

### **KazMunaiGas Exploration Production releases its Annual Report for 2012**

**Astana, 30 April 2013.** JSC KazMunaiGas Exploration Production has published today its Annual Report for 2012\*. The report is posted on the Company's website at [www.kmgep.kz](http://www.kmgep.kz).

Further, the Company provides below the extracts from its Annual Report in unedited full text as required in accordance with DTR 6.3.5 (1)

**\* Information presented in this annual report is as of April 18, 2013.**

## COMPANY OVERVIEW

**Mission:** KMG EP’s mission is to maximize benefits for the shareholders of the Company, by producing hydrocarbons in an efficient and expedient way, creating long-term economic and social value for the regions in which we operate and providing the development of each employee to reach their potential.

**Vision:** KMG EP – a leading company in the field of hydrocarbon exploration and production in Kazakhstan, among the leaders of oil and gas business in the Caspian region, able to compete globally.

KazMunaiGas Exploration Production JSC (“Company” or “KMG EP”) was formed in March 2004 through the merger of JSC Ozenmunaigas (“OMG”) and JSC Embamunaigas (“EMG”). KMG EP is one of the top three leaders in terms of oil production in Kazakhstan. By consolidated production volumes KMG EP controls around 15% of Kazakhstan’s total production and by consolidated proven reserves about 3%. The volume of proved and probable reserves including the Company’s share in Kazgermunai, CCEL and PKI as of 2011 year end were about 285 million tonnes<sup>1</sup> (2,083 million barrels).

Shares of the Company are listed on the Kazakhstan Stock Exchange (KASE) and global depositary receipts (GDRs) on the London Stock Exchange (LSE).

Compared to other companies, KMG EP has unique advantages, which include a relationship with the parent company the National Company KazMunaiGas (“NC KazMunaiGas” or “NC KMG”), through which KMG EP has prioritised access to oil and gas assets and the infrastructure in the territory of Kazakhstan.

## FINANCIAL AND OPERATIONAL HIGHLIGHTS

	2011	2012	Change in %
2P Reserves <sup>1</sup> , mmbbl	2,083	2,083	0%
Production <sup>2</sup> , kbopd	250	247	-2%
Sales <sup>2</sup> , kbopd	253	244	-4%
Export <sup>2</sup> , kbopd	193	191	-1%
Revenue <sup>3</sup> , US\$m	4,919	5,346	9%
Net profit <sup>4</sup> , US\$m	1,425	1,079	-24%
Capex <sup>3</sup> , US\$m	716	725	1%
Net cash <sup>5</sup> , US\$m	4,240	4,637	9%
Dividend per share, KZT	1,300	1,619	25%
Dividend per GDR, US\$	1.46	1.81	24%
Brent, US\$/bbl	111	112	0.4%

<sup>1</sup> Reserves of OMG, EMG, KGM and CCEL as of 2011 year end and PKI as of 2010 year end. Reserves of OMG, EMG, KGM and PKI according to the reports of Gaffney, Cline & Associates and CCEL according to the report of Miller & Lents, Ltd.

<sup>2</sup> Including interest in KGM, CCEL and PKI.

<sup>3</sup> Excluding interest in KGM, CCEL and PKI.

<sup>4</sup> Including impairment charge in the amount of 75 billion tenge (around US\$500m) in 2012.

<sup>5</sup> Cash funds, cash equivalents and other financial assets (including NC KMG Bond) less borrowings (including non-recourse debt of KazMunaiGas PKI Finance B.V.).

# The oil and gas industry of the Republic of Kazakhstan

## Industry Overview<sup>2</sup>

Kazakhstan is in the top 15 countries in the world by proven volumes of reserves, having 2% of the global reserves of oil according to the “BP Statistical Review of World Energy”. Oil and gas-rich regions take up 62% of the area of the country and account for 172 oilfields, of which over 80 are in the development stage.

Over 90% of oil reserves are located in the 15 largest fields – Tengiz, Kashagan, Karachaganak, Uzen, Zhetibai, Zhanazhol, Khalamkas, Kenkiyak, Karazhanbas, Kumkhol, Severnye Buzachi, Alibekmola, Central and Eastern Prorva, Kenbai, Korolevskoe. The fields are located in the territory of 6 out of the 14 regions of Kazakhstan. These are Aktobe, Atyrau, Western Kazakhstan, Karaganda, Kyzylorda and Mangistau regions. At the same time about 70% of carbon reserves are located in the Western part of Kazakhstan.

The most developed oil reserves are in the Atyrau region, as 75 oilfields have been discovered here with commercially exploitable reserves totaling to 930 million tonnes. The largest field of the region is Tengiz with initial extractable reserves of 781 million tonnes. Other fields in the region contain a total of 150 million tonnes. Over half of these reserves are concentrated in two fields: Korolevskoe (55 million tonnes) and Kenbai (31 million tonnes).

Within the territory of the Mangistau region over 70 discoveries with commercially extractable oil reserves of 725 million tonnes and 5.6 million tonnes of condensate have been made. Less than half of these fields are currently in production. Most of them are in late stages of development. The greater part of reserves are in the "difficult to extract" category. The largest fields are Uzen, Zhetibai, Kalamkas and Karazhanbas.

The largest field in the Western Kazakhstan region is Karachaganak, with extractable reserves of liquid hydrocarbons of about 320 million tonnes and over 450 billion cubic metres of gas. In September 2005 an announcement was made for the discovery of hydrocarbon reserves in the Fedorovskiy block, next to Karachaganak.

The Kashagan field was one of the largest discoveries in the world over the past 40 years and also the largest offshore discovery. The field is located in the Kazakhstan sector of the Caspian Sea and occupies an area of approximately 75x45 km. The reservoir is situated about 4,200 metres below the seabed in the northern part of the Caspian Sea. The development of the Kashagan field in the harsh maritime conditions of the northern Caspian represents a unique combination of technological complexities and supply chain difficulties. These complexities are related to the provision of a safe working environment and the resolution of technical engineering, logistical and ecological tasks, which make Kashagan one of the largest and most complex energy projects in the world.

The Tengiz is a giant oil field, related to the Pre-Caspian oil and gas province of the north Caspian Sea. The oil reservoir lies at a depth of about 4,000 metres. The Tengiz reservoir is 19 km long, and 21 km wide, and is 1.6 km high. Total discovered reserves in drilled and undrilled areas of the Tengiz reservoir are estimated at around 3.1 billion tonnes or 26 billion barrels.

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<sup>2</sup> Sources of information: Ministry of Oil and Gas of Kazakhstan, Annual Report of JSC "KazMunaiGas - Refining and Marketing", Analytical report of JSC "RFCA Rating Agency", Informational and analytical magazine «KazEnergy» #3 (53), June 2012, «BP Statistical Review of World Energy June 2012».

Another promising area from the point of view of oil and gas potential is the Aktobe region. About 25 fields have been identified here. The most significant geological discoveries in this region are the Zhanazhol group of fields with extractable reserves of oil and condensate of 170 million tonnes. In 2005 an announcement was made for a discovery in the central block of the eastern part of the Caspian depression of the new Umit field.

The base of the oil production industry of Kyzylorda and Karaganda regions is the Kumkol group of fields - the fifth most important oil and gas province of Kazakhstan. In the summer of 2005, PetroKazakhstan, the oil company operating in this region, announced the finding of commercial oil reserves in the licensed territory of Kolzhan, which lies next to the northern perimeter of the Kyzylkia field.

#### Key indicators

According to data provided by the Ministry of Oil and Gas of the Republic of Kazakhstan, confirmed reserves of hydrocarbons on shore and on the sea shelf are estimated at 4.8 billion tonnes or over 35 billion barrels. For comparison, in 2001 the explored balance reserves of oil were only 2.9 billion tonnes. Moreover, the forecast oil reserves in the Kazakhstan sector of the Caspian Sea alone may exceed 17 billion tonnes or 124 billion barrels, according to some experts. Taking into account both the reserves of oil and gas and constantly growing production, in the foreseeable future, Kazakhstan will continue to be at the center of world oil production.

According to information from the Ministry of Oil and Gas, production of oil and gas condensate in 2012 amounted to 79.2 million tonnes. This compares with oil production of only 25.9 million tonnes in 1998. Kazakhstan is also one of the top gas producers of the CIS member-states, producing 40.1 billion cubic metres in 2012.

In 2012, Kazakhstan's oil and gas-processing plants refined 14.2 million tonnes of crude oil and produced 2.2 thousand tonnes of LPG. Domestic consumption of natural gas last year was 10.5 billion cubic metres.

Kazakhstan exports the bulk of its produced oil via pipelines. In 2012 the volume of oil exported was 68.6 million tonnes, of which 15.4 million tonnes were exported through the "Atyrau-Samara" pipeline and, 27.9 million tonnes through the Caspian Pipeline Consortium (CPC) line. A further 10.4 million tonnes was exported to China through the "Atasu-Alashankou" line. The value of crude oil exports amounted to the equivalent of US\$56.4 billion, which is 60% of Kazakhstan's total exports.

The volume of gas exports from Kazakhstan in 2012 were 8.8 billion cubic metres. Meanwhile, the volume of international gas transit across the territory of the Kazakhstan last year was 96.5 billion cubic metres.

In the future, the volume of production of oil and gas in Kazakhstan will have a tendency to a significant increase. The increase is connected to three main factors, these are the significant growth in capital investment, the expected growth in demand on international markets for hydrocarbons and the fruits of intensive exploration and development work in the hydrocarbon basins of both the Caspian and Aral seas. All these factors will support further growth of the resource potential of this key economic sector.

## Chairman's statement

L. K. Kiinov

2012 was a year of serious changes for the Company in both the social and production spheres. The main priorities of this period were stabilisation of the social situation at the core assets, full-scale modernisation of the production cycle and stabilisation of production for future growth.

KMG EP has undertaken a wide-ranging review and renewal of employee relations, focusing all efforts on developing closer contacts with personnel and local residents wherever we operate. We hope thereby to minimise the risks of protest movements. Today it can be stated that the social environment at JSC Ozenmunaigas has been normalised. KMG EP is following a new path along its road of development but still has major tasks ahead.

As before, the task of increasing production stands high on our list of priorities. The main reason for low productivity is the lack of a technologically reliable production basis because of depreciated equipment and its vulnerability to breakdowns and other negative factors.

For a comprehensive resolution of production problems and the further development of KMG EP, the Board of Directors has agreed a production modernisation plan. The modernisation programme calls not just for the stabilisation of oil production, but also for the improvement of working conditions. The present programme should minimise the risks of production disruption and fully realise the potential of KMG EP's production assets.

Today the Uzen field is one of the largest fields in Kazakhstan - not just measured by the levels of reserves, but also by social significance. It provides employment for around 14,500 people. Uzen is a significant asset for the country as a whole, therefore in 2012 it was not only KMG EP that was involved in resolving of its problems but also our parent company NC KazMunaiGas and the state holding company NWF Samruk-Kazyna as well as the Ministry of Labour and Social Protection and the Ministry of Oil and Gas of the Republic of Kazakhstan.

In 2013, JSC Ozenmunaigas (OMG) plans to produce about 5.3 million tonnes (107 kbopd) while JSC Embamunaigas (EMG) will produce about 2.8 million tonnes (57 kbopd). We consider that this is a totally realistic level of production, provided that we accomplish the tasks set for the modernisation of production and can motivate the constructive work of all employees of the enterprises. We are convinced, that even greater potential remains to be realised in the still vast reserves of the Uzen field as a whole.

In accordance with the official forecasts of the Government of the Republic of Kazakhstan and NC KazMunaiGas of an average price per barrel of Brent crude of US\$ 90, the Board of Directors of KMG EP has approved the budget for 2013. Capital investments in 2013 are planned to reach 191 billion tenge (US\$ 1,288 million). The growth in capital investments is primarily connected with fulfilling the modernisation programme and the implementation of planned geological exploration, the latter being one of the promising areas of development for KMG EP. All these expenditures are directed towards the increase of future operational and financial effectiveness. An important factor underlying approval for this increase in expenditures is the assurance of production viability and the prospective stabilising of future operational and capital expenditures.

KMG EP is a major tax payer and a socially responsible company, playing an important economic role in the regions where it operates. Despite temporary difficulties at its own operations, KMG EP remains one of the leaders of the domestic oil and gas sector and one of the top three producers in Kazakhstan. Equity participation of KMG EP in LLP JV Kazgermunai, CCEL and

PetroKazakhstan Inc. largely offset problems at its core production units with good consolidated production and financial results. Partnerships with these companies have proven to be successful and are a strong foundation for future development.

KMG EP has a special significance to the KazMunaiGas holding company. It is the only Kazakh oil company to have gone through the listing process of both the London and Kazakhstan stock exchanges. This confirms the levels of transparency, openness and high corporate governance. At the same time, KMG EP is the only oil and gas operator in the country which has a state support and is of interest to both domestic and foreign investors.

With access to capital markets, KMG EP is able to independently manage tasks of consolidating oil and gas assets within the NC KMG group without drawing on parent company funds. This permits NC KMG to concentrate on its own key projects.

KMG EP resolves its strategic goals in close partnership with NC KMG. The NC KMG will continue to support the projects of KMG EP in the future, guaranteeing the protection of the interests of the state, company employees and shareholders.

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## Chief Executive's statement

A. A. Nurseitov

I took on the position of Chief Executive Officer of KMG EP in January 2013, having taken over from Alik Aydarbaev, who now heads up the administration of the Mangistau region. As the Deputy CEO for production, I was witness not only to the large-scale changes effected by the Company in 2012, but also took an active part in the completion of projects for bringing the Company out of a reputational crisis, brought on by a drawn-out employment conflict.

We have lived through some difficult times, but have been able to draw lessons from this situation. During the last year the Company carried out intensive work to set up communication channels with employee representatives. Mechanisms were developed and implemented, to obtain feedback from KMG EP employees, so that any topical question could be raised and resolved in the shortest possible time. A system has been developed for raising the motivation of personnel. At the same time training sessions were held on how to resolve labour disputes and events were organised aimed at strengthening the corporate spirit. Our task for 2012 was to recover the trust and loyalty of employees and their representatives and to provide the Company with a "strong rear guard" in its production activities.

Today we are witnessing positive changes in our relationships with personnel and believe that the right decisions have been taken. We hope that they will help in closing the ranks of the many thousands of employees of KMG EP and will provide a fresh impulse to the development of a constructive dialogue and mutual respect. We are not working alone in this area. The Ministry of Oil and Gas of the Republic of Kazakhstan, the fund Samruk-Kazyna, our parent company KazMunaiGas and local executive bodies are all providing us with helpful support.

In 2012 substantial changes were introduced to the management structure and business processes of the Company. The production units OMG and EMG were transformed into joint stock companies 100% owned by KMG EP. This provides for the appropriate reporting structures and the improved responsiveness of management at the production level while enhancing the transparency of enterprises. Apart from that, two new service companies were formed, which will not only be offering services to KMG EP and other oil producing companies, but should also help to dampen social tensions in the region.

The operational results of KMG EP for 2012 confirm that production at the main assets was stabilised last year. Including the Company's stakes in LLP JV Kazgermunai, CCEL and PetroKazakhstan Inc., in 2012 the Company produced 12,191 thousand tonnes of oil (247 kbopd), which is only 1% less than in 2011. After the lengthy strike at the end of 2011, KMG EP still needs time to restore previous volumes of production. The infrastructure at several sites is worn out and not all equipment is up to modern standards. This is why we launched an extensive modernisation programme last year which, on completion, should allow us to stabilize production processes at OMG and to make them more resilient in the face of all negative external factors. At OMG we shall have a workshop which is unique in the CIS area for the diagnostics and repair of underground equipment. We shall also have an oil storage terminal, two zones for the preparation of fluids for capping wells; a workshop for servicing oil production equipment; a workshop for repairing oil production equipment and an automotive repair centre with capacity to service 1,000 vehicles and specialised equipment. In addition to this, repairs will be carried out to the water injection system and connected pumping station and systems for the collection and transportation of liquids. Introduction of these new installations will allow us to greatly enhance the effectiveness of production. The programme will be implemented over the medium term with capex estimated at about 100 billion tenge. During 2013 implementation of this programme, and generally solving

problems with our production assets will receive the maximum amount of attention, resources and energy.

Despite the fact that OMG is operating in an already established field, it has considerable development potential of its own. During 2012 wide scale research into the potential of the Uzen field was carried out. Based on the resulting reports, independent experts concluded that the field has a considerable future. However, research also showed that for production to be viable, it is necessary to review the production process. Consequently, in 2012 work was initiated on the implementation of modern methods of increasing oil production and new equipment was purchased so that the bulk of future production work will be automated.

In 2012 a horizontal well was drilled for the first time at the Uzen field, where the average daily output was 22 tonnes per day. Based on the positive results and taking into account the existing infrastructure, we intend to continue horizontal drilling in 2013.

KMG EP is at the start of a medium-term programme of geological exploratory works. We adhere to the principle that investments into geological exploration must be economically justified. For this reason the Company has undertaken a strict selection of targets, based on prospective returns on investments and intends to continue future exploration and additional exploration on a case-by-case pragmatic basis.

The strategy of KMG EP is now under review considering the revised strategy of NC KazMunaiGas. We are consistently building up the resources to strengthen the position of one of the leading oil and gas companies in Kazakhstan. Our key objectives are to increase the consolidated volume of production, to replenish and increase reserves of hydrocarbons through the acquisition of new assets, as well as through geological exploration and the optimization of production at the core KMG EP fields.

As before, we intend to support the improvement of social conditions in areas where we operate, to support training and the professional advancement of the younger generation of oil professionals and to resolve issues of ecology and safety of production.

Our company has already established itself as a conscientious user of mineral resources, a profitable enterprise and a responsible partner for our shareholders. The goal set for KMG EP today is to live up to this reputation and to continue working towards further harmonic growth.

## **BOARD OF DIRECTORS**

The controlling body of the Company is the Board of Directors and the executive body - the Management Board. The Chief Executive Officer (General Director), who heads up the Management Board, is also a Board of Directors member and the sole representative of the executive body of the Company on the Board of Directors. Another four members of the Board of Directors, including its Chairman Lyazzat Kiinov are representatives of NC KazMunaiGas. The Board of Directors during 2012 also included three independent directors.

**Lyazzat Kiinov** - Chairman of the Board of Directors of KMG EP, Chairman of the Management Board of JSC NC KazMunaiGas

Lyazzat Kiinov, Chairman of the Management Board of JSC NC KazMunaiGas was elected as a member of the BoD of KMG EP on 27th February, 2012 and as Chairman of the BoD on 13th March, 2012. He graduated from the Kazakh Polytechnic Institute. Doctor of technical sciences, academician of the International Academy of Engineering. Has been working in the oil and gas industry since 1971. He passed through all stages of personal development in the oil and gas production industry, having worked as an operator for oil and gas production at Zhetybaineft, as chief engineer of the territorial-production department Mangyshlakneftepromkhim and as head of Karazhanbasstermneft, Komsomolskneft. Has held senior positions at JSC NC KazMunaiGas, the Caspian Pipeline Consortium (CPC) and the Ministry of Oil and Gas of the Republic of Kazakhstan. For several years he headed up the Mangistau region. Has been awarded the "Parasat" order and the "10 years of Independence of the Republic of Kazakhstan" medal.

**Abat Nurseitov** - CEO, Chairman of the KMG EP Management Board (General Director)

Abat Nurseitov took over as CEO of KMG EP in January 2013. Mr. Nurseitov has been working with the Company since October 2006. Previously, he held positions of Deputy General Director for Operations and Managing Director for Operations in KMG EP. He graduated from the Kazakh Polytechnic Institute. Has been working in the oil and gas industry since 1986, having progressed from being a field operator for oil and gas production to head of Zhetybaineft. He has held various management positions at KazNIPIneft, CJSC Turgai-Petroleum and the Kazakhstan affiliate of Lukoil Overseas Service. Has been awarded medals commemorating 100 and 110 years of Kazakhstan oil production.

**Yerzhan Zhangaulov** - Head of legal service of JSC NC KazMunaiGas

Starting from February 2012, Mr. Zhangaulov is a head of legal service of JSC NC KazMunaiGas. Previously, he worked as managing director of legal issue, as the chief executive on legal issues and as an adviser of the vice-president of NC KMG, He also headed the Legal Department of JSC NC Oil and Gas Transportation, the legal service and a personnel department in Presidential Administration of Kazakhstan, worked as a consultant in the Legislation Department, Defense Department and Legal order of in the Front Office of Prime-Minister of the Republic of Kazakhstan. A qualified lawyer, he graduated from Karaganda State Institute in 1992.

**Asiya Syrgabekova** – Financial Director of JSC NC KazMunaiGas

Asiya Syrgabekova was appointed as Financial Director of NC KazMunaiGas in July, 2009 and was elected to the Board of Directors of KMG EP on March 26, 2010. From July 2006, she was Managing Director for Economics and Finance at NC KMG. Prior to this appointment, between 2004-2005 she was Chairman of the Management Board, and between 2003-2004 first deputy of Chairman of the Management Board of Halyk Bank. Between 1998 and 2003 she worked at

national oil and gas companies, occupying various top management positions at Kazakhoil and KaztransGas. She graduated from the economics faculty of the Kazakh State University in 1982.

**Timur Bimagambetov** - Deputy Chairman of the Management Board for production and technical development at NC KazMunaiGas

Timur Bimagambetov was appointed deputy Chairman of the Management Board for production and technical development at NC KazMunaiGas on 20th February, 2012 and elected to the BoD of KMG EP on 29th May, 2012. During the past few years he was CEO of LLP "N Operating Company" and also Executive Director at KMG EP. He graduated from the Kazakh Polytechnical Institute in 1978.

**Philip Dayer** - Independent Non-Executive Director of KMG EP

Philip Dayer LLB, is a member of the Institute of Chartered Accountants, qualifying as a chartered accountant with KPMG. During 25 years he worked in investment banking, specializing in consulting for companies listed on the LSE. He gained significant experience working for companies such as Barclays de Zoete Wedd and Citicorp. In 2005 he left ABN AMRO Hoare Govett. Thereafter he consulted Rosneft on the successful placing of securities in 2006. At present he is on the boards of a number of companies, including Dana Petroleum and AVIVA Group, where he is an INED. In May 2010 Mr Dayer was appointed a member of the BoD of KMG EP. He chairs the Audit and Remuneration Committees and is a member of the Nominations and Strategic Planning Committees.

**Edward Walshe** - Independent Non-Executive Director of KMG EP

Edward Walshe has 35 years' experience working in the oil and gas sector. He worked in various positions with British Petroleum and British Gas and was responsible for exploration and production for these companies in Nigeria, Abu-Dhabi and in Central and South-East Asia. He holds a doctorate in chemistry of crystals from Dublin University. He was elected to the BoD of the Company on 28th August, 2006. He chairs the strategic planning and nominations committees and is a member of the audit and remuneration committees.

**Paul Manduca** - Independent Non-Executive Director of KMG EP

Paul Manduca worked as CEO in such companies as Threadneedle Asset Management, Rothschild Asset Management and Deutsche Asset Management in the UK and in Europe. Mr Manduca has been Independent Director on the boards of a number of companies, including Prudential Group plc., where he was Senior Independent Director .

Due to his appointment as Chairman of Prudential Plc., Mr Manduca decided to stand down from the BoD of KMG EP from 1st October, 2012. Mr Manduca was a member of the remunerations and appointments committees and chaired the audit committee.

## 2012 MILESTONES

### Q1

- In December 2011, the Company was instructed by the government of the Republic of Kazakhstan to improve social conditions in the Mangistau region through creating additional jobs. The Board of Directors has expressed understanding of the Government's position and is setting up two service companies (transportation and drilling) with headcount in excess of 2000 employees, to provide services to KMG EP and other oil companies operating in Mangistau region. According to a preliminary estimate, this leads to increased operating and capital costs in 2012 of 12.3 bn Tenge (US\$ 83 million) and 8.3 bn Tenge (US\$ 56 million) above previously planned levels, respectively.
- The Board of Directors of JSC KazMunaiGas Exploration Production has approved the date and the agenda for the Extraordinary General Meeting of Shareholders ("AGM"). The AGM will take place on 27 February 2012 in Astana. The agenda of the AGM includes early termination of powers of a member of Company's Board of Directors; appointment of a member of Company's Board of Directors.
- At an extraordinary General shareholders' meeting of KMG EP, member of the Company's Board of Directors, Askar Balzhanov, was relieved of his duties. Lyazzat Kiinov has been appointed as a member of the Company's Board of Directors for the whole term.
- At the meeting of the Board of Directors Lyazzat Kiinov was also elected as Chairman of the Board of Directors of KMG EP.
- Taking into account the shares in LLP JV Kazgermunai, CCEL and PetroKazakhstan Inc., KMG EP produced 3,029 thousand tonnes of oil (249 kbopd), during the first three months of 2012 which is 143 thousand tonnes or 5% less than in Q1 2011. The shortfall in Q1 2012 was mainly due to adverse weather conditions in Western Kazakhstan.
- According to the consolidated interim financial statements for the first three months of 2012, revenues grew by 8% to 207 billion tenge (US\$ 1,396 million) compared to the same period in 2011. The increase was due to higher oil prices and higher prices for supplies to the domestic market. Net profits were 75 billion tenge (US\$ 508 million) with profits per share of 1,070 tenge, equivalent to US\$ 1.2 per GDR, an increase of 27% and 32% respectively in comparison with the same period of 2011

### Q2

- KMG EP announced the closing of the transaction to sell a 51% stake in the LLP "Kazakhstan Petrochemical Industries Inc." ("KPI") that operates the construction of the first integrated petrochemical complex in Atyrau region to the LLP «United Chemical Company». As a result KMG EP received 5 billion tenge (US\$ 33.5 million) from the sale of this investment which was without any tax consequences as the initial investment was equal to the amount of sale.
- Between 2<sup>nd</sup> and 5<sup>th</sup> May 2012 Astana hosted the 1<sup>st</sup> spartakiade sports competition between employees of production units and subsidiary organisations of KMG EP. The overall results of the games placed the team of OMG in first place.
- At the KMG EP shareholders' AGM, the dividend per share for 2011 was approved at 1,300 tenge. The total dividend payment for 2011 was around 91 billion tenge (about US\$ 615 million). The approved dividend represents a 62.5% increase in dividend per share compared to the previous year and is the highest amount per share since IPO in 2006.
- The Board of Directors approved increase of capital expenditures in 2012 to 142 billion tenge (US\$ 955 million) from 127 billion tenge (US\$ 852 million). Additional investment will be allocated to the program of modernisation of production infrastructure, in line with previously announced plans, aimed at improving work conditions and ensuring the sustainability and

efficiency of KMG EP production in the future, as well as compliance with environmental and safety standards.

- The Board of Directors decided on early repayment of the debt to KMG PKI Finance BV by 6th July, 2012. The debt had been raised from the acquisition of 33% stake in PKI Inc. in December 2009..
- The Board of Directors of KMG EP decided to allocate 5 billion tenge (US\$ 36 million) towards resettlement of inhabitants in Bayshonas and Eskene villages in the Makat region to the town of Atyrau.
- At the KMG EP shareholders' AGM, the powers of board member Sisengali Utegaliyev were terminated and Timur Bimagambetov was elected as a new member of the Board of Directors of the Company for the term as a whole.
- Drilling of an exploratory well began at the White Bear block in the UK North Sea in accordance with contractual obligations. KMG EP owns a 35% stake in the license; the other partners are BG Group and Maersk Oil UK with respective shares of 45% and 20%.
- Between 13 and 15th May 2012 a competition of children's drawings was held, entitled "My dream. Me and my family". Children of the employees of OMG and EMG took part. The main prize for the 18 finalists was a trip to Astana - the capital of Kazakhstan.
- The Ministry of Oil and Gas of the Republic of Kazakhstan, KMG EP and OMG signed addenda to Contract No. 40 dated 31st May, 1996 on the performance of development works in the oilfields of Uzen and Karamandybas in the Mangistau region. The main objective of the addenda was to provide OMG with subsoil access rights at the Uzen and Karamandybas fields, located in the Mangistau region from 1st July, 2012.
- On 21st June 2012 OMG held their first Board of Directors meeting. Abat Nurseitov, deputy CEO for production at KMG EP was elected as Chairman of the Board of Directors of OMG. Abzal Mendibaev, interim director of production unit OMG was elected as CEO and Chairman of the Executive Board of OMG.
- Including the Company's stakes in LLP JV Kazgermunai, CCEL and PetroKazakhstan Inc., during the first 6 months of 2012, KMG EP produced 6,057 thousand tonnes of oil (248 kbopd), which was 254 thousand tonnes or 4% less than in the same period in 2011.
- According to the consolidated interim financial statements for the 6 months of 2012, revenues amounted to 399 billion tenge (US\$ 2,690 million), which was approximately the same as the equivalent period in 2011. The figures resulted from higher prices for sales to the domestic market, fully offset by lower export volumes. Net profits amounted to 121 billion tenge (US\$ 820 million), with profits per share of 1,740 tenge (US\$ 2.0 per GDR), an increase of 6% and 10% respectively compared to the same period in 2011.

### Q3

- On 1st July, 2012 the production unit OMG was converted into a joint stock company (JSC).
- KMG EP concluded a transaction on sale of 49% of shares in KS EP Investments BV to subsidiary of MOL Hungarian Oil and Gas Plc. ("MOL"). KS EP Investments BV owns 100% interest in the LLP Karpovskiy Severniy which is a subsoil use right holder under the Contract for Exploration of Oil, Gas and Condensate at Karpovskiy Severniy contract area in the Western Kazakhstan region. On 15-17th August, 2012 the production base of JSC Karazhanbasmunai hosted the final stage of the "Uzdik maman" professional mastery competition among workers of the main professions of the KMG EP group of companies. The competition consisted of a theoretical and practical part. Participants who took first, second and third place will receive bonus payments of 30%, 20% and 10% respectively to their basic salaries for one year.
- The Board of Directors of KMG EP decided to change the structure of payments to NC KMG for services. Part of the total will be fixed at 4.5 billion Tenge (US\$ 30 million) for oil export

and other services and payment above this will only be made in the event of the completion of acquisition deals. The total amount shall not exceed 10 billion Tenge (US\$ 67 million).

- On 20th September, 2012 EMG held their first Board of Directors meeting. Abat Nurseitov, deputy CEO for production at KMG EP was elected Chairman of the Board of Directors of EMG. Zhumabek Zhamauov, director of production unit EMG was elected as CEO and Chairman of the Executive Board of EMG.
- Taking into account stakes in LLP JV Kazgermunai, CCEL and PetroKazakhstan Inc., during the first 9 months of 2012, KMG EP produced 9,108 thousand tonnes of oil (246 kbopd), which was 100 thousand tonnes or 1% less than in the same period in 2011.
- According to the consolidated interim financial statements for the 9 months of 2012, revenues amounted at 605 billion tenge (US\$ 4,067 million), which was 11% more than during the same period in 2011, on higher export volumes and higher domestic prices. Net profit amounted to 173 billion tenge (US\$ 1,163 million), with profits per share rising to 2,480 tenge (US\$ 2.8 per GDR), some 5% and 9% respectively higher than the same period in 2011.

