organizations of persons with disabilities. In addition, the Procurement Rules provide special conditions for the procurement of goods that are used by the subsoil users of “Samruk-Kazyna” JSC who have concluded subsoil use contracts before January 1, 2015, before the expiration of such contracts or until January 1, 2021, whichever comes first. These special conditions stipulate that subsoil users are obliged, in accordance with the requirements of paragraph 3 of Article 78 of the Law of the Republic of Kazakhstan “On Subsoil and Subsoil Use”, to purchase goods from Kazakhstani producers of goods subject to their compliance with the requirements of the project document and the legislation of the Republic of Kazakhstan in the area of technical regulation.

The procurement process includes the following main steps:

- development and approval of the annual (long-term) procurement plan;
- selection of the supplier;
- conclusion and execution of the procurement contract.

The choice of the suppliers of KMG and its SDEs is mainly carried out by way of holding an open tender with the use of tenders for downgrade, in the manner of requesting price proposals, as well as from one source, in accordance

with the Rules of Procurement of Goods, Work and Services of “Samruk-Kazyna” JSC (hereinafter – the Rules).

All purchases are conducted through the Electronic Procurement Information System in accordance with the Instructions for the conduct of electronic procurement.

An important aspect when choosing a supplier of goods, works, services is to conduct procurement procedures in strict accordance with the Procurement Rules of “Samruk-Kazyna” JSC without any violations affecting the results. This indicator is included in the Map of Key Performance Indicators of the Management of KMG and its SDEs.

“Samruk-Kazyna” JSC has developed and approved a Special Procurement Procedure for Qualified Potential Suppliers, which includes conducting pre-qualified selection of potential suppliers and forming a database of potential suppliers that have been prequalified.

It should be noted that the possibility of establishing requirements for potential suppliers in terms of social criteria is not provided for in the Procurement Rules for goods, works and services of “Samruk-Kazyna” JSC, which regulate the procurement procedures of KMG organizations. In this regard, the establishment of social criteria when choosing a supplier can be assessed by “Samruk-Kazyna” JSC as a restriction of competition.

At the same time, the provisions on observance of human rights and social criteria are reflected in the model contracts for the procurement of goods, works and services of KMG, as well as in the approved Code of Business Conduct.

The purchases of goods, works and services in 2018 amounted to 2,428 billion tenge.

**The total amount of procurement of goods, works and services and the share of local content (bn, KZT)**

Year	Total	LC share, %	Goods		Works & Services	
			Amount	LC Share, %	Amount	LC Share, %
2016	1,870	76	721	83	1,149	71
2017	2,553	75	863	79	1,690	73
2018	2,428	79	824	77	1,604	80

The above indicators reflect consolidated data for all subsidiaries of KMG, in which fifty or more percent of voting shares (interests) are directly or indirectly owned by KMG under the right of ownership or trust management, and which are subjects of the Procurement Rules for goods, works and services of Samruk-Kazyna JSC.

**The amount of procurement from resident companies of Kazakhstan**

Bn, KZT

Year	Total	Goods	Works & Services
2016	1,602.5	637.5	965
2017	2,257.9	775.1	1,482.8
2018	2,280.8	739.8	1,541

In 2018, the purchase of goods, works and services from resident companies of Kazakhstan (regardless of the citizenship of their employees and the availability of certificates of origin of goods of the form "CT-KZ") amounted to KZT 2,280.8 billion, which is 93.9% of the total amount of purchases.

At the same time, the calculation of the local content share in the procurement of goods,

works and services is made on the basis of the Unified Methodology of Local Content Calculations for the Procurement of Goods, Work and Services, approved by order of the Minister for Investment and Development of the Republic of Kazakhstan No. 260 dated April 20, 2018.

*The word "local" means domestic enterprises that produce goods and have a certificate of origin of the form "ST-KZ", which indicates the percentage of the share of local content. When calculating local content in a contract for the performance of work (the provision of services, except for the contract for performance of work (rendering services) purchased in the framework of subsoil use contracts, the share of the payroll of Kazakhstani personnel in the total wage fund of employees is taken into account.*

## ANTI-CORRUPTION

The Company is taking systematic, organizational and practical measures to prevent corruption among the employees of the Group of companies. In 2017, by the decision of the KMG Management Board, the "Rules for conducting anti-corruption monitoring and internal analysis of corruption risks" (hereinafter – Rules) and "Anticorruption Standard" were approved and implemented.

Previously adopted economic security policy defines main directions for countering corruption and other unlawful manifestations

**GRI 103-1, 103-2, 103-3, 205-1, 205-2, 205-3, 406-1, 409-1**

which are against the interests of the Group of companies and its employees.

The specified documents in the state, Russian and English languages are posted on the websites of KMG and its subsidiaries and affiliates. Data displays in KMG head office regularly broadcast informational clips on matters of preventing and combating corruption among KMG employees the information monitors.

In accordance with the Rules, a system analysis of corruption risks in the Group of companies is carried out on a quarterly basis, the activities of structural units of KMG and its subsidiary dependent entities on anti-corruption and compliance with anticorruption legislation are studied and evaluated.

The regulations for management organization of production and non-production risks, Risk Identification and Assessment Methodology at KMG and its subsidiaries and affiliates conduct quarterly monitoring and analysis of the state of anti-corruption risks for the entire group of the Company, providing a report on risk dynamics and the progress of the implementation of the preventive action plan.

At the same time, in the course of carrying out procedures for identifying risk factors affecting the corruption risks of the Group of companies, methods of quantitative and qualitative risk assessment have been used.

As part of the work carried out in 2018, 3 actualized risks of a corruption nature, such as theft, bribery and conflict of interest (in 2016 – 2 risks, in 2017 – 0) were recorded. For commission of corruption offenses, 2 criminal cases were initiated against 3 employees with whom the employment agreement was terminated on the initiative of the employer and all of them were convicted by the courts with various punitive measures. 5 cases of violation of the rights of workers related to the illegal termination of employment contracts and disciplinary proceedings have been established.

There were no cases of renewal or termination of contracts with business partners due to violations related to corruption during 2018.

The Agency of the Republic of Kazakhstan on Civil Service Affairs and Anti-Corruption (hereinafter – the Agency) and KMG also conducted an external analysis of corruption

risks in the activities of KMG. Based on the results of the analysis, a number of risks were identified when hiring personnel and resolving conflicts of interest, for which appropriate recommendations were given.

With the aim of eliminating and resolving the risks identified by the audit, with the participation of the Agency, a joint Action Plan was developed and implemented. All suppliers of goods, works and services of KMG, its subsidiaries and affiliates have been notified of the presence of anti-corruption requirements in the Group of companies and anti-corruption methods.

Starting from 2017, all contracts of KMG and its subsidiaries and affiliates on the procurement of goods, works and services are supplemented by a section on countering corruption which states that each party to the contract has a zero-tolerance policy to corruption, and each party is governed by applicable law and on its basis, policies and procedures aimed at combating bribery and commercial bribery.

Placing internal documents of KMG and SDEs on anti-corruption issues on corporate websites, broadcasting info-clips, including anti-corruption clauses in contracts with counterparties made it possible to achieve almost full familiarization coverage of employees, as well as potential contractors and other individuals with anti-corruption requirements, profiled in the company.

All employees of the corporate security divisions of the KMG Group of companies carry out their work in accordance with the requirements of the legislation of the Republic of Kazakhstan and are guided by the provisions on structural divisions and job descriptions.

According to information received from the subsidiaries and affiliates, there were no cases of abuse of power, violations of the workers' rights by employees of the corporate security divisions in the exercise of their duties. ■

