ҚазМұнайГаз

БАРЛАУ ӨНДІРУ АКЦИОНЕРЛІК ҚОҒАМЫ

ANNUAL REPORT 2010

KAZMUNAIGAS EXPLORATION PRODUCTION JSC

ANNUAL REPORT 2010 *

* Information presented in this annual report is as of March 25, 2011.

CONTENTS

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.

The Company, KazMunaiGas Exploration Production JSC (KMG EP) was established through the merger of Uzenmunaigas JSC (UMG) and Embamunaigas JSC (EMG) in March 2004.

The total volume of 2P reserves at the UMG and EMG fields is 1.7 billion barrels (over 234 million tonnes). Today the Company operates 41 fields excluding acquisitions made from 2007 through 2010. Including the stakes in JV Kazgermunai LLP, CCEL and PetroKazakhstan Inc. the total volume of proved and probable reserves is about 2.2 billion barrels. KMG EP is the second largest oil producer in Kazakhstan.

The Company's shares are listed on the Kazakhstan Stock Exchange (KASE) and its GDRs are listed on the London Stock Exchange (LSE).

KMG EP has many years' experience of oil production in Kazakhstan and expert geological knowledge of the area.

KMG EP has unique comparative advantages over other companies, since it enjoys privileged access to the oil and gas assets and onshore infrastructure in Kazakhstan as a result of relations with its parent company, National Company KazMunayGas (NC KMG).

FINANCIAL AND OPERATIONAL HIGHLIGHTS

		2009	2010	
RESERVES 2P [1]	MMBBL	2,200	2,141	-3%
PRODUCTION [1]	KBOPD	232	270	16%
EXPORT [1]	KBOPD	181	216	20%
REVENUES [2]	BILLION KZT	485	609	25%
NET INCOME [1]	BILLION KZT	210	235	12%
CAPEX [2]	BILLION KZT	43.3	86.7	100%
NET CASH [3]	BILLION KZT	505	576	14%
DIVIDEND PER SHARE	KZT	704	800	14%
DIVIDEND PER GDR [4]	USD	0.78	0.89	14%

[1] Including interest in KGM, CCEL and PKI.

[2] Excluding interest in KGM, CCEL and PKI.

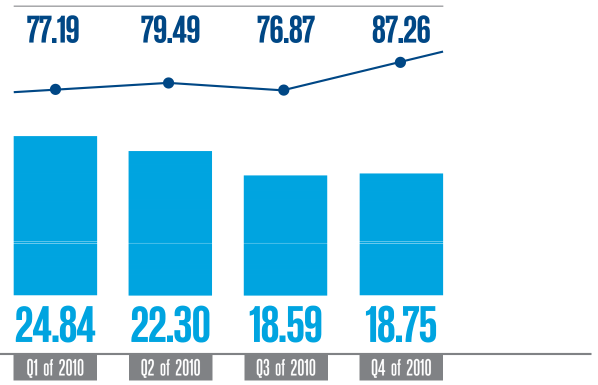
[3] Cash funds, cash equivalents and other financial assets (including NC KMG Bond) less borrowings (including non-recourse debt of KazMunaiGas PKI Finance B.V.).

[4] Translated at the rate of 150.0 KZT/USD for 2010 (a midpoint of the current indicative range established by the National Bank of Kazakhstan).

FINANCIAL AND OPERATIONAL HIGHLIGHTS OF KMG EP

KMG EP SHARE PRICE PERFORMANCE
AVERAGE PRICES

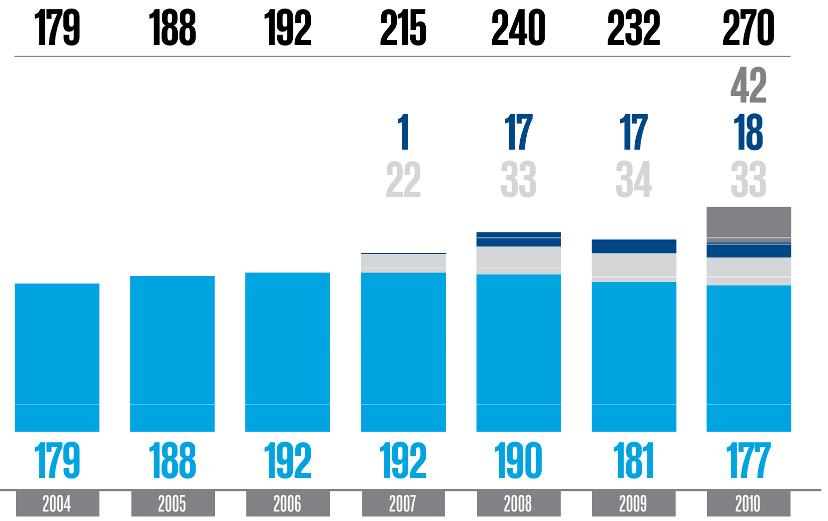
- US$ per 1 GDR
- US$ / 1 bbl of Brent



Source: Bloomberg

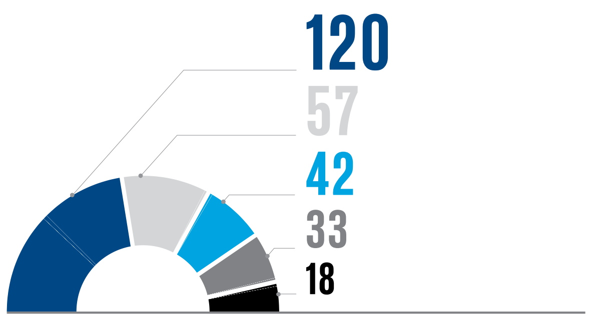
PRODUCTION
KBOPD

- KMG EP
- KGM 50%
- CCEL 50%
- PKI 33%
- Total



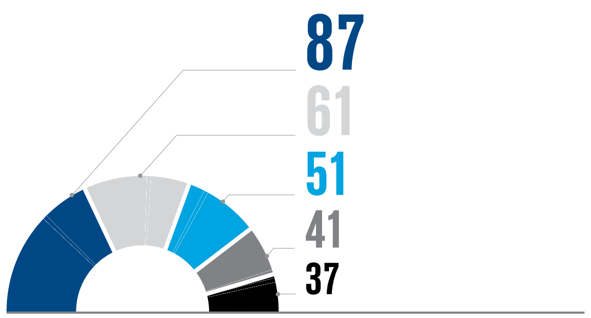
OIL PRODUCTION IN 2010
270 KBOPD

- UMG **120**
- EMG **57**
- PKI 33% **42**
- KGM 50% **33**
- CCEL 50% **18**



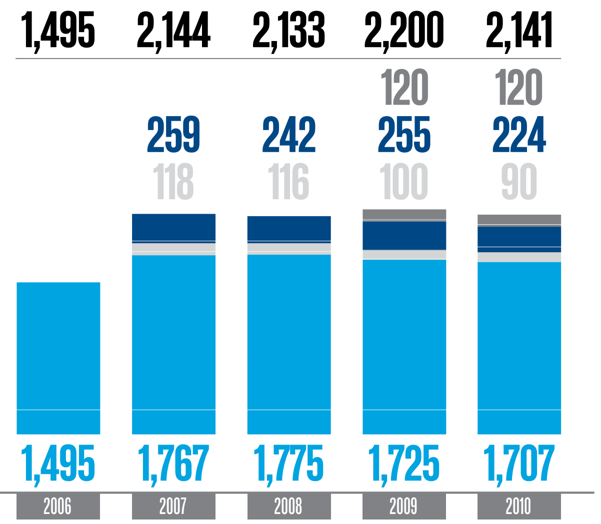
CONSOLIDATED SALES BY ROUTES IN 2010
277 KBOPD

- UAS **87**
- Domestic **61**
- CPC **51**
- Other **41**
- KCP **37**



2P RESERVES GROWTH
MMBBL

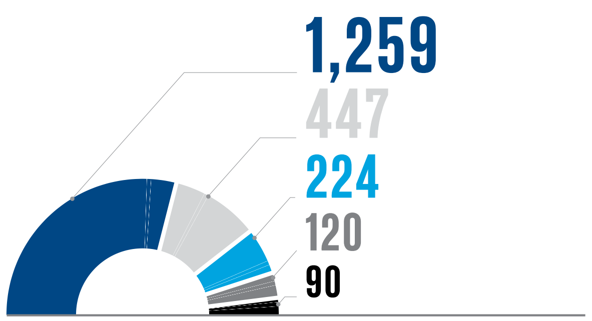
- KMG EP
- KGM 50%
- CCEL 50%
- PKI 33%
- Total



As per assessment reports by Gaffney, Cline & Associates and Miller and Lents

2P RESERVES IN 2010
2,141 MMBBL

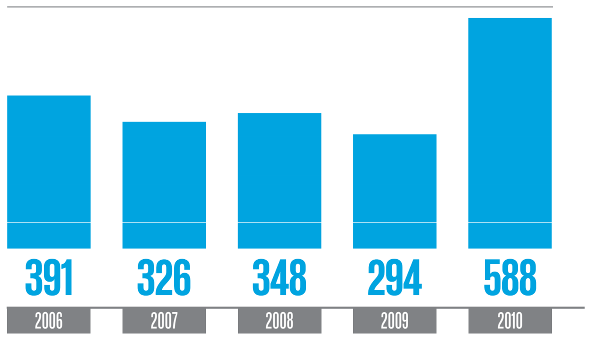
- UMG **1,259**
- EMG **447**
- CCEL 50% **224**
- PKI 33% **120**
- KGM 50% **90**



According to Gaffney, Cline & Associates reports for:
- UMG, EMG, KGM as of 31.12.2010
- PKI as of 31.03.2009

According to Miller and Lents report for:
- CCEL as of 30.11.2010

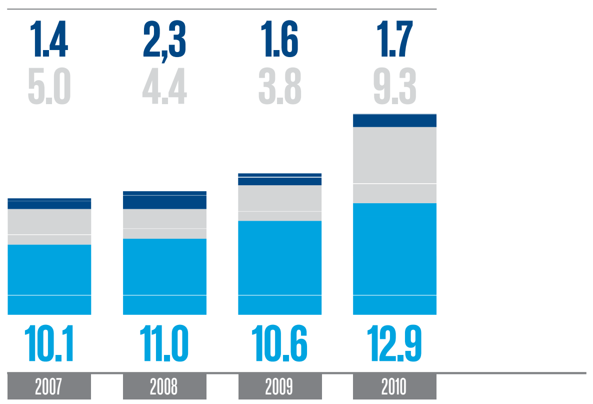
KMG EP (UMG, EMG) CAPEX
USD M



KZT/USD, average:
2006 - 126.09; 2007 - 122.55;
2008 - 120.29; 2009 - 147.50;
2010 - 147.35

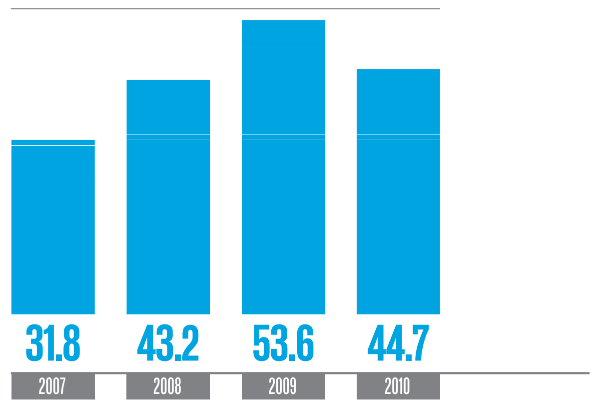
SOCIAL PROJECTS EXPENSES
USD M

- Mangistau region
- Atyrau region
- Other



KZT/USD, average:
2007 - 122.55; 2008 - 120.29;
2009 - 147.50; 2010 - 147.35

ENVIRONMENTAL EXPENSES
USD M



KZT/USD, average:
2007 - 122.55; 2008 - 120.29;
2009 - 147.50; 2010 - 147.35

OWNERSHIP STRUCTURE

REPUBLIC OF KAZAKHSTAN

HOLDING SAMRUK-KAZYNA

MINING
Kazakhmys **11%**

FINANCE SECTOR
BTA **81.48%**
Halyk Bank **26.81%**
Kazkommertsbank **18.3%**
Alliance Bank **67%**

OTHER NATIONAL COMPANIES

NATIONAL COMPANY KAZMUNAYGAS

UPSTREAM
TengizChevroil **20%**
Kashagan **16.81%**
KazMunaiTeniz **100%**
Kazakhoil Aktobe **50%**
Kazakhturkmunai **51%**
Mangistaumunaigas **50%**

TRANSPORTATION
KazTransOil **100%**
KazTransGas **100%**
CPC **19%**
KCP **50%**
KCGP **50%**

REFINING, MARKETING, SERVICES
KMG Refining & Marketing **100%**
Atyrau Refinery **99.5%**
PKOP **50%**
Pavlodar Petrochemical Plant **58%**
KazRosGas **50%**
TenizService **49%**
KING (Research Institute) **90%**
Rompetrol **100%**

KAZMUNAIGAS EXPLORATION PRODUCTION 57.9%

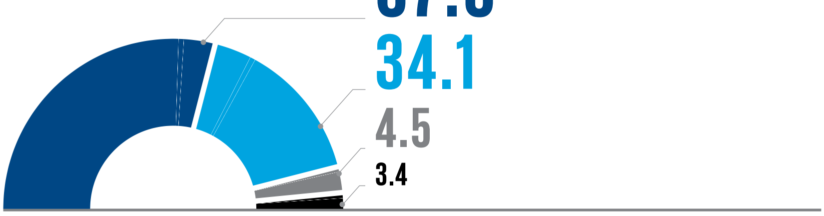
CORE ASSETS
Uzenmunaigas **100%**
Embamunaigas **100%**

ACQUISITIONS SINCE IPO (IN 2006)
Kazgermunai **50%** (2007)
Karazhanbasmunai **50%** (2007)
PetroKazakhstan **33%** (2009)
NBK **100%** (2010)
SBS **100%** (2010)
White Bear **35%** (2010)

FREE FLOAT 34.1% [1]
London (LSE)
Almaty (KASE)

SHARE CAPITAL STRUCTURE [2]
PERCENTAGE

- NC KMG **57.9**
- Free Float **34.1**
- Treasury Shares **4.5**
- Preferred Shares **3.4**



[1] Including 11% owned by CIC according to CIC statement as of September 2009.

[2] Information is based on the shareholder identification conducted in July 2010. Based on total shares issued, including preferred and treasury shares.

KAZAKHSTAN OIL & GAS INDUSTRY

KAZAKHSTAN OIL & GAS INDUSTRY FACTS

Estimated proved oil reserves – **40 bnbbl.**

Oil equivalent production in 2010 was **79.7 mt** (**1.6 mmbopd**) and export of oil equivalent reached **71.4 mt**.

Oil output is projected to reach **100 mtpa** (**2 mmbopd**) by 2015.

Refining in 2010 totalled **13.7 mt**.

There are more than **200** oil and gas fields in Kazakhstan. The largest fields are Kashagan, Tengiz, Karachaganak.

Uzen – Atyrau – Samara (UAS) is one of the three main pipelines which provided transportation of **15.3 mt** or **21%** out of total exported crude oil from Kazakhstan in 2010.

The Caspian Pipeline Consortium's (CPC) current capacity is approximately **30.5 mtpa** (**0.6 mmbopd**) with the expansion plans targeting the capacity of **67 mtpa** (**1.3 mmbopd**) in 2014, of which **50 mtpa** (**1.0 mmbopd**) will be reserved for Kazakhstani oil. In 2010 **28.5 mt** of crude oil was transported through CPC, which is **40%** out of total exported oil from Kazakhstan.

The Kazakhstan-China pipeline's (KCP) current capacity is **10 mtpa** (**200 kbopd**) which can be doubled with the implementation of phase 2 of the project. In 2010 **10.1 mt** of crude oil was transported through the KCP, which is **14%** out of total exported oil from Kazakhstan.

Sea port of Aktau has 3 oil terminals and its total capacity is around **11 mtpa**. Terminals of Aktau port provided transportation of **9.5 mt** or **13%** of total exported crude oil from Kazakhstan.

Oil refining industry of Kazakhstan consists of Atyrau and Shymkent oil refining plants and Pavlodar oil-chemical plant, which in 2010 refined **4.3 mt**, **4.6 mt** and **4.8 mt** of crude oil respectively.

COUNTRY FACTS

POPULATION:
16.4 million (as of 01.01.2011)

AREA:
2.7 million square kilometers

GDP (2010):
21,513 billion Tenge
(US$146.0 bn, 147.35 KZT per US$1)

REAL GDP GROWTH:
7.0% in 2010,
7.8% average in 2002 – 2010

NATIONAL CURRENCY:
Tenge (147.40 KZT per US$1 as at December 31, 2010; 147.35 average for 2010 full year)

CAPITAL CITY:
Astana (moved from Almaty in 1997)

Sources: National Bank of Kazakhstan, Ministry of Oil and Gas, BP Statistical Review of World Energy June 2010.

KAZAKHSTAN OIL & GAS INDUSTRY

1 ABOUT COMPANY

CHAIRMAN'S STATEMENT

ASKAR BALZHANOV

Chairman of the Board of Directors

In 2010 JSC KazMunaiGas Exploration Production once again demonstrated net profit growth, earning about USD$1.6bn for its shareholders. Consolidated production rose by 16% to about 13.3 million tonnes (270kbopd). More than 20% of the oil from the "Ozenmunaigaz" and "EMG" subsidiaries was delivered to the domestic market, with the remainder sold for export. Income from shares in associated companies and jointly controlled entities amounted to more than USD$380m.

These figures testify to the stability of KMG EP and its adherence to the principles and objectives that were stated at the time of the Company's IPO in 2006. Good results in 2010 were largely a result of the very profitable acquisitions that the Company has made in recent years. KMG EP has confirmed its position as Kazakhstan's second largest crude oil producer. In summer of 2010 the Board of Directors approved three additional transactions to acquire large stakes in Mangistaumunaigas, Kazakhoil-Aktobe and Kazakhturkmunai. Now KMG EP is awaiting Government approval for the acquisitions.

In addition, the Board of Directors approved the Company's participation in several projects outside Kazakhstan. In 2010 it signed an agreement on the White Bear project (North Sea), together with BG, and also won a tender to develop the Akkas field (Iraq) together with KOGAS. Participation in the White Bear project will allow the Company to obtain invaluable off-shore experience in cooperation with a large multinational company. The Akkas project is of great interest as it will be the first time that KMG EP has been involved in the development of commercial gas production. In both cases what is particularly appealing is the controllability of risks and, if successful, the profitability of the projects.

In 2010 the reserves replacement ratio at Uzen and Emba was, at 73%, significantly better than in 2009 but still not entirely satisfactory. The current reserves replacement ratio is a consequence of the depletion of deposits. Thanks to the acquisition of new assets this depletion rate has been mitigated, but KMG EP intends to make additional efforts, especially in the field of exploration, to ensure a higher level of reserves replacement at its core assets. This is reflected in the budget of the Company and the Board of Directors approval of a 21% increase in capital expenditure in 2011 to USD$709m. In addition, the Company is expanding its portfolio of exploration assets. In particular, it is working on the transfer of four exploration blocks - Temir, Teresken, Uzen-Karamandybas, Karaton-Sarykamys – from NC KMG to KMG EP.

Now let me say a few words about our plans for the future. I would like to pay special attention to the new development strategy of KMG EP up to 2020, which was approved by the Board of Directors in December 2010. Members of the Board of Directors, as representatives of the shareholders, set an ambitious goal for the management of KMG EP - to become one of the world's top 30 oil and gas companies. The main goal of KMG EP is to increase the Company's shareholder value. KMG EP seeks to achieve value growth through growing its reserves and its production of hydrocarbons, increasing the profitability of existing assets, and by continuing to develop the business in new directions.

Efficiency should become one of the priorities of KMG EP. The first steps have already been made - the Board of Directors has approved the Cost Control Programme and key performance indicators will be taken into account in the balanced scorecard system that will provide better motivation for employees. However, this is only the beginning of an extensive and focused plan which the management will be following over the coming years.

KMG EP plays an important role in the development of the stock market in Kazakhstan. Today, trading in the securities of the Company accounts for a significant share of transactions on the Kazakhstan Stock Exchange. The preferred share buyback programme that started in 2010 has been a success. In addition, the Company also represents the oil and gas sector of Kazakhstan on the London Stock Exchange - a great responsibility that is well understood by all members of the Board of Directors.

The efficient work of the entire Board of Directors and of its Committees was recognized by Standard&Poor's, who confirmed the GAMMA-6 corporate governance rating of the Company in November 2010. The S&P report acknowledged the improvement in our work and governance and we have tackled the small number of points raised by S&P which should help our rating in future.

I am sure that our current team of employees, whose experience and professionalism are beyond any doubt, will be able to meet the challenges before them and will continue our proven track record of working for the interests of all stakeholders. The Board of Directors will continue to ensure that all decisions are taken in the interests of all shareholders.

Askar Balzhanov
Chairman of the Board of Directors

CHIEF EXECUTIVE'S STATEMENT

KENZHEBEK IBRASHEV

Chief Executive Officer
(Chairman of the Management Board)

2010 was an important year for KMG EP, the Company achieved a number of goals that it has been systematically pursuing over the last few years. This period of success is a good time to analyze our core strengths and the opportunities to improve our business; in order to find better solutions for future challenges. This is why, in 2010 we started to review some of our approaches, to make plans for the reorganization of our structure and to continue to look for new sources of steady business growth.

Relying on the support of National Company KazMunaiGas, we have continued to acquire new assets throughout Kazakhstan. We entered transactions for the acquisition of large stakes in Mangistaumunaigas, Kazakhoil Aktobe and Kazakhturkmunai. Completion of these transactions is awaiting approval from the relevant state agencies of the Republic of Kazakhstan.

I would especially like to note the independent acquisition of NBK's and SBS' assets. We are constantly looking out for promising companies in Kazakhstan and these two assets are especially attractive in terms of exploration.

The past year was marked by a great exploration success when the Company made its first significant onshore oil discovery at the Liman Block in West Kazakhstan. The Company has entered into negotiations for exploration rights at a number of other blocks and the search for new and promising oil-bearing structures has become one of our key priorities.

We believe that we should not limit our business activities to operations in Kazakhstan alone. While taking any opportunity for profitable investment in Kazakhstan, we are also looking for relevant international projects.

The Company participated in the consortium which was the successful bidder for the Akkas gas field development in Iraq and we will participate in this project on profitable terms. Another benefit from this field is that the Company's employees will also gain new experience in the area of gas field development. Clearly we have dealt with gas before, as many of the Company's fields have associated gas, and we also operate our own gas processing plant in Kazakhstan, located on the Mangyshlak peninsula. However, our specialists have not been fully engaged in gas production in the past. They will now get detailed, practical experience working in one of the largest oil and gas regions in the world together with one of the largest international gas companies – Korean KOGAS. This experience will serve the Company well in the future.

It is even more important for us to participate in the White Bear Project in the North Sea, where we are partners with BG Group. Marine exploration and, we hope in the future, production are areas of growing importance for us. This again will provide invaluable experience for our specialists, especially in view of our desire to work in the Kazakh sector of the Caspian Sea.

The White Bear Project is being implemented under the broad agreement on cooperation signed between NC KazMunaiGas, KMG EP and BG in 2008. This strategic partnership with such a large and reputable company as BG, opens up many prospects for our Company.