## Q4

- On 1st October, 2012 the production unit EMG was transformed into a joint stock company.
- KMG EP's Board of Directors approved the transfer of subsoil use rights to JSC "EmbaMunaiGas" effective from 1 October, 2012 under the following six contracts: No.37 Kenbay field; No. 61 SE Novobogatinskoye field; No. 211 Botakhan, Makat, Dossor, Tanatar, Kamyshtovoye, etc. 23 fields in total; No. 413 Prorva, Kulsary, Karaton, Koschagyl, etc. 15 fields in total; No. 327 Taisoigan field; No. 992 Novobogatinskoye West field. Independent director Paul Manduca resigned from the Board of Directors and from the Audit Committee of KMG EP as of 1st October, 2012. This decision was taken following his recent appointment to Chairmanship of the Board of Directors of Prudential. The Board of Directors of KMG EP expressed their gratitude to Mr. Manduca for his productive work during six years.
- The first horizontal well was successfully drilled at the Uzen field. The average daily output was 22 tonnes per day. Based on positive results and taking into account the existing infrastructure, the Company intends to continue drilling horizontal wells in 2013.
- At KMG EP shareholders EGM, shareholders voted for amendments to the Company Charter, approved Company's revised Corporate Governance Code and repealed the old one.
- 16<sup>th</sup> November 2012 KMG EP announces the closing of transaction on sale of 49% of shares in KS EP Investments BV to subsidiary of MOL Hungarian Oil and Gas Plc. KS EP Investments BV owns 100% interest in the LLP Karpovskiy Severniy which is a subsoil use right holder under the Contract for Exploration of Oil, Gas and Condensate at Karpovskiy Severniy contract area in the Western Kazakhstan region.
- KMG EP, jointly with MOL Hungarian Oil and Gas Plc and First International Oil Company (FIOC) developed a programme to train production personnel for the oil and gas project of LLP "Ural Oil and Gas". Twelve candidates received grants in 2012 to study at the Budapest university of Technology and Economics and at the Miszcolc Engineering university. The main aim of the programme is to develop Kazakhstani professionals and to train qualified specialists for LLP "Ural Oil and Gas".
- Middle managers of OMG completed a training course in "mediation in socio-employment disputes and conflicts". The main objectives of the course were to familiarise attendees with tools for the effective solution of conflict situations in socio-employment relationships together with training in mediation skills, techniques for conducting negotiations and methods for bringing conflicting parties to a reasonable agreement.
- The Board of Directors of KMG EP approved the budget for 2013 based on an average US\$ 90 per barrel price of Brent crude, in line with the official forecasts of the government of the Republic of Kazakhstan and NC KazMunaiGas. Under the planned production plan for 2013, OMG will produce about 5.3 million tonnes (107 kbopd) and EMG about 2.8 million tonnes

(57 kbopd). Capital expenditure of 191 bln tenge (US\$ 1,288 million) is planned for 2013. The increase in capital expenditure is related to investment in the modernization program and exploration program.

- KMG EP and the National Economic Chamber of Kazakhstan "Soyuz "Atameken" have signed a memorandum of cooperation in the area of support and development of entrepreneurship. The purposes of the undertaking are to create a new platform for the effective interaction of government representatives and commercial and non-commercial organisations for the resolution of social problems in the regions and also for stimulating self-support initiatives among the population. The package is aimed at resolving social problems at a regional level.
- On 31st December, 2012 the KMG EP share buy-back programme was completed. Between the 11th October, 2011 and 31st December, 2012 the Company bought back 19,461 ordinary shares and 14,386,605 GDRs to a total value of US\$ 263 million.
- Taking into account the stakes in LLP JV Kazgermunai, CCEL and PetroKazakhstan Inc., during 2012, KMG EP produced 12,191 thousand tonnes of oil (247 kbopd), which was 150 thousand tonnes or 1% less than in 2011. The main reasons for the decline in production were adverse weather conditions in Q1 2012 and idle wells during the extensive protest action in 2011 at OMG.

## **Evaluation of KMG EP activities by independent experts**

In 2012 the International ratings agency Standard & Poors (S&P) awarded KMG EP a credit rating of BBB-/Stable. As stated in the S&P report, the rating is constrained by the influence of KMG EP's parent company JSC NC KazMunaiGas (KMG; BBB-/Stable) rating and also the mature nature of the core fields of the Company.

In the opinion of S&P, "KMG EP has relatively high and increasing costs, taxes, and capital-expenditure needs. It depends significantly on joint ventures where its access to generated cash flows is only indirect. Furthermore, KMGEP faces exposure, although declining, to the risks of the weak Kazakh banking system."

Among positive factors Standard & Poors notes that "KMGEP benefits from large cash reserves in international banks, which more than cover its debt. The company enjoys positive free operating cash flow (FOCF), which we believe will continue under our oil price scenario. KMGEP benefits from high exports and historically good access to transportation infrastructure."

In August 2012 Moody's rating agency awarded KMG EP a rating of Baa3 with a stable outlook. The baseline credit assessment (BCA) of "11" (out of 21) reflects the significant scale associated with the company's reserve and production base, low leverage and strong cash flow metrics. The rating also notes KMG EP's strategic importance to the state and its main shareholder, particularly illustrated by the company's right of first refusal with respect to the acquisition of existing onshore oil and gas assets, as well as access to new acreage, guaranteed access to pipeline infrastructure and its contribution to the KazMunaiGas group of companies financial results.

Moody's rating also takes into account factors in the interventionist history of the government and the importance of energy export revenues to Kazakhstan's economy.

At the same time, according to the agency, KMG EP's BCA is constrained by fundamental risk factors, such as field concentration and geopolitical risks, as well as limited organic growth prospects, given that nearly all of the company's proved reserves are developed and it is primarily reliant on acquisitions to grow its production and reserves, at least in the medium term.

Initiatives taken by KMG EP towards resolving the acute problems of JSC Ozenmunaigas (OMG) were also reflected in analysts' reports. According to these independent analysts, OMG has a realistic potential to restore production from the present relatively low levels, although doing so will require substantial investment. Analysts at Citi noted, that "the company is rightfully focused on stabilizing social environment, which still remains the primary production constraint. Even though the long-term production targets look optimistic, and unlikely to be credited by the market just yet, any improvement from the current level may change sentiment. In the meantime, we view KMG EP as an attractive dividend play, with sustainable dividend distributions, as confirmed by management. Social stabilization a key focus: Improving workforce motivation is one of the company's primary near-term targets. Although it's hard to quantify numerically, we believe the lack of motivation is still one of the primary reasons for operational under-performance. KMG EP is moving forward with this by gradually improving working conditions, conducting training for employees and negotiating with union leaders".

The analysts from Aton consider that the ability of the Company to sustain stable production levels at Uzen was limited by the dated infrastructure: most of the equipment was installed in the field back in the 1980s and has not been renovated. Therefore, they appreciated the Company's complex approach to comprehensive modernization programme.

Analysts of Halyk Finance commented: "We welcome the use of new technologies, upgrade of the outdated infrastructure and believe that these activities are likely to result in the production ramp-up. The question is whether the costs will be justified".

## **KMG EP share price dynamics**

In 2012 KMG EP paid out the largest dividend since the IPO in 2006, as the dividend for 2011 was set at 1300 tenge per ordinary and preferred share (including taxes, withheld in accordance with the legislation of the Republic of Kazakhstan). The total dividend for 2011 was around 91 billion tenge (US\$ 615 million). Following the 2011 dividend announcement in March 2012 the KMG EP share price reached its highest point in 2012 of 20.95 US\$ per share.

On December 31st, 2012 the buy-back programme of KMG EP shares that was approved by the Board of Directors was successfully completed. This was the third programme of share buy backs since 2008. According to the programme, the Company planned to buy back ordinary shares and global depository receipts (GDRs) on the Kazakhstan stock exchange (KASE) and on the London stock exchange (LSE) up to a total value of US\$ 300 million.

At the start of the buyback programme, members of the Board of Directors stated their belief that the current market price of shares and GDRs did not correctly reflect the real value and the significant potential of the Company's resource base, the real opportunities for business development and the stability of its financial position. These were the circumstances under which the Board of Directors of KMG EP took the decision to buy back part of the listed ordinary shares and GDRs of the Company. The decision demonstrated the confidence of management in the actual and potential value of the Company. In addition, this step permitted the more efficient use of free cash funds in the interests of all shareholders. During the implementation of the programme from 11th October, 2011 to 31st December, 2012, the Company bought back 19,461 ordinary shares and 14,386,605 GDRs with a total value of US\$ 263 million.

Analysts from Visor Capital noted "KMG EP completes its share buyback programme. We believe that whilst the news itself has no impact, the end of the buyback programme can make the GDR's more vulnerable to downward pressure".

On the London stock exchange in 2012 the highest price reached for one GDR of KMG EP was US\$ 20.95 and the lowest was US\$ 14.71. The average price for one GDR in 2012 was US\$ 17.83.

On the Kazakhstan stock exchange in 2012 the highest price for one ordinary share of KMG EP was 18,450 tenge and the lowest was 13,500 tenge. The average price of one ordinary share in 2012 was 15,975 tenge. The highest price of KMG EP preferred shares was 13,700 tenge and the lowest was 9,500 tenge. The average price of one preferred share in 2012 was 11,600 tenge.

Overall, analysts note that shares of KMG EP were undervalued and of interest from the point of view of growth in price with high dividends.

### **KMG EP share price dynamics**

	Average price of GDR, US\$/GDR	Average price of Brent, US\$/bbl
Q1 2012	17.50	118.60
Q2 2012	18.76	108.29
Q3 2012	17.91	109.50
Q4 2012	18.66	110.10

Source: Bloomberg

## OPERATIONAL ACTIVITY

### Production and sales of oil

In 2012 KMG EP produced 12,191 thousand tonnes of crude oil (247 kbopd), including the Company's stakes in Kazgermunai (KGM), CCEL and PetroKazakhstan Inc. (PKI) which is 150 thousand tonnes or 1% less than in 2011.

JSC Ozenmunaigas (OMG) produced 4,950 thousand tonnes (100 kbopd), which is 131 thousand tonnes less than in 2011. JSC Embamunaigas (EMG) produced 2,816 thousand tonnes (57 kbopd), same as in 2011. The total volume of the oil produced at OMG and EMG is 7,766 thousand tonnes of oil (156 kbopd).

The planned volume of production from the main assets for 2012 was 8,615 thousand tonnes (174 kbopd), including 5,800 thousand tonnes from OMG and 2,815 thousand tonnes from EMG. The below plan production performance at EMG was due to poor quality and late delivery of underground equipment and spare parts, the worn conditions of both over ground and underground infrastructure of wells, the problems in the preparation of sea water and waste water for injection, problems chemicalization oil production facilities, poor quality of well dumping. Poor labour management also kept special maintenance and installation teams (well servicing teams) standing idly while awaiting special equipment and also poor discipline and organisation of labour when conducting well servicing works.

The above factors influenced the quality and frequency of conducted maintenance works on underground equipment and wells, which in turn caused an increase in the number of idle wells and of those with declining production levels. This led to the non-fulfillment of the approved oil production programme. Moreover emergency disconnections to electricity supplies by the energy company and sharp worsening of weather conditions (unusually strong freezes, snowfalls, snowstorms and floods in the winter and spring months) all caused delays to the originally approved plan.

KMG EP's stake in production of CCEL, KGM and PKI in 2012 was 4,425 thousand tonnes (90 kbopd), which was practically unchanged from 2011, and in line with the production plans at these joint venture companies.

In October, 2012 OMG drilled its first horizontal well, producing an average output of 22 tonnes per day. Another similar well was drilled in February, 2013. The drilling of horizontal wells allowed more efficient and productive use of horizons, previously impossible to reach. For 2013 it is planned to drill five horizontal wells, ten side cuts and two multi-shaft wells.

### OMG and EMG key figures (100%)

	JSC OMG	JSC EMG	KMG EP
Fields	2	40	42
Production wells	3,698	2,283	5,981
Injection wells	1,212	458	1,670
2P oil reserves <sup>3</sup> , mmbbl	1,228	433	1,661
Oil production, kbopd	100	56	156

<sup>3</sup> The proved and probable reserves as of 2011 year end according to the report of Gaffney, Cline & Associates.

Export volumes of crude oil sales by OMG and EMG in 2012 totalled to 6,078 thousand tonnes (122 kbopd) while supplies to the domestic market were 1,637 thousand tonnes (33 kbopd). The smaller proportion of domestic sales compared to the previous year was due to lower refinery demand.

The share of KMG EP from the volume of sales of CCEL, KGM and PKI totalled 4,412 thousand tonnes of oil (90 kbopd), including 3,430 thousand tonnes of oil (70 kbopd) supplied for export, which makes up 78% of the total volume of sales of the companies. The lowering of the share of domestic sales by KGM and PKI was due to the fall in volumes of oil to compensate for domestic market supply commitments (under a compensation agreement with third parties). As a result, supplies to the domestic market were undertaken primarily from the own resources of these companies.

#### **Kazgermunai LLP key figures (100%)**

Fields	5
Production wells	138
Injection wells	26
2P oil reserves <sup>4</sup> , mmbbl	161
Oil production, kbopd	66

#### **CCEL key figures (100%)**

Fields	1
Production wells	2,460
Injection wells	620
2P oil reserves <sup>5</sup> , mmbbl	415
Oil production, kbopd	37

#### **Petrokazakhstan Inc. key figures (100%)**

Fields	14
Production wells	1,223
Injection wells	330
2P oil reserves <sup>6</sup> , mmbbl	407
Oil production, kbopd	118

#### **Crude oil reserves**

According to the report of Gaffney, Cline & Associates (GCA), as of 31st December, 2011 the total proven and probable (2P) reserves of crude oil of KMG EP, excluding the shares in Kazgermunai, CCEL and PetroKazakhstan Inc. were 226 million tonnes (1,661 million barrels).

<sup>4</sup> The proved and probable reserves as of 2011 year end according to the report of Gaffney, Cline & Associates.

<sup>5</sup> The proved and probable reserves as of 2011 year end according to the report of Miller & Lents, Ltd.

<sup>6</sup> The proved and probable reserves as of 2010 year end according to the report of Gaffney, Cline & Associates.

Reserves of "proven" (1P) category stood at 76 million tonnes (561 million barrels), and reserves in the category of "proven plus probable plus possible" (3P), stood at 267 million tonnes (1,962 million barrels).

DRAFT

## **COMPANY DEVELOPMENT**

In 2012 KMG EP focused attention on recovering workplace moral atmosphere, the stabilization of daily production levels and the modernization of production capacities at the main production sites. Raising productivity is a key factor in the future steady development of the Company. To provide for future improvements in operational performance, a decision was taken to introduce core changes to management processes. The two production units JSC Ozenmunaigas (OMG) and JSC Embamunaigas (EMG) were transformed into joint stock companies and within the framework of the 2012 production modernization programme there has been a significant increase of investment in new infrastructure and the renovation of existing sites. A comprehensive programme for the stabilization of production in the medium term at the main fields of KMG EP has been undertaken. In 2012 the foundation was laid for the future growth of production in the medium term.

### **Optimization of asset structure**

In 2012 KMG EP undertook significant efforts towards improving the ownership and management structure of its subsidiaries. With the aim of increasing production efficiency and ensuring the timely resolution of on-going social issues in working teams, OMG and EMG were transformed into joint stock companies with their own sub-soil mineral exploration rights. This reorganization should help to speed up the provision of needed equipment to production sites, the modernization of operating fields, the improved servicing of equipment and, as a consequence, to help achieve the targets for higher future production.

In January, 2012 two new service companies were formed called PSP "Drilling Well Servicing Division LLP" (UBR), which is based in Zhanaozen and LLP "Support Service Vehicles and Well Servicing Division LLP" (UTTiOS), based in Aktau. Nearly 2,000 ex-employees who had been dismissed in 2011 as a result of illegal labour action have been re-employed in the new companies. Nearly 250 pieces of special equipment have been purchased to equip the new enterprises. At the Karazhanbas site a temporary accommodation camp for shift workers was erected to house employees of UTTiOS with capacity for 400 people and a canteen for 300 people as well as a bath and laundry complex and a sports complex. A shift worker camp complex with associated infrastructure was also erected at the Kalamkas site.

UTTiOS provides services for the provision and servicing of vehicles and mobile homes. In July 2012 the special technical equipment of UTTiOS was dispatched on its first journey for the provision of services to JSC Karazhanbasmunai. During 2012 some of the workers of UTTiOS who were not engaged in line with their professional tasks helped in the construction of the shift worker camps at the Karazhanbas and Kalamkas sites. UBR provides wells servicing, underground workover services and transportation.

UBR and UTTiOS are expected to start providing services not only to KMG EP, but also to other oil producing companies in the region and gradually increase their economic efficiency.

### **Modernisation programme**

To increase crude oil production and to improve the economics of its production assets, KMG EP has developed a medium term programme of technological modernisation.

Projects for the modernisation of production capacity at Uzen are unprecedented in scale. At OMG a workshop for the diagnostics and maintenance of subsoil equipment has been set up, which is unique in the CIS countries. Once commissioned, the new workshop will employ from 300 to 350 staff from OMG. Apart from this the construction of an oil storage depot is also planned together with a raft of other facilities. These include two facilities for preparing fluids used for sealing wells; a workshop for servicing oil drilling equipment; a workshop for maintenance of oil equipment; an automotive service centre with the capacity to service 1,000 vehicles and specialized equipment. At the same time the system for water injection into the strata will be reconstructed, alongside a pumping station and a system for the accumulation and transport of liquids.

At EMG an installation will be erected for the de-sulphurisation of flare gas from the Prorva group of fields and the crude oil pipeline Prorva - Tengiz will be reconstructed. The installation of units to utilize flare gas is under way at S. Balgimbaev and Vostochny Makat fields. A 61 km high-pressure gas pipeline is also being built between Akingenj - Akkuduk - Kisimbai. Apart from that, new roads connecting fields will be built and old ones will be repaired, which will significantly speed up the transportation of people and cargos.

Measures taken within the framework of the technical modernisation programme should help make production more efficient, improve working conditions for staff and enhance ecological and industrial safety.

### **New projects and prospective deals**

In 2012, KMG EP examined over ten potential exploration and production assets both in the Republic of Kazakhstan and abroad. A detailed geological-technical and economic evaluation of the most promising of these has been prepared. KMG EP has experience in the production of both "light" and "heavy" crude oil, which broadens the range of potentially interesting projects.

KMG EP experts are examining all of the oil and gas-bearing provinces within the territory of Kazakhstan without exception, for the purpose of possible addition to the asset base of the Company. Many regions are still poorly explored, so at present it is not possible to provide a definitive evaluation of their potential. The accumulation, processing and analysis of earlier obtained data is required, alongside seismic research to achieve this. Based on the results of these studies the Company will be better able to determine the need for further search and exploratory drilling from both a geological and economic viewpoint.

In July 2010 KMG EP announced the acquisition under agreement with NC KMG of a 50% share in LLP Kazakhoil Aktobe, a 51% share in LLP Kazakhturkmunai and a 50% share in Mangistau Investments BV, which has 100% ownership of JSC Mangistaumunaigas. All the necessary internal corporate consents for the present deals were received from both parties (NC KMG and KMG EP) back in 2010. However, until the present time the appropriate permissions for completing the transactions had not been received from the state authorities, alongside the forfeiting by the state of its priority performance rights. NC KMG and KMG EP twice submitted documents to receive approval for the purchase-sale of the assets of these three companies. However, despite the prescribed deadlines, the government, represented by the Ministry of Oil and Gas of the Republic of Kazakhstan provided neither a positive nor a negative decision. KMG EP continues to be interested in the acquisition of these assets and in the case of a positive decision will be ready to enter into discussions with NC KMG on new deal terms.

## **Geological exploration in the territory of Kazakhstan**

In 2012 KMG EP continued geological exploration works on the Liman, Taysoygan, Karaton-Sarksmys, Uzen-Karamandybas, Novobogatinsk Zapadny, Zharkamys Vostochny-1, Temir, Fedorovskiy and Karpovskiy Severniy blocks and undertook further exploration of the S. Nurzhanov, Zapadnaya Prorva and Makat Vostochny fields. Tests at several promising sites, namely in the Liman and Taysoigan blocks, crude oil and gas condensate flows achieved positive results. In 2013 geological exploration works will be continued. Additionally, the Company will continue further exploration at already active fields of OMG and EMG.

In 2012 KMG EP invited a partner into the geological exploration project "Karpovskiy Severniy". A 49% share in this project was sold to the Hungarian oil and gas company MOL. The conclusion of this deal assured the sharing of geological exploration risks and of future investments. The decision to involve MOL as a partner was taken for a number of reasons. KMG EP and MOL have already established good working relationships within the framework of the joint "Fedorovskiy" project, where MOL is the project operator, successfully conducting geological exploration works on post-salt horizons. It should be noted that, during testing of objects in the "Tournaisian" and "Bobrikov" horizons flow of gas condensate was established. When working through a 11mm socket after treatment with hydrochloric acid, the gas flow rate was 119,000 m<sup>3</sup> per day and condensate - 301 m<sup>3</sup> per day.

The outlook for the "Karpovskiy Severniy" block is connected to deep pre-salt deposits (over 5,000m) and is characterized by a complex geological structure due to the presence of anomalously high strata pressure, high temperatures, the presence of aggressive gases and characteristics similar to the neighboring "Fedorovskiy" exploration block. Because of this, MOL who have significant experience of working with similar structures are the most suitable partner for this project.

Moreover, the setting up of a joint venture with MOL has ensured that KMG EP would acquire both experience and technology transfer. This partnership is another opportunity to raise the level of professionalism of local specialists.

During 2012 the BG Group, KMG EP and Maersk consortium conducted the drilling of an exploratory well with the depth of about 6,000 meters and necessary geophysical research on the White Bear block. At the moment the works on laboratory studies of the sludge, the side wall coring and vertical seismic profiling are in the process. The results of the work will be known following data interpretation, which will take place in 2013.

## **SOCIAL RESPONSIBILITY**

Social policy is a key integral part of the activities of KMG EP. From the time of its creation, the Company has allocated billions of tenge for the construction of residential housing, physical-health centers, kindergartens, health camps, and contributed towards the reconstruction of schools and hospitals in the Atyrau and Mangistau regions. The strategy of KMG EP in the area of social policy remains as before - to develop the regions where it operates. With the transformation in 2012 of the production units of KMG EP into joint stock companies, they received the right to independently deal with applications for local social projects, to estimate the financing requirements and to control the completion of these projects.

### **Social projects in the Mangistau region and in the town of Zhanaozen**

The contractual obligations of KMG EP for the development of the social infrastructure of the Mangistau region in 2012 amounted to 907 million tenge (US\$ 6.0 million). Within the framework of the Programme of social partnership the akimat (administration) of Mangistau region additionally received 200 million tenge (US\$ 1.3 million) from the Company for the creation of 800 work places for the inhabitants of Zhanaozen. Additionally financial aid was provided to the families of those who died and suffered as a result of mass turmoil in December 2011. Medical treatment and rehabilitation in Russian and Kazakh medical institutions has been offered to those who received gunshot wounds.

At the end of 2012 a 200-flat apartment block in Zhanaozen built and funded by KMG EP was also commissioned. Keys to the flats were given to needy families, to Afghan war veterans and social service workers by Prime Minister Serik Akhmetov during his visit to the region.

KMG EP as before, continues to provide support to orphanages, invalid society, sports organisations and Great Patriotic War veterans.

### **Social projects in the Atyrau region**

In the Atyrau region the contractual obligations of KMG EP towards developing the social infrastructure amounted to 287 million tenge (US\$ 1.9 million). Apart from mandatory payouts in 2012, sponsorship support was provided for the completion of social projects worth 350 million tenge (US\$ 2.3 million). These funds were used to complete the construction of five sports health centres in the region; the financing of the reconstruction of heating systems; improvements to courtyards of multi-storey housing blocks and the installation of heating boilers for needy families in Inderbor village. The funds also contributed towards the financing of the design and construction of a 100-child kindergarten in H. Yergalieva village in the Isatay region.

In the spring of 2012 the Board of Directors of KMG EP decided to allocate 5.4 billion tenge towards the relocation of the villages of Bayshonas and Eskene to the regional centre - the town of Atyrau. Bayshonas and Eskene are villages next to fields with the same names, which are being developed by EMG. Work in these fields has been on-going for 80 years and oil supplies are getting exhausted. So the question arose as to the viability of these fields and of the provision of jobs for village inhabitants. As levels of oil production fell unemployment started to rise, while the social and physical infrastructure of the villages fell into decline. Nearly 80% of the houses are in critical condition and the collapse of the water mains meant that there was no possibility of

maintaining water supply to residential houses. Today all 80 families who previously used to live in Eskene village have been relocated to the town of Atyrau and are living in the regional centre. The relocation of the 377 families of the village of Bayshonas is taking place in several stages and will be completed during 2013.

## **Personnel policy**

In 2012 KMG EP faced the task of creating new and better internal communications channels with the aim of building a constructive dialogue with employees and reducing the likelihood of a repeat of labour disputes and conflict situations.

Throughout this period KMG EP worked in the regions of operations of its subsidiaries and affiliated companies forsaking the option of more remote management. As a result, the distance between the central administration and workers at the operational level was shortened and it became possible to speedily resolve current issues.

One of the main lines of activity was the mass training of production personnel in safety measures in accordance with current requirements together with re-training and enhancing the qualifications of employees. Since the start of the year over 586 million tenge (US\$ 3.9 million) has already been allocated for these purposes. Seminars and training for the development of management skills have also been run for senior management, together with training in current management methods.

In order to update trade union leaders on the latest changes to labour legislation a special training seminar was arranged last April, part of which was dedicated to the development of communication skills.

As part of the effort to improve internal communications at an enterprise level team building training was also carried out in the course of the year for managers, shop and shift foremen, store and work units managers in the fields.

Personnel of the production units OMG and EMG received extensive briefings about their transformation into joint stock companies. Each employee had the opportunity to put questions to the top management of KMG EP during face-to-face meetings and to receive detailed responses. They were assured that the same working and pay conditions and social contributions would retain, as guaranteed in the conditions of the collective agreement. These conditions were approved by the work collectives and trade unions.

In 2012 for the first time a professional mastery competition was held for the title "Uzdik Maman" among workers of affiliate companies. Winners receive a bonus to their basic annual salary. KMG EP plans to make these competitions part of a good Company tradition.

Special attention during the course of the year was paid to developing coherence in the working collectives. Thus in Astana the 1<sup>st</sup> spartakiade (multi-disciplinary athletics competition) was held in 11 sport disciplines amongst workers of the KMG EP group of companies. There was also a gala concert, where talented creative workers of KMG EP took part. A competition of children's drawings belonging to employees of OMG and EMG was held. The theme was "My dream. Me and my family", with the aim of supporting children's creativity. Similar events will be held in the future to support the team spirit of our workers.

## **HEALTH & SAFETY AND ENVIRONMENT**

Work safety and environmental protection are the main elements of safety management at KMG EP. Events held are directed towards improving working conditions, preventing accidents and preparing readiness for localising and liquidating any resulting consequences. The Company also guarantees compensation for damage caused to the environment and to third parties and strives to minimise the influence of industrial-operational factors on the environment.

### **Occupational health and safety**

The problem of work-related injuries is still relevant. During 2012 there were 8 injuries at KMG EP production facilities which were work-related. In each case a special investigation was carried out and measures for preventing similar cases in the future were taken. In particular, portable gas-analysers are being purchased; instruction sheets on the newest and safest work methods during underground repair works on wells have been reviewed and approved; special training courses on driving and vehicle maintenance safety have been conducted for drivers. To prevent speeding-related road accidents at production facilities, a system of monitoring vehicles and special equipment has been introduced (GPS). This project allows locating transgressions and the online monitoring of the location of vehicles. It also records the testimony of various sensors and controls the planned technical inspections, etc.

During the past three years over 1.6 billion tenge (US\$ 10.8 million) was spent on the implementation of work safety measures. No less than once a year all production structures of the company hold training sessions for workers in safe working practices, which are confirmed by a final examination. Managers and persons responsible for the provision of industrial safety and protection of the working environment have training and an aptitude/knowledge test once every three years at courses for enhancing qualifications at respective educational institutions.

All purchased items of individual worker protection are analysed on an annual basis. They should provide the highest levels of protection, be lightweight, ergonomic and extremely easy to use. At the same time to improve the individual safety of Company employees, changes have been introduced to the schedules for issuing special work clothing, footwear and other items of individual protection. During the past three years over 4 billion tenge (US\$ 27 million) has been spent for these purposes.

During 2012 expenditures on work and industrial safety at KMG EP totalled 974 million tenge (US\$ 6.5 million).

### **Environmental protection**

The Company allocates significant financial resources towards protection of the environment.

At OMG, for example, expenditure on these environmental protection measures totalled 696 million tenge (US\$ 4.7 million). At EMG 726 million tenge (US\$ 4.9 million) was spent on the same purposes.

The Company conducts annual ecological monitoring of the atmosphere, and underground water, soil and also radiation monitoring. This is done through using the resources of the departmental

ecological laboratory and other organisations equipped with the necessary testing kits, licences and permissions. Monitoring is also carried out on leaking or sunken wells to determine their impact on the eco-system of the Caspian Sea.

KMG EP constantly works to liquidate sources of radiation contamination of the environment through collecting radioactively contaminated equipment from operational areas for storage at a special site for the temporary storage of radioactive waste.

The Company is evaluating new technologies and is conducting experimental industrial tests for cleaning contaminated tubing and equipment.

It is also consistently carrying out the processing, re-cultivation and restoration of contaminated land plots in order to liquidate past contamination in fields under development. Employees of the Company are studying the most up to date methods and technologies, in particular the acquisition of ecologically sound and effective equipment for processing waste and the introduction of new technologies for the re-cultivation and restoration of oil-contaminated soil.

In order to bring industrial safety procedures, protection in the workplace and the environment up to international standards, and make use of best practice from Western countries, KMG EP decided in 2012 to engage the services of Ray Mitcham. He is a top manager with extensive experience working with major international companies.

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## **CORPORATE GOVERNANCE INFORMATION**

### **CORPORATE GOVERNANCE CODE COMPLIANCE**

This section of the Annual Report has been prepared in compliance with the requirements of the FSA's (Financial Services Authority) Disclosure and Transparency Rules (DTR 7.2) (Corporate Governance Statements).

As an overseas company with GDRs admitted to the Official List of the United Kingdom Listing Authority, the Company is not obliged to comply with the UK Corporate Governance Code. However, in accordance with DTR 7.2 the Company is required to disclose in its Annual Report whether or not it complies with the Corporate Governance Code of the Republic of Kazakhstan, as well as disclose actual principles of corporate governance, which being applied in addition to the practices to be observed in accordance with applicable laws of the Republic of Kazakhstan.

Following the adoption of the UK Corporate Governance Code in May 2010 by the Financial Reporting Council, the UK independent corporate governance improvement organization, in 2012 Company's updated its Corporate Governance Code to comply with the UK Corporate Governance Code, except for separate provisions. Specific information on where the Company's current governance practices differ from those set out in the UK Code is given herein.

The directors recognize the importance of the corporate governance and support the development of corporate standards in the Company. The Company intends to develop and implement the corporate governance practices which impose additional obligations on the Company than those required under legislation of Kazakhstan.

### **KAZAKHSTAN CORPORATE GOVERNANCE CODE AND COMPANY'S CORPORATE GOVERNANCE CODE**

Corporate governance best practice in Kazakhstan is set out in the Kazakhstan Corporate Governance Code. This Code is based on the best international practices in the area of corporate governance and Recommendations on Application of Corporate Governance by Kazakhstan Joint Stock Companies, approved by the Securities Market Expert Council of the National Bank of the Republic of Kazakhstan in September 2002. The Code was approved by the Financial Institutions' Association of Kazakhstan in March 2005 and by the Board of Issuers in February 2005.

The Company has adopted the Kazakhstan Corporate Governance Code as its own Code. In 2012 the Corporate Governance Code was amended in order to comply with the UK Corporate Governance Code adopted in 2010 (except for some provisions as set out herein). The amendments adopted by the Company impose additional obligations on KMG EP in respect of corporate governance in addition to those provided by the Kazakhstan Corporate Governance Code. The Company believes that these additional amendments will significantly improve the corporate governance practices applied by the Company. KMG EP also takes into consideration other provisions of the UK Corporate Governance Code and will seek to improve its corporate governance standards in the future.

