

Strategic overview

Chairman's statement

**Christopher Hopkinson**

First Deputy Chief Executive of JSC NC KazMunayGas
Chairman of the Board of Directors of KMG EP

Dear Shareholder,

2015 was a challenging year for KMG EP, in which the firm delivered a negative operating margin as a result of a sharp and rapid fall in the oil price, which came at the same time as social costs increased. Along with the rest of the industry we face the prospect of lower oil prices persisting for longer than had been anticipated barely a year ago.

The Company has so far not been able to respond to these challenges by cutting its cost base with sufficient pace and lifting costs have continued to rise, with the breakeven point in 2015 at around US\$70 per barrel. We anticipate that performance in 2016 will also be negative, as all of KMG EP's operations are currently loss making and significant further deterioration in the cash position is expected in 2016. This situation requires immediate organisational changes.

We have been able to improve the efficiency of our maintenance programme significantly in 2015 and we have benefitted from close cooperation with NC KMG through participation in the Transformation Initiative and the Technical Institute. But we need to do much more.

To achieve our breakeven level in 2016 and 2017, we now need to accelerate progress significantly on our cost cutting and efficiency agenda, which has so far been slowed down by internal bureaucracy and duplication.

We have four clear priorities for 2016:

- Streamlining back office functions;
- Improving functional discipline management;
- Improving centrally driven knowledge and technology sharing;
- Increasing efficiency of well workovers by applying modern technologies in crude oil production.

We anticipate additional tailwinds from upgrades to refining capacity, which should mean improved refining margins under our new agency model for domestic supply, and we are also assisted by the new excise duty regime.

Your Board remains completely focused on this agenda and on embedding the cultural and organisational changes in KMG EP that are required to drive it through. Your Board and our main shareholder are also discussing the scope for changes to our Charter and the Relationship Agreement that will strengthen your Board's control and simplify decision making and organisation.

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