All the priorities for the development of our Company have been reflected in the new Strategy which was approved at the end of 2010. The Company has evolved over the years. First of all, the structure of production assets has changed. If in 2006 KMG EP was just an operating company that worked on the production facilities of the Uzenmunaigas and Embamunaigas fields, today, KMG EP is an operating and holding company with production assets comprising JV Kazgermunai LLP, Karazhanbasmunai JSC, PetroKazakhstan Inc and NBK LLP. In addition, KMG EP is awaiting Government approval for the acquisition of interests in Mangistaumunaigas, Kazakhoil Aktobe and Kazakhturkmunai. The production volume from new assets should reach about 47% of the total consolidated production of the Company, post acquisitions.

The global financial crisis also made us think more about the efficient use of our current assets. In 2011 the Company will focus on containing and reducing costs.

We have set ourselves a very ambitious but achievable target - to become one of the world's top 30 oil and gas companies within ten years. By 2020 the Company intends to achieve the same level of net production per barrel of hydrocarbon material as the top 30 oil and gas companies. This is a hard task, but we have already taken the first steps towards it.

The revised Strategy keeps some of the priority commitments which have brought KMG EP its current success. We will continue searching for, and acquiring, promising new assets, both in Kazakhstan and abroad. Special attention will be paid to exploration, both in the licensed territories which are already in the Company's possession and at new sites located outside Kazakhstan.

Discussion of the new Collective Agreement for the next three years took the best part of 2010. The document provides significant social guarantees for KMG EP employees. We have approached this issue with keen attention to detail. Many meetings with trade union leaders and discussions with employees took place and the new Collective Agreement takes into account workers' needs while keeping expenditure on social projects within acceptable limits.

The Company expects 2011 to become a year of further change. We will start implementing our new Strategy, cost management and efficiency improvement programmes and the overall business management model will be revitalized. We also intend to adjust our HR-policy and increase our influence in the projects in which we have a stake.

The Company looks to the future with confidence. We believe that in the near future we will be able to take great strides in the company's development and to bring the Company to a new level to the benefit of all our shareholders.

Kenzhebek Ibrashev
Chief Executive Officer
(Chairman of the Management Board)

BOARD OF DIRECTORS

THE COMPANY OPERATES WITH A BOARD OF DIRECTORS AND A SEPARATE MANAGEMENT BOARD (THE EXECUTIVE BODY).

THE CHIEF EXECUTIVE OFFICER, WHO HEADS THE MANAGEMENT BOARD, IS ALSO A DIRECTOR OF THE COMPANY, AND IS THE ONLY REPRESENTATIVE OF THE MANAGEMENT BOARD ON THE BOARD OF DIRECTORS.

THE OTHER FOUR MEMBERS OF THE BOARD, INCLUDING THE CHAIRMAN, ASKAR BALZHANOV, ARE REPRESENTATIVES OF NC KMG.

THE BOARD OF DIRECTORS ALSO INCLUDES THREE INDEPENDENT NON-EXECUTIVE DIRECTORS.

ASKAR BALZHANOV

Managing Director on Exploration and Production of NC KMG

He was the CEO of KMG EP from 2006 to 2009. Prior to this, he was CEO of JSC KazMunayTeniz, a subsidiary of NC KMG specialising in offshore oil and gas operations. After graduating from the Moscow Oil and Gas Institute, he gained broad experience in the oil and gas field working in various positions in a range of hydrocarbon enterprises, including Embaneft PB, KazakhstanNefteGas SE, KazakhstanMunaiGas SE, KazRosGas, and NC KMG.

TOLEGEN BOZZHANOV

Managing Director for Corporate Center of NC KMG

He was elected to the Board of Directors of KMG EP on 24 September 2008. He graduated from Kazakh State University and Kazakh State Construction Academy and holds a Bachelor's degree from Warwick University. He has occupied senior executive positions with Kazkommerts Securities, Kar-Tel and NC KMG. Prior to his latest appointment, he was CEO of Trade House KazMunaiGas.

YERZHAN ZHANGAULOV

General Manager on Legal Support of NC KMG

He was elected to the KMG EP Board of Directors on 12 June 2006. Previously, he headed the Legal Service and HR Department in the Administration of the President of the Republic of Kazakhstan and was an adviser to a Vice President of NC KMG. He obtained a law degree from Karaganda State University.

KENZHEBEK IBRASHEV

Chief Executive Officer of KMG EP

Was appointed as the CEO of KMG EP on 1 June 2009. Prior to this appointment he was the Vice President of Exploration and Production at NC KMG. Mr Ibrashev has been a member of the Board of Directors of KMG EP since 2007. He graduated from the Moscow Oil and Gas Institute and gained broad experience working in several senior positions in the oil and gas industry. He was a Director for business development in Kazakhstan at Agip Kazakhstan North Caspian Operating NV, First Deputy CEO, and CEO of KazMunaiTeniz. In 2010, he was honoured with the Parasat Medal of the Republic of Kazakhstan.

ASSIYA SYRGABEKOVA

Managing Director for Economics and Finance of NC KMG

Has been working as Managing Director for Economics and Finance of NC KMG since July 2006. She was elected to the KMG EP Board of Director on 26 March 2010. Prior to that appointment, from 2003 she was the First Deputy Chairman of the National Bank, and from 2004 to 2005 she was the Chairperson of the Management Board of the National Bank of Kazakhstan. Between 1998 and 2003 she worked for the National Oil and Gas Company, taking various senior positions with Kazakhoil and KazTransGas. In 1982, she graduated from the Faculty of Economics of the Kazakh State University.

PHILIP DAYER

Independent Director of KMG EP

LLB FCA qualified as a chartered accountant with KPMG and then pursued a career in investment banking for 25 years, specialising in advising UK listed companies. He gained extensive experience working for companies such as Barclays de Zoete Wedd and Citicorp. He retired from ABN AMRO Hoare Govett in 2005. Since then he acted as an adviser to Rosneft on their successful flotation in 2006 and currently sits on a number of boards as an independent director. Philip joined KMG EP Board of Directors in May, 2010.

PAUL MANDUCA

Independent Director of KMG EP

Has extensive asset and investment management experience having worked as CEO for companies such as Threadneedle Asset Management, Rothschild Asset Management and Deutsche Asset Management in UK and Europe since 1973. Mr Manduca serves on a number of boards as an independent director including the Prudential Group plc where he is the senior independent director. He has also headed audit, remuneration and nomination committees of such boards. He holds a Master's degree from the University of Oxford (Modern Languages). He was elected as a director of the Company on 28 August 2006. Mr. Manduca is Chairman of the Audit Committee and a member of the Remuneration Committee.

EDWARD WALSHE

Independent Director of KMG EP

Has over 35 years experience in the oil and gas sector. Mr Walshe worked in various roles at British Petroleum and British Gas including the overseas exploration and productions operations of these companies in Nigeria, Abu-Dhabi, Central Asia and South-East Asia. Mr Walshe has a PhD in Solid State Chemistry from the University of Dublin. He was elected as a Director of the Company on 28 August 2006. Edward is the Chairman of the Strategy planning committee and a member of the Audit, Remuneration and Nominations Committees.


INVESTMENT IN KGM
FULLY REPAID

2010 MILESTONES

KMG EP IS AMONG THE TOP THREE OIL PRODUCERS IN KAZAKHSTAN

Q1

- In Q1 of 2010 KMG EP produced 3,183 thousand tonnes of crude oil (262 kbopd), including production from the Company's share in Kazgermunai, CCEL and PetroKazakhstan Inc. (PKI). This is 440 thousand tonnes or 16% more than the corresponding period of 2009. This increase in production is mainly attributed to the inclusion of PKI production (487 thousand tonnes) [in the total production volume].

- According to the unaudited interim consolidated financial statements, operating profit for Q1 of 2010 amounted to KZT 54.6 billion (USD 370 million), 174% more than reported for Q1 of 2009. Net earnings amounted to KZT 51.7 billion (USD 350 million). Earnings per share amounted to KZT 708 (USD 0.8 per GDR).

- In accordance with the decision of the Board of Directors, the preferred shares of KMG EP have been listed on the Kazakhstan Stock Exchange (KASE) and the share buyback programme has begun.

- The new Board of Directors of KMG EP was elected at the Extraordinary General Meeting of Shareholders. Askar Balzhanov was elected Chairman of the Board of Directors.

- The transition to the new wage payment system resulted in industrial action in UMG. This was discontinued after a constructive agreement between KMG EP and the participants of the industrial action was negotiated.

Q2

- The Board of Directors approved a decision to adjust the annual oil production targets for the main assets of the Company (UMG and EMG) from 9,200 thousand tonnes to 9,082 thousand tonnes. In addition, the Board of Directors decided to reduce the 2010 Capex budget from KZT 95 billion (USD 633 million) to KZT 83 billion (USD 555 million).

- As decided by shareholders, the 2009 dividends per share (ordinary and preferred) amounted to KZT 704 (including taxes withheld in accordance with the applicable laws of the Republic of Kazakhstan). The total amount of dividends for 2009 was KZT 50.9 billion (about USD 346 million). Dividends paid during 2010 amounted to KZT 48 billion (USD 327 million).

- Philip Dayer was elected Independent Non-Executive Director at the General Meeting of Shareholders.

- After negotiation with trade unions from 1 June 2010 salaries of production staff at the branches' subsidiaries were raised.

- In the first 6 months of 2010, KMG EP produced 6,283 thousand tonnes of crude oil (257 kbopd) including the Company's share of production in JV Kazgermunai LLP, CCEL and PetroKazakhstan Inc.. This is 610 thousand tonnes or 11% more than the same period of 2009. The increase is mainly attributed to the incorporation of PKI production (733 thousand tonnes) in the total production volume.

- Operating profit for the first six months of 2010 amounted to KZT 103.5 billion (USD $703 million), 81% more than the KZT 57.0 billion (USD$394 million) received for the corresponding period of 2009. This was mainly due to higher oil prices. Net earnings for the period amounted to KZT 100billion (USD$679 million) and earnings per share amounted to KZT 1,370 (USD$1.6 per GDR), as compared with KZT 128.8 billion (USD $890 million) and KZT 1,752 (USD$2.0 per share), respectively, for the same period of the previous year.

Q3

- Under an agreement with NC KMG, KMG EP announced the acquisition of a 50% interest in Kazakhoil Aktobe LLP, a 51% stake in Kazakhturkmunai LLP and a 50% stake in Mangistau Investments B.V., the owner of 100% share capital of Mangistaumunaigas JSC. These acquisitions are awaiting Government approval.

- KMG EP purchased bonds issued by NC KMG to the amount of KZT 220 billion (USD $1.5 billion) at a coupon rate of 7% p.a., due in three years.

- KMG EP and BG Group announced the signing of an agreement to farm-in to a BG Group operated license in the British sector of the North Sea for joint production within the White Bear prospect. KMG EP received a 35% interest in the license.

- KMG EP completed its transactions with Eastern Gate Management Ltd. to acquire a 100% interest in NBK LLP and with Halyk Komir to acquire a 100% interest in SapaBarlau Services LLP.

- An export customs duty at a rate of USD 20 per 1 tonne of crude oil was introduced under a Resolution of the Government of the Republic of Kazakhstan.

- In the first 9 months of 2010 KMG EP produced 9,946 thousand tonnes of crude oil (270 kbopd) including the Company's stakes in JV Kazgermunai LLP, CCEL and PetroKazakhstan Inc., which is 1,302 thousand tonnes or 15% more than reported in the corresponding period of 2009.

- Operating profit for the first 9 months of 2010 amounted to KZT 141.9 billion (USD 963 million), 32% more than the KZT 107.2 billion (USD 730 million) received for the corresponding period of 2009, mostly due to higher oil prices. Net earnings for the period amounted to KZT 156.8 billion (USD 1,064 million) and earnings per share were KZT 2,155 (USD 2.44 per GDR), demonstrating a 13% decline as compared with KZT 180.6 billion (USD 1,231 million) and KZT 2,467 (USD 2.8 per GDR), respectively, received for the same period of the previous year.

- PetroKazakhstan Inc. (PKI) and Lukoil Overseas Kumkol B.V. (Lukoil) entered into the Amicable Agreement on the dispute regarding the title of JSC, Turgai Petroleum (TP). According to the Agreement the ownership structure of TP remains unchanged: PKI and Lukoil will continue to own TP in equal shares. In addition, PKI agreed to pay to Lukoil the settlement amount of approximately USD 438 million as compensation. In addition to the aforementioned Agreement, CNPC Exploration and Development Company Limited and KMG EP signed an agreement on the principles in accordance with which the compensation payment to Lukoil would be financed by PKI. KMG EP will not be liable for any damage or liability in relation to the payment of such compensation or any liability associated therewith.

Q4

- Based on the tender results, KMG EP in partnership with Korea Gas Corporation (KOGAS) was awarded the rights to develop the Akkas gas field in the Republic of Iraq.

- An oil discovery was announced at the Liman exploration block. The accumulation is located on the southern slope of the Novobogat salt dome which is in close proximity to the fields operated by Embamunaigas.

- KMG EP was recognized as Company of the Year with the Altyn Zhurek National Award for the implementation of social projects in Kazakhstan.

- KMG EP was ranked 47th out of 91 exploration and production companies in EMEA (Europe, Middle East and Africa) and achieved a ranking of 101 on overall global performance according to the Platts Top 250 Global Energy Companies Rankings.

- The international rating agency Standard&Poor's (S&P) confirmed the GAMMA-6 corporate governance rating of KMG EP.

- KMG EP was awarded the Most Active Player on the M&A Market in the Expert-100-Kazakhstan rating.

- The Board of Directors approved the 2011 budget for KMG EP based on the annual average Brent oil price of USD 65 per barrel in accordance with the official forecasts of the Government of the Republic of Kazakhstan and NC KMG. The Company's capital expenditure for 2011 is expected to be KZT 99.1 billion (USD 661 million). The increase in capital expenditure as compared to 2010 is due to an increase in production drilling from 213 wells to 239 wells and an increase in the exploration budget from KZT 4 billion (USD 27 million) to KZT 8 billion (USD 55 million).

- The Board of Directors approved the KMG EP Development Strategy for 2010-2020. In accordance with the Strategy the Company will focus on the improvement of production efficiency, exploration, participation in offshore Caspian projects, and expansion of the Company's production base in Kazakhstan and its new acquisitions outside the country.

- The international rating agency Standard & Poor's confirmed KMG EP's long-term credit rating at BB+ and gave a "Stable" forecast.

- In 2010 KMG EP produced 13,285 thousand tonnes of crude oil (270 kbopd) including the Company's stakes in JV Kazgermunai LLP, CCEL and PetroKazakhstan Inc., which is 1,788 thousand tonnes or 16% more than reported in 2009. The increase in production is mostly attributed to the acquisition of a 33% interest in PetroKazakhstan Inc. in December 2009. The 2010 production targets were exceeded by all production branches and associated companies, except for UMG.

- Net earnings for 2010 amounted to KZT 235 billion (USD 1,591 million) and earnings per share amounted to KZT 3,232 (USD 3.66 per GDR). Operating profit amounted to KZT 187 billion (USD 1,267 million).

EVALUATION OF KMG EP EFFORTS BY INDEPENDENT EXPERTS

In 2010, the success of KMG EP has been widely noted, not just in Kazakhstan, but also by foreign experts.

KMG EP was ranked 47th out of 91 exploration and production companies in EMEA (Europe, Middle East and Africa) and achieved a ranking of 101 in overall global performance according to the Platts Top 250 Global Energy Companies Rankings.

The Platts Top 250 Global Energy Companies Rankings measures financial performance of public companies by examining each company's assets, revenues, profits and return on invested capital. To be ranked, companies must have assets greater than USD 3 billion.

In November 2010, the international rating agency Standard&Poor's (S&P) confirmed the GAMMA-6 corporate governance rating of KMG EP.

Besides the strength of KMG EP's corporate governance, S&P noted in its report the effective work of independent non-executive directors in balancing the interests of the main shareholder and minority shareholders, as well as thorough monitoring of the Company's management work.

S&P noted that, although there is a significant influence of the Government of the Republic of Kazakhstan and Samruk-Kazyna through KMG EP major shareholder,

NC KMG, the relationship between KMG EP and NC KMG is legally secured and transparent. The obligation of the parent company to use its preemptive right to acquire assets and licenses in the interests of KMG EP has been fulfilled in full during the recent years.

S&P evaluates the level of transparency of KMG EP as high. The Company interacts effectively with its investors and regularly updates its three-language website. The financial statements prepared in accordance with the International Financial Reporting Standards (IFRS) are published quarterly and within reasonable time. The general level of transparency and efficiency of the auditing process is also evaluated as high. The Company's risk management procedures are being successfully and efficiently implemented. The shareholders are empowered with a wide range of rights, the procedures for the preparation and holding of shareholders' meetings are generally evaluated as efficient.

In terms of managing cash funds, S&P regarded a bond deal of USD 1.5 billion with NC KMG as positive, as the credit rating on liabilities in foreign currency of NC KMG was BB + / Stable/-- (at the moment of issue of a KMG EP GAMMA Corporate Governance Report). This was at least three notches above the ratings of domestic banks in which KMG EP was holding deposits. In December 2010 S&P confirmed KMG EP's long-term credit rating at BB+ Stable/--.

In addition, in 2010 the Company was awarded the Most Active Player on the M&A Market in the Expert-100-Kazakhstan rating. KMG EP received that award for implementing its acquisition strategy.

Expert-100-Kazakhstan Project is implemented by the Expert RA Kazakhstan Rating Agency and the Expert of Kazakhstan magazine with the support of the Government of the Republic of Kazakhstan. The purpose of the Project is to identify leaders of the Kazakh national economy, promote the best practices, analyze the main economic development trends of the Republic, develop proposals to improve economic policy.

KMG EP also won awards for the implementation of social projects. In October 2010 KMG EP became a winner of the Altyn Zhurek National Award as Company of the Year for its charity, sponsorship and large-scale social support in the regions where it operates.

The Altyn Zhurek is the annual public national award which expresses great public appreciation of the contribution made by citizens, organizations, enterprises and institutions whose socially important charitable activities have a positive influence on community development.

Financial analysts reacted positively to the decision of KMG EP to list its preferred shares as "such securities efficiently attract the interest of the population to the national stock market". Experts noted that from March 2010 through to the end of the year nearly all trading volume on KASE was due to the interest of investors in KMG EP's preferred shares.

S&P analysts consider that the listing of the preferred shares and the commencement of the buyback programme have significantly improved the position of KMG EP's preferred shareholders.

Throughout the year a number of equity analysts evaluated KMG EP's shares as one of the most attractive instruments for long-term investment in the sector.

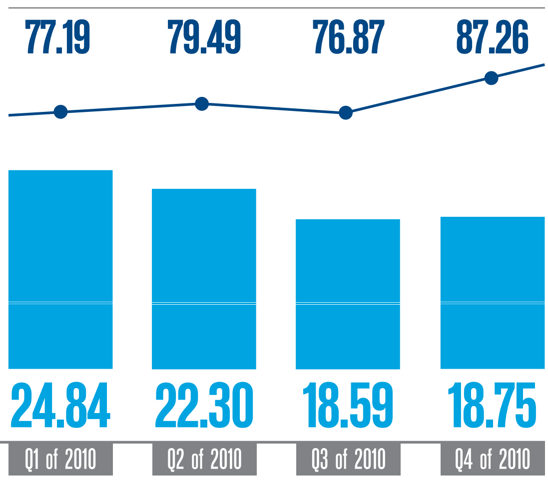
Experts noticed positive trends in key performance indicators of the Company which build a basis for future share performance. Like other petroleum companies, KMG EP operates under significant risk conditions. The risks are partially associated with the specifics of the industry, and to some extent reflect the peculiarities associated with investment in developing markets. However analysts believe that KMG EP's current achievements, business opportunities, and corporate governance system constitute a synergy which creates the potential for generating considerable shareholder value.

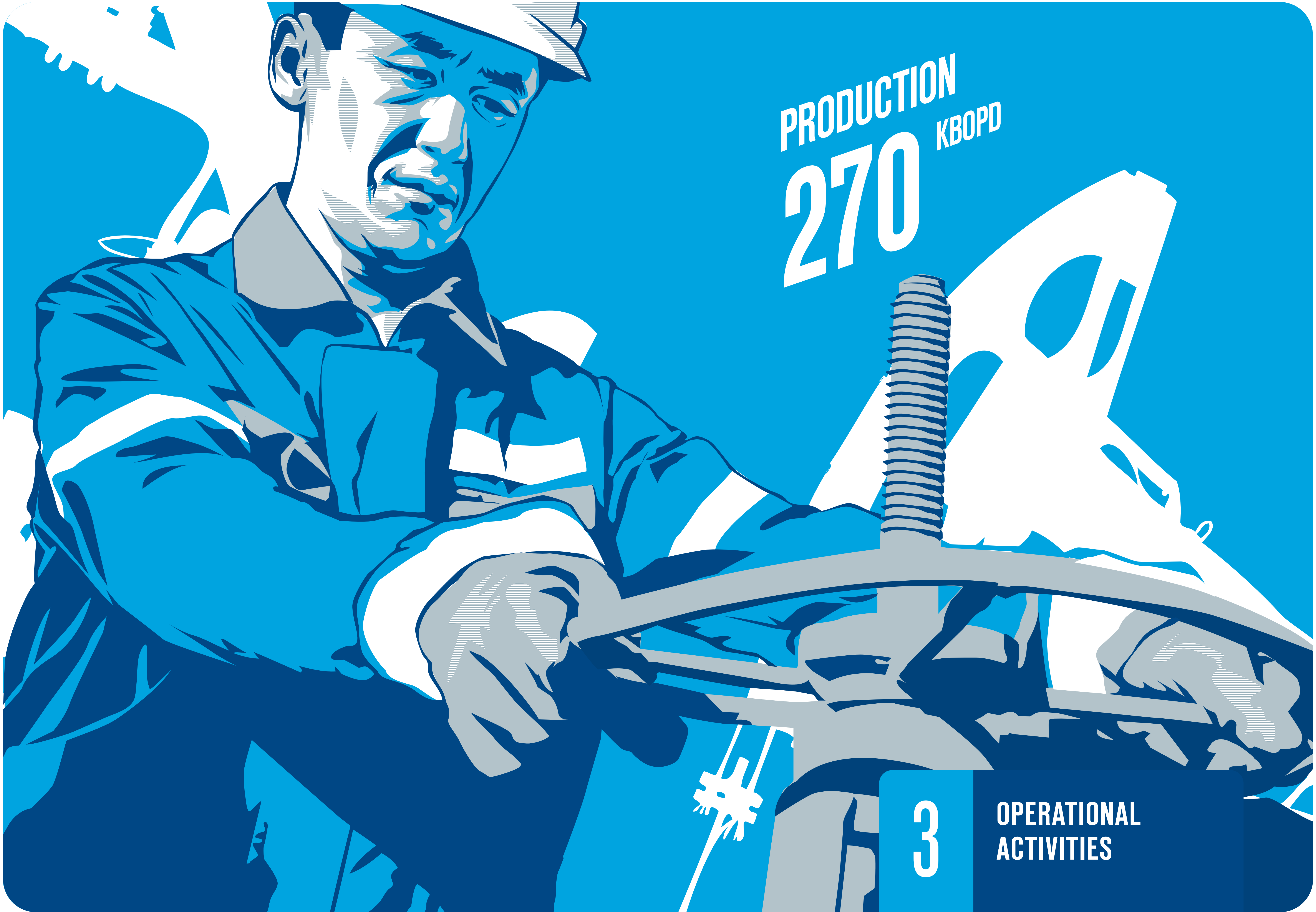
KMG EP SHARE PRICE PERFORMANCE

AVERAGE PRICES

- US$ per 1 GDR
- US$ / 1 bbl of Brent

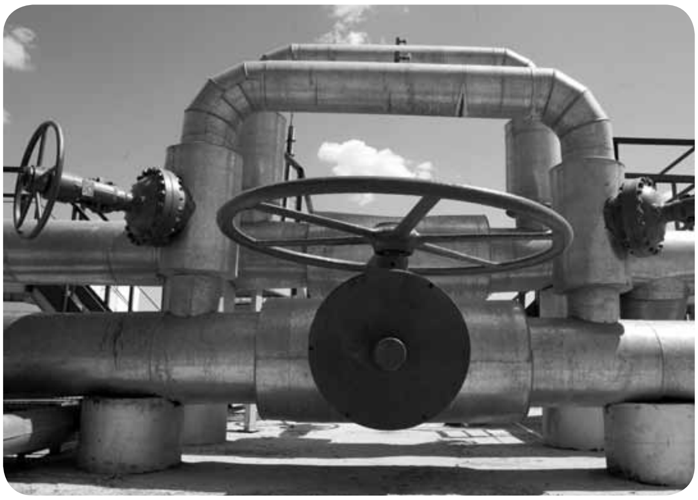
Source: Bloomberg





3 OPERATIONAL ACTIVITIES

OPERATIONAL ACTIVITIES



CRUDE OIL PRODUCTION AND SALES

In the full year of 2010 KMG EP produced 13,285 thousand tonnes (270 kbopd), including the Company's stakes in JV Kazgermunai LLP, CCEL (JSC "Karazhanbasmunai") and JSC "PetroKazakhstan Inc.". This is 1,788 thousand tonnes or 16% more than in 2009. The increase in production mainly results from the acquisition of a 33% stake in PetroKazakhstan Inc. in December 2009. Production plans for 2010 were exceeded by all associated companies and production facilities except Uzenmunaigas.