Additional provisions of the Company's Corporate Governance Code in addition to the requirements of the legislation of the Republic of Kazakhstan (namely, the Kazakhstan Corporate Governance Code) are as follows:

- Additional principles of the corporate governance were introduced:
  - The principle of independent activities of the Company

- The principle of responsibility
- Some of the corporate governance principles were supplemented by various provisions, such as:
  - Social policy principles
  - Provisions regarding relationship with the shareholders of the Company
  - Division of responsibilities between the Chairman of the Board of Directors and General Director
  - Provisions describing the role of the Chairman of the Board of Directors
  - Requirement of a minimum number of independent directors
  - Additional provisions governing the criteria for establishing the “independence” of independent directors
  - Provisions on access to information, and professional development for directors of the Company
  - Provisions governing the principles of directors` remuneration
  - Provisions concerning treatment of inside information
  - Provisions for responsibilities of the Board of Directors to ensure effective risk management system
  - Provisions for evaluation of performance of the Chairman and members of the Board of Directors
  - Provisions for appointment/re- appointment of the Board of Directors members

Current version of the Corporate Governance Code of the Company is available on KMG EP’s website.

During 2012 the Company complied with the provisions of Kazakhstan Corporate Governance Code in all significant aspects.

During 2012 the Company complied with the provisions of its Corporate Governance Code in all significant aspects, except the following:

- The Corporate Governance Code of the Company provides that at least one third of the Board of Directors members must be independent directors.

Until September 2012 the Board of Directors comprised eight members including the Chairman and three independent non-executive Directors: Philip Dayer, Paul Manduca, and Edward Walshe. On October 1, 2012 Paul Manduca left the Board of Directors, and up to the end of 2012 no independent director was appointed. Therefore, from October 1, 2012 the requirement of the Corporate Governance Code of the Company with respect to the number of independent directors within the Board of Directors was not complied.

- The Corporate Governance Code of the Company provides that Nominations Committee formed by the Board of Directors makes recommendations to the Board of Directors on nominees to the Board of Directors for approval of a resolution for the General Meeting of Shareholders when the decision on the appointment of a director is made.

Nominations Committee developed requirements for the position of independent director, and on the basis of surveys made by external consultants made recommendations to the Board of Directors about the candidate to be elected. However the Board of Directors did not decide on the matter due to a disagreement on behalf of the Nominations Committee of NC KMG with the criteria for election of a candidate.

Given the refusal of the Nominations Committee of NC KMG to endorse the candidate proposed to be elected as a third independent director, the Company now has only two independent directors. This represents a breach of the Company's Charter and a violation of the Law of the Republic of Kazakhstan "On Joint Stock Companies". At the time of the Company's IPO in September 2006, NC KMG entered into a Relationship Agreement with the Company whereby NC KMG undertook, inter alia, that 'NC KMG shall not vote on any resolution of the shareholders (or any resolution of the Board of Directors) to appoint or remove any independent director of the Company' except in certain circumstances that are not relevant in this instance.

- According to the Corporate Governance Code of the Company, directors should meet without the participation of the Chairman of the Board of the Directors at least once a year to evaluate the performance of the Chairman of the Board of the Directors, and in other cases, if required.

Throughout 2012 the independent non-executive directors met eight times without the Chairman of the Board to discuss the following issues: Company's development strategy; relationship between the Company and its majority shareholder; cash funds management and observance of the Treasury Policy; internal audit and internal control matters; Company's related party transactions; appointment of the Board of Directors and succession policy; implementation of the insurance program. The evaluation of performance of the Chairman of the Board of Directors was not formally carried out by directors. However, the performance of the Board of Directors is annually evaluated by an independent consultant.

- The Corporate Governance Code of the Company provides an obligation for the Board of Directors (together with the Audit Committee) at least once a year to carry out an evaluation of the effectiveness of the risk management system.

The Board of Directors does not have a separate risk committee, and the role described above has been allocated to the Audit Committee of the Board of Directors according to the provisions of the committee. More detailed information about the Audit Committee is provided on page 31 of this report. In 2012 the evaluation of the effectiveness of the risk management system was not carried out by the Board of Directors. However the information on risk factors is provided in the Annual Report.

## **DIFFERENCES BETWEEN THE CODE ON CORPORATE GOVERNANCE OF THE COMPANY AND THE PROVISIONS OF THE UK CORPORATE GOVERNANCE CODE**

Below are the main differences between the Corporate Governance Code of the Company and provisions of the UK Code:

- According to the provisions of the UK Corporate Governance Code the chairman should upon appointment meet the independence criteria set out therein.

The Corporate Governance Code of the Company does not contain the provisions on independence of the Chairman of the Board of Directors, and according to the opinion of the Directors the Chairman of the Board of Directors would not meet the criteria of independence stated in the respective provisions of the UK Corporate Governance Code or the respective provision of the Corporate Governance Code of the Company. The Chairman of the Board of Directors is representing the majority shareholder.

- According to the UK Corporate Governance Code at least half of the members of the Board of Directors, excluding the Chairman, should be independent non-executive directors.

In contrast, the Corporate Governance Code and the Charter of the Company provide that at least one third of the Board of Directors' members shall be independent non-executive directors.

According to the Charter of the Company a number of key issues including related-party transactions, major transactions, approval of social expenses, subsoil use contracts, require the approval of majority of the independent non-executive directors. The Charter of the Company can be found on the Company's website.

- The UK Corporate Governance Code also states that the Board of Directors shall appoint one of the independent non-executive directors to be a senior independent non-executive director.

The Corporate Governance Code of the Company does not provide for the appointment of a senior independent director by the Board of Directors, taken into account the current shareholders' structure. The requirement for a senior independent director will be taken into consideration from time to time.

- The UK Corporate Governance Code states that non-executive directors should scrutinize the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible.

The Corporate Governance Code of the Company imposes such requirements to all members of the Board of Directors.

- The UK Corporate Governance Code provides that the non-executive directors are responsible for determining appropriate levels of remuneration of executive directors and have a prime role in appointing and, where necessary, removing executive directors, and in succession planning.

The Corporate Governance Code of the Company places responsibility for determining appropriate levels of remuneration of executive directors on the Remuneration Committee of the Board of Directors, and provides for involvement of the Remuneration Committee of the Board of Directors in appointment and removal of executive directors. In practice, determining the level of remuneration of the Board of Directors' members and their appointment is under the influence of the majority shareholder.

## **DIRECTORS' RESPONSIBILITY STATEMENT**

In accordance to the Corporate Governance Code of the Company the Board of Directors and the Management Board shall be responsible for the fair presentation of the Company's Annual Report and Financial Statement.

In compliance with the UKLA Disclosure and Transparency Rules, each of the directors (as stated on pages 7-8 hereof), confirms that to the best of his or her knowledge:

- The financial statement prepared in accordance with the International Financial Reporting Standards (IFRS) gives a true and fair account of the assets, liabilities, financial position, the results of the financial and economic activities of the Company, consolidated balance sheets of the Company and its subsidiaries;
- The management Report includes a fair review of the results of the financial and economic activities, and financial position of the Company, its joint obligations with its subsidiaries, as well as the description of the principal risks and uncertainties they face.

## STRUCTURE OF THE BOARD OF DIRECTORS

As of December 31, 2012 the Board of Directors consisted of seven members, including:

<b>Name</b>	<b>Position</b>
Lyazzat Kiinov	Chairman of the Board of Directors
Alik Aidarbayev	Member of the Board of Directors (General Director)
Yerzhan Zhangaulov	Member of the Board of Directors
Assiya Syrgabekova	Member of the Board of Directors
Timur Bimagambetov	Member of the Board of Directors
Philip Dayer	Independent Director
Edward Walshe	Independent Director

At the extraordinary general shareholder`s meeting on February 27, 2012 the following decisions were made:

- The powers of Askar Balzhanov as a member of the Board of Directors were terminated;
- Lyazzat Kiinov was elected as a member of the Board of Directors.

On March 13, 2012 by the decision of the Board of Directors Lyazzat Kiinov was appointed as the Chairman of the Board of Directors of the Company.

At the annual general shareholders` meeting on May 29, 2012 the following decisions were made:

- The powers of Sisengali Utegaliyev as a member of the Board of Directors were terminated;
- Timur Bimagambetov was elected as a member of the Board of Directors.

Paul Manduca left the Board of Directors from October 1, 2012 due to his appointment as a Chairman of Prudential plc.

In accordance with the Corporate Governance Code of the Company, the Company`s Board of Directors has established the fact of the independence of the Directors and believes that Philip Dayer and Edward Walshe are independent in character and in decision making. The Board of Directors has found no relations or circumstances which had or could have a significant impact on making independent decisions by these directors.

## STRUCTURE OF THE MANAGEMENT BOARD

In 2012, the Management Board of the Company consisted of senior executives, including General Director and his deputies.

The members of the Management Board as of December 31, 2012 are listed below:

<b>Name</b>	<b>Position</b>
Alik Aidarbayev	General Director and Chairman of the Management Board
Abat Nurseitov	Deputy General Director for production
Malik Saulebay	Managing Director for legal issues
Benjamin Fraser	Managing Director – financial controller
Botagoz Ashirbekova	Managing HR Director

During the year the Board of Directors adopted following decisions on the composition of the Management Board:

1. On January 26, 2012 on:
  - Termination of powers of the following members of the Management Board:
    - Eshmanov Kiikbay
    - Bekezhanova Zhanneta
    - Aubakirov Askar
    - Biseken Bagitkali
    - Khituov Taras
    - Zhamauov Zhumabek
  - Election of new members of the Management Board:
    - Nurseitov Abat
    - Fraser Benjamin
    - Saulebay Malik
    - Salimov Eldan
    - Ashirbekova
2. On June 23, 2012 on termination of powers of Miroshnikov Vladimir as a member of the Management Board
3. On September 28, 2012 on termination of powers of Salimov Eldan as a member of the Management Board

## **RESPONSIBILITY OF THE BOARD OF DIRECTORS AND THE MANAGEMENT BOARD**

The responsibilities between the Board of Directors, the Management Board and General Director of the Company are allocated in accordance with the Charter of the Company, Sections 12 and 13. Further the authorities and responsibilities of the Board of Directors and the Management Board are regulated by the Board of Directors Regulation and the Management Board Regulation.

The Board of Directors is responsible to shareholders for effective management and proper control over the activities of the Company, and acts in accordance with the approved decision-making system. The most important functions of the Board of Directors are to identify areas of strategic development and policy of the Company, making decisions on potential acquisitions of oil and gas assets, and other significant issues.

The Management Board, in turn, is responsible for developing an action plan to implement these functions and for daily operational activities of the Company. The Management Board reports to the Board of Directors on the progress towards achieving objectives of the Company.

The Board of Directors meets on a regular basis and as necessary.

During 2012 the Board of Directors held 29 meetings, including 6 meetings in person, 21 in the form of written consent, and 2 meetings via telephone conference call.

During the year the Board of Directors reviewed among others the following issues:

- Review the issues related to implementation of the Company's Development Strategy
- Approval of the Company's budgets and business plans

- Exploration program
- Shares buy-back program
- Health, safety and environment issues
- Issues related to amendments to subsoil use contracts
- Relationship with affiliates, subsidiaries of NC KMG
- Approval of Company's related party transactions (transaction in respect of oil supplies to the domestic market in the second half of the year has not been approved by the Board of Directors. More detailed information is given in note 23 to the consolidated financial statements and the section "Domestic sales in Kazakhstan" of the Operating and Financial Review 2012)
- Setting up two subsidiaries on the basis of the production units: Ozenmunaigaz JSC and Embamunaigaz JSC, as well as Drilling Well Servicing Division LLP and Support Service Vehicles and Well Servicing Division LLP
- Transfer of subsoil use rights to the abovementioned subsidiaries - Ozenmunaigaz JSC and Embamunaigaz JSC
- Sale of interest in Kazakhstan Petrochemical Industries Inc. LLP
- Engagement of a partner in Karpovskiy North project
- Matters within the competence of the supreme bodies of subsidiaries
- Issues of compliance, issues on observance of the UK Bribery Act
- Election of new Chairman of the Board of Directors
- Formation of committees of the Board of Directors
- Election of members of the Management Board
- Determining the amount of salaries and conditions of remuneration and bonuses of the members of the Management Board
- Granting options under the Company's options program
- Preliminary approval of the Company's consolidated financial statements for the 2011
- Introducing proposals on the amount of dividends by the results of 2011
- Report of the Board of Directors and Management Board for 2011
- Report on assessment of performance of the Board of Directors for 2011
- Review of plans and reports of the internal audit department, the status of implementation of the recommendations of the internal audit department
- The performance of key performance indicators (KPIs) of the internal audit department and internal audit department's staff issues

In 2012 the Board of Directors approved the following documents:

- Revised Corporate Governance Code (preliminary approval)
- Code of Corporate Ethics
- Charters and internal documents of subsidiaries

The Board of Directors also reviewed and recommended to the General Meeting of Shareholders to make amendments to the Charter of the Company.

**PRESENCE OF THE MEMBERS OF THE BOARD OF DIRECTORS AND THE MEMBERS OF THE COMMITTEES AT MEETINGS OF THE BOARD OF DIRECTORS AND COMMITTEES (2012)**

	<b>Board of Directors</b>	<b>Audit Committee</b>	<b>Nominations Committee</b>	<b>Remuneration Committee</b>	<b>Strategic Planning Committee</b>
<b>Number of meetings held in 2012</b>	<b>29</b>	<b>5</b>	<b>3</b>	<b>7</b>	<b>1</b>
Lyazzat Kiinov	22	-	1	-	-
Sisengali Utegaliyev	5	-	-	-	-
Alik Aidarbayev	29	-	3	-	1
Yerzhan Zhangaulov	28	-	-	-	-
Assiya Syrgabekova	29	-	-	-	-
Timur Bimagambetov	19	-	-	-	-
Paul Manduca	23	4	2	6	-
Philip Dayer	29	5	3	7	-
Edward Walshe	29	5	3	7	1

The Management Board is an executive authority and regulates the Company's current activities. In 2012 39 meetings of the Management Board were held on a regular basis and as necessary.

In 2012 the Management Board reviewed following key issues related the Company's operating activities:

- On approval of setting up the Drilling Well Servicing Division LLP (UBR)
- On approval of setting up the Support Service Vehicles and Well Servicing Division LLP (UTTiOS)
- On approval of revised budget for 2012
- On investment strategic project "Setting up and development of JSC "Ozenmunaigas" and JCS "Embamunaigas" on the basis of property and property rights of JSC "KMG EP"
- On project "Setting up and business setup of UTTiOS LLP and business unit of OMG UBR LLP
- On approval of number of procedures regulating internal activities of the Company.

The Management Board also makes decisions on other issues of the Company's operations, not pertaining to the exclusive competence of the General Meeting of Shareholders, the Board of Directors and officials of the Company.

## **AUDIT COMMITTEE**

### **MEMBERS OF THE AUDIT COMMITTEE**

In 2012 this committee was composed of only independent Directors, namely, Philip Dayer (Chairman of the committee) and Edward Walshe. From October 1, 2012 due to the early termination of the powers of an independent Director Paul Manduca, Philip Dayer is the Chairman of the committee. Appointments to the Audit Committee are made for the period of three years, and can be extended by the Board of Directors not more than for two additional three years periods, provided that the members of the Audit Committee are independent.

### **NUMBER OF MEETINGS**

During 2012 the Audit Committee held five meetings. The Chairman of the Audit Committee makes the decisions about the frequency and timing of the meetings. The number of meetings is determined in accordance with requirements to the duties of the committee. At the same time at least four meetings per year must be held, which should coincide with key dates of the cycle of preparation of financial reporting and audit of the Company (when audit plans of internal and external auditors are prepared, and when the interim financial statements, preliminary announcements and the annual report near completion).

### **RESPONSIBILITIES AND DUTIES OF THE AUDIT COMMITTEE**

The Audit Committee is responsible, among other things, for any reports containing financial information of the Company, monitoring risk management and internal controls, and for involvement of the auditors of the Company in this process. It also receives information from the internal audit department of the Company, which monitors compliance with internal control procedure of the Company. In particular, the committee deals with issues of compliance with legal requirements, accounting standards, applicable rules of the UK Listing Authority (UKLA) and the Kazakhstan Stock Exchange (KASE), ensuring effective system of internal control. The Board of Directors is also responsible for preliminary approval of annual financial report.

The Audit Committee periodically reviews major transactions on acquisitions and disposals, and considers any issues that the Board of Directors may refer to the Audit Committee's review.

Every year at the General Meeting of Shareholders, the Chairman of the Audit Committee through the Chairman of the Board of Directors shall report the results of the Audit Committee activities and answer questions related to the activities of the Audit Committee.

### **ACTIVITIES OF THE AUDIT COMMITTEE IN 2012**

- Financial statement
  - Review of the issues on preparation of financial statements in compliance with the IFRS
  - Approval of quarterly and annual financial statements to be disclosed to the Kazakhstan and London Stock Exchange
  - Approval of press-releases in relation to financial statements and operating and financial reviews
- Internal audit
  - Review and approval of internal audit department operational plan
  - Internal audit department's staff issues
  - Assessment of the effectiveness of internal audit
- The Company's social expenses
- Forecasts of cash flows of the Company
- Treasury policy compliance

- Compliance
  - Review of the draft of the Code of Corporate Ethics
  - Review of the draft of the revised Corporate Governance Code
  - Review of the draft of the Policy on Countering Bribery;
  - Review of the draft of the Whistleblowing Policy;
  - Review the issues on compliance with the UK Bribery Act

## **REMUNERATION COMMITTEE**

### **MEMBERS OF THE REMUNERATION COMMITTEE**

In 2012 this committee was composed of only independent Directors: Philip Dayer (Chairman of the committee), Paul Manduca until October 1, 2012, and Edward Walshe. Terms of office of the members of the committee coincide with their terms of office as members of the Board of Directors.

### **RESPONSIBILITIES AND DUTIES OF THE REMUNERATION COMMITTEE**

The Remuneration Committee is responsible for monitoring the Company's current system of remuneration of the members of the Board of Directors, General Director, members of the Management Board and other employees of the Company, including the analysis of the remuneration policy in comparison with other companies.

The Remuneration Committee is also responsible for developing and providing recommendations to the Board of Directors on the principles and criteria for determining the amount and terms of remuneration and compensation to the members of the Board of Directors, General Director and members of the Management Board of the Company, and for approving the terms of share option plans of the Company and other long-term incentive programs for managers and employees of the Company.

The Remuneration Committee oversees coordination of the Company's policy of remuneration and current remuneration system of the Company with the development strategy of the Company, its financial situation and the situation on the labour market.

The Remuneration Committee oversees provision of adequate information disclosure in respect of remuneration and compensation of members of the Management Board and the Board of Directors of the Company in accordance with the laws of the Republic of Kazakhstan, the Listing Rules and the Company's internal documents.

In addition, the Remuneration Committee monitors implementation of decisions of the General Meeting of Shareholders with respect to determining the amounts and the procedure in which remuneration is paid to the Board of Directors of the Company.

The Remuneration Committee shall report regularly to the Board of Directors on its work, and also annually review compliance by the committee with the provisions on the Remuneration Committee providing information to the Board of Directors.

### **ACTIVITIES OF THE REMUNERATION COMMITTEE IN 2012**

In 2012 the Remuneration Committee held seven meetings. The committee shall hold meetings as required, but not less than once every six months. Meetings may be convened at the initiative of the Chairman of the committee, any member of the committee or by the decision of the Board of Directors.

In 2012 the Remuneration Committee reviewed the following issues:

- Determining the amount of salaries and conditions of remuneration and bonuses of the members of the Management Board

- Issues related to Options plan
- Issues related to transfer to the personnel incentive system

Total amount of remunerations of independent directors for the year as of December 31, 2012, are listed in the table below:

<b>Name</b>	<b>Annual remuneration, 000 US\$</b>	<b>Physical attendance, 000 US\$</b>	<b>Phone-video conference participation, 000 US\$</b>	<b>Meetings of independent directors, 000 US\$</b>	<b>Committee chairmanship 000 US\$</b>	<b>Total for 2012 (excluding taxes), 000 US\$</b>	<b>Total for 2012 (including taxes), 000 KZT</b>
Paul Manduca	112.5	50	10	15	18.7	206.2	34,126
Edward Walshe	150	60	15	22,5	15	262.5	43,562
Philip Dayer	150	60	15	22,5	15	262.5	43,562
<b>Total</b>	<b>412.5</b>	<b>170</b>	<b>40</b>	<b>60</b>	<b>48.7</b>	<b>731.2</b>	<b>121,250</b>

Other members of the Board of Directors do not receive remuneration as the members of the Board of Directors, but shall be entitled to reimbursement for costs associated with such appointment.

#### **NOMINATION COMMITTEE**

In 2012 the members of the Nominations Committee were: Alik Aidarbayev (the Chairman of the committee until June 26, 2012), Lyazzat Kiinov (from June 26, 2012), Edward Walshe (acting Chairman of the committee), Paul Manduca (member of the committee until October 1, 2012), and Philip Dayer.

The main purpose of the committee is to increase efficiency and quality of work of the Board of Directors in selection of professionals to fill positions in the Company, as well as to ensure succession in changing officers of the Company, to define criteria for selection of candidates for the Board of Directors, General Director, members of the Management Board, and company secretary.

The Nominations Committee considers matters related to changing the membership of the Board of Directors and Management Board, with termination of office and appointment of the Company, his/her retirement, and appointment of additional and alternate directors.

#### **ACTIVITIES OF THE NOMINATIONS COMMITTEE FOR 2012**

During 2012 the committee held three meetings, where the following issues were discussed:

- Involving of a company for searching a candidate to the position of an independent director of the Company
- Defining the criteria of the candidate for the position of the independent director of the Company
- Recommendations to the Board of Directors for election of an independent director
- Recommendation to the Board of Directors on the membership of the committees of the Board of Directors

- Recommendation on election of a member of the Management Board

## **STRATEGIC PLANNING COMMITTEE**

In 2012 the members of the Strategic Planning Committee were: Edward Walshe (Chairman of the committee), Alik Aidarbayev (until January 18, 2013), Timur Bimagambetov, and Philip Dayer (from June 26, 2012).

The main purpose of the committee is to develop and provide recommendations to the Board of Directors on setting the priorities of the Company and its development strategy.

### **ACTIVITIES OF THE COMMITTEE ON STRATEGIC PLANNING FOR 2012**

In 2012 the committee held one meeting, where the following issues were discussed:

- Issues related to implementation of the current Company's Development Strategy
- Exploration program
- Business development, acquisition program
- Problems in implementing production plans and their resolution
- The structure of the interaction with Ozenmunaigaz JSC and Embamunaigaz JSC

The committee was advised during this meeting that NC KMG's strategy was under review and that discussion of the Company's strategy should await the outcome of that review. NC KMG has made a copy of its strategy available to the committee in January 2013.

## **STAKES OF THE MEMBERS OF THE BOARD OF DIRECTORS**

Stakes of the members of the Board of Directors in common, preferred shares and GDRs of the Company, according to information provided by members of the Board of Directors as of December 31, 2012 are the following:

<b>Name</b>	<b>Ordinary shares</b>	<b>GDRs</b>	<b>Preferred shares</b>
Philip Dayer	-	6,828	-
Edward Walshe	-	-	-

## **MAJOR SHAREHOLDERS AND/OR GDR HOLDERS**

In accordance with the laws of the Republic of Kazakhstan below is the list of holders of securities of the Company, who own shares as of December 31, 2012, the number of which must be reported. This requirement does not apply to holders of GDR, however, the Company considers it necessary to specify the information that on September 30, 2009, the State Investment Fund of the People's Republic of China Investment Corporation (CIC) announced on acquisition of GDR amounting to about 11% of the shares of the Company in the form of GDRs.

<b>Shareholder</b>	<b>Ordinary shares</b>	<b>Preferred shares</b>	<b>Total numbers of shares placed</b>
Amount of shares issued	70,220,935	4,136,107	74,357,042
In possession of JSC NC KazMunaiGas	43,087,006	-	43,087,006
Percentage of issued share capital	61.36%	0.00%	57.95%

## **CONTRACTS OF DIRECTORS, LETTER OF APPOINTMENT OF DIRECTORS AND LABOR CONTRACTS OF MEMBERS THE MANAGEMENT BOARD**

## CONTRACTS WITH DIRECTOR

- The powers of Askar Balzhanov as a member of the Board of Directors were terminated on February 27, 2012;
- Lyazzat Kiinov was elected as a member of the Board of Directors on February 27, 2012;
- The powers of Sisengali Utegaliyev as a member of the Board of Directors terminated on May 29, 2012;
- Timur Bimagambetov was elected as a member of the Board of Directors on May 29, 2012.

## LABOUR CONTRACTS OF MEMBERS OF THE MANAGEMENT BOARD

All the members of the Management Board signed labour contracts with the Company in accordance with the internal rules of the Company. Except for the foregoing, it is not expected to enter into any other employment agreements with members of the Company's Board of Directors or Management Board members.

## INTERNAL CONTROL AND RISK MANAGEMENT

Company operates a system of internal control and risk management. The system is developed for identifying, evaluating and managing significant risks in order to achieve its strategic goals and to preserve and increase shareholder value.

System is based on firmly-established international practices, as well as on the requirements of the Listing Rules of the London Stock Exchange and the UK Combined Code of Corporate Governance.

The existing chain of authority and interaction between elements of the internal control system provides a level of independence necessary for its effective functioning, and in line with best international practice in this area.

The key elements of the Company's internal control include:

- The internal company documents such as financial, operational, administrative policies, policies for managing the funds and other procedures.
- Constant monitoring of the operating and financial activities and related work in compliance with the safety requirements of the Company.

The internal audit service of the Company provides the Board of Directors with objective information about how effectively the system of internal control of the Company operates. In its work the internal audit service uses a risk-oriented approach which allows identifying and focusing maximum attention on the critical areas of the Company, thereby helping to improve the Company's overall performance and the quality of its corporate governance. The internal audit service monitors the implementation of the recommendations by the management and reports thereon to the Audit Committee and the Board of Directors.

With regard to risk management, the Management Board established a Committee on Risk Management and more detailed information on its activities is presented below.

## RISK MANAGEMENT COMMITTEE

The Risk Management Committee has been set up under the Management Board.

The main purpose of the committee is a prompt consideration of risk management issues in the Company. The committee may make recommendations to the Management Board on risk management, and monitoring the effectiveness of risk management systems and make recommendations to structural units of the Company to improve the risk management system in order to make business processes more efficient and achieve the strategic goals of the Company.

In addition the financial risks information can be found in the Operating and Financial Review, beginning from page 40. General information on the risk profile of the Company can be found in the Risk Factors section on page 55.

## **INFORMATION ON TAXATION IN THE UK**

The overview given below is based on the UK law and the HM Revenue & Customs practices in force as at the date of this document, both of which are subject to change, possibly with retrospective effect. Except where otherwise stated, the overview discusses only certain UK tax consequences for absolute beneficial owners of shares or GDRs who are (1) considered to be UK residents for tax purposes; (2) considered to be residents for tax purposes in no other jurisdiction; and (3) not in possession of a permanent establishment in the Republic of Kazakhstan to which the holding of shares or GDRs is related (“the UK Holders”).

In addition, this overview (1) addresses only the tax consequences for the UK Holders who own shares and GDRs as capital assets and it does not address the tax consequences that may apply to certain other categories of the UK Holders, e.g. dealers; (2) assumes that the UK Holder does not, directly or indirectly, control 10% or more of the voting shares of the Company; (3) assumes that a holder of the GDRs is beneficially entitled to the underlying shares and to the dividends on those shares; and (4) does not address the tax consequences for the UK Holders that are insurance companies, investment companies or pension funds.

The following is intended only as a general guide and is not intended to be, nor should be considered to be, legal or tax advice to any particular UK Holder. Accordingly, investors should satisfy themselves as to the overall tax consequences, including, specifically, the consequences under the UK law and HM Revenue & Customs practice, of the acquisition, ownership and disposal of shares or GDRs in their own particular circumstances.

### **WITHHOLDING TAX**

On the assumptions that income received from GDRs is from a non-UK source for tax purposes, it should not be subject to withholding tax in the UK. Dividend payments on shares will not be subject to the UK withholding tax.

### **TAXATION OF DIVIDENDS**

A UK Holder receiving a dividend on shares or GDRs may be subject to the UK income tax or corporation tax, as the case may be, on the gross amount of any dividend paid before the deduction of any Kazakhstan withholding taxes, subject to the availability of any credit for Kazakhstan tax withheld. A UK Holder who is an individual resident and domiciled in the UK will be subject to UK income tax on the dividend paid on shares or GDRs and is entitled to a non-refundable tax credit equal to one ninth of the amount of dividend received. A UK Holder who is an individual resident but not domiciled in the UK and who is entitled and prefers to be taxed in the UK on the remittance basis will be subject to the UK income tax on the dividend paid on shares or GDRs to the extent that the dividend is remitted or treated as remitted to the UK, and will also be entitled to a non-refundable tax credit equal to one ninth of the amount of dividend received.

A UK Holder which is a company residing in the UK for tax purposes is not subject to the UK corporate tax on the dividend paid on shares or GDRs, unless certain anti-avoidance rules in the tax law apply.

### **TAXATION OF DISPOSALS OR DEEMED DISPOSALS**

The disposal by a UK Holder of interests in the shares or GDRs may result in a chargeable gain or an allowable loss for the purposes of UK taxation of chargeable gains, depending on the UK Holder’s circumstances and subject to any available exemption or relief. A UK Holder who is an individual resident and domiciled in the UK will generally be liable to UK capital gains tax on chargeable gains made on the disposal of an interest in the shares or GDRs. A UK Holder who is

an individual resident but not domiciled in the UK and who is entitled and prefers to be taxed in the UK on the remittance basis will generally be liable to the UK capital gains tax to the extent that the chargeable gains made on the disposal of an interest in the shares or GDRs are remitted or treated as remitted in the UK. In particular, dealings in the GDRs on the London Stock Exchange may give rise to remitted profits that would, therefore, give rise to the UK capital gains tax liability.

An individual holder of shares or GDRs who ceases to be a resident or an ordinarily resident in the UK for tax purposes for a period of less than five full tax years and who disposes of such shares or GDRs during that period may also be liable on returning to the UK to UK tax on capital gains, even though the individual may not be a resident or an ordinarily resident in the UK at the time of the disposal.

A corporate UK Holder will generally be subject to the UK corporation tax on any chargeable gains arising from a disposal of shares or GDRs.

#### EFFECT OF KAZAKHSTAN WITHHOLDING TAXES

Dividend payments in respect of shares and GDRs are subject to the Kazakhstan withholding tax. A UK Holder, who is an individual resident, should generally be entitled to a credit for Kazakhstan tax properly withheld from such payments of against the UK income tax liability on such amounts, subject to UK tax rules for calculation of such a credit. A UK Holder, which is a company, is not generally subject to UK corporation tax on the dividend payment and so usually is not be able to claim credit for any such Kazakhstan withholding taxes.

#### STAMP DUTY AND STAMP DUTY RESERVE TAX (“SDRT”)

Assuming that any document effecting the transfer of, or containing an agreement to transfer, one or more shares or GDRs is neither (i) executed in the UK nor (ii) relates to any property located in the UK, or to any matter or thing done or to be done in the UK (which may include involvement of UK bank accounts in payment mechanism), then no UK ad valorem stamp duty should be payable on such a document.

Even if the document effecting the transfer of, or containing an agreement to transfer, one or more shares or GDRs is (i) executed in the UK and/or (ii) relates to any property located in the UK, or to any matter or thing done or to be done in the UK, in practice it should not be necessary to pay any UK ad valorem stamp duty on this document unless the document is required for any purposes in the UK. If it is necessary to pay the UK ad valorem stamp duty, it may also be necessary to pay interest and penalties associated therewith.

As the GDRs relate to the securities expressed in a currency other than sterling, no “bearer instrument” stamp duty should be payable on either the issue of the GDRs or any transfer of the securities transferable by means of the GDRs.

Assuming that the shares are neither (i) registered in the UK register nor (ii) paired with shares issued by a company incorporated in the UK, no SDRT should be paid in respect of any agreement to transfer shares or GDRs.

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## OPERATING AND FINANCIAL REVIEW

The following document is intended to assist the understanding and assessment of trends and significant changes in the Company's results and financial condition. This review is based on the consolidated financial statements of the Company and should be read in conjunction with those statements and the accompanying notes. All the financial data and discussions thereof are based on consolidated financial statements prepared in accordance with IFRS.

### Overview

KazMunaiGas Exploration Production Joint Stock Company (“the Company” or “KMG EP”) is engaged in the exploration, development, production, processing, export of hydrocarbons and the acquisition of oil and gas assets. The Company’s core operations are oil and gas properties located in the Pre-Caspian, Mangistau and Southern Torgai basins. The Company’s majority shareholder is JSC National Company KazMunaiGas (NC KMG), the wholly state-owned joint stock company, which represents the state’s interests in the Kazakh oil and gas industry. The Company conducts its core production activities at 47 oil and gas fields, including JSC “Ozenmunaigas” (“OMG”), which consists of 2 fields, JSC “Embamunaigas” (“EMG”), which consists of 40 fields and “Kazakh Gas Refinery” LLP which consists of 5 fields. The Company also has a 51% interest in joint venture KS EP Investments BV, 50% in Kazgermunai LLP, CCEL, Ural Group Limited BVI (“UGL”) and a 33% interest in its associate PetroKazakhstan Inc.

The Company is carrying out onshore exploration in the areas of Liman, Taisoigan, Karaton-Sarkamys, Uzen-Karamandybas, Novobogatinsk Western, Fedorovskiy block (“UGL”), Karpovskiy Severniy (“Karpovskiy KS EP Investments BV), Temir, Teresken, Zharkamys Eastern -1 (“KMG EP Exploration assets”) and also holds a 35% interest in the license to farm-in into a BG Group operated license in the United Kingdom Central North Sea – a production license which contains the White Bear prospect.

The Company’s total oil production in 2012, together with the share of its joint ventures and its associate companies, was approximately 12,191k tonnes or 247kbopd. This includes oil derived from its 50% share in JV Kazgermunai LLP, its 50% share in CCEL and its 33% stake in PetroKazakhstan Inc. OMG and EMG produced 156kbopd with a further 39 kbopd from PetroKazakhstan Inc., 33 kbopd from JV Kazgermunai LLP and 19 kbopd from CCEL.

Operating and Financial Review covers the activities of abovementioned companies.

### Business Environment and Outlook

Macroeconomic factors affecting the Company's financial performance for the year under review include movements in crude oil prices, domestic inflation, and foreign exchange rates, particularly the Tenge-US dollar rate.

#### Business Environment for 2012

The average Brent price in 2012 was US\$ 111.70 per barrel, which is almost the same as in the 2011.

Q4 2012	Q3 2012	Q4 2011	Q4 on Q4 change		2012	2011	Change
	(US\$ /bbl)		%			(US\$ /bbl)	%
110.10	109.50	109.36	0.7%	Brent (DTD)	111.70	111.26	0.4%

Most of the Company's revenues, financial assets and borrowings are denominated in US dollars, while most of the Company's operating expenses are denominated in Tenge. The Company

manages currency risk by reducing or increasing the share of financial instruments denominated in US dollars in its portfolio.

Tenge-US dollar exchange rates and domestic inflation, as measured by the consumer price index ("CPI") were as follows:

Q4 2012	Q3 2012	Q4 2011	Q4 on Q4 change		2012	2011	Change
150.44	149.68	147.91	1.7%	Average US\$ vs KZT	149.11	146.62	1.7%
2.1%	1.2%	1.2%	75.0%	CPI	6.0%	7.4%	-18.9%
150.74	149.86	148.40	1.6%	US\$ vs KZT at balance sheet date	150.74	148.40	1.6%

Source: National Bank of Kazakhstan

The Tenge weakened against the US dollar from average 146.62 KZT/US\$ in 2011 to 149.11 KZT/US\$ in 2012. The inflation rate in 2012 was 6.0% compared to 7.4% in 2011.

## Production Activity

Production of crude oil from core assets in 2012 was 7,766k tonnes which is 2% lower than in 2011.

Q4 2012	Q3 2012	Q4 2011	Q4 on Q4 change		2012	2011	Change
1,251	1,232	1,293	-3%	OMG	4,950	5,082	-3%
720	720	715	1%	EMG	2,816	2,818	0%
<b>1,971</b>	<b>1,952</b>	<b>2,008</b>	<b>-2%</b>	<b>Total production</b>	<b>7,766</b>	<b>7,900</b>	<b>-2%</b>

As previously reported, lower production compared with 2012 reflected an increase in idle wells, lower turnaround time and geological and technical problems which created a backlog in the crude oil production plan.

The backlog was exacerbated by the poor quality and late delivery of some underground equipment and spare parts. Other factors included worn out surface and underground well infrastructure, problems preparing sea water and waste water for injection, difficulties with the application of chemicals at oil production facilities and in well plugging. Poor discipline and work organisation also contributed to other difficulties such as downtime caused when underground well repair teams had to await delivery of machinery and equipment.

All these factors affected the quality and frequency of repair work to underground wells and equipment and contributed to the increase in idle wells and failure to achieve production targets. But production was also adversely affected by disruptions to the electricity supply during 2012 and adverse weather conditions with temperatures falling below minus 20 degrees centigrade, heavy snowfalls, storms and flooding. Taken together these problems led to a sharp decline in oil production and failure to fill the production plan.

As of January 1, 2013, the Company operated a total of 5,981 production and 1,670 injection wells: 3,698 production and 1,212 injection wells at OMG and 2,283 production and 458 injection wells at EMG. Most of the company's existing oil fields are at a mature stage of development, characterized by high water content and declining oil production. In order to mitigate this natural production decline and achieve its production targets the Company engages in production drilling, work-over and enhanced recovery operations.

In 2012 OMG drilled and put into operation 181 wells (104 oil producing, 77 injection), 9 more wells than in 2011. Oil production generated by new wells was 151k tonnes compared to 186k tonnes in 2011. The workover of 675 wells provided an incremental production of 248k tonnes. At

the same time, well operations for hydro-fracturing at OMG declined by 39 to a total of 111 while additional production from hydro-fracturing at 120k tonnes was 103k tonnes less than in 2011.

In 2012 EMG drilled and put into operation 65 wells (59 oil producing, 6 injection), which is around equivalent to 2011. Oil production generated by new wells rose to 86k tonnes compared to 71k tonnes in 2011. The workover of 282 wells provided an incremental production of 90k tonnes. Hydro-fracturing operations took place at 10 wells, similar to 2011. Additional production from hydro-fracturing in 2012 was 25k tonnes, some 9k tonnes more than 2011.

Crude oil production in 2013 at core assets is planned to be 8.1 million tonnes, including 5.3 million tonnes at OMG and 2.8 million tonnes at EMG. In order to ensure this production volume in 2013, the Company is planning to drill 182 oil producing wells and 98 injection wells: 115 production and 93 injection wells at OMG and 67 production and 5 injection wells at EMG. The Company also plans to apply at its existing wells hydraulic fracturing, workover, bottomhole zone treatment and bringing inactive production wells back into production or reactivate them.

## Exploration Activity

In 2012 the Company continued exploration works on the following blocks Liman, Taisoigan, Karaton-Sarkamys, Uzen-Karamandybas, Temir, Zharkamys Eastern-1, Fedorovskiy, Karpovskiy Severniy and White Bear area and appraisal works in the S. Nurzhanov, Prorva Western, Novobogatinsk Western and Eastern Makat fields.

### *Exploration works*

On the Liman block in 2012 drilling of wells G-2 and G-5 on the field Novobogat Southeast on productive postsalt Middle Triassic sediments has been completed, drilled depth was 1200 m and 1328 m respectively. On the well G-2 at the second test object using a jet pump obtained a flow with a debit of 2.5 m<sup>3</sup>/day, the well was put into conservation until the input of field into test operation. Well G-5 is in the stage of testing of productive objects. In addition, on the field Novobogat Southeast continued drilling of well PR-1 for permotriassic subsalt deposits, with a planned depth of 2500m, as of December 31, 2012 1912m has been drilled.

In 2013 the Novobogat Southeast (post-salt) field is planned to go into test operation involving degreasing putting exploratory wells into operation and drilling two new wells. These are the G-6 advanced-mining well and the G-7 exploratory well with a projected depth of 1500m each, in order to clarify the geological structure and determine production potential. On the field Novobogat Southeast the drilling of well PR-1(subsalt) will be completed, by the results of tests, will be decided on drilling of the second exploration well in the PR-2.

At the Taisoigan block, the drilling of exploratory well U-1 was completed to a depth of 1366m. Oil inflow (1m<sup>3</sup>/day) obtained during testing of third object, testing is underway. To revise geological model of the structure Bazhir, 3D-CMP seismic works have been conducted in the volume of 86 sq.km.

At the block Taisoigan exploration drilling is planned for 2 wells at structures Uaz and Bazhir, with a projected depth of 1250m (jurassic sediments) and 1400m (triassic sediments) respectively. Seismic 3D-CMP works for 170 sq. km is planned to be performed on Uaz-Kondybai structure to revise geological model and discover new objects.

At Karaton-Sarkamys block, 160 sq.km 3D-CMP seismic works have been conducted and processed on the structures S. Nurzhanov, Severniy and Bulatai. Magnetotelluric sounding and reprocessing of 1,360 sq.km of 3D-CMP data on Kenaral and Dosmuhambetovskoe structures has been completed.

In 2013, at Karaton-Sarkamys block there has been planned an analysis of geological and geophysical data in order to identify further exploration activities on the block, by the results of which envisaged drilling of 2 exploratory wells with the depth of 3350 and 3000m, respectively.

On the Uzen-Karamandybas block, an adjacent area to Uzen and Karamandybas, preliminary analysis of earlier exploration work has identified minor perspective structures for oil, but with significant geological risks. In order to determine the future direction of exploration activities in the area, the analysis of geological and geophysical data will be continued.

On Zharkamys Eastern-1 block to assess the hydrocarbon potential of the subsalt sediments completed drilling of exploration well RA-2-T at Tuskum structure, the actual depth was 4502m. Interpretation of GIS data identified two promising sites in the sediments of the lower Visean Carbon for further examination. This is planned to start in the second quarter of 2013 with a new exploratory well RA-3-T which will drill down to a planned depth of 4500m to assess the hydrocarbon potential of pre-salt horizons.

In 2012 at Temir block, gravimetric studies have been carried out on 3,500 sq.km.

In 2013, at Temir block, planned works for 3D-CMP seismic survey in the volume of 200 sq. km in order to prepare for exploratory drilling.

At Karpovskiy Severniy block, drilling of exploration well SK-1 with a projected depth of 5600m on the structure Melovaya has started. As of December 31, 2012 3,727m has been drilled.

In 2013, at the block Karpovskiy Severniy exploration drilling is planned for 1 well at Orlovskaya area, with a projected depth of 5250m, drilling of well SK-1 on the structure Melovaya will be continued. Seismic 3D-CMP works for 460 sq. km is planned to be performed to revise geological model and discover new targets at subsalt deposits.

In the reporting period, at Fedorovskiy block at well U-23 of Rozhkovskoye field, from sediments of the Lower Carbon Tournaisian stage when testing the third object, acid treatment resulted in gas and condensate flow to surface with a debit of 120 m<sup>3</sup>/day and 300 m<sup>3</sup>/day respectively at 11 mm choke. Also drilling works on well U-26 with a projected depth of 5,200m have started. As of December 31, 2012 3674m has been drilled. Reprocessing of 952 sq.km of 3D seismic data at the areas Zhaiyk, Rubezhinskaya, Rozhkovskaya and Chinarevskaya has been completed; interpretation of seismic data is planned in 2013.

In 2013, at Fedorovskiy block it is planned to drill 2 exploratory wells U-11 and U-24 with a projected depth of 4500m each on Rozhkovskaya area. The drilling of well U-26 will be continued.

At White Bear block, drilling of an exploration well 22/04b-6 in the North Sea has been completed at the depth of 5937m. The analysis of drilling results and received geological and geophysical data is underway, by the results of which, will be determined the prospects of further exploration.

#### *Appraisal works*

The works on the reprocessing and interpretation of 3D seismic data, synchronous inversion and litho-fluid models of S.Nurzhanov, Eastern Makat, West Prorva, Novobogat SE and Kenbai fields have been completed.

Drilling of exploration well 701 on the S. Nurzhanov field with a projected depth of 2,000m has been completed. By the results of drilling 3 objects indicated for testing.

In 2013, at S. Nurzhanov field planned to drill 2 wells 703 and 705 with the projected depth of 2,000m each.

The drilling of exploration well 401P on the Western Prorva field has been completed. Drilling of the well was completed at a depth of 3,473m. By the results of final GIS, 4 objects indicated for testing at permotriassic sediments. At testing of the 1st object, well began to pour and then spouting water, oil and gas. Currently works on testing of second object is underway.

In 2013, at Western Prorva field planned to drill well 403-P with the projected depth of 3,500 m. The drilling of exploration well 104 on the field Eastern Makat has been completed. Drilling of the well was completed at a depth of 1,425m. By the results of final GIS, 3 objects indicated for testing at permotriassic sediments. At testing a first object obtained flowed gas. At testing of the 2nd object obtained gushing oil flow with a debit of of 14.3 m3/day on a 9 mm choke, at testing of third object is obtained oil flow with a debit of of 25.7 m3/day on a 9 mm choke, selected deep and surface samples of reservoir fluid.

In 2013, at Eastern Makat field planned to drill well 106 with the projected depth of 1,500 m.

At Novobogatinsk Western field, the drilling of exploratory well G-20 with a projected depth of 2,590m has been completed. Due to absence of productive reservoirs according to geophysics and borehole core data the well has been abandoned.

In 2013, at the field SW Kamyshtovoe in order to clarify the geological structure and confirmation of selected reservoirs in the area of distribution of C2 reserves, planned to drill an exploration well 2Rec with a depth of 1300m.

In 2013, at the S.Balgimbayev field planned to drill an exploration well P-1 with a projected depth of 1500m.

At the field Zhanatalap, in order to transfer oil from the C2 to the industrial category B and C1 in 2013, planned to drill 2 exploration wells, with a projected depth of 730m each.

In 2013, at Akkuduk and B.Zholamanov fields in order to revise the geological model, planned 3D seismic works for 40 sq. km and 70 sq.km, respectively.

## Results of Operations

The Company prepares financial statements in Tenge, the amounts shown in US dollars are included solely for the convenience of the information user at the average exchange rate over the respective period for consolidated statement of comprehensive income and consolidated cash flow statement and at the closing rate for consolidated statement of financial position. See “Business Environment and Outlook”.

### Key Figures

Q4 2012	Q3 2012	Q4 2011	Change %		2012	2011	Change %
(KZT millions, unless otherwise stated)					(KZT millions, unless otherwise stated)		
<b>192,528</b>	<b>206,099</b>	<b>175,448</b>	<b>10%</b>	<b>Revenue</b>	<b>797,170</b>	<b>721,194</b>	<b>11%</b>
36,542	33,087	29,619	23%	Production expenses	140,362	117,465	19%
18,433	29,708	23,559	-22%	Selling, general and administrative expenses	93,088	98,520	-6%
55,329	74,570	66,029	-16%	Taxes other than on income	274,171	284,028	-3%
1,047	731	3,356	-69%	Exploration expenses	6,104	5,985	2%
13,977	14,178	12,602	11%	Depreciation, depletion and amortization	53,747	45,494	18%
77,012	(24)	186	41304%	Impairment of property, plant and equipment	77,012	1,653	4559%
1,381	1,408	646	114%	Loss on disposal of fixed assets	3,189	4,044	-21%
<b>(11,193)</b>	<b>52,441</b>	<b>39,451</b>	<b>-128%</b>	<b>Profit from operations</b>	<b>149,497</b>	<b>164,004</b>	<b>-9%</b>
<b>(12,013)</b>	<b>51,371</b>	<b>44,282</b>	<b>-127%</b>	<b>Net income</b>	<b>160,823</b>	<b>208,931</b>	<b>-23%</b>
2,519	2,302	2,004	26%	Production expenses (KZT per bbl) <sup>(1)</sup>	2,456	2,020	22%
16.74	15.38	13.55	24%	Production expenses (USD per bbl) <sup>(1)</sup>	16.47	13.78	20%
31,803	30,329	37,506	-15%	Capital expenditure <sup>(2)</sup>	108,114	104,977	3%

(1) Converted at 7.36 barrels per tonne of crude oil.

(2) According to purchases of PPE and intangible assets in consolidated statement of cash flows for the period ending December 31, 2012 (see Company website for a copy)

## Transport Routes

The Company delivers its crude oil through three principal routes: export markets via the pipeline owned by Caspian Pipeline Consortium (CPC), the Uzen-Atyrau-Samara pipeline (UAS) owned by KazTransOil JSC (in Kazakhstan) and the domestic market, as outlined in the following table:

Q4 2012	Q3 2012	Q4 2011		2012	2011
			<b>Exports sales via UAS</b>		
0.90	1.04	0.86	Volume of crude oil (in million tonnes)	3.56	3.52
48%	55%	46%	% total crude oil sales volume	46%	46%
56%	61%	57%	% total sales value of crude oil	53%	56%
			<b>Exports sales via CPC</b>		
0.56	0.57	0.53	Volume of crude oil (in million tonnes)	2.52	2.24
30%	30%	28%	% total crude oil sales volume	33%	29%
35%	34%	35%	% total sales value of crude oil	39%	37%
			<b>Domestic sales</b>		
0.40	0.28	0.49	Volume of crude oil (in million tonnes)	1.64	1.90
22%	15%	26%	% total crude oil sales volume	21%	25%
9%	5%	8%	% total sales value of crude oil	8%	7%

The relative profitability of the two export routes depends on the quality of oil in the pipeline, the prevailing international market prices and the relevant pipeline tariffs. Specifically, CPC tends to be the more advantageous route owing to the higher quality of crude oil in the CPC pipeline in a higher price oil environment, even after taking into account quality bank payments. It should be noted that the volume of crude oil that can be shipped through the pipelines has to be agreed with the Ministry of Oil and Gas of the Republic of Kazakhstan; the Company's ability to allocate export volume to different pipelines is, therefore, limited.

## Revenue

The following table shows sales volumes and realized prices:

Q4 2012	Q3 2012	Q4 2011	Change		2012	2011	Change	
(KZT millions, unless otherwise stated)				%	(KZT millions, unless otherwise stated)			
				<b>Export sales of crude oil</b>				
				UAS pipeline				
105,461	123,431	97,677	8%	Net sales	417,831	395,583	6%	
899	1,042	863	4%	Volume (in thousand tonnes)	3,555	3,521	1%	
117,369	118,415	113,216	4%	Average price (KZT/tonne)	117,517	112,344	5%	
107.91	109.43	105.87	2%	Average price (US\$/bbl)	109.01	105.98	3%	
				CPC pipeline				
66,850	68,368	60,743	10%	Net sales	302,431	260,012	16%	
556	571	530	5%	Volume (in thousand tonnes)	2,523	2,237	13%	
120,309	119,783	114,590	5%	Average price (KZT/tonne)	119,889	116,239	3%	
110.61	110.69	107.15	3%	Average price (US\$/bbl) <sup>(1)</sup>	111.21	109.65	1%	
172,311	191,799	158,420	9%	Total sales of crude oil-exported	720,262	655,595	10%	
				<b>Domestic sales of crude oil</b>				
16,077	10,839	13,707	17%	Net domestic sales of crude oil	62,668	52,882	19%	
401	279	489	-18%	Volume (in thousand tonnes)	1,637	1,898	-14%	
40,111	38,874	28,013	43%	Average price (KZT/tonne)	38,278	27,858	37%	
36.87	35.93	26.44	39%	Average price (US\$/bbl) <sup>(1)</sup>	35.51	26.28	35%	
				<b>Total sales</b>				
188,388	202,638	172,127	9%	Total net sales of crude oil	782,930	708,477	11%	
1,855	1,892	1,882	-1%	Total volume (in thousand tonnes)	7,715	7,656	1%	
101,556	107,107	91,452	11%	Average price (KZT/tonne)	101,478	92,535	10%	
93.37	98.98	86.31	8%	Average price (US\$/bbl) <sup>(1)</sup>	94.13	87.29	8%	
4,140	3,462	3,320	25%	Other sales	14,240	12,717	12%	
<b>192,528</b>	<b>206,099</b>	<b>175,448</b>	<b>10%</b>	<b>Total revenue</b>	<b>797,170</b>	<b>721,194</b>	<b>11%</b>	

(1) Average sales price under financial statement (realized price), converted at 7.23 barrels per tonne of crude oil.

### Export – UAS Pipeline

Sales of crude oil exported via the UAS pipeline in 2012 increased by 6% to KZT418 billion due to an increase of the average realized price by 5% to KZT117,517 per tonne and increase in exported crude oil volumes via UAS by 1%.

### Export – CPC Pipeline

In 2012 sales of exported crude oil via the CPC pipeline increased by 16% to KZT302 billion in comparisons with 2011.

This is due to a 3% increase in the average realized price to KZT119,889 per tonne and a 13% increase in volume exported via the CPC. The growth of crude oil sales on this route is due to reallocation of volumes of crude oil from the domestic market to export. Moreover, in January 2012 additional sales were realized from 2 tanker loads of 127k tonnes. These should have been shipped in December 2011, but were not shipped then due to adverse weather conditions.

### Domestic Market – Sales of Crude Oil

Domestic sales of crude oil in 2012 increased by 19% to KZT63 billion, compared to 2011, due to a 37% increase in the average sales price and was partially offset by decrease in sales volume by 14% or 261k tonnes.

In February 2012, the Company agreed a revised schedule of prices for domestic sales of crude oil, including a price of KZT 43,500 per tonne with effect from 1 July 2012. Subsequently, those prices were reduced and the price received by the Company for domestic sales of crude oil from 20 July to 30 September has been KZT 38,000 per tonne and from 1 October to 31 December KZT 40,000. In accordance with the terms of the Company's charter, the price reduction, as a related party transaction, should have been approved by the Independent Non-Executive Directors of the Company but no such approval has been given to the reduced price in 2012.

The following table shows the Company's realized sales prices (netback analysis) adjusted for crude oil transportation and other expenses:

Q4 2012	Q3 2012	Q4 2011	Change %		2012	2011 <sup>(1)</sup>	Change %
					(US\$/bbl)		
<b>UAS</b>							
110.10	109.50	109.36	1%	Benchmark end-market quote <sup>(2)</sup>	111.70	111.26	0.4%
107.92	109.40	105.83	2%	Sales price	108.80	106.06	3%
0.10	0.02	0.04	130%	Premium of bbl difference	0.14	(0.08)	-279%
<b>108.02</b>	<b>109.42</b>	<b>105.87</b>	<b>2%</b>	<b>Realized price</b>	<b>108.94</b>	<b>105.98</b>	<b>3%</b>
(23.99)	(22.69)	(22.86)	5%	Rent tax	(23.79)	(23.73)	0%
(6.12)	(5.35)	(5.73)	7%	Export customs duty	(5.62)	(4.98)	13%
(8.94)	(7.31)	(7.91)	13%	Transportation	(7.91)	(7.76)	2%
-	-	(0.07)	-100%	Sales commissions	(0.02)	(0.07)	-69%
<b>68.97</b>	<b>74.06</b>	<b>69.30</b>	<b>-0.5%</b>	<b>Netback price</b>	<b>71.60</b>	<b>69.44</b>	<b>3%</b>
<b>CPC</b>							
110.10	109.50	109.36	1%	Benchmark end-market quote <sup>(2)</sup>	111.70	111.26	0.4%
109.44	108.68	108.70	1%	Sales price	109.83	109.98	-0.1%
(7.73)	(6.67)	(10.83)	-29%	Quality bank	(7.41)	(8.88)	-17%
8.55	8.65	9.28	-8%	Premium of bbl difference	8.76	9.32	-6%
<b>110.26</b>	<b>110.66</b>	<b>107.15</b>	<b>3%</b>	<b>Realized price</b>	<b>111.18</b>	<b>110.42</b>	<b>1%</b>
(20.39)	(23.08)	(23.13)	-12%	Rent tax	(23.23)	(24.07)	-3%
(4.66)	(4.72)	(4.80)	-3%	Export customs duty	(4.91)	(5.13)	-4%
(6.36)	(7.54)	(7.00)	-9%	Transportation	(6.96)	(6.97)	-0.2%
-	-	(0.07)	-100%	Sales commissions	(0.02)	(0.07)	-69%
<b>78.85</b>	<b>75.31</b>	<b>72.15</b>	<b>9%</b>	<b>Netback price</b>	<b>76.06</b>	<b>74.18</b>	<b>3%</b>
<b>Domestic</b>							
36.87	35.89	26.19	41%	Sales price	35.51	26.28	35%
(0.87)	(0.83)	(1.45)	-40%	Transportation	(1.03)	(1.38)	-25%
<b>36.00</b>	<b>35.05</b>	<b>24.74</b>	<b>46%</b>	<b>Netback price</b>	<b>34.47</b>	<b>24.90</b>	<b>38%</b>
<b>64.80</b>	<b>68.86</b>	<b>58.52</b>	<b>11%</b>	<b>Average Netback price</b>	<b>65.18</b>	<b>59.78</b>	<b>9%</b>

(1) The information for 2011 has been adjusted in accordance with the changes made in the method of calculation in 2012

(2) The Brent (DTD) quoted price is used as benchmark

The difference between the benchmark quote and the realized price of sales mainly comprises freight expenses and averaging effects. Averaging effects usually appear because of the difference between the average mean of the quoted price on the sale date and the average published price over the whole period. This difference may be significant on account of the high volatility of oil prices.

### *Production expenses*

The following table presents a breakdown of the Company's production expenses (in KZT millions):

Q4 2012	Q3 2012	Q4 2011	Change %		2012	2011	Change %
22,687	20,517	16,515	37%	Employee benefits	82,959	65,323	27%
4,102	3,097	6,099	-33%	Materials and supplies	14,176	14,691	-4%
3,589	3,314	2,932	22%	Energy	12,884	10,564	22%
7,361	5,251	5,173	42%	Repairs and maintenance	18,162	20,087	-10%
1,581	1,514	1,133	39%	Transportation service	5,758	4,519	27%
143	-	257	-44%	Processing expenses	393	1,041	-62%
(4,738)	(2,178)	(3,831)	24%	Change in crude oil balance	(984)	(3,919)	-75%
1,817	1,572	1,341	35%	Other	7,014	5,159	36%
<b>36,542</b>	<b>33,087</b>	<b>29,619</b>	<b>23%</b>		<b>140,362</b>	<b>117,465</b>	<b>19%</b>

Production expenses in 2012 increased by 19% or KZT22.9 billion compared to 2011. This is primarily due to increased expenses for employee benefits, energy and transportation while repairs and maintenance and processing expenses have decreased

Employee benefits expenses for 2012 increased by 27% compared to 2011 mainly due to an indexation of basic tariffs for production personnel by 9% starting from January 2012 according to the collective agreement, but also due to creation of two new service companies (UBR and UTTiOS).

Energy expenses increased by 22% in 2012 mainly due to the increase in tariffs for electricity consumption.

Transportation expenses increased by 27% mainly due to increase in volumes of work (moto-hours) and tariffs for transportation at subsidiaries.

Processing expenses have decreased by 62% due to the reduction of supplies to the Atyrau refinery. This was due to congestion of the plant associated with the adoption of the act "State regulation of production and turnover of certain types of oil products".

Repairs and maintenance expenses in 2012 declined by 10% compared to 2011, mainly due to the reduced number of repair operations from 1066 to 957 well/operation and hydraulic fracturing from 160 to 121 well/operation according to the production program and due to adverse weather conditions at the beginning of the year.

### *Selling, general and administrative expenses*

The following table presents a breakdown of the Company's selling, general and administrative expenses (in KZT millions):

Q4 2012	Q3 2012	Q4 2011	Change %		2012	2011	Change %
13,443	13,838	12,370	9%	Transportation expenses	53,122	49,578	7%
1,481	4,469	3,922	-62%	Employee benefits	13,936	13,768	1%
(236)	6,751	1,007	-123%	Sponsorship	6,778	4,970	36%
93	2,565	427	-78%	Fines and penalties	8,302	12,738	-35%
713	263	756	-6%	Consulting and audit services	1,382	1,669	-17%
1,004	486	2,184	-54%	Management fees and commissions	4,169	8,752	-52%
585	303	327	79%	Repairs and maintenance	1,339	840	59%
1,350	1,033	2,566	-47%	Other	4,060	6,205	-35%
<b>18,433</b>	<b>29,708</b>	<b>23,559</b>	<b>-22%</b>		<b>93,088</b>	<b>98,520</b>	<b>-6%</b>

Selling, general and administrative expenses decreased in 2012 by 6% or KZT5.4 billion compared to 2011. This is primarily due to decrease in fines and penalties, management fees and commissions and was partially offset by increased expenses for transportation and sponsorship.

The decrease in fines and penalties is due to accrual of fines for export customs duty of the amount of KZT2.3 billion in 2011 and an environmental fine related to gas flaring at Prorva group of fields that totaled KZT2.9 billion in 2011. Main part of fines and penalties for 2012 is explained by accruals of fines and penalties due to results of Complex Tax Audit.

The decrease in management fee and commissions is mainly due to a change in the fee structure of the services agreement with NC KMG.

The growth in transportation expenses is explained by a 13% increase in volumes shipped via the CPC export route. The growth of crude oil sales on this route is related to the increased share of exports in total sales from 75% to 78%. In addition, in January 2012 sales were realized from 2 tankers of a volume of 127k tonnes, which were to be shipped in December 2011, but were not shipped due to adverse weather conditions.

Sponsorship expenses in 2012 increased mainly due to the financing of resettlement of Baychunas and Eskine inhabitants in Atyrau region. For further details please refer to section: Social projects.

#### *Taxes other than on income*

The following table presents a breakdown of the Company's taxes other than on income (in KZT millions):

Q4 2012	Q3 2012	Q4 2011	Change %		2012	2011	Change %
36,733	41,091	35,331	4%	Rent tax	159,822	149,771	7%
7,240	22,928	20,450	-65%	Mineral extraction tax	70,792	78,680	-10%
9,382	9,208	8,240	14%	Export customs duty	36,429	46,979	-22%
1,210	1,073	939	29%	Property tax	4,373	3,454	27%
764	270	1,069	-29%	Other taxes	2,755	5,143	-46%
<b>55,329</b>	<b>74,570</b>	<b>66,029</b>	<b>-16%</b>		<b>274,171</b>	<b>284,028</b>	<b>-3%</b>

Taxes other than on income expenses in 2012 decreased by 3% or KZT9.9 billion compared to 2011. This is primarily due to the decreased expenses for export customs duty, mineral extraction tax and other taxes and was partially offset by increase in rent tax.