In 2010 the Company produced 8,766 thousand tonnes (177kbopd) of oil at the Uzenmunaigas and Embamunaigas production facilities. This is 196 thousand tonnes, or 2% less than the 8,962 thousand tonnes (181kbopd) produced in 2009. Embamunaigas outperformed the production plan by 1%, while Uzenmunaigas produced 1% less than the target.

The decline in Uzenmunaigas production was mainly caused by the failure to perform well service operations and timely oilfield equipment repairs during a strike by Uzenmunaigas workers from 4 March 2010 through 18 March 2010. From June to September 2010 there were also a number of emergency power cuts in the fields, caused by severe weather conditions.

In 2010 the Company's share in production volumes from KGM, CCEL and PKI amounted to 4,519 thousand tonnes (93kbopd).

Planned production from the Company's core assets (Embamunaigas and Uzenmunaigas) is expected to be 9,100 thousand tonnes (183kbpod) in 2011, an increase from the 2010 target of 8,781 thousand tonnes (177kbopd). From this amount 1,900 thousand tonnes will be supplied to the domestic market for processing at Atyrau oil refinery.

UMG AND EMG DATA AS AT THE END OF 2010

	UMG	EMG	TOTAL
Fields	2	39	41
Production wells	3,632	2,252	5,884
Injection wells	1,180	443	1,617
2P oil reserves, million barrels	1,259	447	1,707
Oil production in 2010, kbopd	119	57	177
Reserve-to-production ratio, years	29	22	26

In 2010 the Company supplied 8,643 thousand tonnes of crude oil (174kbopd), excluding the share in supply from KGM, CCEL and PKI. Of this amount, 6,860 thousand tonnes (138kbopd) were exported. The CPC pipeline was a more profitable route in 2010.

In 2010 the Company's share in the sales volumes from KGM, CCEL and PKI was 5,004 thousand tonnes of crude oil (103kbopd), including 3,801 thousand tonnes (78kbopd) supplied to export markets.

KEY FIGURES OF KGM (100%) [1]

	2009	2010
Crude oil production, kbopd	3,202	3,102
Revenue, KZT million	178,167	226,277
Average realized price, KZT/tonne	56,695	72,757
Capital expenditures, KZT million	20,273	12,110
Number of employees	590	681

KEY FIGURES OF CCEL (100%) [2]

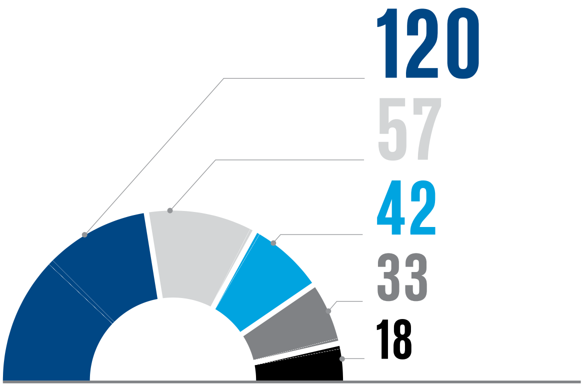
	2009	2010
Crude oil production, kbopd	1,867	1,941
Revenue, KZT million	102,285	136,813
Average realized price, KZT/tonne	54,492	71,160
Capital expenditures, KZT million	17,421	15,821
Number of employees	2,166	2,231

KEY FIGURES OF PETROKAZAKHSTAN INC. (100%) [3]

	2009	2010
Crude oil production, kbopd	6,280	6,053
Revenue, KZT million	426,243	504,260
Average realized price, KZT/tonne	60,139	77,746
Capital expenditures, KZT million	49,102	60,499
Number of employees[4]	3,088	3,105

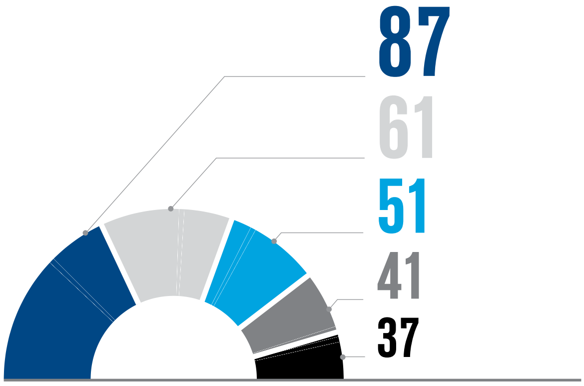
OIL PRODUCTION IN 2010
270 KBOPD

- UMG **120**
- EMG **57**
- PKI 33% **42**
- KGM 50% **33**
- CCEL 50% **18**



CONSOLIDATED SALES BY ROUTES IN 2010
277 KBOPD

- UAS **87**
- Domestic **61**
- CPC **51**
- Other **41**
- KCP **37**



OIL RESERVES

According to the report by Gaffney, Cline & Associates (GCA) as of 31 December 2010 the total Proved and Probable (2P) reserves of KMG EP (excluding its shares in JV Kazgermunai, CCEL and PetroKazakhstan Inc.) were 232 million tonnes (1,707kbopd).

The reserve replacement ratio was 73% which implies that 6.4 million tonnes (47 million barrels) were added to reserves against production of nearly 8.8 million tonnes (65 million barrels). The reserves-to-production ratio at the end of 2010 was 26 years.

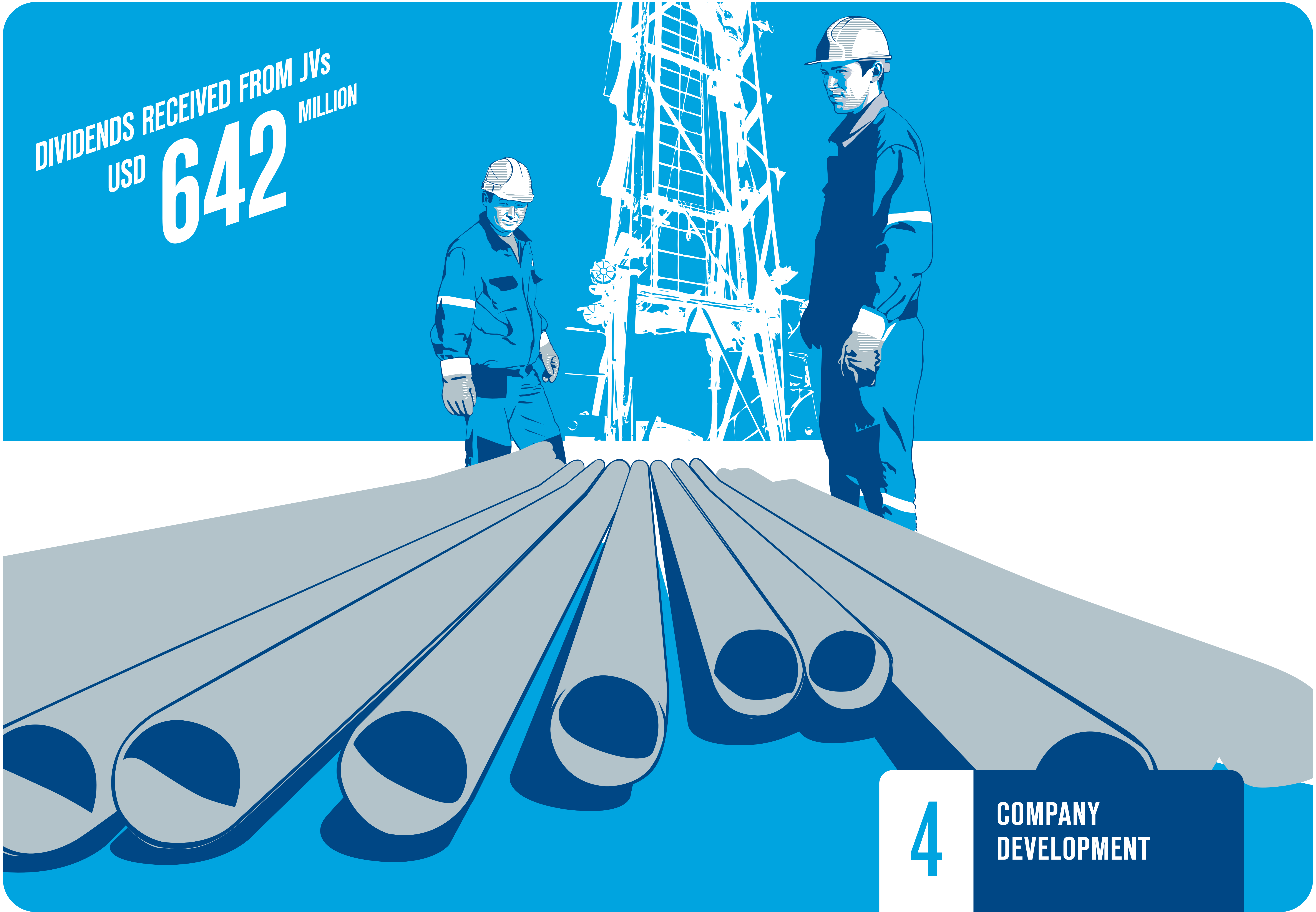
Proved oil reserves (1P) are 88 million tonnes (646 million barrels). Proved, probable and possible reserves (3P) stand at 270 million tonnes (1,989 million barrels).

[1] As at 31 January 2011.

[2] As at 7 February 2011. The data for JSC Karazhanbasmunai were taken from the financial statements net of ATS LLP and TMS LLP.

[3] As at 15 January 2011.

[4] The number of employees for PetroKazakhstan Inc. comprises personnel of JSC PetroKazakhstan Kumkol Resources, JSC Turgai Petroleum and JV Kazgermunai LLP based on the KPI report.



4 COMPANY DEVELOPMENT

COMPANY DEVELOPMENT

As the timeframe covered by the Development Strategy adopted in 2006 has elapsed, and in the light of new factors that influence the Company's priorities, on 13 December 2010 the Board of Directors approved KMG EP's Development Strategy for 2010-2020.

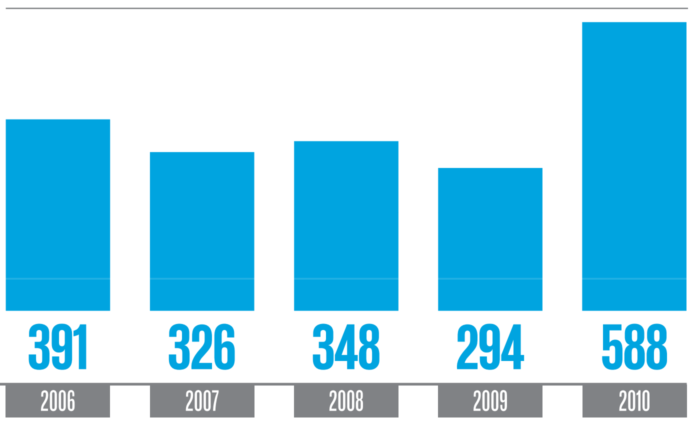
KMG EP has identified several priorities in the implementation of its revised Strategy. The provision of safe working conditions for employees, the rational utilization of natural resources in accordance with world class environmental protection and safety standards are the unconditional top priorities of KMG EP.

Exploration, as one of the key priorities for the long-term development of the Company, is a foreground activity aimed at achieving the growth targets for KMG EP's resource base.

The main purpose of KMG EP is to increase the Company's shareholder value. KMG EP intends to achieve this through the increase of its reserve base and the production of hydrocarbons, the more efficient utilization of its assets and the development of new business opportunities.

KMG EP (UMG, EMG)
CAPEX
USD M

KZT/USD, average:
2006 - 126.09; 2007 - 122.55;
2008 - 120.29; 2009 - 147.50;
2010 - 147.35

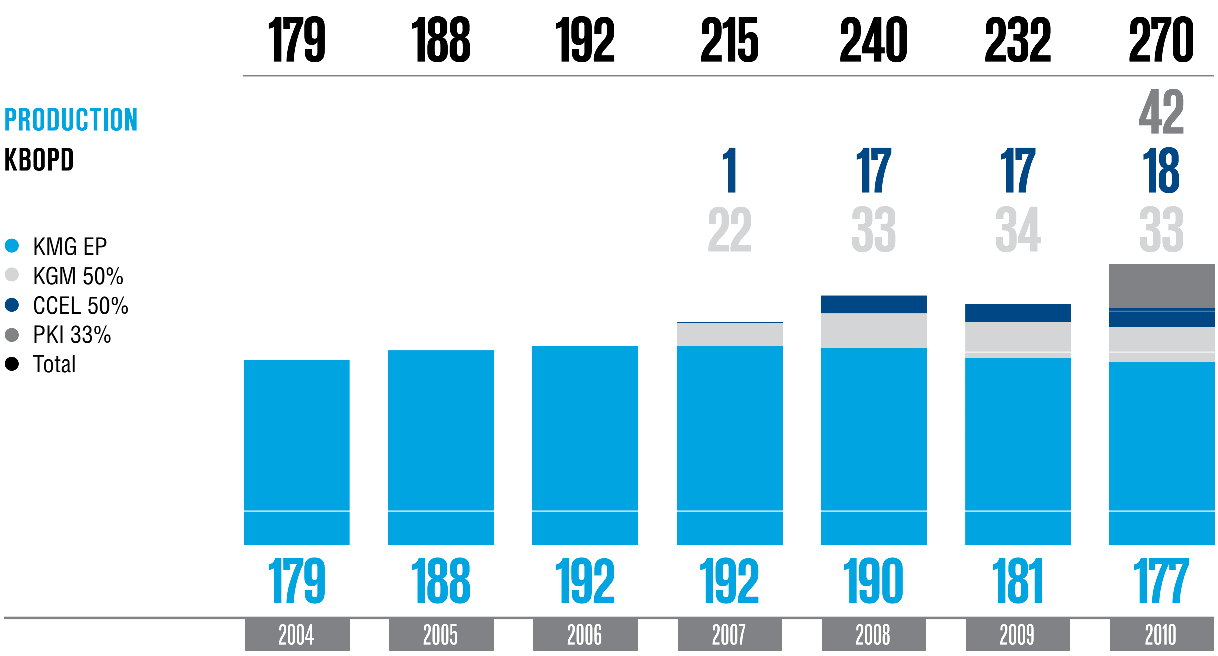


The Company will work on maintaining oil production at the current level, improving oil recovery at existing fields, the exploration of promising sites in Kazakhstan and beyond and the supplementary exploration of the operating fields to provide the targeted growth of production and reserves. In addition, the Company is going to acquire new assets, mainly in the selected regions, and expand its asset portfolio with offshore projects and gas assets, both in Kazakhstan and overseas.

The profitability of current assets will be maintained by means of efficient cost control, improvement of business-processes and workflows, including automation, the implementation of new technologies, asset structure optimization and the improvement of the business management model.

According to this strategy, new business opportunities will be developed by means of building long-term partnerships with leading oil and gas companies in the areas of exploration, production and services together with the training and professional development of highly qualified personnel and the development of our own technical and technological expertise. Performance will also be improved through gaining experience in the management of offshore projects, in the gas business and international assets, including in partnership with large international oil and gas companies.

The Company prefers to invest its funds in Kazakhstan, if an opportunity for the efficient investment is available. At the same time, investing in foreign E&P assets is also an important part of KMG EP's strategy. In view of good intergovernmental relations and similar conditions with respect to the oil operations, KMG EP perceives Russia, Turkmenistan and Uzbekistan as prospective countries for expanding its business interests. KMG EP aims to purchase exploration blocks and projects in these areas with potential for considerable production growth, and production assets with low lifting costs.



Other attractive regions for extending the Company's activities include Iraq, Vietnam, North Africa, the Middle East and undeveloped regions in the North Sea and the Barents Sea.

So far, KMG EP has limited experience of international project management. Therefore, the initial stage of the strategy for entering foreign markets is based on partnerships with international oil and gas companies. Participation of strategic alliances will be based on the need to gain experience in international project management and get access to modern technologies. Thereafter KMG EP will be striving for independent development of international hydrocarbon production projects located outside the territory of Kazakhstan.

EXPLORATION IN KAZAKHSTAN

ONSHORE PROJECTS

At present, KMG EP exploration portfolio comprises three blocks: Liman, R-9 and Taisoigan. The Company processes geological data, drills exploration wells and carries out 2D and 3D seismic surveys at these blocks. In 2010, exploration expenditures[1] amounted to KZT 5.0 billion (USD 33 million). In 2011, the exploration budget will amount to KZT 17.6 billion (USD 117 million).

In October 2010, an oil accumulation was discovered at the Liman block. The accumulation is located on the south slope of the Novobogatinsk Salt Dome 70km west of Atyrau and is in close proximity to the Novobogat Southeast oil field operated by Embamunaigaz.

An oil flow was evident at the first exploration well in Middle Triassic layer which was over 1,200m deep. At the conclusion of geophysical research of wells it was recommended to perform testing of the three layers in production casing. The discovery of light crude oil with 34 API density indicates existing potential of post salt Triassic layers in the region. The Company's 2011 working programme schedules conducting of 3D seismic surveys in the area of 165 sq.km., drilling of two exploration wells for a detailed study of the geological structure of discovered deposits and to assess its commercial importance for the earliest launch of testing operation.

KMG EP is actively working on obtaining exploration and onshore production contracts through outside subsoil users and through its partnership with NC KMG under the Service Agreement. Currently, the Company is analyzing geological data for certain onshore sites in West Kazakhstan and other regions to identify promising blocks.

[1] Including supplemental exploration and 3D seismic research.

In 2010, KMG EP completed its transactions with Eastern Gate Management Ltd. to acquire a 100% interest in NBK LLP (NBK) and with Halyk Komir to acquire a 100% interest in SapaBarlau Services LLP (SBS).

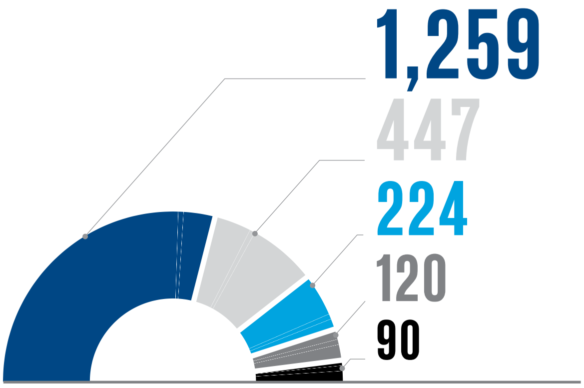
The acquisition price for the 100% interest in NBK was USD 35 million and USD 30 million for the 100% interest in SBS.

NBK develops the “Novobogatinskoe West” field under a Subsoil Exploration and Production Contract expiring in 2027 with an option to extend. The field adjoins the license area of EMG and uses its existing infrastructure for oil treating, storage and transportation. Currently, the field is at the production testing stage. In the future, KMG EP plans to merge the assets of NBK with the assets of EMG in order to realize synergies in exploration and production.

SBS operates under the exploration contract that expires at the end of 2012 with an option to extend. According to KMG EP’s geotechnical service, this license has significant exploration potential in subsalt structures. In view of this fact, in future the Company intends to drill a deep subsalt well there.

2P RESERVES IN 2010
2,141 MMBBL

- UMG **1,259**
- EMG **447**
- CCEL 50% **224**
- PKI 33% **120**
- KGM 50% **90**



According to Gaffney, Cline & Associates reports for:
- UMG, EMG, KGM as of 31.12.2010
- PKI as of 31.03.2009

According to Miller and Lents report for:
- CCEL as of 30.11.2010

The assets being acquired are located in close proximity to the assets of Kazakhoil Aktobe LLP (KOA) and Kazakhturkmunai LLP (KTM), as well as other exploration assets, which may be of interest to KMG EP. The geographical location of the newly acquired assets provides an opportunity for further synergies.

In future the Company intends to expand its exploration portfolio to 10-11 projects by buying additional exploration blocks from NC KMG such as Temir, Terseken, Karaton-Sarkamys, the territories that belong to Uzen-Karamandybas field, and 2 or 3 exploration assets from third parties.

OFFSHORE PROJECTS

As referred to above, KMG EP is awaiting government approval for the acquisition of a 50% interest in Mangistaumunaigas JSC. MMG would provide KMG EP with access to two promising offshore exploration assets in the Kazakhstan sector of the Caspian Shelf.

KMG EP intends to expand the share of offshore assets in its portfolio in line with the strategic ambitions of the Company relating to the Caspian Sea.

INTERNATIONAL EXPANSION

KMG EP is actively looking for attractive opportunities to take part in global projects. Starting in 2008, the Company independently and as a part of consortia participated in license rounds for the rights to explore and develop oil and gas fields in various countries worldwide.

In August 2010, KMG EP added the first international project to its exploration portfolio. KMG EP and BG Group signed an agreement to farm-in to a BG Group operated license in the British sector of the North Sea for joint production within the White Bear prospect. KMG EP acquired a 35% stake in the project.

The White Bear prospect, within the P1722 license, is located close to the BG Group's existing Everest and Armada producing assets. BG retains the remaining interests and will continue to operate the license on behalf of the partners. It is scheduled to drill an exploration well in 2011, as specified by the contractual commitments.