The decrease in MET is mainly explained by the decrease in rates, due to OMG and EMG having become stand-alone Joint Stock Companies in 2012. MET rates depends on the annual production of crude oil, respectively, for 2011, when the volume of production at the Uzen was specified for the entire year, the rate of MET was equal to 13%. In 2012, MET of Uzen has been accrued separately for the first and second half of the year (in the first half of the taxpayer – KMG EP, the second - JSC OMG), respectively, as a result of the separation of production for 2 half years MET rate decreased from 13% to 10%.

The decrease in export customs duties is explained by the recognition in 2011 of KZT15.2 billion of principal for export customs duty in accordance with the decision of the Supreme Court of RK.

Other taxes decreased due to the fact that in 2011, a significant amount of VAT previously referred to offset for the acquisition of assets has been adjusted when contributing these assets to the share capital of subsidiaries. Contribution to share capital is not taxable turnover and in accordance with the Tax Code of RK is subject to adjustment. Appropriate changes were reflected in 2011. Other taxes in 2012 decreased also due to a decrease in fees for environmental pollution.

Rent tax expense is higher in 2012 compared to 2011 due to higher volumes of exported oil.

#### *Impairment of property, plant and equipment*

Management of the Company has carried out a formal assessment of the recoverable amount of OMG due to the presence of impairment indicators. The result of this assessment indicated that the carrying value of OMG exceeded the estimated recoverable amount by KZT75 billion, resulting in

impairment charge during 2012. The impairment charge in OMG has resulted from slower than expected production rehabilitation and increased capital and operating expenditures and transportation costs.

Management believes that the resulting impairment charge on OMG assets could be reversed in future periods if actual production over the next years exceeds expectations used in this impairment assessment or if there are indicators of sustainable increases in market prices for crude oil.

### *Share of Income in Associate and Joint Ventures*

	2012	2011	Change	Change in %
	(KZT millions, unless otherwise stated)			
Share of income from PetroKazakhstan Inc.	33,724	45,675	(11,951)	-26%
Share of income from JV Kazgermunai LLP	33,333	38,373	(5,040)	-13%
Share of income from UGL, KMG-Service, KSEP Investments BV	385	228	157	69%
<b>Share of Income in Associate and Joint Ventures</b>	<b>67,442</b>	<b>84,276</b>	<b>(16,834)</b>	<b>-20%</b>

The Company's income from its share in associate and joint ventures in 2012 decreased to KZT67.4 billion compared with KZT84.3 billion in 2011. The share of income from PetroKazakhstan Inc. was KZT33.7 billion and JV Kazgermunai LLP was KZT33.3 billion. The shortfall was mainly due to reallocation of volumes of crude oil from export sales to the domestic market, due to a drop in import of volumes from Russia.

For further details please refer to section: Overview of Associate and Joint Ventures Operations.

### *Income Tax Expense*

Q4 2012	Q3 2012	Q4 2011	Change %		2012	2011	Change %
(KZT millions, unless otherwise stated)					(KZT millions, unless otherwise stated)		
6,302	80,611	60,830	-90%	Profit before tax	253,749	272,592	-7%
1,890	58,486	46,318	-96%	Profit before tax (net of JV's and associates results)	186,307	188,316	-1%
18,315	29,241	16,548	11%	Income tax	92,926	63,661	46%
<b>291%</b>	<b>36%</b>	<b>27%</b>	<b>968%</b>	Effective tax rate	<b>37%</b>	<b>23%</b>	<b>57%</b>
<b>969%</b>	<b>50%</b>	<b>36%</b>	<b>2613%</b>	Effective tax rate (net of JV's and associates results)	<b>50%</b>	<b>34%</b>	<b>48%</b>

The main reasons for income tax expense and effective tax rate increase in 2012 compared with 2011 is taxable income from capital gain on the disposal of newly formed joint stock companies OMG and EMG and also increase in revenues due to higher exported crude oil volumes. The increase in income tax in connection with the disposal of assets to OMG and EMG was KZT13.8 billion. In this case, the assets are accounted for OMG and EMG for tax purposes at market value, which has the effect of reducing the CIT due to increased amortization of the tax base in the current and future periods. Increase of income tax due to higher exported crude oil volumes amounted to KZT15 billion.

Moreover, effective income tax rate increased due to the EPT for contracts of OMG in the amount of KZT7.3 billion and EMG in the amount of KZT7.9 billion due to a significant increase in revenues, while expenses increased less significantly.

In 2011, Uzen contract did not incur EPT. In 2012, the taxable income increased by 20% and the deductible expenses by 5%, resulting in Uzen contract incurring EPT.

At the same time, impairment of OMG assets has affected to decrease of income tax, which resulted in the increase of deferred income tax in the amount of KZT17.6 billion.

### *Profit for the Period*

As a result of the factors mentioned above, in 2012 the Company's profit for the period decreased by 23% to KZT160.8 billion compared with 2011.

## Overview of Associate's and JVs Operations

### PetroKazakhstan Inc.

PetroKazakhstan Inc.'s key financial and operational indicators are shown below:

Q4 2012	Q3 2012	Q4 2011	Change		2012	2011	Change
947,013	1,064,216	968,916	-2%	Revenue, US\$ thousands	3,992,017	4,964,794	-20%
(635,222)	(623,825)	(579,255)	10%	Operating expenses, US\$ thousands	(2,309,104)	(3,076,029)	-25%
(5,388)	(6,602)	(6,948)	-22%	Finance cost, US\$ thousands	(24,587)	(17,934)	37%
(265,326)	(129,984)	(194,284)	37%	Income tax expense, US\$ thousands	(766,836)	(686,394)	12%
41,077	303,805	188,429	-78%	Net income, US\$ thousands	891,490	1,184,437	-25%
(50,610)	(114,206)	(153,629)	-67%	Capital expenditure, US\$ thousands	(312,268)	(373,230)	-16%
1,352	1,407	1,458	-7%	Crude oil production, th. tonnes	5,589	5,912	-5%
1,292	1,545	1,534	-16%	Crude oil and oilproducts sales, th. tonnes	5,599	7,154	-22%
466	524	268	74%	Export via KCP (PKKR 100%)	1,663	2,180	-24%
40	37	32	23%	Export via KCP (Kolzhan 100%)	141	145	-2%
340	274	211	61%	Export via KCP (KGM 50%)	1,012	1,008	0%
58	113	89	-35%	Export Aktau (KGM 50%)	266	390	-32%
45	49	44	4%	Export Uzbekistan (TP 50%)	182	226	-19%
134	127	114	18%	Export via KCP(TP 50%)	502	633	-21%
209	423	776	-73%	Domestic sales - thousand tonnes	1,833	2,573	-29%

Crude oil production of PetroKazakhstan Inc. in 2012 was 5,589k tonnes (33% share of Company is 1,844k tonnes), 5% less than in 2011. The decline in production is due to natural decline of mature fields and high watering.

Revenues declined by 20% in 2012 compared to 2011, primarily due to a decrease in crude oil sales volumes. This was due to lower imports of oil purchased to fulfill the PetroKazakhstan's obligations to supply the domestic market. Imports made under the replacement contract dropped from 1301k tonnes in 2011 to 211k tonnes in 2012. The 25% drop in operating expenses is mainly explained by lower spending on the purchase of imported oil from Russia.

Decrease of operating expenses by 25% is mainly explained by a decrease of expenses for purchase of imported oil from Russia.

The decrease in the sale of oil products in 2012 is due to the termination of oil supplies for the processing and sale of oil products in April 2012. This is related to the conclusion of a contract with LLP «Petrosun» for the replacement of oil supplies to the domestic market.

Capital expenses in 2012 were KZT46.6 billion (US\$ 312.3 million).

During 2012 the Company received dividends from PetroKazakhstan Inc. in the amount of KZT49,8 million (US\$ 332 million), while in 2011 dividends were equal to KZT53.2 billion (US\$ 361 million).

For 2012 the Company recognized share income from its investment in PetroKazakhstan Inc. (33% share) of KZT33.7 billion (US\$ 226 million), which is KZT12 billion (US\$ 80 million) less than in 2011.

## JV Kazgermunai LLP

JV Kazgermunai LLP's (Kazgermunai) key financial and operational indicators are shown below:

Q4 2012	Q3 2012	Q4 2011	Change		2012	2011	Change
640,181	634,402	561,863	14%	Revenue, US\$ thousands	2,310,222	2,354,240	-2%
(369,387)	(351,990)	(313,820)	18%	Operating expenses, US\$ thousands	(1,220,733)	(1,343,142)	-9%
63	(535)	(3,175)	-102%	Finance cost, US\$ thousands	(6,959)	(6,967)	0%
(157,188)	(108,827)	(106,377)	48%	Income tax expense, US\$ thousands	(469,832)	(375,268)	25%
113,669	173,050	138,491	-18%	Net income, US\$ thousands	612,698	628,862	-3%
(27,926)	(22,198)	(43,140)	-35%	Capital expenditure, US\$ thousands	(61,769)	(73,723)	-16%
820	748	783	5%	Crude oil production, th. tonnes	3,124	3,000	4%
796	838	802	-1%	Crude oil sales, th. tonnes	3,075	3,017	2%
116	226	179	-35%	Export via Aktau	532	780	-32%
681	547	422	61%	Export via Kazakh-Chinese pipeline	2,025	2,016	0%
-	65	202	100%	Domestic market	518	222	133%

Kazgermunai oil production in 2012 was 3,124k tonnes (50% share of Company is 1,562k tonnes), 4% more than in 2011.

Capital expenditures for the period were KZT9.2 billion (US\$ 61.8 million), which is 12% less than in 2011.

The increase of crude oil sales to the domestic market in 2012 compared with 2011 is due to a decrease in imports of oil from Russia to replace supplies of Kazgermunai to the domestic market. Consequently, supply of the domestic market in 2012 mainly carried out by own resources of Kazgermunai.

Company received dividends from Kazgermunai in the amount of KZT67.2 billion (US\$ 450 million), while in 2011 dividends were equal to KZT36.6 billion (US\$ 250 million).

The Company's share in income from the joint venture included in the consolidated financial statements of the Company for 2012 is KZT33.3 billion (US\$ 223.5 million), which is KZT5 billion (US\$ 38.2 million) less than in 2011.

## CCEL

CCEL's key financial and operational indicators are shown below:

Q4 2012	Q3 2012	Q4 2011	Change		2012	2011	Change
341,320	356,492	303,432	12%	Revenue, US\$ thousands	1,466,282	1,367,173	7%
(247,744)	(267,871)	(246,770)	0%	Operating expenses, US\$ thousands	(1,104,090)	(1,025,163)	8%
(4,580)	(4,957)	(2,986)	53%	Finance cost, US\$ thousands	(19,396)	(6,698)	190%
(18,070)	(22,454)	(48,811)	-63%	Income tax expense, US\$ thousands	(87,029)	(121,128)	-28%
70,927	61,210	4,866	1358%	Net income, US\$ thousands	255,767	214,184	19%
(17,089)	(13,507)	(28,025)	-39%	Capital expenditure, US\$ thousands	(56,670)	(102,464)	-45%
511	522	510	0%	Crude oil production, th. tonnes	2,037	1,981	3%
480	507	446	8%	Crude oil sales, th. tonnes	2,054	1,957	5%
207	263	217	-5%	Export via Novorossiysk	1,168	1,195	-2%
215	182	177	21%	Export via Primorsk	649	552	18%
-	-	-	-	Export via Gdansk	-	24	-100%
58	64	51	14%	Domestic market	237	187	27%

Crude oil production of CCEL in 2012 was 2,037k tonnes (50% share of Company is 1018.5k tonnes), 3% more than in 2011.

The increase in operating expenses by 8% compared to 2011 mainly due to the increase in energy expenses due to increase of tariffs, increase in labor costs as a result of salary indexation by 7% in 2012, growth of tariffs and volumes of underground repair of wells.

Increase in finance costs in 2012 related to the increase in expenses related to the amortization of discount due to the growing number of liquidated wells and increase in the cost of liquidation, as

well as increased expenses on compensation due to changes in the average rate of Libor from 0.4% to 0.7%. In addition, in 2012, gain dropped on forex compared to 2011 from KZT0.7 billion (US\$ 4.8 million) to KZT 0.2 billion (US\$ 1.5 million).

In 2012 capital expenditures were KZT 8.4 billion (US\$ 56.7 million), which is 45% less than in 2011.

The Company has no obligation to pay amounts to CITIC unless it receives an equivalent amount from CCEL. Accordingly, the Company recognizes in its statement of financial position only the right to receive dividends from CCEL in the Guaranteed Amount on an annual basis until 2020, plus the right to retain any dividends in excess of the total Maximum Guaranteed Amount. As of December 31, 2012 the Company has KZT 18.2 billion (US\$ 121 million) as a receivable from CCEL, a jointly controlled entity with CITIC Group. The Company has accrued KZT2.73 billion (US\$ 18.3 million) of interest income in 2012 related to the US\$ 26.87 million annual priority return from CCEL.

## Social projects

	2012	2011	Change %
	(KZT millions, unless otherwise stated)		
<b>Employment project (UBR and UTTiOS)</b>			
UBR	6,495	-	100%
UTTiOS	4,433	-	100%
	<b>10,928</b>	<b>-</b>	<b>100%</b>
<b>Sponsorship</b>			
Sponsorship and charity	1,378	4,970	-72%
Resettlement of Baychunas and Eskine inhabitants	5,400	-	100%
	<b>6,778</b>	<b>4,970</b>	<b>36%</b>
<b>Obligation from exploration and production licenses</b>			
Social programs fund	1,162	1,389	-16%
Training costs	2,018	857	136%
	<b>3,180</b>	<b>2,246</b>	<b>42%</b>
<b>Impairment of social objects</b>	<b>1,593</b>	<b>1,465</b>	<b>9%</b>
<b>Total</b>	<b>22,479</b>	<b>8,681</b>	<b>159%</b>

Social responsibility is one of the priorities in the activities of KMG EP. Since its establishment, the Company has allocated significant funds for the construction of sports centers, summer camps, reconstruction of schools and hospitals, repairing roads in the Atyrau and Mangistau regions.

In 2012 two service companies - UBR and UTTiOS were created to ensure the employment of around 2000 people in the Mangistau region. The Company has incurred KZT 10.9 billion of operating expenses at UBR and UTTiOS, including KZT 9.5 billion (UBR: KZT 5.3 billion, UTTiOS: KZT4.2 billion) as an employee benefit expense and KZT 1.4 billion (UBR: KZT 1.1 billion, UTTiOS: KZT0.3 billion) for materials, supplies and other expenses. In addition, the Company has invested KZT14.2 billion for construction of rotational camps, production facilities and purchase of special transport and other equipment, to support the operations at UBR and UTTiOS.

In 2012 the Company has spent KZT6.8 billion for sponsorship and charity, which is KZT1.8 billion more than in 2011. The main part of the expenses (KZT5.4 billion) was used to finance resettlement of Baychunas and Eskine inhabitants of villages at mature fields in Atyrau region to Atyrau city. In addition, KZT1.4 billion was used to finance social funds, support of the war veterans, organizing sport events and some local community events.

Obligations from exploration and production licenses are arising from contracts for subsoil use and include the social programs fund and the commitment to train personnel. In 2012, social expenses of the Company in the execution of contractual obligations amounted to KZT2.3 billion,

including the training of specialists in the amount of KZT1.1 billion and social programs in the amount of KZT1.2 billion.

Impairment of social objects is mainly related to construction of sports centers, summer camps and other social objects in the regions of the Company's activity.

## Liquidity and Capital Resources

### Summary of Cash Flows

The Company's liquidity requirements arise principally from the need to finance its existing operations (working capital) the need to finance investment (capital expenditure) and to realize its growth targets via acquisitions. The management believes that the Company has adequate liquidity to meet its obligations and pursue investment opportunities.

Q4 2012	Q3 2012	Q4 2011		2012	2011	Change
(KZT millions, unless otherwise stated)				(KZT millions, unless otherwise stated)		%
59,800	4,355	38,233	Net cash generated from operating activities	154,879	148,210	4%
33,630	78,334	31,678	Net cash generated from/ (used in) investing activities	(52,131)	34,326	-252%
(11,166)	(123,954)	(5,773)	Net cash (used in) from financing activities	(154,555)	(74,934)	106%

In 2012 net cash generated from operating activities was KZT154.8 billion and increased by KZT6.7 billion compared to 2011. The change is mainly due to increase of profitability during 2012 in comparison with 2011 due to increase in average sales price for domestic market and reallocation of domestic sales volumes to export, which was partially offset by increase in payments and advances for taxes (CIT, EPT, MET).

Net cash outflow from investing activities amounted to KZT52.1 billion in 2012. The increase in outflow is mainly due to opening of new HTM deposits in the amount of KZT142.1 billion. This change was partially offset by increase in dividends received from joint ventures and associates by KZT24.4 billion. Also the change was affected by acquisition of share in joint venture UGL in 2011 for KZT23.9 billion, while in 2012 a similar acquisition have not been made.

Net cash outflows from financing activities in 2012 were KZT154.6 billion. This was mainly associated with the full repayment of remaining principal and accrued interest of the KMG PKI Finance notes in the amount KZT80 billion and KZT3 billion respectively, repurchase of treasury shares for KZT36.2 billion and also by payment of dividends to shareholders for 2011 in the amount of KZT34 billion.

### Borrowings

The table below shows the Company's net cash:

	As at December 31, 2012	As at September 30, 2012	As at December 31, 2011	December to December change
	(KZT thousands, unless otherwise stated)			%
Current portion	2,462	2,497	54,931	-96%
Non-current portion	4,848	4,999	33,034	-85%
<b>Total borrowings</b>	<b>7,310</b>	<b>7,496</b>	<b>87,965</b>	<b>-92%</b>
Cash and cash equivalents	154,705	72,438	206,512	-25%
Other current financial assets	550,556	556,970	321,890	71%
Non-current financial assets	1,085	1,068	188,803	-99%
<b>Total financial assets</b>	<b>706,346</b>	<b>630,476</b>	<b>717,205</b>	<b>-2%</b>
<b>US\$-denominated cash and financial assets, %</b>	<b>78%</b>	<b>81%</b>	<b>72%</b>	<b>8%</b>
<b>Net cash</b>	<b>699,036</b>	<b>622,980</b>	<b>629,240</b>	<b>11%</b>

As of December 31, 2012 total borrowings were KZT7.3 billion. On July 5, 2012 the Company fully repaid remaining principal and accrued interest of the KMG PKI Finance notes in the amount KZT80 billion and KZT3 billion respectively.

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### ***Forward-looking Statements***

*This document includes statements that are, or may be deemed to be, "forward-looking statements". These forward-looking statements can be identified by the use of forward-looking terminology including, but not limited to, the terms "believes", "estimates", "anticipates", "expects", "intends", "may", "target", "will", or "should" or, in each case, their negative or other variations or comparable terminology, or by discussions of strategy, plans, objectives, goals, future events or intentions. These forward-looking statements include all matters that are not historical facts. They include, but are not limited to, statements regarding the Company's intentions, beliefs and statements of current expectations concerning, amongst other things, the Company's results of operations, financial condition, liquidity, prospects, growth, potential acquisitions, strategies and as to the industries in which the Company operates. By their nature, forward-looking statements involve risk and uncertainty because they relate to future events and circumstances that may or may not occur. Forward-looking statements are not guarantees of future performance and the actual results of the Company's operations, financial condition and liquidity and the development of the country and the industries in which the Company operates may differ materially from those described in, or suggested by, the forward-looking statements contained in this document. The Company does not intend, and does not assume any obligation, to update or revise any forward-looking statements or industry information set out in this document, whether as a result of new information, future events or otherwise. The Company does not make any representation, warranty or prediction that the results anticipated by such forward-looking statements will be achieved.*

## **RISK FACTORS**

The Company is subject to several risks, including environmental, market, operational, financial, investment and corporate governance risks.

The company exercises risk management in accordance with Risk Management Policy. The Company's Risk Management Policy aims at increasing shareholder value and improving corporate governance through risk identification, assessment and analysis of its significance, as well as development of measures to minimize and control risks.

### **Environmental Risks**

The main risks associated with the external environment of the Company include political, economic and regional risks.

#### **Political risks**

- Ability to change the external or domestic policy by the leadership of the country, which may significantly affect the investment attractiveness of the country in general and the Company in particular;
- The likelihood of negative changes to legislation, including tax legislation, aimed at maximizing budget revenues from raw materials industries;
- In the process of reforming the public authorities the abolition and the creation of new ministries and agencies regulating the operation of the Company may take place, which may lead to a lack of or delay of approval of regulations affecting the Company;
- Government of Kazakhstan can significantly limit the claimed scope of export quotas or modify the mandatory volume of supply to the domestic market, which could have a material impact on the Company's financial results;
- Government of Kazakhstan can constrain cash management in the form of depositing in banks. The state represented by SWF "Samruk-Kazyna" and NC KMG may have an impact on KMG EP in the interests of the state as a whole, which may be contrary to the interests of other groups of shareholders of KMG EP.

#### **Economic risks**

- The economy of the Republic of Kazakhstan is poorly diversified and depends significantly on world commodity prices. A significant and sustained fall in global commodity prices could lead to a drop in profits of mineral companies, and eventually economic decline;
- Aging infrastructure of the economy could have a material adverse effect on the efficiency of the Company's business.
- Current legislation in the area of procurement of goods and services does not allow for increases in the efficiency of logistics.
- Lack of a competitive environment among suppliers and contractors reduces the quality of work and services provided by the company.
- Level of development of financial system of Kazakhstan may worsen the conditions of allocation of free funds (for details see below – in Financial Risks section).

#### **Regional risks**

Regions of the Company's activity are: Magistau, Atyrau, Aktyubinsk and Kyzylorda regions.

The main production units of the Company carry out its production activity in regions characterized by severe climatic conditions, and some regions are characterized by shortage of highly skilled professionals in the field of oil production and gas processing. At the same time these regions are the regions with high social and economic risks which have a substantial impact

on the operations of the Company.

For the assets of Mangistau region the risk of social conflicts and strikes is relatively high, as is often demonstrated, and has had a significant impact on the Company's operations and performance of its obligations under subsoil use contracts.

The company has consistently sought to promote and maintain social stability in the regions, interacts with local governments and communities to find solutions for social issues in the regions.

An appropriate set of measures, including the following steps is being developed to reduce the negative impact of changes in the situation in the country and the main regions:

- Actions aimed at addressing the situation, including changes in business - model of the Company, the transfer of production units in independently operating companies in order to promote regional development
- Actions aimed at increasing the geographic diversification of the Company's operation, in order to minimize the risk of a given region;
- Actions aimed at minimizing the social tensions in the regions of the core business;
- Actions to improve business efficiency, to minimize the risks with a significant adverse effect on the ability of the Company to develop business.

The Company strives to ensure that its social programs are the most carefully targeted and meet the needs of society. However, the increase in non-commercial costs associated with the minimization of the risk of strikes and social strain could have a negative impact on the financial performance of the Company.

Climatic conditions in these regions are quite varied. In addition, their geographical distance calls attention to the transport component and supply of electricity for continuous operation of the Company.

In order to minimize the possible consequences of the risks associated with climatic features of the regions where it has a presence, including the threat posed by natural disasters, the Company pays special attention to business continuity and safety

### Partners

The Company collaborates with and involves foreign and domestic companies in various areas of its activity. The Company has a limited ability to exert influence on the behavior or operational activities of its partners, which may affect the Company's operations or finances. Therefore, the Company is developing long-term and mutually beneficial partner relationships.

### Market risks

Market risks include risks of adverse impact of oil price changes, exchange rates, and interest rates (for more details about currency risk and interest rate risk, see the Financial Risks Section below).

The company provides wholesale supply of oil, for both internal and external markets. The main possible deterioration, both for internal and external markets, is a decline in oil prices, which can be characterized by significant volatility due to a number of factors: the balance of supply and demand, the impact of policies of major oil-producing countries or the political situation in the main producing regions of energy. A decline in world oil prices would significantly result in a deteriorating financial performance of the Company.

The company does not at the moment resort to hedging the risks of oil prices falling, but in each situation uses internal cost management tools to reduce the negative impact of the risk.

## **Financial Risks**

The Company is exposed to various financial risks, among which are the currency risks, inflation risks, risks of changes in interest rates on the allocated temporarily free funds, credit and tax risks. The probability of their occurrence and degree of impact on the financial results of the Company are continually evaluated and taken into account in drawing up development plans.

### Inflation risks

The company conducts its principal operations in the Republic of Kazakhstan and uses KZT as a basic currency of accounts. The costs associated with the payment of wages, energy costs, the cost of logistics services are sensitive to the inflation of KZT.

### Interest rate exposures

The operation of the Company is exposed to interest rate changes, which may adversely affect the value of temporarily funds assets and, accordingly, the financial results of operations of the Company.

### Currency risks

Currency risk is the fluctuation in exchange rates, which has a multidirectional impact on financial and economic activities of the Company.

A considerable part of the Company's revenues is denominated in US dollars (USD) or linked to USD. A part of the Company's expenses is denominated in foreign currency, or otherwise significantly dependent on the fluctuations of foreign currencies (mainly the USD and to a lesser extent the euro and the ruble) for KZT. Currently, the majority of operating costs of the Company are paid at prices fixed in KZT.

A rise in the value of the dollar would make oil exports more profitable.

In the case of a negative impact of changes in interest rates and exchange rates the Company will perform the following steps to reduce the negative effects:

- expansion of the number of partner banks, primarily drawn from the institutions least affected by the current global financial crisis;
- greater use of trade finance instruments (letters of credit, guarantees) allowing the Company to reduce the dependence of its activities on base interest rates.

The following indicators of the Company's financial statements are most susceptible to changes as a result of the influence of financial risk:

- net income;
- revenues;
- costs;
- receivables.

### Credit risks

Operations associated with the movement of material and cash flows for contractors, beginning with financial institutions serving the financial flows of the Company, and ending with the end

buyers of products and contractors providing various services for the Company, are all subject to credit risks.

An efficient centralized cash management system implemented by the Treasury of the Company allows it to minimize credit risks.

Financial risks, their probability and nature of changes in the statements.

<b>Risk</b>	<b>Risk probability</b>	<b>Nature of changes in the statements</b>
Falling of bank deposit rates	average	Decrease in profit due to falling of revenues for the placement of temporarily free funds
Foreign exchange risk (the risk of devaluation of the exchange rate of the KZT against the Euro and USD)	average	Increased cost of purchased equipment - increased depreciation
Inflation risk	average	Increase in accounts receivable, increase in costs of outputs
Credit risk	average	Problem with receivables. Reduction of profit

### **Tax risks**

The tax system of the Republic of Kazakhstan is characterized by small volumes of law enforcement practice in respect of the recently adopted regulations. It is also characterized by the risk of additional taxation, fines and penalties based on improper interpretation of the legislation. These factors complicate the planning of the tax costs of the Company. The Company's Management develops actions to minimize the risk, based on participation in the work of improving the quality of both the Tax Code, and amendments thereto. In addition, the Company continues to defend its interests in the courts.

### **Change in customs regulations and duties**

Considering that the Company carries out foreign trade activities, changes in customs regulations, volatility of ICD and lack of a transparent formula for calculating the ICD, could adversely affect the Company's financial results.

However, the Company carries out continuous monitoring of changes in the current legislation of the Republic of Kazakhstan and takes them into account in its activities. This allows it to minimize the risks associated with these changes.

### **Operational risks**

The main operational risks of the Company lie in the field of exploration and production, and relate to the implementation of continuous operations of the Company.

Below is a list of key operational risks, to minimize which the Company allocates considerable resources and pays them much attention, both in their daily activities, and in the process of planning and operating efficiency evaluation.

### **Exploration**

There is always a risk of non-commercial discovery of hydrocarbons and/or drilling a "dry" well in carrying out exploration work. To reduce the risk of exploration a complex geological and

geophysical investigation is carried out. In addition to traditional seismic surveys this includes geochemical studies, high-resolution electrical exploration and special methods for seismic and gravics data processing, as well as for the analysis of geological risks.

### Production

One of the most important tasks of the Company is to maintain an optimal level of production in its own fields, most of which are located at the late stage of operation. To this end, the Company uses modern methods and technologies of impact on the oil reservoirs and well bottom zones.

The main key factors in reducing the efficiency of production activities of the Company:

- Status of firm wells.
- Technical integrity of equipment
- Continuity of supply.
- Weather conditions.
- Timeliness of procurement and supply of equipment.
- Quality of the delivered equipment.
- Timeliness and quality of service provided by the contractors.
- Safety of operating personnel.
- Environmental security.
- Effectiveness of planning.
- Compliance with state regulators.

However, the production activity of the Company is subject to the risks of failures and breakdowns of primary equipment. To reduce these risks, the Company carries out a set of preventive measures and a program of modernization and repair of equipment. The main production equipment is insured against loss from fire, explosion, natural and other hazards, and the Company additionally insures against the risk of a well out-of-control.

### Health, safety and environment

Production activities of the Company involve a wide range of risks to workers' health and the environment. These risks include unsafe practices, industrial accidents, environmental damage, environmental pollution and natural disasters.

Consequences of these risks can be very severe, including fatal accidents, air pollution, soil and water pollution, fire, suspension or stop of production. Depending on the cause of occurrence of these events, the consequences could adversely affect the reputation, financial and operating policies of the Company. In this regard, the Company performs various measures to prevent the occurrence of such threats, including the control of occupational health and safety, hazards identification and training. The current labour protection systems and health, safety and environment of the Company have been introduced and function in accordance with ISO 14001, OHSAS 18001. Every year the company insures the risks of occupational safety and the environment associated with its own activities and projects.

### Information Technology

The Company is subject to risks in the field of information technology in connection with the use and implementation of a large number of high-tech equipment and software for effective operating activity. It is in connection with these that problems of adapting new equipment and software, as well as secure storage of sensitive business data, may arise. In order to ensure effective work in this direction the Company annually analyzes the technologies used. In its selecting and purchasing policy the Company gives preference to the most adaptable and recommended information technologies, so as to provide reliable control of access to business data.

## **Investment risks**

The main factors affecting the Company's investment activities are:

- Limitation of new assets on the ground in Kazakhstan available for the purchase.
- Increased competition from large international oil companies for access to oil and gas assets.
- Lack of its own high-performance service expertise, which would enable KMG EP to participate in offshore projects in Kazakhstan, as well as attractive international projects.

Furthermore, KMG EP is the largest oil and gas company controlled by the Government of Kazakhstan. In this regard, the state represented by SWF "Samruk-Kazyna" and NC KMG may have an impact on KMG EP in the interests of the state as a whole, which may be contrary to the interests of the shareholders of KMG EP.

All of these factors, both separately and in combination, can lead to an underestimation or overestimation of the attractiveness of the projects, inefficient investment decisions and, consequently, a reduction in inventory levels and a decrease in the value of the Company.

## **Risks of corporate governance**

### **Reducing the organizational capacity**

One of the major factors affecting the efficient operation of the Company is the reduction of its organizational capacity. Highly qualified personnel are the basis of competitive advantage and the basis for achieving the strategic goals of the Company. Each year, the Company faces the challenge of attracting staff with appropriate qualifications. This is primarily due to the impossibility of recruiting staff due to shortage of the necessary category of professionals in the labour market in some regions.

To reduce this risk, the Company has developed a series of measures aimed at increasing loyalty, motivation and the professional level of staff. In addition, considerable attention is paid to improving the leadership skills of management and development of a personnel reserve.

### **Fraud and Corruption**

Resource allocation that does not comply with best interests of the Company, damage to the Company for personal gain, or any other evidence of corruption is totally unacceptable to the Company regardless of the size of the financial damage.

The company is taking all possible steps to prevent illegal activities that can cause reputational damage to the Company. The Company is subject to the Law on Combating Corruption which came into force in July 2011 as well as the UK Bribery Act 2010 and builds its own internal policies and procedures in strict accordance with the above laws.

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**KazMunaiGas Exploration Production Joint Stock Company**

Consolidated Financial Statements

For the year ended December 31, 2012

Independent Auditors' Report

*Consolidated Financial Statements*

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## Independent Auditors' Report

To the shareholders and management of Joint Stock Company KazMunaiGas Exploration Production

We have audited the accompanying consolidated financial statements of Joint Stock Company KazMunaiGas Exploration Production and its subsidiaries ("the Company"), which comprise the consolidated statement of financial position as at 31 December 2012 and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Consolidated Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the consolidated financial statements present fairly, in all material respects the financial position of Joint Stock Company KazMunaiGas Exploration Production and its subsidiaries as of 31 December 2012, and their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards.

*Ernst & Young LLP*

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Paul Cohn  
Audit Partner

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Evgeny Zhemaletdinov  
Auditor / General Director Ernst & Young LLP

State Audit License for audit activities on the territory of the Republic of Kazakhstan: series MΦЮ-2 No. 0000003 issued by the Ministry of Finance of the Republic of Kazakhstan on 15 July 2005

Auditor Qualification Certificate No. 0000553 dated 24 December 2003

06 March 2013

Tenge million

		As at December 31,	
	Notes	2012	2011
<b>ASSETS</b>			
<b>Non-current assets</b>			
Property, plant and equipment	6	325,520	338,860
Intangible assets	7	19,584	26,638
Investments in joint ventures	5, 9	89,252	116,526
Investments in associate	10	118,959	133,228
Receivable from a jointly controlled entity	9	14,326	18,138
Loans receivable from joint ventures	5, 9	13,150	8,494
Other financial assets	8	1,085	188,803
Deferred tax asset	22	31,968	9,450
Other assets		17,200	19,593
<b>Total non-current assets</b>		<b>631,044</b>	<b>859,730</b>
<b>Current assets</b>			
Inventories	11	25,058	22,651
Income taxes prepaid		17,806	9,971
Taxes prepaid and VAT recoverable		56,257	22,738
Mineral extraction tax prepaid		8,073	–
Prepaid expenses		15,539	12,054
Trade and other receivables	8	101,168	84,126
Receivable from a jointly controlled entity	9	3,895	1,361
Other financial assets	8	550,556	321,890
Cash and cash equivalents	8	154,705	206,512
<b>Total current assets</b>		<b>933,057</b>	<b>681,303</b>
<b>Total assets</b>		<b>1,564,101</b>	<b>1,541,033</b>
<b>EQUITY</b>			
Share capital	12	162,952	198,452
Other capital reserves		2,474	2,124
Retained earnings		1,154,335	1,083,749
Other components of equity		18,009	14,354
<b>Total equity</b>		<b>1,337,770</b>	<b>1,298,679</b>
<b>LIABILITIES</b>			
<b>Non-current liabilities</b>			
Borrowings	14	4,848	33,034
Deferred tax liability	22	–	2,049
Provisions	15	36,927	37,846
<b>Total non-current liabilities</b>		<b>41,775</b>	<b>72,929</b>
<b>Current liabilities</b>			
Borrowings	14	2,462	54,931
Income taxes payable		32,103	–
Mineral extraction tax and rent tax payable		50,417	50,908
Trade and other payables		82,255	48,680
Provisions	15	17,319	14,906
<b>Total current liabilities</b>		<b>184,556</b>	<b>169,425</b>
<b>Total liabilities</b>		<b>226,331</b>	<b>242,354</b>
<b>Total liabilities and equity</b>		<b>1,564,101</b>	<b>1,541,033</b>

The notes on pages 68 to 96 are an integral part of these consolidated financial statements.

Tenge million

	Notes	For the year ended December 31.	
		2012	2011
Revenue	16	797,170	721,194
Share of results of associate and joint ventures	9, 10	67,442	84,276
Finance income	21	34,528	28,843
<b>Total revenue and other income</b>		<b>899,140</b>	<b>834,313</b>
Production expenses	17	(140,362)	(117,465)
Selling, general and administrative expenses	18	(93,088)	(98,520)
Exploration expenses		(6,104)	(5,985)
Depreciation, depletion and amortization	6, 7	(53,747)	(45,494)
Taxes other than on income	19	(274,171)	(284,028)
Impairment of property, plant and equipment	20	(77,012)	(1,653)
Loss on disposal of fixed assets		(3,189)	(4,044)
Finance costs	21	(7,231)	(7,223)
Foreign exchange gain, net		9,513	2,691
<b>Profit before tax</b>		<b>253,749</b>	<b>272,592</b>
Income tax expense	22	(92,926)	(63,661)
<b>Profit for the year</b>		<b>160,823</b>	<b>208,931</b>
Exchange difference on translating foreign operations		3,655	1,978
<b>Other comprehensive income for the year, net of tax</b>		<b>3,655</b>	<b>1,978</b>
<b>Total comprehensive income for the year, net of tax</b>		<b>164,478</b>	<b>210,909</b>
EARNINGS PER SHARE – Tenge thousands			
Basic and diluted	13	2.32	2.95

The notes on pages 68 to 96 are an integral part of these consolidated financial statements.

		<b>For the year ended December 31,</b>	
	<b>Notes</b>	<b>2012</b>	<b>2011</b>
<b>Cash flows from operating activities</b>			
Profit before tax		253,749	272,592
Adjustments to add / (deduct) non-cash items			
Depreciation, depletion and amortization	6, 7	53,747	45,494
Share of result of associate and joint ventures	9, 10	(67,442)	(84,276)
Loss on disposal of property, plant and equipment (PPE)		3,189	4,044
Impairment of PPE and intangible assets	6, 7	77,012	2,439
Dry well expense on exploration and evaluation assets	7	4,321	2,586
Recognition of share-based payments		354	408
Forfeiture of share-based payments		(4)	(24)
Unrealised foreign exchange gain on non-operating activities		(6,835)	(2,306)
Other non-cash income and expense		420	4,591
Add finance costs	21	7,231	7,223
Deduct finance income	21	(34,528)	(28,843)
Working capital adjustments			
Change in other assets		101	(817)
Change in inventories		(2,267)	(4,822)
Change in taxes prepaid and VAT recoverable		(33,519)	(2,105)
Change in prepaid expenses		(3,577)	15,839
Change in trade and other receivables		(16,599)	(18,487)
Change in trade and other payables		13,925	(3,600)
Change in mineral extraction and rent tax payable		(8,564)	4,854
Change in provisions		10,663	7,621
Income tax paid		(96,498)	(74,201)
<b>Net cash generated from operating activities</b>		<b>154,879</b>	<b>148,210</b>
<b>Cash flows from investing activities</b>			
Purchases of PPE		(99,240)	(92,760)
Proceeds from sale of PPE		1,054	753
Purchases of intangible assets		(8,874)	(12,218)
Acquisition of share in a joint venture	9	–	(23,907)
Loans provided to the joint ventures	5, 9	(5,081)	(1,923)
Dividends received from joint ventures and associate, net of withholding tax	9, 10	114,207	89,795
Interest received from investment in Debt Instruments of NC KMG		11,280	13,006
(Purchase) / sale of financial assets held to maturity		(85,257)	56,836
Proceeds from sale of other financial assets		5,546	–
Repayments of loans receivable from related parties		7,657	3,940
Proceeds from disposal / (acquisition) of subsidiary, net of cash acquired	5	3,601	(8,799)
Interest received		2,976	9,603
<b>Net cash (used in) / generated from investing activities</b>		<b>(52,131)</b>	<b>34,326</b>
<b>Cash flows from financing activities</b>			
Share buy back	12	(36,203)	(15,763)
Repayment of borrowings	14	(81,406)	(35,219)
Dividends paid to Company's shareholders	3, 12	(33,971)	(19,287)
Interest paid	14	(2,975)	(4,665)
<b>Net cash used in financing activities</b>		<b>(154,555)</b>	<b>(74,934)</b>
Net change in cash and cash equivalents		(51,807)	107,602
Cash and cash equivalents at the beginning of the year	8	206,512	98,520
Exchange gain on cash and cash equivalents		–	390
<b>Cash and cash equivalents at the end of the year</b>	<b>8</b>	<b>154,705</b>	<b>206,512</b>

The notes on pages 68 to 96 are an integral part of these consolidated financial statements.

	Share capital	Treasury stock	Other capital reserves	Retained earnings	Foreign currency translation reserve	Total Equity
<b>As at December 31, 2010</b>	<b>263,095</b>	<b>(49,013)</b>	<b>1,740</b>	<b>931,455</b>	<b>12,376</b>	<b>1,159,653</b>
Profit for the year	–	–	–	208,931	–	208,931
Other comprehensive income	–	–	–	–	1,978	1,978
<b>Total comprehensive income</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>208,931</b>	<b>1,978</b>	<b>210,909</b>
Recognition of share-based payments (Note 12)	–	–	408	–	–	408
Forfeiture of share-based payments (Note 12)	–	–	(24)	–	–	(24)
Exercise of employee options (Note 12)	–	133	–	–	–	133
Share buy back (Note 12)	–	(15,763)	–	–	–	(15,763)
Dividends (Note 12)	–	–	–	(56,637)	–	(56,637)
<b>As at December 31, 2011</b>	<b>263,095</b>	<b>(64,643)</b>	<b>2,124</b>	<b>1,083,749</b>	<b>14,354</b>	<b>1,298,679</b>
Profit for the year	–	–	–	160,823	–	160,823
Other comprehensive income	–	–	–	–	3,655	3,655
<b>Total comprehensive income</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>160,823</b>	<b>3,655</b>	<b>164,478</b>
Recognition of share-based payments (Note 12)	–	–	354	–	–	354
Forfeiture of share-based payments (Note 12)	–	–	(4)	–	–	(4)
Exercise of employee options (Note 12)	–	703	–	–	–	703
Share buy back (Note 12)	–	(36,203)	–	–	–	(36,203)
Dividends (Note 12)	–	–	–	(90,237)	–	(90,237)
<b>As at December 31, 2012</b>	<b>263,095</b>	<b>(100,143)</b>	<b>2,474</b>	<b>1,154,335</b>	<b>18,009</b>	<b>1,337,770</b>

The notes on pages 68 to 96 are an integral part of these consolidated financial statements.

## 1. CORPORATE INFORMATION AND PRINCIPAL ACTIVITIES

KazMunaiGas Exploration Production Joint Stock Company (the “Company”) is incorporated in the Republic of Kazakhstan and is engaged in the acquisition, exploration, development, production, processing and export of hydrocarbons with its core operations of oil and gas properties located in the Pre-Caspian and Mangistau basins of western Kazakhstan. The Company’s direct majority shareholder is Joint Stock Company National Company KazMunaiGas (“NC KMG” or the “Parent Company”), which represents the state’s interests in the Kazakh oil and gas industry and which holds 63.22% of the Company’s outstanding shares as at December 31, 2012 (2011: 61.3%). The Parent Company is 100% owned by Joint Stock Company Samruk-Kazyna Sovereign Welfare Fund (“Samruk-Kazyna SWF”), which is in turn 100% owned by the government of the Republic of Kazakhstan (the “Government”).

The Company conducts its principal operations through the wholly owned subsidiaries JSC “Ozenmunaigas” and JSC “Embamunaigas”. In addition the Company has oil and gas interests in the form of other wholly owned subsidiaries, jointly controlled entities, associate and certain other controlling and non-controlling interests in non-core entities. These consolidated financial statements reflect the financial position and results of operations of all of the above interests.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

### 2.1 Basis of preparation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”). The consolidated financial statements have been prepared under the historical cost convention except for financial instruments. These consolidated financial statements are presented in Tenge and all values are rounded to the nearest million unless otherwise stated.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Company’s accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4.

#### *Adopted accounting standards and interpretations*

The Company has adopted the following new and amended IFRS during the year, which did not have any material effect on the financial performance or position of the Company:

- IFRS 7 Disclosures: enhanced derecognition disclosure requirements – Amendment;
- IAS 12 Deferred Tax: Recovery of underlying Assets – Amendment;
- IFRS 1 Severe hyperinflation and removal of fixed dates for first-time adopters – Amendment;
- IAS 1 Presentation of items of other comprehensive income – Amendment (early adopted);
- Improvements to IFRSs (May 2012) (early adopted).

#### *Standards issued but not yet effective*

The standards and interpretations that are issued but not yet effective up to the date of issuance of the Company's financial statements listed below, are those that the Company reasonably expects will have an impact on the disclosures, financial position or performance when applied at future date. The Company intends to adopt these standards and interpretations, if applicable when they become effective.

- IAS 28 Investments in associates and joint ventures (2011). The Company is currently assessing the impact that this standard will have on the financial position and performance;
- IFRS 10 Consolidated financial statements. The Company is currently assessing the impact that this standard will have on the financial position and performance;

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.1 Basis of preparation (continued)

#### *Standards issued but not yet effective (continued)*

- IFRS 11 Joint arrangements. The Company is currently assessing the impact that this standard will have on the financial position and performance;
- IFRS 12 Disclosure of interest in other entities. A number of new disclosures will be required under this standard, however no impact on Company's financial position or results is expected;
- IAS 27 Separate financial statements (2011). The Company does not present separate financial statements;
- IFRS 13 Fair value measurement. The Company does not expect to have any material impact from adopting this standard in the future;
- IFRS 9 Financial instruments: classification and measurement. The Company will quantify the effect in conjunction with the other phases, when the final standard including all phases is issued;
- IAS 19 Employee benefits (Revised). The Company does not expect to have any material impact from adopting this standard in the future.

### 2.2 Change in presentation of the consolidated statement of comprehensive income

The Company changed the presentation of certain expenses in the consolidated statement of comprehensive income by separating impairment of property, plant and equipment into a separate line. The presentation of comparative information was also changed in line with the current year.

### 2.3 Consolidation

#### *Subsidiaries*

Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Company controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are no longer consolidated from the date that control ceases.

Inter-company transactions, balances and unrealised gains on transactions between companies are eliminated. Unrealised losses are also eliminated but considered an impairment indicator of the asset transferred. Accounting policies of subsidiaries are consistent with those of the Company.

#### *Investment in associates and interests in joint ventures*

The Company's investment in its associates and joint ventures are accounted for using the equity method. An associate is an entity in which the Company has significant influence. The Company also has interests in joint ventures, which are jointly controlled entities, whereby the venturers have a contractual arrangement that establishes joint control over the economic activities of the entities.

Under the equity method, the investment in the associate and joint ventures are carried in the statement of financial position at cost plus post acquisition changes in the Company's share of net assets of the associates and joint ventures.

The Company's investment in associates includes purchase price premium identified on acquisition, which is primarily attributable to the value of the licenses based on their proved reserves. The licenses are amortized over the proved developed reserves of the associate and joint ventures using the unit-of-production method.

The consolidated statement of comprehensive income reflects the share of the results of operations of each associate and joint venture. Where there has been a change recognised directly in the equity of an associate or joint venture, the Company recognises its share of any changes and discloses this, when applicable, in the statement of changes in equity. Unrealised gains and losses resulting from transactions between the Company and its associates are eliminated to the extent of the interest in the associate.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **2.3 Consolidation (continued)**

#### *Investment in associates and interests in joint ventures (continued)*

The share of profit of associates and joint ventures are shown on the face of the consolidated statement of comprehensive income. This is the profit attributable to equity holders of the associates and joint ventures and therefore is profit after tax and non-controlling interests in the subsidiaries of the associates.

The financial statements of the associates are prepared for the same reporting period as the parent company. Where necessary, adjustments are made to bring the accounting policies in line with those of the Company.

After application of the equity method, the Company determines whether it is necessary to recognise an additional impairment loss on the Company's investment in its associates or joint ventures. The Company determines at each reporting date whether there is any objective evidence that the investment in the associate or joint venture is impaired. If this is the case the Company calculates the amount of impairment as the difference between the recoverable amount of the associate or joint venture and its carrying value and recognises the amount in the statement of comprehensive income.

Upon loss of significant influence over the associate, the Company measures and recognises any retaining investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retaining investment and proceeds from disposal is recognised in profit or loss.

Upon loss of joint control and provided the former jointly controlled entity does not become a subsidiary or associate, the Company measures and recognises its remaining investment at its fair value. Any difference between the carrying amount of the former jointly controlled entity upon loss of joint control and the fair value of the remaining investment and proceeds from disposal is recognised in profit or loss. When the remaining investment constitutes significant influence, it is accounted for as investment in an associate.

### **2.4 Foreign currency translation**

The consolidated financial statements are presented in Kazakhstan Tenge ("Tenge"), which is the Company's functional and presentation currency. Each subsidiary, associate and joint venture of the Company determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency. Transactions in foreign currencies are initially recorded at the functional currency rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. All differences are taken to profit or loss. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined.

The assets and liabilities of foreign operations are translated into Tenge at the rate of exchange ruling at the reporting date and their statements of comprehensive income are translated at the exchange rates at the date of transaction. The exchange differences arising on the translation are recognised in other comprehensive income or loss. On disposal of a foreign entity, the accumulated foreign currency translation reserve relating to that particular foreign operation is recognised in profit or loss.

### **2.5 Oil and natural gas exploration and development expenditure**

#### *Exploration license costs*

Exploration license costs are capitalized within intangible assets and amortized on a straight-line basis over the estimated period of exploration. Each property is reviewed on an annual basis to confirm that drilling activity is planned. If no future activity is planned, the remaining balance of the license cost is written off. Upon determination of economically recoverable reserves ("proved reserves" or "commercial reserves"), amortization ceases and the remaining costs are aggregated with exploration expenditure and held on a field-by-field basis as proved properties awaiting approval within other intangible assets. When development is approved internally, and all licenses and approvals are obtained from the appropriate regulatory bodies, then the relevant expenditure is transferred to property, plant and equipment (oil and natural gas properties).

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **2.5 Oil and natural gas exploration and development expenditure (continued)**

#### *Exploration expenditure*

Geological and geophysical exploration costs are charged against income as incurred. Costs directly associated with an exploration well are capitalized within intangible assets (exploration and evaluation assets) until the drilling of the well is complete and the results have been evaluated. These costs include employee remuneration, materials, fuel and energy used, rig costs and payments made to contractors. If hydrocarbons are not found, the exploration expenditure is written off as a dry hole. If hydrocarbons are found and, subject to further appraisal activity, which may include the drilling of further wells (exploration or exploratory-type stratigraphic test wells), are likely to be capable of commercial development then, the costs continue to be carried as an asset.

All such carried costs are subject to technical, commercial and management review at least once a year to confirm the continued intent to develop or otherwise extract value from the discovery. When this is no longer the case, the costs are written off.

When proved reserves of oil and natural gas are determined and development is sanctioned, the relevant expenditure is transferred to property, plant and equipment (oil and natural gas properties).

#### *Development expenditure*

Expenditure on the construction, installation or completion of infrastructure facilities such as platforms, pipelines and the drilling of development wells, except for expenditure related to development or delineation wells which do not find commercial quantities of hydrocarbons and are written off as dry hole expenditures in the period, is capitalized within property, plant and equipment.

### **2.6 Property, plant and equipment**

Property, plant and equipment are stated at cost less accumulated depreciation, depletion and impairment.

The initial cost of an asset comprises its purchase price or construction cost, any costs directly attributable to bringing the asset into operation and the initial estimate of decommissioning obligation, if any. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Oil and gas properties are depreciated using a unit-of-production method over proved developed reserves. Certain oil and gas property assets with useful lives less than the remaining life of the fields are depreciated on a straight-line basis over useful lives of 4-10 years.

Other property, plant and equipment principally comprise buildings and machinery and equipment which are depreciated on a straight-line basis over average useful lives of 24 and 7 years respectively.

The expected useful lives of property, plant and equipment are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

The carrying value of property, plant and equipment is reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable.

An item of property, plant and equipment, inclusive of production wells which stop producing commercial quantities of hydrocarbons and are scheduled for abandonment, is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the item) is included in the statement of comprehensive income in the period the item is derecognized.

### **2.7 Impairment of non-financial assets**

The Company assesses assets or groups of assets for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Individual assets are grouped for impairment assessment purposes at the lowest level at which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets. If any such indication of impairment exists or when annual impairment testing for an asset group is required, the Company makes an estimate of its recoverable amount. An asset group's recoverable amount is the higher of its fair value less costs to sell and its value in use. Where the carrying amount of an asset group exceeds its recoverable amount, the asset group is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are adjusted for the risks specific to the asset group and are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **2.7 Impairment of non-financial assets (continued)**

An assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in profit or loss.

After such a reversal, the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

### **2.8 Intangible assets**

- Intangible assets are stated at cost less accumulated amortization and accumulated impairment losses. Intangible assets include capitalized expenditure for exploration and evaluation and other intangible assets, which are mainly comprised of computer software. Intangible assets acquired separately from a business are carried initially at cost. The initial cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset. Computer software costs have an estimated useful life of 3 to 7 years and are amortized on a straight line basis over this period.

- The carrying value of intangible assets is reviewed for impairment whenever events or changes in circumstances indicate the carrying value may not be recoverable.

### **2.9 Financial assets**

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, held to maturity investments, available for sale financial assets, loans and trade and other receivables, as appropriate. When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

The Company determines the classification of its financial assets on initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.

All regular way purchases and sales of financial assets are recognized on the trade date, which is the date that the Company commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the marketplace.

#### *Held to maturity investments*

Non derivative financial assets with fixed or determinable payments and fixed maturities are classified as held to maturity when the Company has the positive intention and ability to hold to maturity. After initial measurement held to maturity investments are measured at amortized cost using the effective interest method.

#### *Trade and other receivables*

Trade and other receivables are non derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement trade and other receivables are carried at amortized cost using the effective interest method less any allowance for impairment.

#### *Available for sale financial investments*

Available for sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified in any of the other categories. After initial measurement, available for sale financial assets are measured at fair value with unrealized gains or losses recognized in other comprehensive income or loss until the investment is derecognized or determined to be impaired at which time the cumulative reserve is recognized in profit or loss.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **2.9 Financial assets (continued)**

*Available for sale financial investments (continued)*

#### **Fair value**

The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business on the reporting date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions, reference to the current market value of another instrument, which is substantially the same, discounted cash flow analysis or other valuation models.

#### **Impairment of financial assets**

The Company assesses at each reporting date whether a financial asset or group of financial assets is impaired.

*Assets carried at amortised cost*

If there is objective evidence that an impairment loss on assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss shall be recognised in profit or loss.

If in a subsequent period the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date. Any subsequent reversal of an impairment loss is recognized in profit or loss.

In relation to trade receivables, a provision for impairment is made when there is objective evidence (such as the probability of insolvency or significant financial difficulties of the debtor) that the Company will not be able to collect all of the amounts due under the original terms of the invoice. The carrying amount of the receivable is reduced through use of an allowance account. Impaired debts are derecognised when they are assessed as uncollectible.

*Available for sale financial investments*

If an available for sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognised in profit or loss, is transferred from equity to profit or loss. Reversals in respect of equity instruments classified as available for sale are not recognised in profit or loss. Reversals of impairment losses on debt instruments are reversed through profit or loss, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

#### **Derecognition of financial assets**

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired;
- the Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement; or
- the Company has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

### **2.10 Inventories**

Inventories are stated at the lower of cost determined on a first-in first-out ("FIFO") basis and net realizable value. Cost includes all costs incurred in the normal course of business in bringing each item to its present location and condition. The cost of crude oil is the cost of production, including the appropriate proportion of depreciation, depletion and amortization ("DD&A") and overheads based on normal capacity. Net realizable value of crude oil is based on estimated selling price in the ordinary course of business less any costs expected to be incurred to complete the sale. Materials and supplies inventories are carried at amounts that do not exceed the expected amounts recoverable in the normal course of business.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **2.11 Value added tax (VAT)**

The tax authorities permit the settlement of VAT on sales and purchases on a net basis. VAT recoverable represents VAT on domestic purchases net of VAT on domestic sales. Export sales are zero rated.

### **2.12 Cash and cash equivalents**

Cash and cash equivalents include cash on hand, deposits with banks, other short-term highly liquid investments with original maturities of three months or less.

### **2.13 Share capital**

#### *Share Capital*

Ordinary shares and non-redeemable preference shares with discretionary dividends are both classified as equity. External costs directly attributable to the issue of new shares are shown as a deduction from the proceeds in equity.

#### *Treasury Shares*

Where the Company or its subsidiaries purchases the Company's shares, the consideration paid, including any attributable transaction costs, net of income taxes, is deducted from equity as treasury shares until such time as the shares are cancelled or reissued. No gain or loss is recognized in the statement of comprehensive income on the purchase, sale, issue or cancellation of the Company's own equity instruments. Where such shares are subsequently sold or reissued, any consideration received is included in equity. Treasury shares are stated at weighted average cost.

#### *Dividends*

Dividends are recognised as a liability and deducted from equity at the reporting date only if they are declared before or on the reporting date. Dividends are disclosed when they are proposed before the reporting date or proposed or declared after the reporting date but before the financial statements are authorised for issue.

#### *Share-based payment transactions*

Employees (including senior executives) of the Company receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

In situations where equity instruments are issued and some services received by the entity as consideration cannot be specifically identified, the unidentified goods or services received (or to be received) are measured as the difference between the fair value of the share-based payment transaction and the fair value of any identifiable goods or services received at the grant date. This is then capitalized or expensed as appropriate.

The cost of equity-settled transactions with employees for awards granted on or after July 1, 2007 is measured by reference to the fair value at the date on which they are granted. The fair value is determined by using a Black-Scholes-Merton option pricing model.

The cost of equity-settled transactions is recognised, together with a corresponding increase in equity, over the period in which the service conditions are fulfilled. The cumulative expense recognised for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Company's best estimate of the number of equity instruments that will ultimately vest.

The expense or credit for a period, in the statement of comprehensive income, represents the movement in cumulative expense recognized as at the beginning and end of that period. No expense is recognised for awards that do not ultimately vest.

Where an equity-settled award is cancelled, it is treated as if it vested on the date of cancellation, and any expense not yet recognised for the award is recognised immediately. This includes any award where non-vesting conditions within the control of either the entity or the employee are not met. All cancellations of equity-settled transaction awards are treated equally. Where the share-based award is cancelled on forfeiture any cost previously recognized is reversed through equity.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of diluted earnings per share.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **2.14 Trade payables**

Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

### **2.15 Provisions**

Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Company expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the statement of comprehensive income net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost.

### **2.16 Borrowings**

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently measured at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the statement of comprehensive income over the period of the borrowings using the effective interest method. Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date. Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are capitalised.

### **2.17 Deferred income tax**

Deferred tax assets and liabilities are calculated in respect of temporary differences using the balance sheet method. Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the reporting date.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

### **2.18 Employee benefits**

The Company withholds 10% from the salary of its employees as the employees' contribution to their designated pension funds. The pension deductions are limited to a maximum of 130,793 Tenge per month in 2012 (2011: 119,993 Tenge per month). Under the current Kazakhstan legislation, employees are responsible for their retirement benefits.

### **2.19 Revenue recognition**

The Company sells crude oil under short-term agreements priced by reference to Platt's index quotations and adjusted for freight, insurance and quality differentials. Title typically passes and revenues are recognized when crude oil is physically placed onboard a vessel or off loaded from the vessel, transferred into pipe or other delivery mechanism depending on the contractually agreed terms.

The Company's crude oil sale contracts generally specify maximum quantities of crude oil to be delivered over a certain period. Crude oil shipped but not yet delivered to the customer is recorded as inventory in the statement of financial position.

## **2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **2.20 Income taxes**

Excess profit tax (EPT) is treated as an income tax and forms part of income tax expense. In accordance with the applicable tax legislation enacted as of January 1, 2009, the Company accrues and pays EPT in respect of each subsurface use contract, at varying rates based on the ratio of aggregate annual income to deductions for the year for a particular subsurface use contract. The ratio of aggregate annual income to deductions in each tax year triggering the application of EPT is 1.25:1. EPT rates are applied to the part of the taxable income (taxable income after corporate income tax and allowable adjustments) related to each subsurface use contract in excess of 25% of the deductions attributable to each contract.

### **3. SIGNIFICANT NON-CASH TRANSACTIONS**

During the year ended December 31, 2012 the Company excluded from the consolidated statement of cash flows a non-cash transaction related to the offset of withholding income tax payable against the interest receivable on financial assets in the amount of 856 million Tenge (2011: 1,497 million Tenge) and against dividends received from the associate in the amount of 2,763 million Tenge (2011: 298 million Tenge).

On May 29, 2012 the Company declared dividends of 1,300 Tenge per share outstanding as at June 11, 2012 (Note 12). Pursuant to the NC KMG Debt Instrument agreement, on July 16, 2012 the Company performed a non-cash off-set of the declared dividends payable to Parent Company against part of the Debt Instrument (Note 8) for the amount of 56,013 million Tenge including principal of 55,785 million Tenge and interest of 228 million Tenge (during 2011: offset of 34,470 million Tenge, including principal of 33,335 million Tenge and interest of 1,135 million Tenge).

### **4. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS**

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities during the reporting period. The most significant estimates are discussed below:

#### *Oil and gas reserves*

Oil and gas reserves are a material factor in the Company's computation of DD&A. The Company estimates its reserves of oil and gas in accordance with the methodology of the Society of Petroleum Engineers (SPE). In estimating its reserves under SPE methodology, the Company uses long-term planning prices. Using planning prices for estimating proved reserves removes the impact of the volatility inherent in using year end spot prices. Management believes that long-term planning price assumptions, which are also used by management for their business planning and investment decisions, are more consistent with the long-term nature of the upstream business and provide the most appropriate basis for estimating oil and gas reserves.

All reserve estimates involve some degree of uncertainty. The uncertainty depends chiefly on the amount of reliable geological and engineering data available at the time of the estimate and the interpretation of this data.

The relative degree of uncertainty can be conveyed by placing reserves into one of two principal classifications, either proved or unproved. Proved reserves are more certain to be recovered than unproved reserves and may be further sub-classified as developed and undeveloped to denote progressively increasing uncertainty in their recoverability. Estimates are reviewed and revised annually. Revisions occur due to the evaluation or re-evaluation of already available geological, reservoir or production data, availability of new data, or changes to underlying price assumptions. Reserve estimates may also be revised due to improved recovery projects, changes in production capacity or changes in development strategy. Proved developed reserves are used to calculate the unit of production rates for DD&A. The Company has included in proved reserves only those quantities that are expected to be produced during the initial license period. This is due to the uncertainties surrounding the outcome of such renewal procedures, since the renewal is ultimately at the discretion of the Government. An increase in the Company's license periods and corresponding increase in reported reserves would generally lead to lower DD&A expense and could materially affect earnings. A reduction in proved developed reserves will increase DD&A expense (assuming constant production), reduce income and could also result in an immediate write-down of the property's book value. Given the relatively small number of producing fields, it is possible that any changes in reserve estimates year on year could significantly affect prospective charges for DD&A.