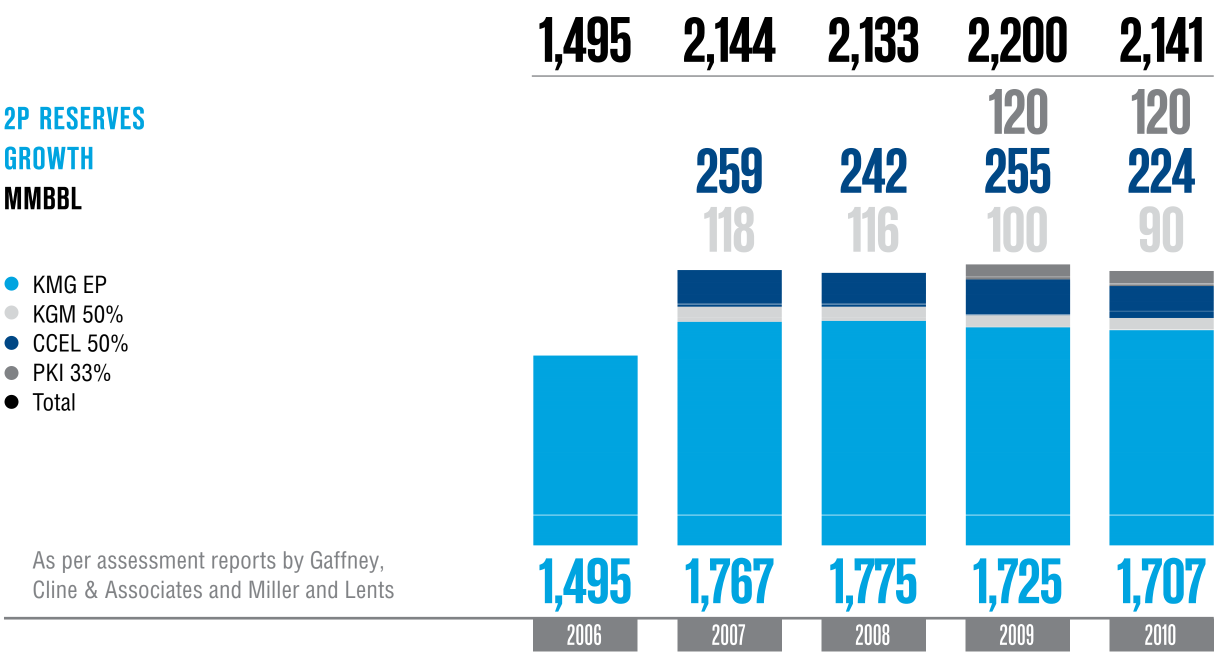
The transfer of an interest meets the terms and conditions of the cooperation agreement signed in 2008. KMG EP's farm-in financial risks, including drilling costs and other project liabilities at the HC pre-discovery stage, are estimated to be USD 25-30 million. KMG EP's evaluation of the project was based on the corporate investment payback criteria reflecting the cost of capital and the risks associated with such projects.

Thanks to this project the Company gets access to BG Group's offshore skills, techniques and experience which is important for KMG EP's mid and longer-term development and for the future expansion of its exploration and production activity on the Caspian Shelf.

In October 2010 KMG EP, in partnership with Korea Gas Corporation (KOGAS) was awarded the rights to develop the Akkas gas field in the Republic of Iraq in the Third Licensing Round organized by the Petroleum Contracts & Licensing Directorate of the Iraqi Ministry of Oil. The terms of the proposed deal implied a USD 5.5/boe Remuneration Fee Bid and a 400 MMSCFD plateau production target.

In accordance with the conditions of the Third Licensing Round, the State Company owned by the Iraqi Government will hold a 25% equity share in the final consortium with the remainder equally split between KMG EP and KOGAS (37.5% / 37.5%).

2P RESERVES GROWTH
MMBBL



As per assessment reports by Gaffney, Cline & Associates and Miller and Lents

The Akkas gas field is located in Anbar province, in the Western part of Iraq near the Syrian border. The Oil Ministry of Iraq estimates its gas reserves at 5.6 TSCF.

Not only does the Akkas project expand KMG EP's international portfolio, but it is also the first large gas asset that supports the Company's intention to develop gas production as its new business priority. Iraq is quite an attractive region for any oil and gas company, as it is famous for its considerable reserves and extremely low production costs.

KMG EP believes that these foreign projects meet its criteria for international expansion; they will provide access to the skills and technology that will allow The Company to achieve the goal of becoming one of the world's top 30 oil and gas companies.

ACQUISITION OF NEW ASSETS

KMG EP considers the acquisition of onshore assets in Kazakhstan to be one of the major priorities for the Company's development in the mid-term.

Relations with NC KMG and its preemptive right to acquire the assets in Kazakhstan in accordance with national law enables KMG EP to participate successfully in acquisitions of oil and gas assets in Kazakhstan on favorable economic terms. The previous transactions demonstrate the effectiveness of this strategy.

In July 2010, KMG EP announced the acquisition of a 50% interest in Kazakhoil Aktobe LLP (KOA), a 51% stake in Kazakhturkmunai LLP (KTM) and 50% in Mangistau Investments B.V. (MIBV), the owner of 100% share capital of Mangistaumunaigas JSC (MMG). According to the preliminary estimates, these acquisitions will result in an over 27% growth in the consolidated oil production of KMG EP and an increase of 406 million barrels in 2P reserves (18.5%).

The acquisition price of the three assets is USD 750 million, of which USD 350 million is for the interest in KOA, USD 70 million for the interest in KTM and USD 330 million for the interest in MIBV. The acquisitions will be financed from KMG EP's own cash funds. The total net debt for the interests being acquired is USD 1,499 million, of which USD 116 million is KOA's net debt, USD 53 million is KTM's net debt and USD 1,330 million is MIBV's consolidated net debt.

The transaction is subject to a number of conditions, including obtaining the approval of the regulatory agencies and, pursuant to the law of the Republic of Kazakhstan, and a written waiver by the remaining KOA and KTM shareholders of their preemptive right.

5 CORPORATE SOCIAL RESPONSIBILITY

CORPORATE SOCIAL RESPONSIBILITY

Social responsibility is one of the key features of KMG EP's operation. The Company's efforts in this area focus on creating safe and comfortable working conditions, providing social protection for employees and their families, providing for the continuous professional development of personnel, and facilitating the sustainable development of regions where the Company operates.

KMG EP implements its social policy in strict compliance with the programmes developed both independently and jointly with local and regional authorities. The Company annually allocates considerable funds to improving the living standards of the population in the regions where it operates, and monitors all social projects to ensure they are implemented in full and on schedule.

KMG EP SOCIAL PROJECTS IN MANGISTAU REGION AND ZHANAOZEN

Starting from 2008, KMG EP annually allocates KZT 900 million (USD 6.1 million) to fulfil its contractual obligations in accordance with the Social Infrastructure Development Programme for the town of Zhanaozen and Karakiya district. The funds are spent on the development of municipal housing, public services and the social infrastructure of the city.

Aside from that, KMG EP and the Mangistau Region Administration (Akimat) signed a Memorandum for additional financial support for regional social projects. Under the memorandum in 2010, the Company allocated over KZT 970 million (USD 6.6 million) for municipal needs, in addition to the Company's contractual commitments. The funds were used in Zhanaozen to create 1,000 social jobs, build a 200-apartment communal residential building and expand the territory of a subsistence farm in Tenirekshin village to 500 hectares. They were also used to construct playgrounds in 63 residential yards and provide sports grounds with artificial cover for 10 of the town's schools. The funds were also used to pay the utility bills for veterans of the World War II.

The Company has also undertaken a commitment to improve the supply of drinking water to Senek village.

Disabled children, families with many children and families in need, war and labour veterans, and the vulnerable elderly are also not ignored.. The Company supported the Junior Boxing Federation and a sports club for disabled people. In 2010, KMG EP spent a total of KZT 37 million (USD$0.25 million) from its net profit on sponsorship and charity in the Mangistau Region.

In addition, a medical centre with an in-patient department with a capacity of 50 beds will be built in Zhanaozen within the 2010-2012 period. In 2010, work started on remodelling the Kenderly recreation zone into a medical rehabilitation centre. A children's holiday camp for 250 kids is also being built on the Caspian coast, costing over KZT 570 million (USD$3.9 million). It will provide remedial treatment and rehabilitation for employees of oil companies and their family members. The renovation and complete overhaul of existing social facilities will be carried out along with the improvement of adjacent territories.

KMG EP supports about three thousand people under its social programme for non-working pensioners. KMG EP is one of a few companies in Kazakhstan that provides financial assistance to its non-working pensioners in the form of travel tours to health centres and free annual subscriptions to national and regional printed media. The Company also finances recreation projects in summer camps for the children of oil industry workers in Kazakhstan and neighbouring countries.

The Company pays special attention to the development of sport and the promotion of a healthy lifestyle in the region. A multifunctional sports and leisure complex, costing more than KZT 2 billion to build operates in Zhanaozen. The sports complex has boxing, judo, aikido, basketball, volleyball, football and rhythmic gymnastics facilities. It also has a 25-metre swimming pool, a 50-metre shooting gallery and a weight-lifting room. Zhanaozen also enjoys a stadium with 3,000 seats which was also built with funds from KMG EP.

SOCIAL PROJECTS IN ATYRAU REGION

In 2010, KMG EP paid KZT 276.5 million (USD 1.9 million) in line with its commitments under the subsoil use contracts to finance projects envisaged by the Atyrau Region Social Development Programme for 2010-2014.

In the same year, under the social partnership programme for the support of social infrastructure being implemented jointly with the Administration (Akimat) of Atyrau Region, KMG EP allocated KZT 970 million (USD 6.6 million) for social projects in Makat, Kyzylkugin, Zhylyoy and Makhambet districts. The Company also allocated KZT 750 million (USD 5.1 million) to relocate people from Komsomol, Koshkar, Bek-Bike villages. In Makat a rehabilitation centre was opened for patients of the local tuberculosis hospital. In Miyaly village of Kyzylkoginskiy district the design and construction of a sports and leisure complex has been started and is to be completed in 2011.

KMG EP continues to provide fuel oil to public utility enterprises for heating houses in Baichunas and Iskene villages of Makat district.

KMG EP annually provides sponsorship and charitable assistance to the Ak-Bota Orphanage, the orphan home for disabled children, the Association of Mothers of Disabled Children, the Association of Disabled Persons and the Association of Blind Persons, large and needy families in Atyrau, city sports organisations; as well as financial assistance to World War II veterans and those who worked on the home front. In 2010, the Company spent KZT 125 million (USD 0.8 million) for that purpose.

PROJECTS OF JV KAZGERMUNAI LLP

Signing of a Memorandum for Social and Economic Development of the Region with the local Administration (Akimat) is one of the components of social policy of JV Kazgermunai.

In May 2010 Kazgermunai allocated almost USD 2 million to Igilik Corporate Fund for the development of regional economic and social projects.

In addition, the company agreed with the regional Akimat to provide social sponsorship worth USD 1 million to support education, healthcare, sports, cultural heritage, the disabled, children with disabilities, and the low-income population of Kyzylorda Region. In total the Company allocated more than KZT 600 million (USD 4.1 million) for the different social needs of the regional population.

To date, JV Kazgermunai is the only company in the region that provides the city with dry gas. This is supplied at a fixed price agreed with the regional Akimat of KZT 20 per cubic meter in 2010.

JV Kazgermunai was named the Most Socially Responsible Company in the 2010 Paryz contest.

PROJECTS OF KARAZHANBASMUNAI JSC

Karazhanbasmunai JSC actively supports socially important projects in Mangistau Region, which are mostly focused on the support of the low-income population, on education and the extension of regional infrastructure .

In 2010 the amount of sponsorship was about KZT 300 million (USD$2 million), It was spent on the repair and construction of the Aktau-Kalamkas Road and for gasification of the houses of the low-income and socially vulnerable population of Fort-Shevchenko city, Bautino and Atash villages. In addition, the Company provided assistance to World War II veterans, sportsmen of the Kazakhstan Boxing Federation and also financially supported large sports and cultural events in the region.

PROJECTS OF PETROKAZAKHSTAN INC.

PetroKazakhstan Inc's main priority is to support programmes focused on assistance to the low-income population; support of qualified personnel and the creation of jobs; the popularization of sports; as well as environmental and educational projects. Memorandums of Cooperation were signed with the Administrations of South-Kazakhstan and Kyzylorda Regions so that this work could be carried out on a continuous basis. The Company provides its financial assistance for gasification, the installation of telephones, water and electric power supplies in villages, and contributes to the development of culture and sports.

With the support of PetroKazakhstan the Youth Achievement Public Fund has been functioning in Kyzylorda Region since 2008. The purpose of the fund is to teach schoolchildren the laws of economics and inculcate practical entrepreneurial skills. The financial support of the fund's activity enabled 37 thousand schoolchildren to learn the laws of market relations. In addition, the fund trained and issued its certificates to 210 teachers of the region.

For many years PetroKazakhstan has been a sponsor of a number of schools in the region and Sairam Orphanage No. 4. The Company financially supports the only ballet school in the region working in Shymkent city. The school is for 250 children, out of which 38 children are from Sairam Orphanage No. 4 and Komesh Bulak Orphanage.

Along with the support of various sports organizations, PetroKazakhstan is a sponsor for the National Federation of Jujitsu. The sportsmen of the Federation actively participate in international competitions and honorably represent Kazakhstan- taking prize-winning places.

In Almaty city the Company supports the Mercy Voluntary Society and is a permanent partner in the campaign "Save Children's Lives" administered by the Society. The campaign provides assistance to children suffering from diseases currently untreatable in Kazakhstan.

IMPROVEMENT OF WORKING CONDITIONS

The management of KMG EP considers maintenance of good working conditions for the Company's employees to be one of the most important aspects of increasing productivity.

KMG EP has developed a programme for the improvement of social and living conditions at the structural subdivisions of UMG for 2009–2012. In 2010, over KZT 1.6 billion (USD 10.7 million) was allocated in the budget for that purpose. These funds were spent on building new dining halls and amenity blocks for personnel of the structural subdivisions and the acquisition and installation of modular offices for operators who work in group units. First-aid medical stations are being built and the Company has purchased ambulance cars and special vehicles for the delivery of hot food. The contract for the fleet of buses for the transportation of personnel has been renewed.

The Company annually allocates funds for the improvement of social and living conditions in the structural subdivisions of Embamunaigas Production Branch (EMG). According to the expenditure budget for 2009-2010, about KZT 700 million (USD 4.7 million) was allocated for the renovation of functioning dormitories and dining halls located at oilfield facilities and the construction of new ones, the replacement of household equipment and the reconstruction of sports and recreation facilities.

HR POLICY

The development of human resources is considered by the Company to be the main factor supporting its long-term growth.

Investment in human capital is among the strategic priorities of the Company. KMG EP will continue to promote the professional development of its employees, the realization of their talents and creative initiatives. In its turn, KMG EP expects employees to enhance their contribution to the Company's development.

The HR policy of KMG EP is focused on identifying the need for specialists in strategically important areas for the optimal distribution of human resources and the development of workforce motivational schemes. It is aligned with the profit received by the Company, and aims to produce a working environment based on respect for individuals.

The competence of KMG EP personnel is evaluated not just during the hiring process, but continuously. The Company certifies all its employees on a regular basis. This enables it to make an objective judgment of each employee's professional level; to focus his/her efforts on the factors, tasks and areas of operation that will lead to the improvement of his/her performance and the efficiency of the Company as a whole. It also enables evaluation of the manager's work over the reporting period and his/her contribution to the achievement of corporate goals.

Today, the Company employs professionals of the highest quality, many of whom have extensive experience of the oil and gas industry of Kazakhstan, as well as young specialists who studied abroad and had internships with foreign companies. The constant improvement of employees' qualifications is a necessary condition of KMG EP's success. It is impossible to achieve higher production and economic indicators without training personnel in new work methods and the use of new equipment and technologies.

In 2010, 4500 employees of the Company improved their level of qualification through participation in seminars, training, certification programmes and conferences.

Special attention is paid to the training of workers, and the engineering and technical personnel of the Company. During the year employees were also trained in crisis and emergency situation response, occupational health and safety, blowout safety, hazardous cargo handling safety, etc.

In 2010, several large corporate training exercises for the managers of central administrative offices and branches were conducted to improve the level of corporate governance and the efficiency of the Company.

The Company spent KZT 500 million (USD 3.4 million) on training in the reporting period.

The Company attaches great importance to communicating its development strategy and the short-term and long-term plans to its personnel. During 2010 the core business working groups of the Company held a series of meetings with personnel where the new wage payment system was introduced, entailing a raise of salary by 25% on average. Together with the trade unions of the production branches, a collective agreement for 2011-2013 was developed that determined the basis of the employer - employee relations. This includes guarantees and benefits, wage forms and rates, compensation and financial assistance, standard working and rest hours.

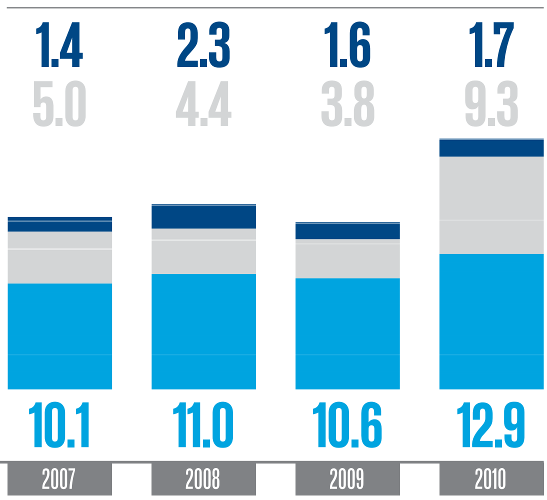
The management of the Company regularly holds meetings with representatives of employees during which the trade union representatives and informal leaders of personnel from the production branches discuss matters related to personnel development, work improvement and other areas of HR policy.

The Company publishes The Munaily Meken newspaper which is distributed among all employees of KMG EP to raise the awareness of personnel and discuss important social and HR-related problems.

SOCIAL PROJECTS EXPENSES
USD M

- Mangistau region
- Atyrau region
- Other

KZT/USD, average:
2007 - 122.55; 2008 - 120.29;
2009 - 147.50; 2010 - 147.35



6 HEALTH, SAFETY AND ENVIRONMENT

HEALTH, SAFETY AND ENVIRONMENT

OCCUPATIONAL HEALTH AND SAFETY

Occupational health and safety is one of the main priorities for management at KMG EP. Company personnel and top managers of its structural subdivisions are personally liable for the observance of the standards and requirements of the labour and environmental protection laws during the production process. The implemented measures are aimed at improving working conditions, accident prevention, readiness to localise and eliminate the consequences of accidents and guarantee indemnity of damage inflicted upon third parties and the environment. All measures are supported financially and performed, in full, year after year.

The permanent commission carries out comprehensive audits and analyses of occupational safety and environmental conditions, inspects equipment, protective means and the whole working environment for compliance with safety-related requirements and international standards.

To prevent and reduce occupational diseases, the staff of KMG EP head office and branches have to pass an annual medical check-up while drivers and other personnel must pass a medical check-up before their shifts.

The production facilities of oil companies are inherently hazardous, therefore KMG EP is actively working to reduce risks that pose a threat to the health and safety of personnel. Analysis of the last few years clearly shows stabilisation of the level of industrial injuries. Nevertheless, the problem of occupational accidents is still an issue. In 2010, three hazard-related incidents at the Company's production facilities were reported.

In 2010 the number of accidents was 4 times less than in 2004, when the Company was established.

ENVIRONMENTAL PROTECTION

The environmental policy of the Company comprises the following main tasks: to provide environmental protection through the application of the best technologies and practices; to observe environmental legislation; to maintain implementation of the quality control system (according to ISO 9001) and environmental management system (according to ISO 14001); to utilize production wastes and eliminate land contamination.

The Company operates in compliance with all applicable requirements in the area of health, safety and environment, methods and best international petroleum industry practices for the development of oilfields.

In 2010, the Company allocated KZT 6.6 billion (USD$44.7 million) for the implementation of environmental measures.

The funds were spent to eliminate contamination that occurred previously, to utilize accumulated production wastes, prevent contamination of the Caspian Sea and to conduct ecological monitoring of the environmental situation.

For the current year the Company obtained the ecological permits and approval of its environmental protection plans from the Ministry for Environmental Protection, which must be fulfilled.

In addition, the Company has developed and coordinated with the Ministry for Environmental Protection and Ecological Control Programme through which the ecosystems of the fields are being permanently monitored.

The Company monitors the environmental situation of its production facilities annually. For this purpose the Company engages independent specialized organizations which have necessary permits, licenses and accredited laboratories to carry out tests.

The financing of measures for the elimination of historical contamination from fuel oil grows every year. The Company has been carrying out measures to process oil-contaminated ground and clean up contaminated lands using the latest biotechnologies for the reclamation of oil-contaminated land. For this purpose the Company has supplied specialized companies with the necessary permits, licenses, equipment and qualified personnel.

The volume of oil-contaminated soil processed in 2010 amounted to 120,000 tonnes. Land cleaned with the use of biotechnologies amounted to 106.4 hectares while 0.816 hectares of contaminated land were technically reclaimed.

UTILIZATION OF ASSOCIATED GAS

From 2005 through 2010 work at 8 facilities of Embamunaigas PB was completed under the Associated Gas Utilization Programme and, starting from 2011 these facilities have made possible the complete utilization of associated gas, just as the facilities of Uzenmunaigas did.

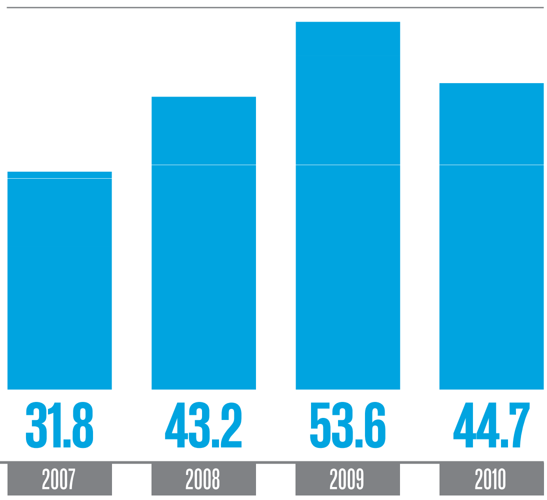
The volume of associated gas consumed by the production branches was increased and helped to reduce gas flaring and increase gas utilization by up to 65%.

The multi-staged selection of associated petroleum gas (APG) desulfurization technology for the Prorva group of fields was completed. The technology provides a high level of APG treatment and the conversion of hydrogen sulfide into elemental sulphur.

In 2011, two options for the implementation of the gas transportation project at the Prorva group of fields are to be considered. The first requires construction of a 75km long gas pipeline from the Prorva Oil Gathering Center to the Oil and Gas Production Department of Tolkynmunaigas LLP (Borankol Oil Refinery). The second calls for the construction of a110km long gas pipeline from the Prorva Oil Gathering Center to the Central Asia – Center Gas Pipeline System (Opornaya Compressor Station).

Taking into account the need for the full utilization of gas before 2014, KMG EP intends to organize production of natural gas at the Prorva group of fields and transport it, together with associated gas, to the Tolkynneftegas Oil and Gas Production Department or to the Central Asia – Center Gas Pipeline System.

ENVIRONMENTAL EXPENSES
USD M



KZT/USD, average:
2007 - 122.55; 2008 - 120.29;
2009 - 147.50; 2010 - 147.35

7

CORPORATE GOVERNANCE INFORMATION

CORPORATE GOVERNANCE INFORMATION

COMBINED 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 required to comply with the UK Code on Corporate Governance or its previous version, the Combined Code on Corporate Governance. However, in accordance with DTR 7.2 it is required to disclose in its Annual Report whether or not it complies with the corporate governance code of the Republic of Kazakhstan and the 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. In addition, the Company shall specify where its actual governance practices differ from those set out in the Combined Code. The Directors recognize the importance of the corporate governance and support the development of high corporate governance standards in the Company.