#### 4. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

##### *Recoverability of oil and gas assets*

The Company assesses each asset or cash generating unit (CGU) every reporting period to determine whether any indication of impairment exists. Where an indicator of impairment exists, a formal estimate of the recoverable amount is made, which is considered to be the higher of the fair value less costs to sell and value in use. These assessments require the use of estimates and assumptions such as long-term oil prices (considering current and historical prices, price trends and related factors), discount rates, operating costs, future capital requirements, decommissioning costs, exploration potential, reserves and operating performance (which includes production and sales volumes). These estimates and assumptions are subject to risk and uncertainty. Therefore, there is a possibility that changes in circumstances will impact these projections, which may impact the recoverable amount of assets and/or CGUs. Fair value is determined as the amount that would be obtained from the sale of the asset in an arm's length transaction between knowledgeable and willing parties. Fair value for oil and gas assets is generally determined as the present value of estimated future cash flows arising from the continued use of the assets, which includes estimates such as the cost of future expansion plans and eventual disposal, using assumptions that an independent market participant may take into account. Cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Management of the Company has carried out a formal assessment of the recoverable amount of JSC "Ozenmunaigas" due to the presence of impairment indicators. The main indicators were the level of production being materially lower than planned in the last two years and the increasing levels of operational and capital expenditure. The result of this assessment indicated that the carrying value of JSC "Ozenmunaigas" assets exceeded the estimated recoverable amount by 75 billion Tenge, resulting in an impairment charge during 2012 (Note 6, 20). The estimated recoverable amount was based on management's estimate of its fair value, which was derived using discounted cash flow approach. The results of the assessment were most sensitive to assumptions related to production and pricing.

The assumed production profile was based on an assessment performed by accredited third party oil and gas consultants that envisages growth of more than 20% in production within four years. If the production profile had been assumed to be 5% higher or lower than the assumed production profile used in the assessment, this would have had the effect of reducing impairment by more than 55 billion Tenge or increasing impairment by more than 55 billion Tenge, respectively. If production had been assumed to have remained fixed at the 2012 level, the impairment would have been over 200 billion Tenge.

Brent crude oil price assumptions were based on market expectations together with the expectations of an independent industry analysis and research organization, adjusted for the average realized historical discount on quoted price. If Brent crude oil prices had been assumed to be 5% higher or lower than the price assumptions used in the assessment, this would have had the effect of reducing impairment by more than 40 billion Tenge or increasing impairment by more than 40 billion Tenge, respectively.

The projection of cash flows was limited by the date of license expiry in 2021. Expenditure cash flows up to 2017 were obtained from the approved budget and business plan of the Company. Most of the projections beyond that period were inflated using Kazakhstan inflation estimates, except for capital expenditure projections, which represent management's best available estimate as at the date of impairment assessment. For the purposes of the assessment it was assumed that management would not be able to significantly reduce operational or capital expenditure in the final years before license expiry in order to make cost savings. An exchange rate of 150.45 KZT/USD, which is the official exchange rate as at the date of the impairment assessment, was used to convert US Dollar denominated sales. All the derived cash flows were discounted using after tax weighted average cost of capital ("WACC") of 13.09%.

Management believes that the resulting impairment charge on JSC "Ozenmunaigas" assets could be reversed in future periods if actual production over the next years exceeds expectations used in this impairment assessment or if there are indicators of sustainable increases in market prices for crude oil.

##### *Asset retirement obligations*

Under the terms of certain contracts, legislation and regulations the Company has legal obligations to dismantle and remove tangible assets and restore the land at each production site. Specifically, the Company's obligation relates to the ongoing closure of all non-productive wells and final closure activities such as removal of pipes, buildings and recultivation of the contract territories. Since the license terms cannot be extended at the discretion of the Company, the settlement date of the final closure obligations has been assumed to be the end of each license period.

#### **4. SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)**

##### *Asset retirement obligations (continued)*

If the asset retirement obligations were to be settled at the end of the economic life of the properties, the recorded obligation would increase significantly due to the inclusion of all abandonment and closure costs. The extent of the Company's obligations to finance the abandonment of wells and for final closure costs depends on the terms of the respective contracts and current legislation. Where neither contracts nor legislation include an unambiguous obligation to undertake or finance such final abandonment and closure costs at the end of the license term, no liability has been recognized. There is some uncertainty and significant judgment involved in making such a determination. Management's assessment of the presence or absence of such obligations could change with shifts in policies and practices of the Government or in the local industry practice. The Company calculates asset retirement obligations separately for each contract.

The amount of the obligation is the present value of the estimated expenditures expected to be required to settle the obligation adjusted for expected inflation and discounted using average long-term risk-free interest rates for emerging market sovereign debt adjusted for risks specific to the Kazakhstan market. The Company reviews site restoration provisions at each reporting date, and adjusts them to reflect the current best estimate in accordance with IFRIC 1 Changes in Existing Decommissioning, Restoration and Similar Liabilities.

Estimating the future closure costs involves significant estimates and judgments by management. Most of these obligations are many years in the future and, in addition to ambiguities in the legal requirements, the Company's estimate can be affected by changes in asset removal technologies, costs and industry practice. Approximately 15.80% and 13.84% of the provision at December 31, 2012 and 2011 relates to final closure costs. The Company estimates future well abandonment cost using current year prices and the average long-term inflation rate.

The long-term inflation and discount rates used to determine the carrying value of obligation at December 31, 2012 were 5.0% and 7.9% respectively (2011: 5.0% and 7.9%). Movements in the provision for asset retirement obligations are disclosed in Note 15.

##### *Environmental remediation*

The Company also makes judgments and estimates in establishing provisions for environmental remediation obligations. Environmental expenditures are capitalized or expensed depending upon their future economic benefit. Expenditures that relate to an existing condition caused by past operations and do not have a future economic benefit are expensed.

Liabilities are determined based on current information about costs and expected plans for remediation and are recorded on a discounted basis based on management's expectations with regard to timing of the procedures required. The Company's environmental remediation provision represents management's best estimate based on an independent assessment of the anticipated expenditure necessary for the Company to remain in compliance with the current regulatory regime in Kazakhstan. As at the date of these financial statements the scope and timing of the remediation plan has not been formally agreed with the Government, except as agreed in the annual budget. For environmental remediation provisions, actual costs can differ from estimates because of changes in laws and regulations, public expectations, discovery and analysis of site conditions and changes in clean-up technology.

Further uncertainties related to environmental remediation obligations are detailed in Note 26. Movements in the provision for environmental remediation obligations are disclosed in Note 15.

##### *Taxation*

Deferred tax is calculated with respect to both corporate income tax ("CIT") and excess profit tax ("EPT"). Deferred CIT and EPT are calculated on temporary differences for assets and liabilities allocated to contracts for subsoil use at the expected rates. Both deferred CIT and EPT bases are calculated under the terms of the tax legislation enacted in the tax code disclosed in Note 22. Further uncertainties related to taxation are detailed in Note 26.

#### **5. CHANGE IN INVESTMENT OWNERSHIP INTERESTS**

On November 16, 2012 the Company concluded the sale of 49% of its 100% subsidiary KS EP Investments BV ("KS EP Investments") to Karpinvest Oil and Gas Ltd. ("Karpinvest"), a subsidiary of MOL Hungarian Oil and Gas Plc. KS EP Investments owns a 100% interest in LLP Karpovskiy Severniy ("KS LLP"), which is a subsoil use right holder under the Contract for Exploration of Oil, Gas and Condensate at Karpovskiy Severniy contract area in western Kazakhstan. Under the terms of a shareholders agreement, joint control has been established over the operations of KS EP Investments and no single shareholder is in a position to control the activity unilaterally, making it a jointly controlled entity for both shareholders.

## 5. CHANGE IN INVESTMENT OWNERSHIP INTERESTS (continued)

At the date of loss of control net assets of KS EP Investments were as follows:

	Assets and liabilities as at November 16, 2012
Cash	1,884
Current assets	100
Non-current assets	8,360
	<b>10,344</b>
Current liabilities	113
Non-current liabilities	3,821
	<b>3,934</b>
<b>Net assets</b>	<b>6,410</b>

Consideration received from Karpinvest for 49% share in KS EP Investments amounted to 36,455,170 US Dollars (5,485 million Tenge). The resulting gain on disposal of investment amounted to 4,784 million Tenge. As a result of this transaction the Company has derecognized the assets and liabilities of the former subsidiary, when the control was lost and recognized under the equity method its retained 51% interest in KS EP Investments at its fair value of 5,709 million Tenge.

Company's retained interest in KS EP Investments assets and liabilities allocated based on its fair values as at November 16, 2012 and the corresponding share of carrying values immediately before the disposal of 49% share and as at December 31, 2012 are as follows:

	Carrying values as at November 16, 2012	Fair values as at November 16, 2012	Assets and liabilities as at December 31, 2012
Cash	961	961	82
Current assets	51	51	373
Non-current assets	1,793	7,313	7,583
	<b>2,805</b>	<b>8,325</b>	<b>8,038</b>
Current liabilities	58	58	553
Non-current liabilities	1,454	2,558	2,586
	<b>1,512</b>	<b>2,616</b>	<b>3,139</b>
<b>Net assets</b>	<b>1,293</b>	<b>5,709</b>	<b>4,899</b>

The operating activities of KS LLP are dependent upon continued financing in the form of shareholder loans to enable KS LLP to meet its current obligations and to continue its activities. As a result the Company has provided financing in the form of additional shareholder loan to KS EP Investments in the amount of 11,828 thousand US dollars (1,763 million Tenge) during 2012. The fair value of shareholder loans, which are given at 6.5% interest rate, is determined by discounting future cash flows for the loans using a discount rate of 15%.

## 6. PROPERTY, PLANT AND EQUIPMENT

	Oil and gas properties	Other assets	Construction work- in-progress	Total
<b>2011</b>				
Opening net book amount at January 1, 2011	<b>255,031</b>	<b>31,437</b>	<b>11,041</b>	<b>297,509</b>
Additions	1,672	1,492	84,158	87,322
Change in ARO estimate	374	-	-	374
Disposals	(3,771)	(735)	(2,638)	(7,144)
Transfer from exploration and evaluation assets	1,407	-	-	1,407
Transfers from construction work-in-progress	69,782	10,908	(80,690)	-
Internal transfers	39	(195)	156	-
Depreciation charge	(34,642)	(4,313)	-	(38,955)
Reversal / (Impairment) (Note 20)	47	(40)	(1,660)	(1,653)
<b>Closing net book amount at December 31, 2011</b>	<b>289,939</b>	<b>38,554</b>	<b>10,367</b>	<b>338,860</b>
<b>At December 31, 2011</b>				
Cost	490,309	60,630	10,367	561,306
Accumulated depreciation	(200,370)	(22,076)	-	(222,446)
<b>Net book amount</b>	<b>289,939</b>	<b>38,554</b>	<b>10,367</b>	<b>338,860</b>

## 6. PROPERTY, PLANT AND EQUIPMENT (continued)

	Oil and gas properties	Other assets	Construction work- in-progress	Total
<b>2012</b>				
Opening net book amount at January 1, 2012	<b>289,939</b>	<b>38,554</b>	<b>10,367</b>	<b>338,860</b>
Additions	1,383	2,694	113,310	117,387
Change in ARO estimate	(1,865)	–	–	(1,865)
Disposals	(3,541)	(1,001)	(2,137)	(6,679)
Transfers from construction work-in-progress	79,008	13,496	(92,504)	–
Internal transfers	(562)	22	540	–
Depreciation charge	(40,580)	(4,591)	–	(45,171)
Impairment (Note 20)	(64,696)	(7,872)	(4,444)	(77,012)
<b>Closing net book amount at December 31, 2012</b>	<b>259,086</b>	<b>41,302</b>	<b>25,132</b>	<b>325,520</b>
<b>At December 31, 2012</b>				
Cost	493,981	66,860	25,132	585,973
Accumulated depreciation	(234,895)	(25,558)	–	(260,453)
<b>Net book amount</b>	<b>259,086</b>	<b>41,302</b>	<b>25,132</b>	<b>325,520</b>

## 7. INTANGIBLE ASSETS

	Exploration and evaluation assets	Other intangibles	Total
<b>2011</b>			
Opening net book amount at January 1, 2011	<b>12,755</b>	<b>2,430</b>	<b>15,185</b>
Acquisition of exploration licenses	15,794	–	15,794
Additions	6,246	1,074	7,320
Dry well write-off	(2,586)	–	(2,586)
Transfers	(1,407)	–	(1,407)
Disposals	(339)	(4)	(343)
Amortization charge	(5,667)	(872)	(6,539)
Impairment	(761)	(25)	(786)
<b>Closing net book amount at December 31, 2011</b>	<b>24,035</b>	<b>2,603</b>	<b>26,638</b>
<b>At December 31, 2011</b>			
Cost	39,500	6,072	45,572
Accumulated amortization	(15,465)	(3,469)	(18,934)
<b>Net book amount</b>	<b>24,035</b>	<b>2,603</b>	<b>26,638</b>
<b>2012</b>			
Opening net book amount at January 1, 2012	<b>24,035</b>	<b>2,603</b>	<b>26,638</b>
Additions	12,143	2,137	14,280
Dry well write-off	(4,321)	–	(4,321)
Loss of control over subsidiary (Note 5)	(8,190)	–	(8,190)
Disposals	(210)	(37)	(247)
Amortization charge	(7,668)	(908)	(8,576)
<b>Closing net book amount at December 31, 2012</b>	<b>15,789</b>	<b>3,795</b>	<b>19,584</b>
<b>At December 31, 2012</b>			
Cost	40,292	8,170	48,462
Accumulated amortization	(24,503)	(4,375)	(28,878)
<b>Net book amount</b>	<b>15,789</b>	<b>3,795</b>	<b>19,584</b>

In 2012 the Company recognized dry well expenses related to exploratory wells drilled on its East Zharkamys, NBK and Bodrai blocks.

## 8. FINANCIAL ASSETS

### *Other financial assets*

	2012	2011
Tenge denominated held to maturity deposits	1,083	989
Investments in Debt Instrument of NC KMG (Note 3, 23)	–	187,810
Other	2	4
<b>Total non-current</b>	<b>1,085</b>	<b>188,803</b>
US dollar denominated term deposits	333,218	169,806
Investments in Debt Instrument of NC KMG (Note 3, 23)	134,360	219
Held to maturity financial assets	42,596	109,542
Tenge denominated term deposits	40,382	36,116
Great Britain pound denominated term deposits	–	6,207
<b>Total current</b>	<b>550,556</b>	<b>321,890</b>
	<b>551,641</b>	<b>510,693</b>

The weighted average interest rate on US dollar denominated term deposits in 2012 was 2.4% (2011: 3.6%). The weighted average interest rate on Tenge denominated term deposits in 2012 was 1.4% (2011: 1.4%).

### *Investments in Debt Instrument of NC KMG*

On July 16, 2010 the Company purchased unsubordinated, coupon indexed, unsecured bonds issued by NC KMG (“Debt Instrument”) on the Kazakhstan Stock Exchange (“KASE”) in the amount of 221,543 million Tenge (1,499,649 thousand US Dollars). The Debt Instrument carries an annual coupon rate of 7% per annum, paid semi-annually, is indexed to the USD/KZT exchange rate at the date of issuance and matures in June 2013. As at December 31, 2012 the outstanding amount of the Debt Instrument and related accrued interest is 134,204 million Tenge and 156 million Tenge, respectively (2011: 187,810 million Tenge and 219 million Tenge, respectively).

The Debt Instrument contains the following key provisions:

- Whilst there are no fixed repayment terms, NC KMG will mandatorily use any future dividends from the Company to repay against the outstanding Debt Instrument (Note 3).
- If the Company acquires assets from NC KMG during the life of the Debt Instrument with an aggregate value of more than 800 million US Dollars, then the Company will be able to finance the portion of the cost of such acquisitions exceeding the 800 million US Dollars threshold through transferring or selling to NC KMG the relevant portion of the Debt Instrument at par value plus accrued coupon indexed to the USD/KZT exchange rate at the issuance date.
- If at maturity, NC KMG does not settle its outstanding Debt Instrument for cash, the Company shall pay a Special Dividend to its shareholders of a quantum, where NC KMG’s share is sufficient to settle the outstanding Debt Instrument.
- The Company will ensure that it will have sufficient cash reserves, which are in compliance with Company’s treasury policy, to pay its minority shareholders their portion of the Special Dividend, should it become necessary. Special monitoring and control mechanisms have been put in place to ensure that the Independent Non-Executive Directors could exercise control over expenditures exceeding budgeted amounts in the event that the amount of cash, held in appropriate banks, falls below required levels.

### *Trade and other receivables*

	2012	2011
Trade receivables	100,698	83,587
Other	980	923
Allowance for doubtful receivables	(510)	(384)
	<b>101,168</b>	<b>84,126</b>

In the second quarter of 2012 the Company concluded a crude oil sales contract with Vector Energy AG (“Vector”), a subsidiary of the Parent Company. Previously export sales were made to KazMunaiGas Refining and Marketing JSC (“KMG R&M”), another subsidiary of the Parent Company. As at December 31, 2012 the Company’s trade receivables included receivables from export sales of crude oil to Vector of 96,401 million Tenge (December 31, 2011: nil) and from sales of crude oil to KMG R&M of 2,957 million Tenge (December 31, 2011: 81,686 million Tenge). Of the total amount owed by Vector 32,657 million Tenge is overdue (December 31, 2011: 25,701 million Tenge was overdue from KMG R&M).

## 8. FINANCIAL ASSETS (continued)

### Trade and other receivables (continued)

Payments for oil delivered shall be made by Vector on the 60-th day after the date of delivery. In case of untimely payment Vector shall pay an interest penalty ranging at the rates from one month LIBOR plus 2% to six month LIBOR plus 3% depending on the amount owed and period overdue.

As of December 31, 2012 US dollar denominated trade and other receivables represented 95% of total receivables (2011: 93%). The remaining balances are Tenge denominated. Trade receivables are generally on 30 days' terms.

The ageing analysis of trade and other receivables is as follows as at December 31:

	2012	2011
Current	68,409	51,074
0-30 days overdue	9,637	18,494
30-60 days overdue	21,555	14,539
90-120 days overdue	1,507	–
120 and more days overdue	60	19
	<b>101,168</b>	<b>84,126</b>

### Cash and cash equivalents

	2012	2011
Tenge denominated term deposits with banks	38,813	28,112
US dollar denominated term deposits with banks	30,681	157,092
Euro denominated term deposits with banks	75	389
US dollar denominated cash in banks and on hand	51,951	2,916
Tenge denominated cash in banks and on hand	29,519	17,564
Great Britain pound denominated cash in bank and on hand	3,666	439
	<b>154,705</b>	<b>206,512</b>

Cash with banks earns interest based on daily bank deposit rates. Deposits with banks are made for varying periods of between one day and three months, depending on the immediate cash requirements of the Company, and earn interest at the respective deposit rates.

The weighted average interest rate on Tenge denominated deposits in 2012 was 1.3% (2011: 0.5%). The weighted average interest rate on US dollar denominated deposits in 2012 was 0.4% (2011: 0.3%).

## 9. INVESTMENTS IN JOINT VENTURES AND RECEIVABLE FROM A JOINTLY CONTROLLED ENTITY

	Ownership share	2012	2011
Interest in JV Kazgermunai LLP (“Kazgermunai”)	50%	65,287	98,823
Interest in JV Ural Group Limited BVI (“UGL”)	50%	19,066	17,703
Interest in JV KS EP Investments (Note 5)	51%	4,899	–
Receivable from jointly controlled entity		18,221	19,499
		<b>107,473</b>	<b>136,025</b>

### • JV Kazgermunai

The Company's share of Kazgermunai's assets and liabilities as at December 31 is as follows:

	2012	2011
Cash	11,079	23,710
Current assets	20,011	15,055
Non-current assets	102,029	114,126
	<b>133,119</b>	<b>152,891</b>
Current liabilities	37,936	26,539
Non-current liabilities	29,896	27,529
	<b>67,832</b>	<b>54,068</b>
<b>Net assets</b>	<b>65,287</b>	<b>98,823</b>

## 9. INVESTMENTS IN JOINT VENTURES AND RECEIVABLE FROM A JOINTLY CONTROLLED ENTITY (continued)

- *JV Kazgermunai (continued)*

The share of results of Kazgermunai included into the consolidated financial statements of the Company is as follows:

	2012	2011
Revenues	172,238	172,591
Operating expenses	(100,856)	(109,927)
Profit from operations	71,382	62,664
Finance cost, net	(165)	(511)
Profit before tax	71,217	62,153
Income tax expense	(37,883)	(23,781)
<b>Profit for the year</b>	<b>33,334</b>	<b>38,372</b>
<b>Foreign currency translation gain recognized in other comprehensive income</b>	<b>300</b>	<b>340</b>

Profit for the year in 2012 is net of the effect of amortization of the fair valuation of the licenses and related deferred tax benefit in the amount of 8,131 million Tenge (2011: 7,730 million Tenge).

During 2012 the Company received dividends from Kazgermunai in the amount of 67,170 million Tenge (2011: 36,627 million Tenge).

- *JV Ural Group Limited BVI (“UGL”)*

On April 15, 2011 the Company acquired from Exploration Venture Limited (EVL) 50% of the common shares of UGL. UGL holds 100% equity interest in Ural Oil and Gas LLP (UOG), which has an exploration license for the Fedorovskiy hydrocarbons field located in western Kazakhstan.

The Company’s share of UGL assets and liabilities as at December 31 is as follows:

	2012	2011
Cash	739	31
Current assets	26	9
Non-current assets	36,631	31,240
	<b>37,396</b>	<b>31,280</b>
Current liabilities	1,820	220
Non-current liabilities	16,510	13,357
	18,330	13,577
<b>Net assets</b>	<b>19,066</b>	<b>17,703</b>

The operating activities of UGL are dependent upon continued financing in the form of shareholder loans to enable UGL to meet its current obligations and to continue its activities. As a result the Company has provided financing in the form of additional shareholder loans in the amount of 22,250 thousand US dollars (3,318 million Tenge) during the year ended December 31, 2012. The fair value on initial and additional shareholder loans, which are given on an interest free basis, is determined by discounting future cash flows for the loans using a discount rate of 15%.

*Receivable from jointly controlled entity CITIC Canada Energy Limited (“CCEL”)*

In 2007 the Company purchased a 50% interest in a jointly controlled entity, CCEL, whose investments are involved in oil and natural gas production in western Kazakhstan, from its co-investor, State Alliance Holdings Limited, a holding company ultimately belonging to CITIC Group, a company listed on the Hong Kong Stock Exchange.

CCEL is contractually obliged to declare dividends on an annual basis based on available distributable equity. At the same time, for the period until 2020 the Company is contractually obliged to transfer any dividends received from CCEL, in excess of a Guaranteed Amount, to CITIC, up to the Total Maximum Amount, which amounts to 572.3 million US dollars (86,273 million Tenge) as at December 31, 2012 (2011: 627.3 million US dollars or 93,084 million Tenge). The Total Maximum Amount represents the balance of the Company’s share of the original purchase price funded by CITIC plus accrued interest. The Company has no obligation to pay amounts to CITIC unless it receives an equivalent amount from CCEL. Accordingly, the Company recognizes in its statement of financial position only the right to receive dividends from CCEL in the Guaranteed Amount on an annual basis until 2020, plus the right to retain any dividends in excess of the total Maximum Guaranteed Amount. The carrying amount of this receivable at December 31, 2012, amounted to 119.7 million US dollars (18,039 million Tenge) (2011: 129.2 million US dollars or 19,170 million Tenge).

## 9. INVESTMENTS IN JOINT VENTURES AND RECEIVABLE FROM A JOINTLY CONTROLLED ENTITY (continued)

Receivable from jointly controlled entity CITIC Canada Energy Limited ("CCEL") (continued)

Additionally, the Company has the right, subject to certain conditions precedent, to exercise a put option and return the investment to CITIC in exchange for 150 million US dollars plus annual interest of 8% less the cumulative amount of the guaranteed payments received.

On November 17, 2008, the annual Guaranteed Amount has been increased from 26.2 million US dollars to 26.9 million US dollars, payable in two equal installments not later than June 12 and December 12 of each year. After the above amendment the effective interest rate on the receivable from CCEL is 15% per annum.

The Company's share of the jointly controlled entity's assets and liabilities is as follows:

	2012	2011
<b>Current assets</b>	26,616	25,967
<b>Non-current assets</b>	104,773	112,997
	<b>131,389</b>	<b>138,964</b>
<b>Current liabilities</b>	40,191	42,149
<b>Non-current liabilities</b>	91,198	96,815
	<b>131,389</b>	<b>138,964</b>
<b>Net assets</b>	-	-

Equity is nil as CCEL is contractually obliged to distribute all income to its participants, therefore, classifying all distributable income as a liability.

## 10. INVESTMENTS IN ASSOCIATE

	Ownership share	2012	2011
Interest in Petrokazakhstan Inc. ("PKI")	33%	118,959	133,228

The Company's share of PKI's assets and liabilities as at December 31 is as follows:

	2012	2011
<b>Cash</b>	10,886	14,475
<b>Current assets</b>	27,463	21,715
<b>Non-current assets</b>	138,928	155,335
	<b>177,277</b>	<b>191,525</b>
<b>Current liabilities</b>	23,582	39,232
<b>Non-current liabilities</b>	34,736	19,065
	<b>58,318</b>	<b>58,297</b>
<b>Net assets</b>	<b>118,959</b>	<b>133,228</b>

The share of results of the associate included into the consolidated financial statements of the Company is as follows:

	2012	2011
<b>Revenue</b>	127,485	171,662
<b>Operating expenses</b>	(74,511)	(110,173)
<b>Profit from operations</b>	52,974	61,489
<b>Finance cost, net</b>	(859)	(672)
<b>Profit before tax</b>	52,115	60,817
<b>Income tax expense</b>	(18,391)	(15,142)
<b>Profit for the period</b>	<b>33,724</b>	<b>45,675</b>
<b>Foreign currency translation gain recognized in other comprehensive income</b>	<b>1,807</b>	<b>1,556</b>

Profit for the year in 2012 is net of the effect of amortization of the fair valuation of the licenses in the amount of 10,143 million Tenge (2011: 11,620 million Tenge).

During 2012 the Company received dividends from PKI in the amount of 49,800 million Tenge (2011: 53,168 million Tenge).

## 11. INVENTORIES

	2012	2011
Crude oil	14,801	13,817
Materials	10,257	8,834
	<b>25,058</b>	<b>22,651</b>

As at December 31, 2012 the Company had 361,521 tons (2011: 414,180 tons) of crude oil in storage and transit.

## 12. SHARE CAPITAL

	Shares outstanding	
	Number of shares	Tenge million
<b>As at January 1, 2011</b>	<b>71,219,565</b>	<b>214,082</b>
Reduction of treasury stock due to exercise of share options	12,302	133
Increase of treasury stock due to share repurchases	(938,479)	(15,763)
<b>As at December 31, 2011</b>	<b>70,293,388</b>	<b>198,452</b>
Reduction of treasury stock due to exercise of share options	70,127	703
Increase of treasury stock due to share repurchases	(2,205,813)	(36,203)
<b>As at December 31, 2012</b>	<b>68,157,702</b>	<b>162,952</b>

### 12.1 Share capital

#### *Authorized shares*

The total number of authorized shares is 74,357,042 (2011: 74,357,042). 43,087,006 of the outstanding shares are owned by the Parent Company as at December 31, 2012 (2011: 43,087,006). The shares of the Company have no par value.

#### *Dividends*

In accordance with Kazakhstan legislation, dividends may not be declared if the Company has negative equity in its Kazakh statutory financial statements or if the payment of dividends would result in negative equity in the statutory financial statements. Total dividends per share recognized as distributions to equity holders during 2012 amounted to 1,300 Tenge per share (2011: 800 Tenge per share) for both of the outstanding ordinary and preferred shares as at June 11, 2012, the date of record.

### 12.2 Employee share option plans

The expense recognized for share option plans related to employee services received during the year is 354 million Tenge (2011: 408 million Tenge).

#### *Employee option plans*

Under the employee option plan 1 ("EOP 1"), an award of global depositary receipt ("GDR") options with an exercise price equal to the market value of GDRs at the time of award was made to executives. The exercise of options is not subject to performance conditions and vests 1/3 each year over 3 years and is exercisable till the fifth anniversary from the vesting date.

Under the employee option plan 2 ("EOP 2"), share options are granted to incentivize and reward key employees, senior executives and members of the Board of Directors of the Company, except for independent directors. The exercise price of the options is equal to the market price of GDRs on the date of grant. The exercise of these options is not subject to the attainment of performance conditions. Options granted on or after July 1, 2007 vest on the third anniversary of the date of the grant and are exercisable till the fifth anniversary from the vesting date.

## 12. SHARE CAPITAL (continued)

### 12.2 Employee share option plans (continued)

#### *Movement in the year*

The following table illustrates the number of GDR's (No.) and weighted average exercise prices in US dollars per GDR (WAEP) of and movements in share options during the year:

	2012		2011	
	No.	WAEP	No.	WAEP
Outstanding at January 1	2,118,984	18.26	2,246,195	18.15
Granted during the year	–	–	7,845	21.50
Exercised during the year	(420,763)	13.12	(73,810)	14.19
Forfeited during the year	(20,273)	26.08	(61,246)	19.44
Outstanding at December 31	1,677,948	19.47	2,118,984	18.26
Exercisable at December 31	636,760	19.77	1,051,017	17.11

The weighted average remaining contractual life for share options outstanding as at December 31, 2012 is 4.53 years (2011: 5.35 years). The range of exercise price for options outstanding at December 31, 2012 was 13.00 US Dollars – 26.47 US dollars per GDR (2011: 13.00 US Dollars – 26.47 US Dollars). The EOP 1 and EOP 2 are equity settled plans and the fair value is measured at the grant date.

### 12.3 Kazakhstan Stock Exchange disclosure requirement

The Kazakhstan Stock Exchange has enacted on October 11, 2010 a requirement for disclosure of the total equity less other intangible assets (Note 7) per shares outstanding as at year end. As at December 31, 2012 the amount per share outstanding is 19,572 Tenge (December 31, 2011: 18,437 Tenge).

## 13. EARNINGS PER SHARE

	2012	2011
Weighted average number of all shares outstanding	69,301,529	70,803,127
Profit for the year	160,823	208,931
Basic and diluted earnings per share	2.32	2.95

The above presentation includes both ordinary and preferred shares as preferred shareholders equally share distributable profits, which results in identical earnings per share for both classes of shares.

## 14. BORROWINGS

	2012	2011
Fixed interest rate borrowings	7,310	8,172
Weighted average effective interest rate	7.35%	7.19%
Floating interest rate borrowings	–	79,793
Weighted average effective interest rates	–	3.88%
<b>Total borrowings</b>	<b>7,310</b>	<b>87,965</b>
Current	2,462	54,931
Non-current	4,848	33,034

On July 5, 2012 the Company fully repaid remaining principal and accrued interest of the KMG PKI Finance notes in the amount of 538.2 million US dollars (80,011 million Tenge) and 20 million US dollars (2,975 million Tenge), respectively.

As at December 31, 2012 the Company's borrowings balance primarily relates to fixed rate US dollar denominated obligation to reimburse historical costs incurred by the Government prior to the acquisition of licenses by the Company, which will expire in 2023. The Company has discounted this obligation at an interest rate of 7.93% and accounts for these borrowings at amortized cost.