The Company acknowledges the issue of the Code on Corporate Governance (the "Code") adopted in May 2010 by the Financial Reporting Council, UK's independent regulator responsible for promoting high quality corporate governance. The Code applies to the companies with a premium listing of shares in the UK for the reporting periods starting on or after 29 June 2010. Therefore, the Company will report on compliance with the UK Code on Corporate Governance in its annual report for 2011.

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.

Throughout 2010 the Company has complied with the provisions of the Code on Corporate Governance of Kazakhstan in all material respects.

The Company has adopted the Code on Corporate Governance of Kazakhstan as its own Code, amended to include certain provisions of the Combined Code. The amendments adopted by the Company impose additional obligations on KMG EP in respect of corporate governance. The Company believes that these additional amendments will significantly strengthen the corporate governance practices applied by the Company. KMG EP also takes into consideration other provisions of the UK Combined Code and will seek to improve its standards of corporate governance in the future.

Additional provisions of the Code on Corporate Governance of the Company in addition to the requirements of applicable laws of the Republic of Kazakhstan (namely, the Code on Corporate Governance of the Republic of Kazakhstan) are as follows:

- Additional principles of corporate governance were introduced:

  Principle of independent activities of the Company.
  The principle of responsibility.

- Some of the corporate governance principles are supplemented by various provisions, such as:

  Social Policy principles.
  Provisions regarding relationship with shareholders.
  Division of responsibility between the Chairman of the Board of Directors and the Chief Executive Officer (CEO).
  The 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, which are similar to the equivalent provisions of the Combined Code.
  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.

The copy of the Code on Corporate Governance of the Company along with description of the Company's practices on corporate governance are available on KMG EP's website.

DIFFERENCES BETWEEN THE CODE ON CORPORATE GOVERNANCE OF THE COMPANY AND PROVISIONS OF THE COMBINED CODE

Below are the main differences between the Code on Corporate Governance of the Company and provisions of the Combined Code.

- According to the Combined Code, the Directors should meet without the Chairman of the Board of Directors present at least annually to appraise the Chairman's performance and on such other occasions as are deemed appropriate. The KMG EP's Code on Corporate Governance has no such requirement.

  Throughout 2010, the Independent Non-Executive Directors met eight times without the Chairman of the Board to discuss the following issues: development of the updated Company's strategy; acquisition projects for oil and gas assets in the Republic of Kazakhstan and abroad, relations of the Company with its major shareholder, cash funds management and observance of the Treasury Policy, internal audit and control matters, election to the Board of Directors and to the Management Board, Succession Policy.

  No official evaluation of the activity of the Chairman of the Board of Directors was made by the Non-Executive Directors. The Board's activity was evaluated by an external independent consultant. More detailed information on the Board of Directors evaluation may be found on page 53 of this report.

- According to the Combined Code, the Chairman should on appointment meet the independence criteria set out therein.

  The Code on Corporate Governance of the Company does not contain the provision on independence of the Chairman of the Board of Directors, and, in the opinion of the Directors, the Chairman would not meet the criteria of independence stated in the respective provisions of the Combined Code.

  The Audit Committee Provision specifies that the Chairman of the Board of Directors must not be a member of the Audit Committee, notwithstanding such an option in the Combined Code. This difference is intentionally included in the Audit Committee Provision as the Chairman of the Board of Directors is the representative of the major shareholder.

- According to the Combined Code at least half of the Board of Directors, excluding the Chairman, should comprise of Independent Non-Executive Directors. On the other hand, the Code on Corporate Governance of the Company and the Charter specify that Independent Non-Executive Directors shall make at least one third of the Board of Directors.

  The term of appointment of the previous Board of Directors expired in March 2010. Christopher Mackenzie decided to withdraw from the reappointment process to the Board of Directors at the Extraordinary General Meeting of Shareholders on 26 March 2010. Two out of three Independent Non-Executive Directors were reappointed at the meeting: Paul Manduca and Edward Walshe. According to the Company's Charter, the Board of Directors shall have at least eight Directors (in the absence of temporary positions), and the Independent Non-Executive Directors shall make at least one third of the total number of members. Therefore, one position of an Independent Non-Executive Director was temporarily vacant until election of the new Independent Non-Executive Director. Accordingly, Philip Dayer was elected to the Board as an Independent Non-Executive Director at the Annual General Meeting as of May 25 2010, by the Board of Directors upon recommendation of the Nominations Committee, in which the Independent Non-Executive Directors constituted a majority.

  According to the Charter of the Company a number of key issues, including related-party transactions, shall be approved by a majority of the Independent Non-Executive Directors. The Charter of the Company is available for review at the corporate website.

- The Combined Code also states that the Board shall appoint one of the Independent Non-Executive Directors to be the Senior Non-Executive Director.

  The Board of Directors did not appoint the Senior Non-Executive Director in a view of the current structure of shareholders. The requirement on appointment of the Senior Non-Executive Director will be a subject for consideration from time to time.

DIRECTORS' RESPONSIBILITY STATEMENT

In accordance with the Code on Corporate Governance 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 statements.

In compliance with the UKLA Disclosure and Transparency Rules, each of the Directors (as stated on pages 12-15 hereof), confirms that to the best of his or her knowledge:

- the financial statements prepared in accordance with the International Financial Reporting Standards (IFRS), give a true and fair account of the Company's assets, liabilities, and financial position, the results of its financial and economic activities and those of the subsidiary enterprises included in the consolidated Company's balance sheet taken as a whole; and
- the management report includes a fair review of the development and performance of the business and the financial position of the Company and its joint obligations in the matter of subsidiary enterprises, together with the description of the principal risks and uncertainties they face.

STRUCTURE OF THE BOARD OF DIRECTORS

As of 31 December 2010 the Board of Directors comprised the following eight members:

Name	Title
Askar Balzhanov	Chairman of the Board of Directors
Kenzhebek Ibrashev	Member of the Board of Directors (CEO)
Yerzhan Zhangaulov	Member of the Board of Directors
Tolegen Bozzhanov	Member of the Board of Directors
Assiya Syrgabekova	Member of the Board of Directors
Philip Dayer	Independent Non-Executive Director
Paul Manduca	Independent Non-Executive Director
Edward Walshe	Independent Non-Executive Director

In connection with the expiration of the term of appointment, pursuant to Article 12.2 (2) of KMG EP's Charter, the Board of Directors resolved to call an Extraordinary General Meeting of Shareholders on 26 March 2010 where the following changes were approved:

- Kairgeldy Kabyldin, Chairman of the Board, and Christopher Mackenzie, Independent Non-Executive Director, decided to withdraw from the Board reappointment process.
- As proposed by the major shareholder (NC KMG), Assiya Syrgabekova was elected as a member of KMG EP's Board of Directors.
- Pursuant to the Article 12.16 of KMG EP's Charter, the Chairman of the Board is elected from among its members by a simple majority of votes. Accordingly, on 30 March 2010 Askar Balzhanov was elected as the new Chairman of the Board.
- In accordance with the resolution of the annual General Meeting of Shareholders, Philip Dayer was elected to the Board of Directors as an Independent Non-Executive Director on 25 May 2010.

In compliance with the Corporate Governance Code of the Company, the Board of Directors established the independence of the Directors and considers that Philip Dayer, Paul Manduca and Edward Walshe are independent by nature and in decision-making. The Board of Directors determined that there exist no relations or circumstances that have or may have significant impact on independent decisions made by these Directors.

STRUCTURE OF THE MANAGEMENT BOARD

In 2010 the Management Board comprised senior executives of the Company, including CEO and his deputies.

The members of the Management Board as of 31 December 2010 are as follows:

Officer Name	Title in the Company
Kenzhebek Ibrashev	CEO and Chairman of the Management Board
Vladimir Miroshnikov	First Deputy CEO, Production – Head of Operational Management Group in Aktau
Zhanneta Bekezhanova	CFO
Askar Aubakirov	Deputy CEO, Corporate Development and Asset Management
Taras Khituov	Managing Director, Human Resources and Social Policy
Kiikbai Yeshmanov	Director of UMG
Zhumabek Zhamauov	Director of EMG

During 2010-2011, based on resolutions of the Board of Directors the structure of the Management Board was changed as follows:

- On 26 January 2010 the BoD's decision on the resignation of Dovulbai Abilkhanov and Kairolla Yerezhepov from the Management Board was approved. Bagitkali Biseken (as a Director of UMG) was elected to the Management Board.
- On 30 March 2010 the BoD's decision on the resignation of Bagitkali Biseken, who was transferred from the position of Director of UMG, was approved and Kiikbai Yeshmanov was elected to the Management Board.
- On 21 September 2010 Taras Khituov was elected to the Management Board.

- On 13 December 2010 the BoD's decision on the resignation of Isturgan Baimukhanov (Director PF EMG) from the Management Board was approved, and Zhumabek Zhamauov was elected to the Management Board.

RESPONSIBILITY OF THE BOARD OF DIRECTORS AND THE MANAGEMENT BOARD

The distribution of authority between the Board of Directors, the Management Board and the CEO of the Company is set out in Articles 12 and 13 of the Company's Charter.

The Board of Directors is responsible to shareholders for effective management and control of the Company and acts in compliance with the approved decision-making system. The most important functions of the Board of Directors are to determine the main directions of the Company's strategic development and policy, make decisions on potential acquisitions of the oil and gas assets, and review other essential matters.

The Management Board, in its turn, is responsible for developing an action plan for the implementation of these functions and for the current operating activity of the Company. The Management Board reports to the Board of Directors on progress made in achieving the Company's goals.

The Board of Directors holds its meetings on a regular basis and as required.

In 2010, the Board of Directors held 21 meetings, including seven meetings held by voting in person and 14 by proxy voting.

Throughout the year, the Board of Directors reviewed such issues as:

- Approval of the 2010-2020 Strategy of the Company.
- Acquisition of the oil and gas assets by the Company: a 51% interest in Kazakhturkmunai LLP, 50% interest in Kazakhoil Aktobe LLP, 50% interest in Mangistau Investments B.V.; a 100% interest in NBK LLP; a 100% interest in SapaBarlauService LLP; a 50% interest in Ural Group Limited; a 100% subsoil use rights under the contracts for exploration of hydrocarbons in Mangistau and Atyrau Regions.
- Participation of the Company in the project in the North Sea and in the Third Licensing Round in the Republic of Iraq.
- Consideration of prospective development plans for the fields of Uzenmunaigas and Embamunaigas Production Branches.
- Purchase of NC KMG's bonds.
- Buyback programme for preferred shares of the Company.
- Treasury Policy compliance.
- Preliminary approval of the Company's consolidated financial statements for the previous year.
- Matters on relations with the affiliated persons, subsidiaries of NC KMG.
- The performance report of the Board of Directors and the Management Board for 2009.
- Performance evaluation report of the Board of Directors for 2009.
- Consideration of plans and reports of the Internal Audit Service, status of the implementation of recommendations made by the Internal Audit Service.
- Conclusion of related-party transactions by the Company.
- Matters pertaining to the competence of superior bodies of the subsidiaries.
- Election of the Chairman of the Board of Directors.
- Formation of the Committees of the Board of Directors.
- Labor relations issues.
- Final results of the key performance indicators (KPI) of the Management Board, Head of the Internal Audit and Corporate Secretary of the Company.
- Election of members to the Management Board.
- Granting options in accordance with the Option Programme.
- Determination of remuneration for members of the Management Board.
- HR-related matters of the Internal Audit Service and the Corporate Secretary.

In 2010, the Board of Directors approved the following documents:

- The 2010-2020 Development Strategy of the Company.
- Perspective development plans for the fields of Uzenmunaigas and Embamunaigas Production Branches.
- Cost Control Policy.
- Cost Control Programme.
- Wage payment rules for employees.
- Changes and amendments to the Audit Committee Provision.
- Amendments to the Treasury Policy and Budgeting Regulations.
- Annex "Procedure for Distribution of General Costs for the Purposes of Separate Tax Accounting" to the Accounting Policy.
- Regulations for branches of the Company's subsidiary.

The Board of Directors also considered amendments to the Charter of the Company and recommended to the General Meeting of Shareholders to approve them.

DIRECTORS' ATTENDANCE AT THE MEETINGS OF THE BOARD OF DIRECTORS AND COMMITTEES

Number of meetings in 2010	Board of Directors	Audit Committee	Nominations Committee	Remuneration Committee	Strategic Planning Committee
Kairgeldy Kabyldin	7	-	-	-	-
Askar Balzhanov	21		3	1	1
Kenzhebek Ibrashev	21	2	2	8	2
Asia Syrgabekova	13	-	-	-	-
Tolegen Bozzhanov	16	-	-	-	-
Yerzhan Zhangaulov	18	-	-	-	-
Christopher Mackenzie	7	-	-	-	-
Paul Manduca	21	6	3	8	2
Philip Dayer	11	3	2	6	2
Edward Walshe	21	6	3	8	2

The Management Board is an executive body, managing daily activities of the Company. In 2010, the Management Board held 46 regular and extraordinary meetings.

During 2010, the Management Board considered and approved the following most important issues relating to the Company's operating activity:

- Acquisition of the participating interest and a 100% subsoil rights in a number of oil and gas companies in Kazakhstan.
- Participation of the Company in the licensing rounds in the Republic of Iraq for the development of gas condensate fields that thereafter allowed the Company to win the tender and enter the international level.
- KMG EP Development Strategy.
- Production Programme for 2011.
- Prospective development plans for the fields of Uzenmunaigas and Embamunaigas Production Branches for 2010-2020.
- Buyback Programme for Preferred Shares of the Company.
- Cost Control Programme.
- Principal parameters of the new wage payment system for the KMG EP production personnel.
- KMG EP Business Plan for 2010-2014.
- A number of procedures regulating internal activities of the Company in accordance with the Integrated Management Standards.

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.

PERFORMANCE EVALUATION OF THE BOARD OF DIRECTORS

The Board evaluation has been carried out by an external independent consulting company.

The KMG EP Board has been comprehensively assessed on its performance and the performance of its committees in 2010. The review covered the analysis of 12 months of board agendas and minutes, the detailed questionnaires and discussions with directors and key management. The review examined the implementation of top-priority goals by the Board, the professional balance and independence of the Board, its interaction with the management, and the quality of key procedures of the Board.

The report has concluded that the KMG EP Board is led by the Chairman well and the standards of governance and Board performance are in line with the good practice.

The areas for improvement were identified and discussed with the Board. The recommendations were to continue to improve the quality of information for the Board and to re-order agendas to spend more time on the substantive issues and less on administrative matters. Some observations were also made to the Board to improve the risk assessment and management process along with succession planning at the board and key management level. An action plan reflecting these areas has been developed for its further implementation.

AUDIT COMMITTEE

MEMBERS

In 2010 the Audit Committee comprised only Independent Non-Executive Directors: Paul Manduca (Chairman), Christopher Mackenzie (until 26 March 2010), Philip Dayer (since 29 June 2010) and Edward Walshe. The appointment to the Audit Committee is made for a period not exceeding three years which may be extended for no longer than two additional periods of three years, if so decided by the Board of Directors, provided the members of the Audit Committee continue to be independent.

NUMBER OF MEETINGS

During 2010 the Audit Committee held five meetings. The Chairman of the Audit Committee decides on the frequency and timing of the Committee's meetings. The number of meetings is determined in accordance with the requirements for the role and responsibilities of the Committee. However, there should be at least four meetings within the year which must coincide with the key dates of financial statements preparation and audit cycle of the Company (when internal and external audit plans are available and when interim financial statements, preliminary announcements and the annual report are close to being completed).

ROLE AND RESPONSIBILITIES

The Audit Committee is responsible, among other things, for any statements containing financial information of the Company, monitoring of the risk management and internal control systems, as well as involving the Company's auditors in this process. Also, it receives information from the Internal Audit Service that monitors compliance with internal control procedures of the Company. In particular, the Committee deals with the issues related to compliance with legal requirements, accounting standards and applicable rules of the UKLA and the Kazakhstan Stock Exchange (KASE), provision of the effective internal control system. The Board of Directors is responsible for the preliminary approval of the annual financial report.

The Audit Committee regularly checks major acquisition and disposal transactions and considers any other matters which may be addressed to the Audit Committee by the Board of Directors.

Annually, at the General Meeting of Shareholders the Chairman of the Audit Committee through the Chairman of the Board of Directors reports on the Audit Committee's performance and answers questions related to the Audit Committee's activity.

THE 2010 ACTIVITIES

- Financial reporting.

  Reviewed the preparation of financial statements in compliance with the IFRSs.
  Approved quarterly and annual financial statements to be disclosed to the Kazakhstan and London Stock Exchanges.

- Internal control and risk management systems.

  Assessed the effectiveness of the internal control and risk management systems.
  Self-assessed the performance of the Audit Committee.

- Internal audit.

  Reviewed and approved a three-year plan of the Internal Audit Service.
  Assessed the internal audit effectiveness.
  Reviewed and approved the 2009 work progress report of the Audit Committee.

- External audit.

  Recommended the appointment of an external auditor of the Company for 2011-2013.

- Other issues.

  Reviewed the mid-term cash flows forecasts of the Company.
  Audited for compliance with the Treasury Policy of the Company.

REMUNERATION COMMITTEE

MEMBERS

In 2010 the Remuneration Committee comprised only Independent Non-Executive Directors, namely those were: Christopher Mackenzie (Chairman of the Committee through 26 March 2010), Philip Dayer (Chairman of the Committee since 29 June 2010), Paul Manduca and Edward Walshe. The terms of office of the Committee members coincide with their terms of office as members of the Board of Directors.

ROLE AND RESPONSIBILITIES

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

In addition, the Remuneration Committee is responsible for developing and making recommendations to the Board of Directors on principles and criteria for the determination of amount and payment terms of remuneration and compensations to the members of the Board of Directors, CEO and members of the Management Board. It is also responsible for the approval of terms and conditions of the Company's option plans and long-term incentive programmes for senior managers and other personnel of the Company.

The Remuneration Committee supervises the Company's remuneration policy and current remuneration system for compliance with the Company's strategy, financial position and the labour market situation.

The Remuneration Committee supervises the disclosure of information related to remuneration and compensations paid to the members of the Management Board and the Board of Directors to be in compliance with the requirements of applicable laws of the Republic of Kazakhstan, Listing Rules and internal documents of the Company.

In addition, the Remuneration Committee controls the implementation of decisions approved by the General Meeting of Shareholders in terms of determining the amount and procedure of remuneration payment to the members of the Board of Directors.

The Remuneration Committee regularly reports on its work to the Board of Directors and annually submits to the Board an analysis on compliance of the Committee's activities with its Terms of Reference.

THE 2010 ACTIVITIES

During 2010 the Remuneration Committee met on seven occasions. The meetings were held when required, but in any case no less than once in six months. The meetings may be convened on the initiative of the Chairman or members of the Committee or upon a decision of the Board of Directors.

In 2010 the Remuneration Committee considered the following issues:

- Granting options to the Company's management and employees.
- Remuneration and approval of KPI for members of the Company's Management Board, employees of the Internal Audit Service and Corporate Secretary.
- Review of the 2009 results as per KPI of the members of the Management Board.
- Payment of the annual remuneration (bonus) for 2008 and 2009.
- Succession of the positions held by expatriates.

The total amount of remuneration accrued to the Independent Non-Executive Directors for the year ended 31 December 2010 is presented in the table below:

Name	Annual Fee 000 USD	Physical Attendance 000 USD	INED Meeting Fee 000 USD	Committee Chairmanship Fee 000 USD	Total 2010 (excluding taxes) 000 USD	Total 2010 (including taxes) 000 KZT
Christopher Mackenzie	25	10	10	4	49	7,968
Paul Manduca	138	70	20	25	253	41,478
Edward Walshe	138	70	20	15	243	39,840
Philip Dayer	90	50	10	8	158	25,911
Total	**392**	**200**	**60**	**52**	**704**	**115,197**

Other members of the Board of Directors receive no remuneration as members of the Board, but are entitled to compensation for the costs associated with such appointment.

The total amounts of remuneration accrued to the members of the Management Board for the year ended 31 December 2010 are presented in the tables below:

Name	Title	Salary 000 KZT	Other Annual Payments 000 KZT	Total 2010 000 KZT	Total 2009 000 KZT	Total 2010 000 USD	Total 2009 000 USD
Kenzhebek Ibrashev	CEO	32,408	24,860	57,268	18,098	389	123
Askar Balzhanov	CEO	1,145	4,346	5,491	47,891	37	325
Vladimir Miroshnikov	First Deputy CEO, Production – Head of Operational Management Group in Aktau	28,238	38,324	66,562	25,610	452	174
Zhanneta Bekezhanova	CFO	15,830	29,854	45,684	17,716	310	120
Askar Aubakirov	Deputy CEO, Corporate Development and Asset Management	20,847	9,308	30,155	1,770	205	12
Kairolla Yerezhepov	Managing Director, Human Resources and Social Policy	334	15,234	15,568	12,406	106	84
Taras Khituov	Managing Director, Human Resources and Social Policy	6,683	245	6,928	0	47	0
Zhumabek Zhamauov	Director EMG	1,663	0	1,663	0	11	0
Bagitkali Biseken [1]	Director UMG	4,560	51,280	55,840	30,485	379	207
Kiykbai Eshmanov	Director UMG	10,203	1,944	12,147	0	82	0
Isturgan Baimukhanov	Director EMG	14,097	12,315	26,412	9,783	179	66
Kairbek Yeleusinov	Director UMG	0	1,348	1,348	18,527	9	126
Dovulbai Abilkhanov	Director UMG	0	0	0	10,200	0	69
Murat Kurbanbayev	Director UMG	0	0	0	4,445	0	30
Total		**136,009**	**189,058**	**325,066**	**196,930**	**2,206**	**1,335**

[1] In 2010, Bagitkali Biseken was granted the right of redemption of an apartment in Atyrau city for 15% of book value. The total amount of gain received by Bagitkali Biseken from the acquisition was 40,132 thousand tenge.

The members of the Board of Directors and Management Board were granted KMG EP's GDR Options in accordance with the provisions of the Option Programme.

The table below represents GDR options which were granted but have yet to be exercised:

Name	Option award date	Number of GDRs participating in the option scheme	Option exercise price	Maturity date
Kairgeldy Kabyldin	-	-	-	-
Askar Balzhanov	December 4, 2007 December 2, 2008	15,300 23,576	US$26.47 US$13.00	December 4, 2010 December 2, 2011
Assiya Syrgabekova	-	-	-	-
Yerzhan Zhangaulov	-	-	-	-
Tolegen Bozzhanov	-	-	-	-
Christopher Mackenzie	-	-	-	-
Paul Manduca	-	-	-	-
Edward Walshe	-	-	-	-
Philip Dayer	-	-	-	-
Kenzhebek Ibrashev	June 1, 2009 January 1, 2010 July 20, 2010	20,327 18,034 17,813	US$21.80 US$24.90 US$19.05	June 1, 2012 January 1, 2013 July 20, 2013
Vladimir Mirsoshnikov	October 4, 2006 December 4, 2007 December 2, 2008 July 20, 2010	22,563 12,240 18,861 14,250	US$14.64 US$26.47 US$13.00 US$19.05	Fully matured at October 4, 2009 December 4, 2010 December 2, 2011 July 20, 2013
Zhanneta Bekezhanova	October 4, 2006 December 4, 2007 December 2, 2008 July 20, 2010	19,508 10,880 16,765 12,667	US$14.64 US$26.47 US$13.00 US$19.05	Fully matured at October 4, 2009 December 4, 2010 December 2, 2011 July 20, 2013
Askar Aubakirov	December 1, 2009 July 20, 2010	5,978 11,875	US$25.00 US$19.05	December 1, 2012 July 20, 2013
Kairolla Yerezhepov	October 4, 2006 December 4, 2007 December 2, 2008	14,684 4,604 8,513	US$14.64 US$26.47 US$13.00	Fully matured at October 4, 2009 December 4, 2010 December 2, 2011
Isturgan Baimukhanov	June 29, 2010 July 20, 2010	9,480 9,500	US$19.09 US$19.05	June 29, 2013 July 20, 2013
Taras Khituov	October 19, 2010	9,835	US$18.05	October 19, 2013
Bagitkali Biseken	May 18, 2007 December 4, 2007 December 2, 2008 June 29, 2010	16,968 6,347 11,736 8,623	US$20.00 US$26.47 US$13.00 US$19.09	Fully matured at May 18, 2010 December 4, 2010 December 2, 2011 June 29, 2013
Kiykbai Eshmanov	December 4, 2007 December 2, 2008 June 29, 2010 July 20, 2010	1,038 1,781 9,480 9,500	US$26.47 US$13.00 US$19.09 US$19.05	December 4, 2010 December 2, 2011 June 29, 2013 July 20, 2013
Zhumabek Zhamauov	February 1, 2011	7,845	US$21.50	February 1,2014

NOMINATIONS COMMITTEE

In 2010 the Nominations Committee comprised: Kairgeldy Kabyldin (Chairman of the Committee through 26 March 2010), Askar Balzhanov (Chairman of the Committee through 30 March 2010), Christopher Mackenzie (through 26 March 2010), Edward Walshe, Paul Manduca and Philip Dayer (since 29 June 2010).

The main purpose of the Committee's activity is to improve the effectiveness and quality of work of the Board of Directors in the selection of suitable candidates to fill vacancies in the Company's structure as and when they arise. It also ensures continuity in the replacement of the Company's personnel and determines criteria for election of candidates for the positions in the Board of Directors, CEO, members of the Management Board and Corporate Secretary of the Company.

The Nominations Committee reviews issues related to changes in the membership structure of the Board of Directors and the Management Board, resignation and appointment of the Corporate Secretary, retirement and appointment of additional and substituting directors.

THE 2010 ACTIVITIES

During 2010 the Committee met on two occasions to consider the following issues:

- Recommendations to the General Meeting of Shareholders on election of an Independent Non-Executive Director.
- Election of Chairman of the Remuneration Committee and members of the Internal Audit and Nominations Committees.
- Election of members to the Management Board.

STRATEGIC PLANNING COMMITTEE

In 2010 the Committee comprised: Edward Walshe (Chairman of the Committee), Askar Balzhanov (through 26 March 2010), Tolegen Bozzhanov (since 30 March 2010), Kenzhebek Ibrashev.

The main purpose of the Committee's activity is to develop and advise the Board of Directors on the foreground directions of activities and development strategy.

THE 2010 ACTIVITIES

During 2010 the Committee met on two occasions to consider the following issues:

- The 2010-2020 Development Strategy of the Company.
- Prospective development plans for the fields of Uzenmunaigas and Embamunaigas Production Branches.
- Acquisition of the oil and gas assets by the Company: a 51% interest in Kazakhturkmunai LLP, 50% interest in Kazakhoil Aktobe LLP, 50% interest in Mangistau Investments B.V.; a 100% interest in NBK LLP; a 100% interest in SapaBarlauService LLP; a 50% interest in Ural Group Limited; a 100% subsoil use rights under the contracts for exploration of hydrocarbon material in Mangistau and Atyrau Regions.
- Participation of the Company in the project in the North Sea.
- Participation of the Company in the Third Licensing Round in the Republic of Iraq.
- Prospective acquisition projects in the Republic of Kazakhstan and abroad.
- Cost Control Policy.

INTERESTS OF THE DIRECTORS AND MEMBERS OF THE MANAGEMENT BOARD

The interests of the Directors and Management Board members in ordinary shares, preferred shares and GDRs, according to the information provided by the Board of Directors and the Management Board as of 31 December 2010 are as follows:

Name	Ordinary shares	GDRs	Preferred shares
Kairgeldy Kabyldin	-	-	-
Askar Balzhanov	-	49,102	-
Kenzhebek Ibrashev	-	-	-
Yerzhan Zhangaulov	-	8,681	-
Tolegen Bozzhanov	-	-	-
Christopher Mackenzie	-	6,996	-
Paul Manduca	-	6,828	-
Edward Walshe	-	6,828	-
Philip Dayer	-	-	-
Assiya Syrgabekova	-	-	-
Vladimir Miroshnikov	1,163	9,494	-
Zhanneta Bekezhanova	-	-	2,203
Askar Aubakirov	-	-	34
Taras Khituov	-	-	-
Kiykbai Eshmanov	-	-	-
Zhumabek Zhamauov	-	-	-

PRINCIPAL SHAREHOLDERS AND/OR GDR HOLDERS

Below is the list of shareholders of the Company as at 31 December 2010, which must be reported in accordance with the legislation of the Republic of Kazakhstan.

This requirement is not applicable to GDR holders, however the Company considers it necessary to note that on 30 September 2009 the State Investment Fund of the People's Republic of China, China Investment Corporation (CIC), announced the purchase of about 11% of the Company's shares in the form of GDRs.

Shareholder	Number of ordinary shares	Number of preferred shares	Total share capital
Number of shares issued[1]	70,220,935	4,136,107	74,357,042
Owned by NC KMG	43,087,006	-	43,087,006
Percentage of issued share capital	61.36%	0.00%	57.95%

DIRECTORS' EMPLOYMENT CONTRACTS, LETTERS OF APPOINTMENT AND EMPLOYMENT CONTRACTS OF MEMBERS OF THE MANAGEMENT BOARD

EMPLOYMENT CONTRACTS WITH DIRECTORS

On 26 March 2010 the new members to the Board of Directors were elected for the following three years as the previous tenure of appointment had expired.

Kairgeldy Kabyldin was Chairman of the Board of Directors of the Company until 26 March 2010.

Askar Balzhanov was re-elected the member of the Board of Directors on 26 March 2010. On 30 March 2010 the Board of Directors elected him as the Chairman of the Board of Directors of the Company.

Kenzhebek Ibrashev was a member of the Board of Directors, CEO and Chairman of the Management Board of the Company. He was re-elected the member of the Board of Directors at the General Meeting of Shareholders on 26 March 2010.

Erzhan Zhangaulov was a member of the Board of Directors of the Company. He was re-elected the member of the Board of Directors on 26 March 2010.

Tolegen Bozzhanov was a member of the Board of Directors of the Company. He was re-elected the member of the Board of Directors on 26 March 2010.

Christopher Mackenzie decided not to participate in the re-election to the Board of Directors as the term of office expired in 2010.

Paul Manduca was re-elected the Independent Non-Executive Director of the Company on 26 March 2010.

Edward Walshe was re-elected the Independent Non-Executive Director of the Company on 26 March 2010.

Phillip Dayer was elected the Independent Non-Executive Director of the Company on 25 May 2010.

EMPLOYMENT CONTRACTS OF MEMBERS OF THE MANAGEMENT BOARD

All members of the Management Board have entered into employment contracts with the Company that generally provide for business travel insurance and reimbursement of costs incurred during business trips on the Company's behalf in accordance with the Company's internal regulations. Other than those set out above, no employment contracts exist, or are anticipated to be entered into, between the Company and members of the Board of Directors or the Management Board.

INTERNAL CONTROL AND RISK MANAGEMENT

The Company has a system of internal control and risk management. This system is designed to identify, evaluate and manage significant risks associated with the Company's achievement of its business objectives, taking into account the safeguarding of shareholders' investments into the Company.

The Directors confirm that throughout the year ended 31 December 2010 there have been processes in place for identifying, evaluating and managing the significant risks faced by the Company. In addition, the Directors have used a risk-based approach in establishing the system of internal control and reviewing its effectiveness.

The key elements of the Company's system of internal control are as follows:

- Internal documentation of the Company, such as financial, operating, administrative and treasury policies along with other procedures.
- Continuous monitoring of operating and financial performance, safety-related activities of the Company.

[1] Including 3,373,907 Treasury shares.

The Internal Audit provides the Board of Directors of the Company with objective data on efficiency and adequacy of the established internal control system. The reports of the Internal Audit include recommendations on the design and work of the internal control system. The Internal Control Service supervises the implementation of recommendations by the management and reports on that to the Audit Committee.

In addition, the information on financial risks can be found in the Operating and financial review starting from page 63, the general information on risk profile can be found in the section "Risk Factors" on page 75 and information on initiatives in the area of health, safety and environment can be found in the "Health, Safety and Environment" section on page 46.

In respect of risk management, the Management Board has established a Risk Management Committee. More details on its performance can be found below.

RISK MANAGEMENT COMMITTEE

In 2010 the Risk Management Committee was headed by Kenzhebek Ibrashev. It comprised the deputy CEO for Production – Head of Operating Management Group in Aktau, CFO, Deputy CEO for Corporate Development and Asset Management, Managing Director – Financial Controller, Managing Director for Economics and Finance, Managing Director for Legal Issues, Managing Director for Information Technologies, Managing Director for Human Resources and Social Policy, Managing Director for HSE and Corporate Secretary. The head of Internal Audit participated in the Committee's meetings as an observer.

The primary goal of the Committee is to provide prompt consideration of issues related to risk management, preparation of recommendations to the Management Board to support decision-making on such issues, and monitoring of the risk management system performance. It is also concerned with formulating recommendations to the structural subdivisions of the Company on improving the risk management system in order to increase the effectiveness of business processes and reach the Company's strategic goals.

In 2010 the Risk Management Committee had three meetings where it considered and made decisions on the following issues:

- Annual plan of the Risk Management department and risk management system development for 2010-2011.
- Report on identification and evaluation of the Company's risk portfolio.
- Legal security programme of the Company.
- Improvement of corporate governance, GAMMA rating.
- Organizational structure in the risk management system of the Company.
- Key risks of the Company.
- Automation of contract making processes and claim administration data accounting in the Company.
- Activities to manage some key risks.
- Succession plans in respect of the key positions.
- Discussion on managing free cash flows of the Company.
- Implementation of recommendations provided by the Internal Audit Service.
- Corporate insurance programme for 2010.
- Consideration of current situations arisen in the course of operation of the structural subdivisions of the Company in 2010.

UK TAX CONSIDERATIONS

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 the UK residents for tax purposes; (2) considered to be non-residents for tax purposes in any 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, but it does not addresses 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 connected with the Company.

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, potential 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

If assumed that income received from GDRs is from the non-UK source, 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 dividend on shares or GDRs may be subject to the UK income tax or corporate 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 the UK income tax on the dividend paid on shares or GDRs and who 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 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 residing in the UK is, effective from 1 July 2009, not subject to the UK corporate tax on the dividend paid on shares or GDRs, unless it relates to certain anti-avoidance rules in the tax law.

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 and domiciled in the UK will generally be liable to the 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 but not domiciled in the UK and who is entitled 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 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 against the income tax liability on such amounts, subject to the UK tax rules for calculation of such a credit. From 1 July 2009 the UK Holder, residing in the UK, is not subject to the UK corporate tax on the dividend payment and so is not be able to claim credit for any Kazakhstan 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.

8

OPERATING AND FINANCIAL REVIEW

OPERATING AND FINANCIAL REVIEW

The following document is intended to assist the understanding and assessment of trends and significant changes in the Group's results and financial condition. In this document, the consolidated financial statements presented are those of the Company. 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 upon financial statements prepared in accordance with IFRS.

OVERVIEW

KazMunaiGas Exploration Production Joint Stock Company ("the Company" or "KMG EP") is engaged in the acquisition, exploration, development, production, processing and export of hydrocarbons. The Company's core operations are oil and gas properties located in the Pre-Caspian and Mangistau basins of western Kazakhstan. The Company's majority shareholder is KazMunaiGas, 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 41 oil and gas fields, including "Uzenmunaigas" ("UMG"), which consists of two fields, and "Embamunaigas" ("EMG"), consisting of 39 fields. The Company also has a 50% interest in the oil and gas production joint ventures Kazgermunai LLP and CCEL, and a 33% interest in its associate PetroKazakhstan Inc.

Total 2010 oil production of the Company, together with the share of its joint ventures and its associate company, was approximately 13.285k tonnes or 270kbopd. This includes oil derived from its 50% share in JV Kazgermunai LLP, its 50% share in CCEL and its 33% stake in PetroKazakhstan Inc., The stake in UMG and EMG produced 177kbopd with a further 33kbopd from JV Kazgermunai LLP, 18kbopd from CCEL and 42kbopd from PetroKazakhstan Inc.[1]

Further details of the above joint ventures and associate are given in the section: Overview of Joint Ventures and Associates' Operations. Elsewhere in this Operating and Financial Review the discussion is limited to the core assets of the Company unless indicated otherwise.

BUSINESS ENVIRONMENT AND OUTLOOK

Economic factors affecting the Company's financial performance for the 2010 year under review include movements in crude oil prices, domestic inflation, and foreign exchange rates, particularly the tenge-US dollar rate.

BUSINESS ENVIRONMENT IN 2010

The average price for Brent type oil in 2010 was US$79.18 per barrel; an increase of US$17.51 per barrel from the average price in 2009.

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
	(US$ /bbl)			%	(US$ /bbl)		%
Brent (DTD)	86.46	75.69	74.53	16%	79.18	61.67	28%

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 impact of foreign currency fluctuations on the Company's results depends on its net foreign currency position and the magnitude and direction of any fluctuation in foreign exchange rates.

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

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
Average US$ vs KZT	147.49	147.41	149.77	-2%	147.35	147.50	-0.1%
CPI	2.6%	0.8%	1.4%	86%	7.8%	6.2%	26%
US$ vs KZT at balance sheet date	147.40	147.47	148.36	-1%	147.40	148.36	-1%

Source: National Bank of Kazakhstan

[1] Including 50% share in operational results of JSC "Turgai Petroleum" for 12 month 2010.

The tenge weakened insignificantly against the US dollar from average 147.50 KZT/US$ in 2009 to 147.35 KZT/US$ average in 2010. The inflation rate in 2010 was 7.8 % compared to 6.2 % in 2009.

PRODUCTION ACTIVITY IN 2010

The Company narrowly missed its target production goals for 2010 with oil production of 8,766 thousand tonnes compared to 8,781 thousand tonnes planned. Actual oil production in 2010 decreased by 2% in comparison with 2009.

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
UMG	1,492.15	1,523.00	1,543.43	-3%	5,965.75	6,250.81	-5%
EMG	718.14	716.92	670.70	7%	2,800.01	2,711.34	3%
Total production	**2 210.29**	**2 239.92**	**2 214.13**	**-0.2%**	**8 765.76**	**8 962.15**	**-2%**

As of December 31, 2010, the number of wells operated by the company included 5,884 production and 1,623 injection wells.

The majority of the Company's existing oil fields are at the mature stage of development, characterized by high water cuts and declining oil production. The Company engaged in production drilling, work-over operations and enhanced recovery in order to mitigate the natural production decline and accomplish its oil production targets.

In 2010 the Company drilled and put into operation 215 production wells, 120 more than in 2009. Oil production generated by new wells rose to 206.99 thousand tonnes compared to 133.44 thousand tonnes in 2009. The workover of 1234 wells provided an incremental production of 674.14 thousand tonnes. In this period the Company also applied enhanced recovery techniques, including hydro-fracturing and polymer systems to boost production. As a result of 295 enhanced recovery operations, an additional 327.94 thousand tonnes were produced.

During 2010 the Company carried out exploration works in the R-9, Liman and Taisoigan blocks together with appraisal works in the S. Nurzhanov, Eastern Makat, Prorva Western, Zhanatalap oilfields.

On block R-9, the technical project for field work and the processing and interpretation of 3D seismic data was developed and agreed for a 400 square kilometer block together with 2D-MOGT seismic data for 40 square kilometers on structures Kyzylkuduk and Zhantai. Recommendations were also made for further exploratory drilling in 2011 – 2012 on future structures in both sub-salt and supra-salt parts of the block.

Discovery of a new deposit on the area South-East Novobogat allowed continuing the process to extend the period of exploration for another three years to conduct appraisal work in the area of detection. According to the terms of the existing contract, area of Liman block will be fully refunded to the State except for the assessment section.

In the reporting period on the block Taisoigan performed works on reserves estimation, field supervision and extension of the trial phase of the fields Uaz and Kondybay till January 9, 2012.

On the S. Nurzhanov field the Company commenced drilling at wells 507, 508, 700 with a total planned depth of 9000 meters. It was established industrial productivity of Valanginian deposit.

The Central Committee for Exploration and Development (CCED) and the Committee of Geology also approved the project for further exploration of fields in Western Prorva, S. Nurzhanov, East Makat to a total projected depth of 5000 meters.

On Kenbay field, the processing and interpretation of 3D-MOGT seismic exploration of an area of 128 square kilometers on the Eastern Moldabek and Northern Kotyrtas sites were completed.

On Zhanatalap field, the processing and interpretation of 3D-MOGT seismic exploration of an area of 300 square kilometers on the Zhanatalap, Balgymbayev, Karachaganak fields and the Northern Martysh structure were also completed.

PLANNED PRODUCTION ACTIVITY IN 2011

Crude oil production in 2011 is expected to be 9.1 million tonnes, which is 4% or 334 thousand tonnes higher than produced in 2010. In order to ensure this increase and compensate for the natural production decline in 2011, the Company is planning to drill 185 oil producing wells and 54 injections wells. In addition to well workovers, the Company will apply bottomhole treatment and will bring some inactive wells back on line.

In 2011 the Company is also planning exploration works on prospective blocks to specify the geological structure and justify the objects for prospect drilling and to increment the proven reserves of oil and gas. In particular, on the block R-9 Company is planning to continue drilling of five supra-salt wells on the Southern Kamyskol, Northern Kamyskol, South - Eastern Kyzylkala, Northern Esbolai, Masabai and continue works to evaluate the structure of the rocks of the upper Paleozoic. Drilling of exploratory wells and 3D seismic research on the prospective structure South Eastern Novobogatinsk will be continued and will be conducted over 165 square kilometers area.

On the Taisoigan block will be drilled 3 wells on the Kondybay field according to the trial exploration project. Also planned to conduct 3D-MOGT seismic works on the Uaz field over 68 square kilometers and on the Kondybay field over 82 square kilometers in order to create solid model of the objects and planning of further exploration works. It is planned to begin drilling of exploratory well to determine the hydrocarbon potential of Middle Triassic deposits on the structure Bazhir East.

At the S. Nurzhanov field well 509 will be drilled to a planned depth of 3500 meters to explore and assess oil and gas prospects in the upper part of the Valanginian horizon of the lower cretaceous. A second exploration well with planned depth of 2000 meters is also scheduled for 2011 as part of the wider exploration project for the Valanginian horizon at S. Nurzhanov.

At the Eastern Makat field to clarify the geological structure in the prospective productive layer of the well 101, will be drilled second exploratory well down to the 1500 meter.

On the Western Prorva field work proceeded to clarify the geological structure and determine the hydrocarbon potential in the Triassic and Jurassic deposits. Detailed exploration work was drafted and drilling is recommended for the 3 independent and 1 dependent wells. As a result of the interpretation of seismic data 3D-MOGT clarified the fault tectonics of the block, and of new areas not yet included in the drilling area.

In accordance with contractual obligations in 2011 will begin large-scale geological-geophysical research on the exploration block East Zharkamys.

In 2011 the capital expenditure of the Company is expected to reach KZT106.4 billion. The Company's budget will be periodically reviewed to reflect changes in the crude oil price, and foreign exchange and inflation rates, among other factors.

RESULTS OF OPERATIONS

Amounts shown in US dollars are included solely for the convenience of the reader at the average exchange rate over the applicable period. Assets and liabilities are translated at the closing rate. Income and expenses are translated at the average exchange rate. See "Business Environment and Outlook".

KEY INDEXES

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
	(KZT thousands, unless otherwise stated)			%	(KZT thousands, unless otherwise stated)		%
Revenue	164,212,857	148,424,375	137,838,565	19%	609,242,398	485,493,479	25%
Operating expenses	119,326,557	110,056,257	90,113,109	32%	422,493,059	330,605,629	28%
Operating expenses (KZT per bbl)[1,2]	5,291	5,219	4,242	25%	4,937	4,123	20%
Operating expenses (US$ per bbl)[1,2]	35.87	35.40	28.32	27%	33.51	27.95	20%
Profit from operations	44,886,300	38,368,118	47,725,456	-6%	186,749,339	154,887,850	21%
Net income[3]	77,693,561	56,774,223	29,151,097	167%	234,501,890	209,726,900	12%
Oil Production and other costs[1,4]	37,964,599	36,550,792	30,140,501	26%	131,544,149	105,691,438	24%
Oil Production and other costs (US$ per bbl)[1,4]	15.82	15.04	12.35	28%	13.84	10.86	27%
Capital expenditure	34,834,011	25,398,401	17,817,479	96%	86,679,884	42,844,814	102%

[1] Converted at 7.36 barrels per tonne of crude oil.

[2] Operating expenses net of rent tax and customs duty.

[3] Net income for the period.

[4] Oil production and other costs represent an aggregate of the following operating expenses line items (as presented in the Company's consolidated financial statement for the period ending December 31, 2010 (see Company website for a copy): employee benefits, materials and supplies, repairs, maintenance and other services, energy and other costs. These include costs related to gas producing and processing activities, oil processing activities and general and administrative costs which are not directly related to oil production and which increased the US dollar cost per barrel by approximately US$1.91 and US$1.55 for the years 2010 and 2009 respectively (US$2.61 and 1.58 for the quarters ending December 31, 2010 and December 31, 2009 respectively).

TRANSPORT ROUTES

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

	Q4 2010	Q3 2010	Q4 2009	2010	2009
Exports sales via UAS					
Volume of crude oil (in million tonnes)	1.0	1.1	1.2	4.3	4.9
% total crude oil sales volume	48%	49%	55%	50%	56%
% total sales value of crude oil	56%	57%	67%	58%	66%
Exports sales via CPC					
Volume of crude oil (in million tonnes)	0.7	0.6	0.4	2.5	2.0
% total crude oil sales volume	31%	29%	19%	29%	22%
% total sales value of crude oil	38%	35%	25%	35%	25%
Other sales					
Volume of crude oil (in million tonnes)	0.4	0.5	0.6	1.8	2.0
% total crude oil sales volume	21%	22%	27%	21%	21%
% total sales value of crude oil	7%	8%	8%	7%	8%

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 more the 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 Kazakh Ministry for Oil and Gas; the Company's ability to allocate export volume to different pipelines is, therefore, limited.