**15. PROVISIONS**

	Environmental remediation	Taxes	Asset retirement obligation	Other	Total
<b>At January 1, 2011</b>	<b>19,801</b>	<b>11,685</b>	<b>14,622</b>	<b>5,379</b>	<b>51,487</b>
Additional provisions	–	6,283	305	1,277	7,865
Unused amounts reversed	–	(3,839)	(9)	–	(3,848)
Unwinding of discount	–	–	1,158	–	1,158
Changes in estimate	–	–	374	–	374
Used during the year	(1,273)	(2,002)	(602)	(407)	(4,284)
<b>At December 31, 2011</b>	<b>18,528</b>	<b>12,127</b>	<b>15,848</b>	<b>6,249</b>	<b>52,752</b>
Current portion	1,432	12,127	748	599	14,906
Non-current portion	17,096	–	15,100	5,650	37,846
Additional provisions	–	9,619	281	3,068	12,968
Unused amounts reversed	–	(8,801)	–	–	(8,801)
Unwinding of discount	–	–	1,254	–	1,254
Changes in estimate	(958)	–	(1,865)	–	(2,823)
Used during the year	(266)	–	(399)	(439)	(1,104)
<b>At December 31, 2012</b>	<b>17,304</b>	<b>12,945</b>	<b>15,119</b>	<b>8,878</b>	<b>54,246</b>
Current portion	2,940	12,945	809	625	17,319
Non-current portion	14,364	–	14,310	8,253	36,927

**16. REVENUE**

	2012	2011
Export:		
Crude oil	720,262	655,595
Domestic (Note 26):		
Crude oil	60,559	49,555
Gas products	7,700	7,339
Refined products	2,109	3,327
Other sales and services	6,540	5,378
	<b>797,170</b>	<b>721,194</b>

**17. PRODUCTION EXPENSES**

	2012	2011
Employee benefits	82,959	65,323
Repairs and maintenance	18,162	20,087
Materials and supplies	14,176	14,691
Energy	12,884	10,564
Transportation services	5,758	4,519
Processing expenses	393	1,041
Change in crude oil balance	(984)	(3,919)
Other	7,014	5,159
	<b>140,362</b>	<b>117,465</b>

**18. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES**

	2012	2011
Transportation expenses	53,122	49,578
Employee benefits	13,936	13,768
Sponsorship	6,778	4,970
Accrual of fines and penalties (Note 26)	8,302	12,738
Management fees and commissions	4,169	8,752
Consulting and audit services	1,382	1,669
Repairs and maintenance	1,339	840
Other	4,060	6,205
	<b>93,088</b>	<b>98,520</b>

## 19. TAXES OTHER THAN ON INCOME

	2012	2011
Rent tax	159,822	149,771
Mineral extraction tax	70,792	78,680
Export customs duty	36,429	46,979
Property tax	4,373	3,454
Other taxes	2,755	5,144
	<b>274,171</b>	<b>284,028</b>

## 20. IMPAIRMENT OF PROPERTY, PLANT AND EQUIPMENT

	2012	2011
Impairment from complex assessment (Note 4)	75,000	–
Social objects impairment	1,593	1,465
Individual impairment	419	188
	<b>77,012</b>	<b>1,653</b>

## 21. FINANCE INCOME / COSTS

### 21.1 Finance income

	2012	2011
Interest income on Debt Instrument of NC KMG (Note 23)	11,403	14,064
Interest income on deposits with banks	7,306	10,575
Gain on sale of other financial assets	5,546	–
Interest income on receivable from jointly controlled entities	4,821	3,719
Capital gain on sale of subsidiary (Note 5)	4,784	–
Interest income on held to maturity financial assets	663	475
Other	5	10
	<b>34,528</b>	<b>28,843</b>

### 21.2 Finance costs

	2012	2011
Interest expense	5,601	5,865
Unwinding of discount on asset retirement obligation	1,254	1,158
Other	376	200
	<b>7,231</b>	<b>7,223</b>

## 22. INCOME TAXES

Income tax expense comprised the following for the years ended December 31:

	2012	2011
Corporate income tax	77,993	50,059
Excess profit tax	38,541	15,745
<b>Current income tax</b>	<b>116,534</b>	<b>65,804</b>
Corporate income tax	(19,175)	(1,938)
Excess profit tax	(4,433)	(205)
<b>Deferred income tax</b>	<b>(23,608)</b>	<b>(2,143)</b>
<b>Income tax expense</b>	<b>92,926</b>	<b>63,661</b>

## 22. INCOME TAXES (continued)

The following table provides a reconciliation of the Kazakhstan income tax rate to the effective tax rate of the Company on profit before tax.

	2012	2011
Profit before tax	253,749	272,592
Income tax	92,926	63,661
<b>Effective tax rate</b>	<b>37%</b>	<b>23%</b>
Statutory income tax	20%	20%
Increase / (decrease) resulting from		
Capital Gain on reorganization of the Company	5%	0%
Withholding tax	1%	0%
Excess profit tax	12%	5%
Corporate income tax of prior years	3%	2%
Share of result of associate and joint ventures	(5%)	(6%)
Non-taxable income	(2%)	(1%)
Tax provisions	1%	1%
Non-deductible expenses	2%	2%
<b>Effective tax rate</b>	<b>37%</b>	<b>23%</b>

During 2012 the Company underwent a reorganization, when former production branches “Ozenmunaigas” and “Embamunaigas” were separated into wholly owned subsidiaries JSC “Ozenmunaigas” and JSC “Embamunaigas”. All fixed assets of the former production branches were transferred to newly created companies at fair value in accordance with Kazakhstan legislation. As a result the Company has recognized a significant amount of taxable capital gain, which has also resulted in an increase in excess profit tax for Uzen, Tengiz and the 23 fields contracts.

The movements in the deferred tax assets relating to CIT and EPT were as follows:

	Fixed and Intangible assets	Provisions	Taxes	Other	Total
<b>At January 1, 2011</b>	<b>10,824</b>	<b>(1,469)</b>	<b>(11,746)</b>	<b>(4,187)</b>	<b>(6,578)</b>
Deferred taxes acquired in business combinations	1,320	–	–	–	1,320
Recognized in profit and loss	(843)	(175)	(930)	(195)	(2,143)
<b>At December 31, 2011</b>	<b>11,301</b>	<b>(1,644)</b>	<b>(12,676)</b>	<b>(4,382)</b>	<b>(7,401)</b>
Loss of control over subsidiary (Note 5)	(959)	–	–	–	(959)
Recognized in profit and loss	(21,724)	(518)	(1,295)	(71)	(23,608)
<b>At December 31, 2012</b>	<b>(11,382)</b>	<b>(2,162)</b>	<b>(13,971)</b>	<b>(4,453)</b>	<b>(31,968)</b>

## 23. RELATED PARTY TRANSACTIONS

The category “entities under common control” comprises entities controlled by the Parent Company. The category “other state controlled entities” comprises entities controlled by Samruk-Kazyna SWF, except for banks, controlled by Samruk-Kazyna SWF. BTA Bank and Alliance Bank are related parties since they are controlled by Samruk-Kazyna SWF and Kazkommertsbank is a related party due to Samruk Kazyna SWF holding 21.2% of the bank’s ordinary shares. Starting from 2012, Halyk Group is no longer a related party to the Company since the group is no longer controlled by a member of the management board of Samruk-Kazyna SWF.

### 23. RELATED PARTY TRANSACTIONS (continued)

Sales and purchases with related parties during the years ended December 31, 2012 and 2011 and the balances with related parties at December 31, 2012 and 2011 are as follows:

	2012	2011
<b>Revenue and other income</b> (Note 16)		
Entities under common control	787,838	711,888
Other state controlled entities	4,863	7
Associates	708	48
Joint ventures	329	415
<b>Purchases of goods and services</b> (Note 17 and 18)		
Entities under common control	22,280	22,852
Other state controlled entities	14,120	11,916
Parent Company	4,018	8,320
Associates	1,130	982
Halyk Bank of Kazakhstan affiliates	–	1,190
<b>Purchase of exploration licenses from Parent Company</b>	–	5,745
<b>Interest earned on financial assets</b>		
Interest earned on Debt Instrument	11,403	14,064
Effective interest rate on Investments in Debt Instrument of NC KMG – indexed USD/KZT	7.00%	6.97%
Interest earned on loans to Joint ventures	2,090	779
Average interest rate on loans to Joint ventures	15.00%	15.00%
Kazkommertsbank	1,082	1,415
Average interest rate on deposits	4.69%	6.65%
Halyk Bank of Kazakhstan	–	4,598
Average interest rate on deposits	–	2.69%
<b>Fair value loss on loans provided</b>		
Joint ventures	2,049	1,312
<b>Salaries and other short-term benefits</b>		
Members of the Board of Directors	121	133
Members of the Management Board	207	295
<b>Share-based payments</b>		
Members of the Board of Directors	–	1
Members of the Management Board	10	36
	<b>December 31, 2012</b>	<b>December 31, 2011</b>
<b>Cash and cash equivalents</b> (Note 8)		
Alliance Bank	208	–
Kazkommertsbank	110	925
BTA Bank	4	15
Halyk Bank of Kazakhstan	–	37,009
<b>Financial assets</b> (Note 8)		
Investments in Debt Instrument of NC KMG – indexed USD/KZT	134,360	188,029
Kazkommertsbank	38,207	–
Halyk Bank of Kazakhstan	–	37,115
<b>Trade and other receivables</b> (Note 5 , Note 8 and Note 9)		
Entities under common control	104,593	85,156
Joint ventures	31,506	28,107
Other state controlled entities	1,106	755
Halyk Bank of Kazakhstan affiliates	–	38
<b>Trade payables</b>		
Parent Company	1,125	777
Associates	837	723
Entities under common control	512	456
Other state controlled entities	101	244

### **23. RELATED PARTY TRANSACTIONS (continued)**

#### *Sales and receivables*

Sales to related parties comprise mainly export and domestic sales of crude oil and oil products to subsidiaries of NC KMG. Export sales to related parties represented 6,078,074 tons of crude oil in 2012 (2011: 5,758,008 tons). The sales of crude oil are priced by reference to Platt's index quotations and adjusted for freight, trader's margin and quality differentials. For these exports of crude oil the Company received an average price per ton of approximately 122,103 Tenge in 2012 (2011: 117,830 Tenge).

In addition, the Company supplies oil and gas products to the local market through a subsidiary of the Parent Company at the directive of the Kazakhstan government, the ultimate controlling shareholder of the Parent Company. Those supplies to the domestic market represented 1,595,399 tons of crude oil production in 2012 (2011: 1,812,156 tons). Prices for the local market sales are determined by agreement with the Parent Company. In February 2012, the Company agreed a revised schedule of prices for domestic market sales of crude oil, including a price of 43,500 Tenge per tonne effective from July 1, 2012. Subsequently, actual prices for domestic market were reduced and amounted to 38,000 Tenge per tonne for the sales from July 20 to September 30, 2012, and 40,000 Tenge per tonne for the sales from October 1 to December 31, 2012. In accordance with the terms of the Company's charter, such price reduction, as a related party transaction, should have been approved by the Independent Non-Executive Directors of the Company, but no such approval was given to reduce prices for domestic crude oil sales in 2012. As a result, in 2012 the Company received an average price per tonne of around 37,906 Tenge (2011: 27,290 Tenge) for deliveries to the local market.

Trade and other receivables from related parties principally comprise amounts related to export sales transactions.

#### *Purchases and payables*

Management fees to the Parent Company amounted to 4,018 million Tenge in 2012 (2011: 8,320 million Tenge). Agency commissions for crude oil sales amounted to 151 million Tenge in 2012 (2011: 432 million Tenge). Transportation services related to the shipment of 5,198,600 tons of crude oil in 2012 (2011: 5,475,921 tons) were purchased from a subsidiary of the Parent Company for 18,457 million Tenge in 2012 (2011: 17,161 million Tenge). The remaining services purchased from subsidiaries of NC KMG include primarily payments for security services, processing and demurrage expenditures.

#### *Share based payments to members of the Management Board*

Share based payments to members of the Management Board represents the amortization of share based payments over the vesting period. During 2012 the Company granted no options (2011: 7,845 options at average exercise prices of 21.5 US dollars or 3,158 Tenge).

### **24. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES**

The Company has various financial liabilities such as borrowings, trade and other payables. The Company also has various financial assets such as trade receivables, short and long-term deposits and cash and cash equivalents.

The Company is exposed to interest rate risk, foreign currency risk, credit risk, liquidity risk and commodity price risk. The Company's Finance Committee assists management in the oversight of the monitoring and where it is deemed appropriate, mitigation of these risks in accordance with approved policies such as the treasury policy.

#### *Interest rate risk*

The Company's exposure to the risk of changes in market interest rates related mainly to the Company's floating rate on KMG PKI Finance notes, which were fully settled on July 5, 2012 (Note 14). As of December 31, 2012 the Company has no floating interest rate borrowings and no exposure to interest rate risk.

#### *Foreign currency risk*

The Company's exposure to the risk of changes in foreign exchange rates relates mainly to the Company's operating activities, as the majority of its sales are denominated in US dollars whilst almost all of its costs are denominated in Tenge, and to its investments denominated in foreign currencies.

The following table demonstrates the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other variables held constant, of the Company's profit before tax (due to changes in the fair value of monetary assets and liabilities).

## 24. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

### Foreign currency risk (continued)

	Increase/ decrease in Tenge to US dollar exchange rate	Effect on profit before tax
<b>2012</b>		
US dollar	+ 10.00%	66,855
US dollar	- 10.00%	(66,855)
<b>2011</b>		
US dollar	+ 10.00%	53,299
US dollar	- 10.00%	(53,299)

### Credit risk

The Company is exposed to credit risk in relation to its trade receivables. The Company's vast majority of sales are made to an affiliate of the Parent and the Company has a significant concentration risk of the receivable from this affiliate (Note 8, 23). An additional number of minor receivables are grouped into homogeneous groups and assessed for impairment collectively on an ongoing basis with the result that the Company's exposure to bad debts is not significant.

The Company is also exposed to credit risk in relation to its investing activities. The Company places deposits with Kazakhstan and foreign banks and purchases National Bank notes. In addition, the Company has purchased Debt Instruments issued by its Parent Company (Note 8, 23).

Credit risk from balances with financial institutions is managed by the Company's treasury department in accordance with the Company's treasury policy, which is approved by the Company's Board of Directors. The Company's maximum exposure to credit risk arising from default of the financial institutions equals to the carrying amounts of these financial assets.

The table below shows the balances of the financial assets held in banks and Debt Instruments of NC KMG at the reporting date using the Standard and Poor's credit ratings, unless otherwise stated.

Banks	Location	Rating <sup>7</sup>		2012	2011
		2012	2011		
Investment in Debt Instrument of NC KMG	Kazakhstan	BBB- (stable)	BBB- (stable)	134,360	188,029
Halyk Bank	Kazakhstan	BB (stable)	BB (stable)	131,207	74,124
BNP Paribas	France	A+ (negative)	AA- (negative)	75,319	42,421
HSBC Plc	UK	AA- (negative)	AA- (stable)	75,044	80,799
Deutsche Bank	Germany	A+ (negative)	A+ (negative)	47,328	19,524
National Bank of Republic of Kazakhstan	Kazakhstan	BBB+ (stable)	BBB+ (stable)	42,596	109,542
ING Bank	Netherlands	A+ (negative)	A+ (stable)	41,873	484
Kazkommertsbank	Kazakhstan	B+ (negative)	B+ (stable)	38,317	925
ATF Bank (Moody's)	Kazakhstan	B1 (stable)	Ba3 (negative)	37,696	62,417
Citi Bank Kazakhstan	Kazakhstan	Not available	Not available	26,247	19,534
Citi Bank N.A.	UK branch	A (negative)	A (negative)	21,712	50,658
RBS Kazakhstan	Kazakhstan	Not available	Not available	13,208	18,028
Credit Suisse	British Virgin Islands	A+ (negative)	A+ (negative)	12,366	5,750
HSBC Kazakhstan	Kazakhstan	BBB (stable)	BBB (stable)	7,016	7,324
BankCenterCredit (Moody's)	Kazakhstan	B1 (negative)	B1 (negative)	1,654	19
Alliance Bank (Moody's)	Kazakhstan	B3 (negative)	B3 (stable)	208	-
HSBC Ltd.	Hong Kong	AA - (stable)	AA - (stable)	-	31,147
Royal Bank of Scotland NV	Netherlands	A (stable)	A (stable)	-	6,207
Other				195	273
				<b>706,346</b>	<b>717,205</b>

<sup>7</sup>Source: Interfax – Kazakhstan, Factivia, official sites of the banks and rating agencies as at December 31 of the respective year

## 24. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

### *Liquidity risk*

The Company monitors its liquidity risk using a liquidity planning tool. This tool considers the maturity of both its financial investments and financial assets (e.g. accounts receivables and other financial assets) and projected cash flows from operations.

The Company's objective is to maintain a balance between continuity of funding and flexibility through the use of short and long-term deposits in local banks.

The table below summarizes the maturity profile of the Company's financial liabilities at December 31, 2012 based on contractual undiscounted payments:

<b>Year ended</b>		<b>Less than 3</b>			<b>more than</b>	
<b>December 31, 2011</b>	<b>On demand</b>	<b>months</b>	<b>3-12 months</b>	<b>1-5 years</b>	<b>5 years</b>	<b>Total</b>
Borrowings	–	588	54,343	33,706	3,113	91,750
Trade and other payables	48,680	–	–	–	–	48,680
	<b>48,680</b>	<b>588</b>	<b>54,343</b>	<b>33,706</b>	<b>3,113</b>	<b>140,430</b>

<b>Year ended</b>		<b>Less than 3</b>			<b>more than</b>	
<b>December 31, 2012</b>	<b>On demand</b>	<b>months</b>	<b>3-12 months</b>	<b>1-5 years</b>	<b>5 years</b>	<b>Total</b>
Borrowings	–	271	2,262	4,646	2,002	9,181
Trade and other payables	82,255	–	–	–	–	82,255
	<b>82,255</b>	<b>271</b>	<b>2,262</b>	<b>4,646</b>	<b>2,002</b>	<b>91,436</b>

### *Commodity price risk*

The Company is exposed to the effect of fluctuations in the price of crude oil, which is quoted in US dollars on international markets. The Company prepares annual budgets and periodic forecasts including sensitivity analyses in respect of various levels of crude oil prices in the future.

### *Capital management*

Capital includes total equity. The primary objective of the Company's capital management is to ensure that it maintains a strong credit rating and healthy capital ratios in order to support its business and maximize shareholder value.

As at December 31, 2012 the Company had a strong financial position and a conservative capital structure. Going forward, the Company intends to maintain a capital structure which allows it the flexibility to take advantage of growth opportunities as and when they arise.

The Company manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Company may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares. No changes were made in the objectives, policy or processes during the years ended December 31, 2012 and 2011.

## 25. FINANCIAL INSTRUMENTS

Set out below is a comparison by category of carrying amounts and fair values of all of the Company's financial instruments:

	Carrying amount		Fair value	
	2012	2011	2012	2011
<b>Current financial assets</b>				
US dollar-denominated term deposits	333,218	169,806	333,218	169,806
Cash and cash equivalents	154,705	206,512	154,705	206,512
Investment in Debt Instrument of NC KMG	134,360	219	134,360	219
Held to maturity financial assets	42,596	109,542	42,596	109,542
Tenge denominated term deposits	40,382	36,116	40,382	36,116
Great Britain Pound denominated held to maturity deposits	–	6,207	–	6,207
Receivable from jointly controlled entity	3,895	1,361	3,895	1,361
<b>Non-current financial assets</b>				
Receivable from jointly controlled entity	14,326	18,138	14,326	18,138
Loan receivable from a joint venture	13,150	8,494	13,150	8,494
Tenge denominated term deposits	1,083	989	1,083	989
Other financial assets	2	4	2	4
Investment in Debt Instrument of NC KMG	–	187,810	–	187,810
<b>Financial liabilities</b>				
Borrowings fixed rate interest	7,310	8,172	7,310	8,172
Borrowings floating rate interest	–	79,793	–	79,793

The fair value of borrowings has been calculated by discounting the expected future cash flows at prevailing interest rates. The fair value of financial assets has been calculated using market interest rates.

## 26. COMMITMENTS AND CONTINGENCIES

### *Operating environment*

Kazakhstan continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Kazakhstan economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the Government.

The Kazakhstan economy has been affected by the global financial crisis. Despite some indications of recovery there continues to be uncertainty regarding further economic growth, access to capital and cost of capital, which could negatively affect the Company's future financial position, results of operations and business prospects.

While management believes it is taking appropriate measures to support the sustainability of the Company's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Company's results and financial position in a manner not currently determinable.

### *Local market obligation*

The Kazakhstan government requires oil producers to supply a portion of their crude oil production to meet domestic energy requirements. While the price for such supplies of crude oil is agreed with the Parent Company, this price may be materially below international market prices and may even be set at the cost of production (Note 23). If the Government does require additional crude oil to be delivered over and above the quantities currently supplied by the Company, such supplies will take precedence over market sales and will generate substantially less revenue than crude oil sold on the export market, which may materially and adversely affect the Company's business, prospects, financial condition and results of operations.

During the current year, in accordance with their obligations, the Company delivered 1,645,926 tons of oil (2011: 1,951,356 tons) and joint venture Kazgermunai delivered 517,991 tons of oil (2011: 221,915 tons) to the domestic market.

## 26. COMMITMENTS AND CONTINGENCIES (continued)

### *Taxation*

Kazakhstan's tax legislation and regulations are subject to ongoing changes and varying interpretations. Instances of inconsistent opinions between local, regional and national tax authorities are not unusual. The current regime of penalties and interest related to reported and discovered violations of Kazakhstan's tax laws are severe. Because of the uncertainties associated with Kazakhstan's tax system, the ultimate amount of taxes, penalties and interest, if any, may be in excess of the amount expensed to date and accrued at December 31, 2012.

The Company's management believes its interpretations of the tax legislation are appropriate and that the Company has justifiable arguments for its tax positions.

On July 12, 2012 the Tax Committee of the Ministry of Finance of the Republic of Kazakhstan completed the 2006-2008 comprehensive tax audit of the Company. As a result of the tax audit, which was commenced in October 2011, the tax authorities provided a tax assessment to the Company of 16,938 million Tenge, including 5,800 million Tenge of principal, 7,160 million Tenge of administrative fines and 3,978 million Tenge of late payment interest. Matters involved in the assessment relate mainly to reallocation of certain revenues and expenditures among the subsoil use contracts, timing of recognition of demurrage expenses and adjustment of revenues based on transfer pricing regulations.

The Company disagreed with the above assessments and filed an appeal to the Ministry of Finance. The Company's management believes its interpretations of the tax legislation were appropriate. However, as management believes the outcome of the dispute is uncertain and further believes that it is more likely than not that the Company may not be entirely successful in its appeals, due to the ambiguity contained in the tax legislation and a history of varying interpretations and inconsistent opinions of the authorities and courts, management has accrued for certain matters that arose in the assessment. As at December 31, 2012, existing provision for tax contains 9,619 million Tenge in respect of this matter, including principal of 4,158 million Tenge, fines of 2,307 million Tenge and late payment interest of 3,154 million Tenge (Note 15). The management believes that the Company will be successful in appealing the remaining balances of principal, fines, and late payment interest of the assessments.

In addition the Company has revised its previously estimated tax provisions in respect of 2006-2008 to bring them in line with the actual assessments made by the tax authorities. As a result the tax provision was also reversed by 8,801 million Tenge.

### *Environment*

Environmental regulation in Kazakhstan is evolving and subject to ongoing changes. Penalties for violations of Kazakhstan's environmental laws can be severe. Other than those amounts provided for in provisions (Note 15) management believes that there are no probable environmental liabilities, which could have a material adverse effect on the Company's financial position, statement of comprehensive income or cash flows.

### *Oilfield licenses*

The Company is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its oilfield licenses and related subsoil use contracts. Management cooperates with governmental authorities to agree on remedial actions necessary to resolve any findings resulting from these reviews. Failure to comply with the terms of a license could result in fines, penalties, license limitation, suspension or revocation. The Company's management believes that any issues of non-compliance will be resolved through negotiations or corrective actions without any material effect on the Company's financial position, statement of income or cash flows.

The Company's oil and gas fields are located on land belonging to the Mangistau and Atyrau regional administrations. Licenses are issued by the Ministry of Oil and Gas of Kazakhstan and the Company pays mineral extraction and excess profits tax to explore and produce oil and gas from these fields.

The principle licenses of the Company and their expiry dates are:

<b>Field</b>	<b>Contract</b>	<b>Expiry date</b>
Uzen (8 fields)	No. 40	2021
Emba (1 field)	No. 37	2021
Emba (1 field)	No. 61	2017
Emba (23 fields)	No. 211	2018
Emba (15 fields)	No. 413	2020

## 26. COMMITMENTS AND CONTINGENCIES (continued)

### *Commitments arising from oilfield and exploration licenses*

<b>Year</b>	<b>Capital expenditures</b>	<b>Operational expenditures</b>
2013	150,764	7,138
2014	5,685	4,324
2015	2,511	3,235
2016	61	3,277
2017-2024	–	12,621
	<b>159,021</b>	<b>30,595</b>

### *Crude oil supply commitments*

The Company has obligations to supply oil and oil products to the local market under government directives (Note 23).

### *Commitments of Kazgermunai*

The Company's share in the commitments of Kazgermunai is as follows as at December 31, 2012:

<b>Year</b>	<b>Capital expenditures</b>	<b>Operational expenditures</b>
2013	4,593	4,109

### *Commitments of UGL*

Under the UGL exploration license the partners to the share purchase agreement have agreed to capital expenditure commitments in order to satisfy the minimum work program. As at December 31, 2012 the Company's share in the capital commitments of UGL is as follows:

<b>Year</b>	<b>Capital expenditures</b>
2013	9,881
	<b>9,881</b>

### *Commitments of KS EP Investments*

The Company's share in the commitments of KS EP Investments is as follows as at December 31, 2012:

<b>Year</b>	<b>Capital expenditures</b>	<b>Operational expenditures</b>
2013	4,665	196
2014	1,502	34
	<b>6,167</b>	<b>230</b>

## 27. SUBSEQUENT EVENTS

### *Change of the Chief Executive Officer*

On January 23, 2013 at a meeting of the Board of Directors Abat Nurseitov was elected as a Chief Executive Officer (CEO) of the Company, succeeding Alik Aidarbayev.

These consolidated financial statements have been signed below by the following persons on behalf of the Company and in the capacities indicated on March 06, 2013:

Chief Executive Officer

Nurseitov A. A.

Acting Chief Financial Officer

B. Fraser, ACA.

## REFERENCE INFORMATION

- 1P  
Proved Reserves
- 2P  
Proved and Probable Reserves
- 3P  
Proved, Probable and Possible Reserves
- ANPZ  
LLP Atyrau refinery
- bbl  
Barrel
- bopd  
Barrels per day
- Caspian Pipeline Consortium (CPC)  
This pipeline connects Tengiz field in Kazakhstan with Novorossiysk, Russian port on the Black Sea. It is an important route of oil transportation from the Caspian shores to the international market.
- CCEL  
CCEL (CITIC Canada Energy Limited, 100% owner of CCPL, previously Nations Energy Company Ltd, develops Karazhanbas field). Owns 95% stake in JSC Karazhanbasmunai.
- China Investment Corporation (CIC)  
State investment fund of the People's Republic of China. The main mission of CIC is long-term investment in order to reduce financial risks for its shareholders.
- CIT  
Corporate Income Tax
- CIS  
Commonwealth of Independent States
- Conversion factors  
KMG EP -7.36 bbl/ton; KGM - 7.7; Karazhanbasmunai - 6.68; PKI – 7.75; others - 7.33.
- ED/CED  
Export Duty/Customs Export Duty
- EMG  
JSC Embamunaigas, one of two major production assets of KMG EP, operating in 40 main fields in Atyrau Region in Western Kazakhstan.
- EPT  
Excess Profit Tax

- GCA  
Gaffney, Cline & Associates - Independent international consulting company specialising in evaluating hydrocarbon reserves.
- GAMMA  
GAMMA rating (from English governance, accountability, management metrics and analysis) reflects the opinion of Standard & Poor's Corporate Ratings Service on the relative strength of a company's corporate governance practices. It takes into account level of shareholder protection from investment risk associated with poor governance systems. Practices and Policies are measured against S&P's corporate governance criteria, which are based on a synthesis of international codes, best corporate governance practices and guidelines.
- KBM  
JSC Karazhanbasmunai (please see CCEL)
- KASE  
Kazakhstan Stock Exchange
- KOA  
Kazakhoil Aktobe LLP
- KTM  
KazakhTurkMunai Ltd.
- KGM  
LLP JV Kazgermunai
- kbopd  
Thousand barrels per day
- KCGP  
Kazakhstan-China gas pipeline
- KCP  
Kazakhstan-China pipeline
- KMG EP  
KazMunaiGas Exploration Production JSC
- KPI  
LLP Kazakhstan Petrochemical Industries Inc. is the Operator of the Project "Construction of the first Integrated Gas Chemical Complex in Atyrau region".
- LSE  
London Stock Exchange
- MET  
Mineral Extraction Tax

- mmbbl  
One million barrels
- MMG  
JSC Mangistaumunaigaz
- MOL  
Plc MOL is an integrated oil and gas group in Hungary with interests in exploration, production, refining, marketing and petrochemicals.
- NC KMG (National Company KazMunayGas)  
A state oil and gas company of the Republic of Kazakhstan, in the form of a joint-stock company with 100% of its shares held in Sovereign Wealth Fund Samruk-Kazyna.
- PKI  
PetroKazakhstan Inc.
- PKOP  
PetroKazakhstan Oil Products
- Sovereign Wealth Fund Samruk-Kazyna  
National Prosperity Fund, managing state assets, shares of national companies and financial institutions for Kazakhstan development.
- SBS (SapaBarlau Service)  
KMG EP Exploration Assets LLP (previously SapaBarlau Service) holds the license rights, under Subsoil Use Contract Number 2193 (issued in November 2006) for oil and gas exploration at the “East Zharkamys -1 block” in the Aktobe region.
- Standard & Poor’s/Moody’s  
International rating agencies that award short-term and long-term credit ratings.
- TP  
JSC Turgai Petroleum
- Uzen – Atyrau – Samara (UAS)  
An oil pipeline, a 1,500 km-long link over the territory of Atyrau and Mangistau Regions to Russia.
- UBR  
LLP Drilling Well Servicing Division
- OMG  
JSC Ozenmunaigas, one of two production assets of KMG EP, operating in 2 main fields in Mangistau Region.
- UTTiOS  
LLP Support Service Vehicles and Well Servicing Division

## INFORMATION FOR SHAREHOLDERS

### SHAREHOLDERS' ANNUAL GENERAL MEETING

The annual general meeting of shareholders will be held at 10:30, on May 21, 2013 at:

Duman Hotel, Kurgalzhinskoye Shosse 2A, Astana, Republic of Kazakhstan

### WEBSITE

A wide range of information on the Company is available at [www.kmgep.kz](http://www.kmgep.kz) including details of activities, press releases and annual and interim reports.

### SHAREHOLDER QUESTIONS

For information about proxy voting, dividends and to report changes in personal details, shareholders should contact the Company's registrar/ depository:

Holders of ordinary or preferred shares: JSC "The Integrated Securities Registrar", 141, Abylai Khan prospect, Almaty, Republic of Kazakhstan. Tel. +7(727) 2724760

Holders of Global Depositary Receipts (GDRs): The Bank of New York Mellon, Shareholder Services, PO Box 358516, Pittsburgh PA 15252-8516, USA. Tel. +1 888 269 2377 (toll free within the USA), Tel. +1 201 680 6825 (outside USA), Email: [shrrelations@bnymellon.com](mailto:shrrelations@bnymellon.com), [www.adrbnymellon.com](http://www.adrbnymellon.com)

### NUMBER OF SHARES IN ISSUE

	Ordinary shares	Preferred shares	Total issued capital (2)
Number of issued shares (1)	70,220,935	4,136,107	74,357,042

(1) Including GDRs purchased to implement the Company's Option Program and held in trust (as of December 31, 2012 – 9,589,219 GDRs), and the shares and GDRs purchased in accordance with own share buyback programme (as of December 31, 2012 – 14,386,605 GDRs, 130,093 shares and 2,073,276 preferred shares).

(2) The Company's shares are listed on Kazakhstan Stock Exchange and the GDRs are listed on the London Stock Exchange. One GDR corresponds to one sixth of an ordinary share.

### CONTACT DETAILS

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#### Corporate secretary

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