REVENUE

The following table shows sales volumes and realised prices for Q3 2010, Q4 2010, Q42009, 12m 2010 and 12m 2009:

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
	(KZT thousands, unless otherwise stated)			%	(KZT thousands, unless otherwise stated)		%
Export sales of crude oil							
UAS pipeline							
Net sales	89,561,927	83,369,774	91,632,184	-2%	345,485,101	313,121,601	10%
Volume (in thousand tonnes)	1,032	1,064	1,180	-13%	4,314	4,947	-13%
Average price (KZT/tonne)	86,748	78,329	77,654	12%	80,086	63,293	27%
Average price (US$/bbl)[1]	81.35	73.50	71.71	13%	75.17	59.35	27%
CPC pipeline							
Net sales	60,452,326	50,560,145	33,565,242	80%	211,081,198	123,693,779	72%
Volume (in thousand tonnes)	672	633	408	65%	2,546	1,999	27%
Average price (KZT/tonne)	89,965	79,875	82,258	9%	82,893	61,389	35%
Average price (US$/bbl)[1]	84.37	74.95	75.96	11%	77.81	57.57	35%
Total sales of crude oil-exported	**150,014,253**	**133,929,918**	**125,197,426**	**20%**	**556,566,299**	**435,815,380**	**28%**
Domestic sales of crude oil							
Domestic sales of crude oil	10,932,163	11,185,692	11,205,243	-2%	40,707,699	36,861,944	10%
Volume (in thousand tonnes)	443	489	576	-23%	1,783	1,959	-9%
Average price (KZT/tonne)	24,665	22,874	19,442	27%	22,830	18,818	21%
Average price (US$/bbl)[1]	23.13	21.46	17.95	29%	21.43	17.65	21%
Total domestic sales of crude oil	**10,932,163**	**11,185,692**	**11,205,243**	**-2%**	**40,707,699**	**36,861,944**	**10%**
Total sales of crude oil							
Total sales of crude oil	160,946,416	145,115,610	136,402,668	18%	597,273,998	472,677,324	26%
Total volume (in thousand tonnes)	2,148	2,186	2,164	-1%	8,643	8,905	-3%
Average price (KZT/tonne)	74,942	66,374	63,021	19%	69,101	53,082	30%
Average price (US$/bbl)[1]	70.28	62.28	58.20	21%	64.86	49.78	30%
Other sales	3,266,441	3,308,765	1,435,899	127%	11,968,400	12,816,155	-7%
Total revenue	**164,212,856**	**148,424,375**	**137,838,567**	**19%**	**609,242,398**	**485,493,479**	**25%**

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

CRUDE OIL SALES IN 2010

The total value of sales of crude oil in 2010, increased by 26% to KZT597 billion compared to 2009. This was due to, a 30% increase in the average sales price and a 3% or 261 thousand tonnes decrease in the volume of sales. The overall decrease in the volume of sales was caused by a reduction in the volume of crude oil produced in comparison with 2009.

EXPORT – UAS PIPELINE

Sales of crude oil exported via the UAS pipeline in 2010 increased by 10% to KZT345 billion owing to the increase of the average sales price by 27% to KZT80,086 per tonne which was partially offset by the decrease of volume exported via the UAS which declined by 633 thousand tonnes, or 13%.

Revenue from export sales through the UAS pipeline in Q4 2010 in comparison with Q4 2009 decreased by 2% owing to a 13% drop in the volume in sales, which were 148 thousand tonnes lower. This effect was partially offset by a 12% increase in the average sales price to KZT86,748 per tonne.

The decrease of sales volume in 2010 was also caused by a 5% decline in OMG oil production, which dropped 292 thousand tonnes, in comparison with 2009 mainly due to walkouts by employees in March 2010.

EXPORT – CPC PIPELINE

In 2010 sales of exported crude oil via the CPC pipeline increased by 72% to KZT211 billion in comparison with 2009. The increase was due to an increase in the average realization price of 35% to KZT82,893 per tonne and the 27% increase of volume exported via the CPC.

Revenues from export sales through the CPC pipeline in Q4 2010 increased by 80% compared with Q4 2009, due to the 9% increase in the average sales price to KZT89,965 and the 65% or 264 thousands tonnes increase in the volume of sales.

DOMESTIC MARKET – SALES OF CRUDE OIL

Domestic sales of crude oil in 2010 increased by 10% to KZT41 billion, compared to 2009, due to a 21% increase in the average sales price. Sales volume decreased by 9% or 176 thousand tonnes.

In Q4 2010 domestic sales decreased by 2% to KZT11 billion, compared with Q4 2009, influenced by the decline in sales volume by 23% or 133 thousand tonnes. However, the average sales price in domestic market increased by 27%.

The following table shows the Company's realized sales prices adjusted for crude oil transport and other expenses for the periods ending 2010, December 31 and 2009, December 31, 2010, September 30.

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
	(US$/bbl)			%	(US$/bbl)		%
UAS							
Benchmark end-market quote[1]	86.46	75.69	74.53	16%	79.18	61.67	28%
Sales price	81.53	73.69	71.76	14%	75.35	59.26	27%
Premium of bbl difference	-0.17	-0.20	-0.05	240%	-0.18	0.09	-300%
Realised price[2]	**81.36**	**73.49**	**71.71**	**13%**	**75.17**	**59.35**	**27%**
Export customs duty – Rent tax	17.70	12.40	11.49	54%	13.82	7.94	74%
Transportation	7.17	7.17	7.38	-3%	7.32	7.32	0%
Sales commissions	0.06	0.06	0.06	0%	0.07	0.06	17%
Netback price	**56.43**	**53.86**	**52.78**	**7%**	**53.96**	**44.03**	**23%**
CPC							
Benchmark end-market quote[1]	86.46	75.69	74.53	16%	79.18	61.67	28%
Sales price	85.28	75.95	73.61	16%	78.70	58.32	35%
Quality bank	-7.75	-7.14	-4.03	92%	-6.98	-5.68	23%
Premium of bbl difference	6.84	6.14	6.39	7%	6.09	4.93	24%
Realised price[2]	**84.37**	**74.95**	**75.97**	**11%**	**77.81**	**57.57**	**35%**
Rent tax-Export customs duty	17.82	12.43	11.49	55%	13.97	7.29	92%
Transportation	8.20	7.79	6.93	18%	7.62	7.15	7%
Sales commissions	0.06	0.06	0.06	0%	0.07	0.06	17%
Netback price	**58.29**	**54.67**	**57.49**	**1%**	**56.15**	**43.07**	**30%**
Domestic Market							
Sales price	23.13	21.46	17.95	29%	21.43	17.65	21%
Transportation	1.92	1.46	1.22	57%	1.58	1.30	22%
Netback price	**21.21**	**20.00**	**16.73**	**27%**	**19.85**	**16.35**	**21%**
Average							
Sales price	71.00	62.95	58.03	22%	65.50	50.06	31%
Quality bank	-2.43	-2.07	-0.76	220%	-2.06	-1.28	61%
Premium of bbl difference	1.71	1.39	0.93	84%	1.41	0.99	42%
Realised price[2]	**70.28**	**62.27**	**58.20**	**21%**	**64.85**	**49.77**	**30%**
Rent tax-Export customs duty	14.09	9.64	8.43	67%	11.01	6.05	82%
Transportation	6.40	6.09	5.74	11%	6.20	5.96	4%
Sales commissions	0.05	0.05	0.04	25%	0.06	0.05	20%
Netback price	**49.74**	**46.49**	**43.99**	**13%**	**47.58**	**37.71**	**26%**

The difference between the benchmark quote and the realized price of sales through the CPC mainly comprises freight expenses, port charges, customs fees, certain sales commissions and averaging effects. Averaging effects usually appear because of the difference between the average mean of 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. The price received for domestic sales of crude oil is determined primarily by the agreement with NC KMG (production cost + 3%).

[1] The Brent (DTD) quoted price is used as benchmark.

[2] Average realized price by financial report converted at 7.23 barrels per tonne of crude oil.

OPERATING EXPENSES

The following table presents a breakdown of the Company's operating expenses:

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
	(KZT thousands, unless otherwise stated)			%	(KZT thousands, unless otherwise stated)		%
Rent tax	28,222,445	22,577,325	20,980,278	35%	97,484,646	58,673,500	66%
Mineral Extraction Tax	19,740,317	17,106,172	15,485,285	27%	70,932,591	55,087,266	29%
Employee benefits	18,342,854	18,543,657	12,957,292	42%	66,241,795	50,876,767	30%
Transportation	15,035,605	14,503,313	13,860,131	8%	57,794,777	53,793,843	7%
Depreciation, depletion and amortization	10,197,074	8,899,214	8,099,843	26%	35,486,128	31,155,360	14%
Repairs, maintenance and other services	8,189,528	8,391,560	5,352,486	53%	28,857,572	21,178,039	36%
Materials and supplies	4,175,255	3,301,757	2,823,961	48%	12,007,713	10,135,010	18%
Energy	2,906,235	2,586,000	2,884,186	1%	10,987 439	10,429,959	5%
Management fees and sales commissions	2,071,698	2,071,169	1,908,184	9%	8,281,574	7,648,453	8%
Export customs duty	5,032,165	1,445,570	-	100%	6,477,735	-	100%
Other taxes	1,284,322	1,258,568	1,917,797	-33%	4,815,027	5,031,000	-4%
Social projects	1,439,694	1,038,781	537,870	168%	4,137,051	2,239,845	85%
Fines and penalties	- 2,626,333	4,390,099	- 4,439,022	-41%	2,805,102	8,132,702	-66%
Loss on disposal of fixed assets	621,334	1,016,838	1,157,634	-46%	2,200,613	2,547,437	-14%
Dry well expense	1,103,615	-	-	100%	1,103,615	-	100%
Geological and geophysical expense	968,648	-	390,950	148%	968,648	390,950	148%
Change in crude oil balance	- 1,728,626	-801,583	73,658	-2447%	-1,538,597	213,835	-820%
Other	4,350,727	3,727,818	6,122,576	-29%	13,449,630	13,071,663	3%
Total	**119,326,557**	**110,056,257**	**90,113,109**	**32%**	**422,493,059**	**330,605,629**	**28%**

Operating expenses in 2010 increased by 28% or KZT91.9 billion, compared to 2009. This is primarily due to the increased rent tax, mineral extraction tax (MET), employee benefits, transportation, depreciation, depletion and amortization, export customs duty, repairs, maintenance and other services.

Rent tax expenses in 2010 increased by 66% in comparison with 2009 due to the increase in crude oil market prices. In 2010 Brent price increased by 28% to 79.18 USD per barrel. As a result, the rent tax rate increased from 12% during 2009 to 16% in 2010.

The increase of Mineral Extraction Tax expenses in 2010 compared to 2009 is due to the increased crude oil market prices, which was partially offset by a decrease in production volume.

Employee benefits expenses for 2010 increased by 30% compared to 2009, owing to the 28% increase in average expenses per employee and 2% increase in number of personnel. The increase of personnel by 294 employees was due to changing production needs. The average salary increased owing to adjustments in the basic tariffs by 9% due to inflation and by 60% - due to the new compensation plan introduced in 01 June, 2010. This was partially offset by the decrease of production personnel bonuses from 80% to 33% in accordance with Labor Code requirements (the variable part of the payroll should not exceed 25%) and strike downtime in OMG from 1 to18 March, 2010.

Transportation expenses increased by 7% compared to 2009 mainly due to the increase in CPC transportation volumes by 27% from 1.99 ktonnes during 2009 to 2.54 ktonnes during 2010 and an increase in depressor mixture expenses by 12% from KZT1,430 to KZT1,600 per tonne. Also "Transneft" increased its tariff for transportation through Russian territory by 10%.

Depreciation, depletion and amortization expenses increased by 14%. This was mainly due to the increased number of production units and an increase in the depletion rate from 10.34% in 2009 to 11.38% in 2010.

Repairs, maintenance and other service expenses increased by 36% and material expenses by 18% compared to 2009. This was caused by an increase in well workovers due to postponed tenders and the delayed signing of contracts in 2009. In 2010 some 1234 well workovers were performed compared with

1206 in 2009 while electric fracturing increased from 143 in 2009 to 188 wells in 2010 and hydrofracturing rose from 120 to 205 wells. Reperforation rose from 409 to 418 wells. Additionally, the cost of materials also increased because of higher prices for solvents, inhibitors and other chemicals.

Energy expenses also increased by 5% owing to an increase in power tariffs and power transmission tariffs from KZT8.71 to KZT14.1 per thousands kilowatt-hours.

Management fees are paid according to the management services agreement with NC KMG adjusted for a budgeted inflation rate of 7.8%.

Export customs duties were introduced starting from August 16, 2010, which was not used in 2009.

The Company committed more funds to social infrastructure projects to finance the "Zharylkau" and "Zhaiyk" social funds, allocating KZT780 and KZT65 millions more than 2009 respectively. It also supported the Atyrau oblast akimat with a KZT750 million for social development

Fines and penalties for the 2010 decreased compared to 2009 due to the following facts: during 2009 the Company provided accruals due to results of Complex Tax Audit for 2004-2005, in contrast during 2010 the Company reversed part of provision related to Transfer Pricing.

Expense related to the disposal of dry exploratory wells occurred due to an increase in the investments program of KMG EP for exploration projects, particularly at the Liman, R-9 and Taisoigan projects. During 2010 wells on R9 block were found to be dry and were subsequently disposed of.

The increase in G&G expenses during 2010 compared to 2009 is due to the increase in 3D and other seismic research expenses mainly for the Liman and R9 fields.

Expenses listed under "Change in crude oil balance" reflect the change in the balance of crude oil stocks at the end of the year.

Other expenses in 2010 compared to 2009 increased mainly due to reversal of bad debt allowance and impairment of investments in KPI in 2009, also by impairment of assets owned by "EmbaEnergoMunai" LLP due to its liquidation.

FINANCE INCOME (COST) AND EXCHANGE RATE DIFFERENCE (NET FINANCE INCOME/EXPENSE)

The Company's financial income in each of the periods relates mainly to interest on deposits, and, when the tenge depreciates, foreign exchange gains. The Company's financial expenses in each of the periods comprise mainly interest on borrowings and the termination of a discount related to asset retirement obligations and historical obligations.

The net financial income for 2010 was KZT27.08 billion which is KZT105.9 billion less than the net financial income for 2009. This was due to the foreign exchange gain of KZT89.53 billion, resulting from devaluation of the tenge in February 2009 and a KZT15.26 billion decrease in interest income. Interest income decreased due to a reduction in the average rate of interest on deposits.

SHARE OF INCOME IN ASSOCIATES AND JOINT VENTURES

The Company's income from its share in associates and joint ventures in 2010 was KZT56.6 billion compared to KZT2.5 billion losses in 2009. Increase is explained by the fact that consolidated financial statements of the Company for the year 2009 included share of income in PetroKazakhstan Inc. from acquisition date December 22, 2009 to December 31 2009. Whereas, share of income in PetroKazakhstan Inc in 2010 was consolidated for a full year. Share of income in JV Kazgermunai LLP increased due to high prices for crude oil in 2010 and decrease in fines and penalties in comparison with 2009. In 2010 income from the share in JV Kazgermunai LLP equaled to KZT22.6 billion and recognition of share in Petrokazakhstan Inc. equaled to KZT34.08 billion.

INCOME TAX EXPENSE

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
	(KZT thousands)			%	(KZT thousands)		%
Profit before tax	83,548,990	71,972,753	44,985,160	86%	291,947,153	285,472,729	2%
Profit before tax (net of JV's results)	51,050,145	45,206,612	48,533,375	5%	213,834,120	287,940,280	-26%
Income tax	5,855,429	15,198,530	15,834,063	-63%	57,445,263	75,745,829	-24%
Effective tax rate	**7%**	**21%**	**35%**	**-80%**	**20%**	**27%**	**-26%**
Effective tax rate (net of JV's results)	**11%**	**34%**	**33%**	**-65%**	**27%**	**26%**	**2%**

The income tax expenses in 2010 decreased mainly due to applied in 2010 double tax depreciation, increased MET, Rent tax, customs duty and salary expenses. The effective tax rate increased to 27% due to huge amount of foreign exchange gain in 2009 which was partially offset by decrease in EPT in 2010.

PROFIT FOR THE PERIOD

As a result of the factors mentioned above, in 2010 the Company's profit for the period increased by 12% to KZT234.5 billion compared to 2009.

OVERVIEW OF JVS AND ASSOCIATES' OPERATIONS

JV KAZGERMUNAI LLP

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

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
Revenue, US$ thousands	414,284	402,196	363,902	14%	1,526,749	1,172,888	30%
Operating expenses, US$ thousands	243,449	202,688	176,083	38%	811,853	736,554	10%
Income tax expense, US$ thousands	115,189	57,166	97,207	18%	285,761	178,553	60%
Net income, US$ thousands	54,795	142,342	61,759	-11%	426,705	228,948	86%
Capital Expenditures, US$ thousands	41,716	24,013	73,549	-43%	74,107	99,683	-26%
Crude oil production, thousand tonnes	748	808	817	-8%	3,102	3,202	-3%
Crude oil sales, thousand tonnes	727	838	775	-6%	3,073	3,037	1%
Export via Kazakh-Chinese pipeline	367	327	355	3%	1,261	1,249	1%
Export via Uzbekistan	-	-	10	-100%	-	10	-100%
Export via Aktau	240	286	280	-14%	1,028	1,163	-12%
Domestic market	120	225	130	-8%	784	615	27%

The Company's share (50%) in Kazgermunai oil production in 2010 was 1 551 thousand tonnes. Capital expenditure for the period was US$74.1 million. The company's share in income of the joint venture agreed to consolidated financial statements of the Company for 2010 is KZT22.6 billion, which is KZT25 billion greater than in 2009. The increase in income is due to a 30% increase in revenue. The Company received dividends for 2010 of KZT47.8 billion from Kazgermunai LLP.

CCEL

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

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
Revenue, US$ thousands	260,656	243,820	195,934	33%	924,424	687,731	34%
Operating expenses, US$ thousands	178,574	194,547	144,353	24%	690,888	568,884	21%
Income tax expense, US$ thousands	29,650	10,520	18,311	62%	59,555	-5,930	-1104%
Net income, US$ thousands	52,432	38,754	33,271	58%	173,981	124,778	39%
Capital expenditures, US$ thousands	33,163	37,617	28,736	15%	109,357	94,612	16%
Crude oil production, thousand tonnes	506	514	460	10%	1,941	1,867	4%
Crude oil sales, thousand tonnes	492	525	430	14%	1,914	1,861	3%
Export via Makhachkala	326	350	281	16%	1,300	1,254	4%
Export via Primorsk	92	80	90	2%	314	419	-25%
Export via Odessa	-	-	-	-	-	6	-100%
Export via Gdansk	20	40	-	-	85	-	-100%
Domestic market	54	55	60	-10%	215	183	18%

For the year 2010 the Company recognized financial income receivable from CCEL (50% share) of KZT3.1 billion and receivables amounted to of KZT20.4 billion. Capital expenses in 2010 were US$109.3 million, which is 16% greater than in 2009. On December 29, 2010 Company received annual guaranteed payment equal to USD26.87 million from CCEL.

PETROKAZAKHSTAN INC.

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

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
Revenue, US$ thousands	951,395	902,444	939,151	1%	3,422,195	2,889,584	18%
Operating expenses, US$ thousands	661,431	298,391	772,176	-14%	1,962,173	2,084,488	-6%
Income tax expense, US$ thousands	113,671	96,725	158,888	-28%	448,617	301,929	49%
Net income, US$ thousands	176,293	507,328	8,087	2080%	1,011,405	503,167	101%
Capital Expenditures	153,881	93,757	121,439	27%	410,582	332,870	23%
Crude oil production, thousand tonnes[1]	1,516	1,311	1,621	-6%	6,053	6,280	-4%
Crude oil sales, thousand tonnes[1]	1,349	1,441	1,471	-8%	5,397	5,252	3%
Export via Kazakh-Chinese pipeline (PKKR + Kolzhan 100%)	643	756	806	-20%	2,816	2,738	3%
Export via - CPT Aktau (KGM 50%)	120	143	137	-12%	514	582	-12%
Export via Kazakh-Chinese pipeline (KGM 50%)	184	161	177	3%	630	624	1%
Export Uzbekistan (TP 50%)	62	52	70	-11%	252	294	-14%
Export via - DDU CPC-K Atyrau (TP 50%)	-	-	35	-100%	-	256	-100%
Export Uzbekistan (KGM 50%)	-	-	5	-100%	-	5	-100%
Export via- DDU A Alashankou, KKT (TP 50%)	211	176	152	38%	684	423	62%
Domestic market- crude oil, th tonnes	129	153	88	46%	501	331	52%
Export oil products, th. tonnes	107	143	195	-45%	579	867	-33%
Domestic market -oil products, th. tonnes	347	472	383	-9%	1,633	1,800	-9%

Actual oil production in 2010 was 6,053 thousand tonnes compared with 6,280 thousand tonnes in 2009. For 2010, the Company recognized share income from its investment in Petrokazakhstan (33% share) of KZT34.08 billion. The Company received dividends in the amount of KZT46.7 billion from PetroKazakhstan in 2010.

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 short-term obligations and pursue investment opportunities.

	Q4 2010	Q3 2010	Q4 2009	Q4 on Q4 change	2010	2009	Change
	(KZT thousands)			%	(KZT thousands)		%
Net cash generated from operating activities	39,321,704	35,387,225	67,322,503	-42%	115,694,318	149,159,221	-22%
Net cash used in investing activities	-56,490,018	81,254,976	-98,871,879	-43%	-31,492,441	- 252,701,063	-88%
Net cash used in financing activities	-10,550,783	-75,576 239	-835,957	1162%	- 93,234,670	- 73,962,333	26%

[1] Including a 50% share in operating results of Turgai Petroleum for FY 2010.

In 2010 net cash generated from operating activities was KZT115.7 billion, decrease of KZT33.4 billion compared to 2009. This change is mainly due to an increase in adjustments for non-cash items, particularly an increase of the share in the income of joint ventures and associates but also by changes in working capital.

Net cash used in investment activities amounted to KZT31.5 billion in 2010. Cash flow was mainly derived from the sale of investments held to maturity to the amount of KZT146.7 billion, dividends received from joint ventures and associates amounting to KZT94.5 billion and interest on deposits amounting to KZT33.9 billion. This effect was offset by the purchase of NC KMG bonds and by the purchase of fixed assets totaling KZT308.2 billion. In 2009, net outflow amounted to 252.7 billion tenge and was associated with the acquisition of investments held to maturity of 242.8 billion.

Net cash outflows from financing activities increased by KZT19.2 billon in 2010 compared with the 2009 results and totaled KZT93.2 billions in 2010. This was mainly due to increase in repayment of borrowings and interest by KZT8.2 and KZT5.7 billions, respectively. In addition, the Company increased dividend payments by KZT2.1 billion and increased repurchase of treasury shares by KZT3.1 billion.

BORROWINGS AND CASH POSITION

The table below shows the Company's net cash for the periods ended December 31, 2010, December 31, 2009 and September 30, 2010:

	As at December 31, 2010	As at September 30, 2010	As at December 31, 2009	December to December change
	(KZT thousands, unless otherwise stated)			%
Current portion	60,194,818	59,074,330	45,650,017	32%
Maturity over 1 year	62,286,045	62,330,689	92,023,143	-32%
Total borrowings	**122,480,863**	**121,405,019**	**137,673,160**	**-11%**
Cash and cash equivalents	98,519,680	126,318,737	107,626,368	-8%
Other current financial assets	377,800,956	302,841,604	534,288,078	-29%
Non-current financial assets	221,825,818	221,780,996	797,931	27 700%
Total financial assets	**698,146,454**	**650,941,337**	**642,712,377**	**9%**
US$-denominated cash and financial assets, %	**81%**	**39%**	**74%**	**7%**
Net cash	**575,665,591**	**529,536,318**	**505,039,217**	**14%**

As of 31 December 2010 total borrowings were KZT122.5 billion, including KZT114.3 billion related to the KMG PKI Finance notes issued in 2006 for the acquisition of a 33% share in PetroKazakhstan Inc.

The increase in financial assets denominated in US dollars was mainly due to the purchase of NC KMG bonds. On July 16, 2010 the Company purchased unsubordinated, coupon indexed, unsecured bonds issued by NC KMG on the Kazakhstan Stock Exchange in the amount of USD1.5 billion.

RISK FACTORS

The Company's activity involves many risks and uncertainties in the economic, political, legislative, social and financial spheres. In making decisions, stakeholders should take into consideration the risk factors that may affect the financial and operational success of the Company.

In order to increase efficiency, maximize value and ensure sustainable development, a risk management system has been introduced into the Company.

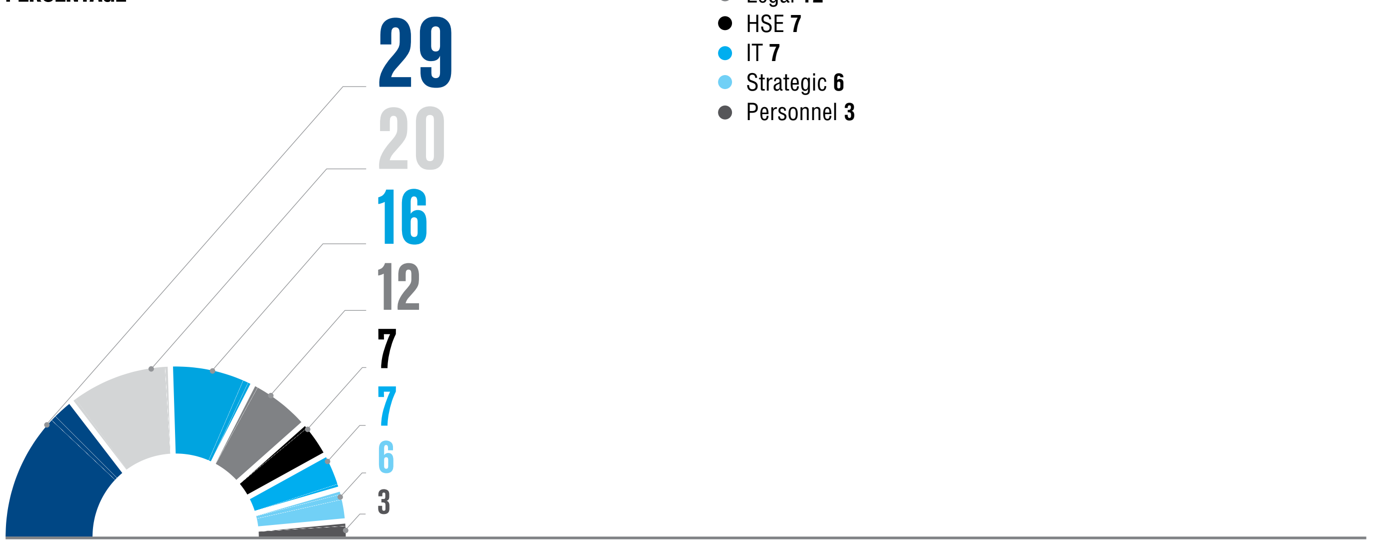
The risk management system forms an integral part of the Company's management system and is a constantly evolving process; in following this process, the Company systematically identifies, evaluates and manages its risk portfolio, analyzing its past, present and future development.

The Company's risk management system includes a system for monitoring the tasks in hand, a procedure for evaluating the efficacy of measures undertaken, and a system for developing strategic and tactical solutions after taking the risk analysis into account.

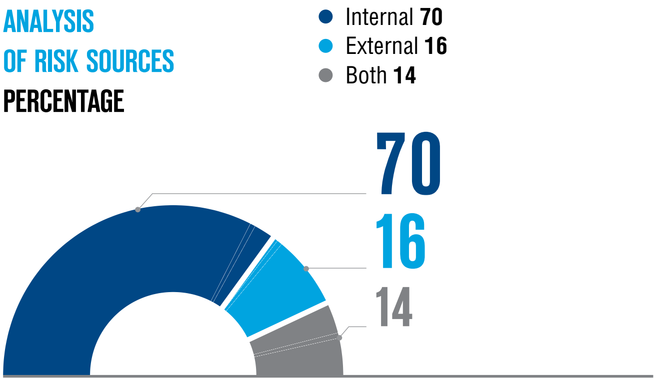
The risk management procedure is carried out by the Board of Directors, the Management Board, the Risk Management Committee, the divisional heads and all employees of the Company. The sharing of responsibility and roles in the risk management process is set out in the Risk Management Policy.

The Company's risk portfolio was formed on the basis of an annual survey and evaluation of risks by the Risk Management Committee (see page 60).

RISK PORTFOLIO CLASSIFIED BY CATEGORIES
PERCENTAGE



ANALYSIS OF RISK SOURCES
PERCENTAGE



Risks from external and internal sources account for respectively 16% and 70% of the Company's risk portfolio.

Internal source risks are fully within the Company's management and control and are directly connected with the efficacy of management and of the internal control system.

External source risks are outside the Company's management and control, but the Company undertakes all possible measures to minimize and reduce such risks.

Some risk information is contained in the Offering Memorandum for Ordinary Shares and GDR, published 29 September 2006; analysis of key financial risks is also contained in annual audited statements (see page 108).

An additional, less than exhaustive list of the main risks is presented below.

EXPLORATION

During geological exploratory work, there is always a risk of non-commercial discovery of hydrocarbon deposits and/or of drilling a 'dry' well. To reduce the risk involved in geological exploration, a set of geoscience tests is carried out. Apart from traditional seismic testing, it includes geochemical testing and high-resolution electrical exploration, as well as special methods of processing seismic and gravity data, and analysis of geological risks.

PRODUCTION

One of the key aims of the Company is to sustain an optimum production level at its own fields, most of which are at advanced stage of production. To this end, the Company uses modern methods and technologies to impact the oil beds and wellbore zones.

The Company carries out a detailed analysis of production risks in order to increase the efficiency of the production process by timely risk identification and management and by ensuring communication, coordination and cross-checking between various levels of production personnel.

Key factors influencing the Company's operations:

- State of the firm's wells.
- Electrical supply.
- Weather conditions.
- Punctual procurement and supply of equipment.
- Quality of equipment supplied.
- Punctuality and quality of service by contractors.
- Strikes by the Company's production personnel.
- Safety of the production personnel.
- Effective planning.
- Ecological safety.
- Observance of state regulatory requirements.

At the same time, the Company's operations are subject to the risk of incidents and breakdowns of the main production equipment. To mitigate these risks, the Company carries out a set of preventive measures and a programme of equipment replacement and overhaul. The main production equipment is insured against loss due to fire, explosion, natural and other hazards; the risk of a well going out of control is also insured.

LABOUR PROTECTION, WORK SAFETY AND ENVIRONMENTAL PROTECTION

The Company's operational activity involves a wide range of health and environmental risks. These may include non-compliance with work safety rules, incidents at work, harm to the environment, ecological pollution and natural disasters. The consequences of these can be most severe, including a fatal accident at work, atmospheric, soil and water pollution, fires, and temporary suspension or complete cessation of business. Depending on the cause of these events, the consequences may negatively affect the Company's reputation, finances and operations. The Company undertakes various measures to prevent the occurrence of such threats, including health and safety checks at work, hazard identification and personnel training. The labour protection, occupational safety and environmental protection systems in the Company are implemented and function in accordance with ISO 14001 and OHSAS 18001 standards. Company annually insures health, safety and environmental risks associated with its activities and projects.

VOLATILITY OF THE PRICE OF CRUDE OIL AND PETROLEUM PRODUCTS

The price of crude and petroleum products is affected by the state of the global economy, political instability or conflicts, actions by the main oil-exporting states, weather and natural disasters. Changes in the price of oil and petroleum products may affect the level of expected profits, investment decision-making and operational activity. Therefore the Company prepares annual budgets and regular forecasts, including sensitivity analysis with regard to various levels of crude oil prices in the future. A certain amount of crude oil is hedged.

STRIKES

Exacerbation of social problems in Kazakhstan, including in the Company's regions of operation, may negatively affect business continuity and cause protests and strikes. As a result, wildcat strikes may have a significant adverse impact on the Company's reputation, operations and finances.

To prevent strikes, it has been explained to the teams in the various departments that any labour disputes must be resolved constructively, via the trade unions. Special conciliatory commissions are formed for resolving labour disputes, with local authorities, trade unions and protesters represented.

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. To minimize the breach or non-performance of obligations, the Company stipulates serious penalties in its contracts and keeps a database of unscrupulous contractors.

CHANGES IN LEGISLATION, TAXATION AND REGULATIONS

Changes of legislation on sub-soil use or in tax and customs regulations may lead to an increase of the Company's fiscal burden, a decrease in its profits, operational difficulties and a reduction of its available investment resources. In response to changes in the tax and customs burden, the Company intends to revise its production and investment plans and amend them as required.

PERSONNEL RISK

Highly qualified personnel are a competitive advantage and a foundation for achieving the Company's strategic goals. Every year, the Company faces the problem of attracting suitably qualified personnel: a problem chiefly due to a shortage of the required experts on the labour market. On the evidence of certain reviews, the Company's current salary level is lower than the market indicators of salary level for comparably financed and operating companies. To reduce this risk, the Company has an employee incentive scheme in order to attract and retain highly qualified personnel. In 2010, by resolution of the Company's Management Board, salaries were recalculated to allow for the level of inflation.

INFORMATION TECHNOLOGY

The Company is exposed to risks in the area of information technology through its dependence on a variety of high-technology hardware and software to maintain effective operations. There may be problems in adapting the new hardware and software and providing for the safe storage of confidential business data. In order to ensure effective work in this area, the Company carries out an annual examination of the technology used and takes care to purchase only the most adaptable and reputable information technology, while ensuring reliable control of access to business data.

9

CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED DECEMBER 31, 2010

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 2010 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 2010, and their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards.

Paul Cohn
Audit Partner

Evgeny Zhemaletdinov
Auditor / General Director
Ernst & Young LLP

11 February 2011

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

TENGE THOUSANDS

		As at December 31,	
	Notes	2010	2009
ASSETS			
Non-current assets			
Property, plant and equipment	5	297,508,553	255,993,908
Intangible assets	6	15,185,859	4,022,140
Investments in joint ventures	8	96,737,910	122,424,309
Investments in associates	9	139,952,442	131,723,609
Receivable from a jointly controlled entity	8	19,153,089	20,268,928
Other financial assets	7	221,825,818	797,931
Deferred tax asset	18	8,408,967	10,265,537
Other assets		13,858,297	7,291,870
Total non-current assets		**812,630,935**	**552,788,232**
Current assets			
Inventories	10	18,779,936	15,525,704
Taxes prepaid and VAT recoverable		26,529,298	9,969,965
Prepaid expenses		27,815,083	21,595,622
Trade and other receivables	7	65,529,767	49,710,916
Receivable from a jointly controlled entity	8	1,203,834	1,082,100
Other financial assets	7	377,800,956	534,288,078
Cash and cash equivalents	7	98,519,680	107,626,368
Total current assets		**616,178,554**	**739,798,753**
Total assets		**1,428,809,489**	**1,292,586,985**

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

TENGE THOUSANDS

(CONTINUED)

		As at December 31,	
	Notes	2010	2009
EQUITY			
Share capital	11	214,081,197	238,546,914
Other capital reserves		1,739,901	1,474,089
Retained earnings		931,455,065	747,820,751
Other components of equity		12,376,574	12,937,395
Total equity		**1,159,652,737**	**1,000,779,149**
LIABILITIES			
Non-current liabilities			
Borrowings	13	62,286,045	92,023,143
Deferred tax liability	18	1,829,852	-
Provisions	14	35,625,247	35,319,443
Total non-current liabilities		**99,741,144**	**127,342,586**
Current liabilities			
Borrowings	13	60,194,818	45,650,017
Income taxes payable		-	21,138,596
Mineral extraction and rent tax payable		46,054,359	36,177,299
Trade and other payables		47,304,799	34,402,259
Provisions	14	15,861,632	27,097,079
Total current liabilities		**169,415,608**	**164,465,250**
Total liabilities		**269,156,752**	**291,807,836**
Total liabilities and equity		**1,428,809,489**	**1,292,586,985**

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

TENGE THOUSANDS

		For the year ended December 31,	
	Notes	2010	2009
Revenue	15	609,242,398	485,493,479
Operating expenses	16	(422,493,059)	(330,605,629)
Profit from operations		**186,749,339**	**154,887,850**
Finance income	17	38,039,785	46,758,905
Finance costs	17	(7,495,555)	(3,241,289)
Foreign exchange (loss) / gain		(3,459,449)	89,534,814
Other income	9	21,471,195	-
Share of result of associates and joint ventures		56,641,838	(2,467,551)
Profit before tax		**291,947,153**	**285,472,729**
Income tax expense	18	(57,445,263)	(75,745,829)
Profit for the year		**234,501,890**	**209,726,900**
Exchange difference on translating foreign operations		(560,821)	13,013,592
Other comprehensive (loss) / income for the year, net of tax		**(560,821)**	**13,013,592**
Total comprehensive income for the year, net of tax		**233,941,069**	**222,740,492**
EARNINGS PER SHARE			
Basic and diluted	12	3.23	2.87

CONSOLIDATED STATEMENT OF CASH FLOWS

TENGE THOUSANDS

		For the year ended December 31,	
	Notes	2010	2009
Cash flows from operating activities			
Profit before tax		291,947,153	285,472,729
Adjustments to add / (deduct) non-cash items			
Depreciation, depletion and amortization	5, 6	35,486,128	31,155,359
Other income	9	(21,471,195)	-
Share of result of associates and joint ventures		(56,641,838)	2,467,551
Settlement of crude oil under the terms of a pre-export financing agreement		-	(10,830,585)
Loss on disposal of property, plant and equipment (PPE)		2,200,613	2,547,437
Impairment / (reversal of impairment) of PPE	5	16,194	(590,558)
Dry well expense on exploration and evaluation assets	6	1,103,615	-
Recognition of share-based payments		309,987	248,106
Forfeiture of share-based payments		(49,809)	(164,690)
Unrealised foreign exchange gain on non-operating activities		(73,832)	(7,993,206)
Other non-cash income and expense		916,338	2,673,712
Add finance costs		7,495,555	3,241,289
Deduct finance income relating to investing activity		(38,039,785)	(46,758,905)
Working capital adjustments			
Change in other assets		630,450	(4,352,007)
Change in inventories		(3,463,525)	(1,282,335)
Change in taxes prepaid and VAT recoverable		(11,312,224)	(2,818,233)
Change in prepaid expenses		(6,351,679)	(13,762,247)
Change in trade and other receivables		(18,377,144)	(9,697,855)
Change in trade and other payables		10,918,152	(6,558,436)
Change in mineral extraction and rent tax payable		9,877,060	36,177,299
Change in provisions		3,500,215	5,670,976
Income tax paid		(92,926,111)	(115,686,180)
Net cash generated from operating activities		**115,694,318**	**149,159,221**

CONSOLIDATED STATEMENT OF CASH FLOWS

TENGE THOUSANDS

(CONTINUED)

		For the year ended December 31,	
	Notes	2010	2009
Cash flows from investing activities			
Purchases of PPE		(86,679,884)	(42,844,814)
Proceeds from sale of PPE		139,497	1,221,183
Purchases of intangible assets		(1,572,033)	(497,033)
Contribution to the capital of a joint venture		-	(3,043,907)
Dividends received from joint ventures and associates	8, 9	94,458,518	3,768,250
Purchase of investments in debt instruments of NC KMG	7	(221,543,183)	-
Interest received from investment in debt instruments of NC KMG		7,691,113	-
Sale / (purchase) of financial assets held-to-maturity		146,680,715	(242,838,804)
Loan repayments received from related parties		3,959,137	5,028,216
Acquisition of subsidiary, net of cash acquired		(8,614,935)	459,646
Interest received		33,988,614	26,046,200
Net cash used in investing activities		**(31,492,441)**	**(252,701,063)**
Cash flows from financing activities			
Purchase of treasury shares	11	(24,531,975)	(21,392,129)
Repayment of borrowings		(14,614,702)	(6,352,778)
Dividends paid to Company's shareholders		(48,235,969)	(46,108,343)
Interest paid		(5,852,024)	(109,083)
Net cash used in financing activities		**(93,234,670)**	**(73,962,333)**
Net change in cash and cash equivalents		(9,032,793)	(177,504,175)
Cash and cash equivalents at beginning of the year	7	107,626,368	285,131,743
Exchange losses on cash and cash equivalents		(73,895)	(1,200)
Cash and cash equivalents at end of the year	**7**	**98,519,680**	**107,626,368**

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

TENGE THOUSANDS

	Share capital	Treasury stock	Other capital reserves	Retained earnings	Foreign currency translation reserve	Total Equity
As at January 1, 2009	**263,094,581**	**(3,369,734)**	**1,385,036**	**586,058,950**	**(76,197)**	**847,092,636**
Profit for the year	-	-	-	209,726,900	-	209,726,900
Other comprehensive income	-	-	-	-	13,013,592	13,013,592
Total comprehensive income	**-**	**-**	**-**	**209,726,900**	**13,013,592**	**222,740,492**
Recognition of share-based payments	-	-	248,106	-	-	248,106
Forfeiture of share-based payments	-	-	(164,690)	-	-	(164,690)
Exercise of employee options	-	203,266	5,637	-	-	208,903
Share buy back (Note 11)	-	(21,381,199)	-	-	-	(21,381,199)
Dividends (Note 11)	-	-	-	(47,965,099)	-	(47,965,099)
As at December 31, 2009	**263,094,581**	**(24,547,667)**	**1,474,089**	**747,820,751**	**12,937,395**	**1,000,779,149**
Profit for the year	-	-	-	234,501,890	-	234,501,890
Other comprehensive loss	-	-	-	-	(560,821)	(560,821)
Total comprehensive income	**-**	**-**	**-**	**234,501,890**	**(560,821)**	**233,941,069**
Recognition of share-based payments	-	-	309,987	-	-	309,987
Forfeiture of share-based payments	-	-	(49,809)	-	-	(49,809)
Exercise of employee options	-	66,258	5,634	-	-	71,892
Share buy back (Note 11)	-	(24,531,975)	-	-	-	(24,531,975)
Dividends (Note 11)	-	-	-	(50,867,576)	-	(50,867,576)
As at December 31, 2010	**263,094,581**	**(49,013,384)**	**1,739,901**	**931,455,065**	**12,376,574**	**1,159,652,737**

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

TENGE THOUSANDS UNLESS OTHERWISE STATED

1. ORGANIZATION AND PRINCIPAL ACTIVITIES

KazMunaiGas Exploration Production Joint Stock Company (the "Company") has been 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 60.50% of the Company's outstanding shares as at December 31, 2010 (2009: 59.38%). The Parent Company is 100% owned by joint stock company Samruk-Kazyna National Welfare Fund ("Samruk-Kazyna NWF") which in turn is 100% owned by the government of the Republic of Kazakhstan (the "Government").

The Company conducts its principal operations through the UzenMunaiGas and EmbaMunaiGas production divisions. In addition the Company has oil and gas interests in the form of wholly owned subsidiaries, jointly controlled entities, associates 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 thousand 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 3.

ADOPTED ACCOUNTING STANDARDS AND INTERPRETATIONS

The Company has adopted the following new and amended IFRS and International Financial Reporting Interpretations Committee ("IFRIC") interpretations during the year, which did not have any material effect on the financial performance or position of the Company.

- IAS 27 Consolidated and Separate Financial Statements – amendment
- IAS 39 Financial Instruments: Recognition and Measurement – Eligible Hedged Items
- IFRS 1 First-time Adoption of International Financial Reporting Standards – Additional Exemptions for First-time Adopters
- IFRS 1 First-time Adoption of International Financial Reporting Standards – Structural Amendmend
- IFRS 2 Group Cash-settled Share-based Payment Transactions
- IFRS 3R Business Combinations
- IFRIC 17 Distributions of Non-cash Assets to Owners
- Improvements to IFRSs (April 2009)

NEW ACCOUNTING DEVELOPMENTS

The following IFRS, IFRIC interpretations and improvements to IFRS are not yet in effect for the year ended December 31, 2010:

- IAS 24 Related Party Disclosures – amendment

- IAS 32 Financial Instruments: Presentation - Classification of right issues
- IFRS 9 Financial Instruments: Classification and measurement
- IFRS 1 First-time Adoption of International Financial Reporting Standards – Limited exemption from Comparative IFRS 7 Disclosures
- IFRIC 14 Prepayments of a minimum funding requirement (amendment)
- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments
- IAS 12 Recovery of Underlying Assets
- IFRS 1 Severe Hyperinflation and Removal of Fixed Dates for First-Time Adopters
- IFRS 7 New disclosures for derecognition of financial instruments.
- Improvements to IFRSs (May 2010)

Management does not expect the above standards and interpretations to have a material impact on the Company's financial position or results of operations.

2.2 RECLASSIFICATIONS

In 2010, the Company reviewed the presentation of exploration and evaluation assets in the consolidated statement of financial position and has determined that a better presentation of the exploration and evaluation assets is to record them within intangible assets rather than property, plant and equipment. As a result exploration and evaluation assets as at December 31, 2009 have been reclassified from property, plant and equipment to intangible assets in the amount of 1,745,395 thousand Tenge.

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.

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 are 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 are 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).

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 natural 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.

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 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.

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.

2.11 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, demand 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.

2.14 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 112,140 Tenge per month in 2010 (2009: 101,025 Tenge per month in first six months of 2009 and 102,877 Tenge per month in last six months of 2009). 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 offloaded 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.

2.20 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 ACCOUNTING ESTIMATES AND JUDGMENTS

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.

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. 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 13.93% and 12.8% of the provision at December 31, 2010 and 2009 relates to final closure costs, respectively. 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, 2010 were 5.0% and 7.9% respectively (2009: 5.0% and 7.9%). Movements in the provision for asset retirement obligations are disclosed in Note 14.

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 an undiscounted basis if the timing of the procedures has not been agreed with the relevant authorities. 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. Accordingly, the liability has not been discounted as the terms of the liability have not yet been established. The Company has classified this obligation as non-current except for the portion of costs, included in the annual budget for 2011. 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 22. Movements in the provision for environmental remediation obligations are disclosed in Note 14.

TAXATION

Taxable income is computed in accordance with the tax legislation enacted as of January 1, 2009. The Company accrues and pays corporate income tax (CIT) at a rate of 20% of taxable income in 2010. In November 2010 the Government of the Republic of Kazakhstan passed legislation, which was enacted as of January 1, 2011 cancelling the initially adopted gradual reduction of CIT rates and confirming the CIT rate at 20% for the foreseeable future. The above legislation also eliminated the planned increase of the mineral extraction tax (MET) rates.

Deferred tax is calculated with respect to both CIT and 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 above mentioned new tax code disclosed in Note 18.

4. BUSINESS COMBINATIONS

ACQUISITION OF NBK LLP ("NBK")

On September 24, 2010 the Company acquired a 100% interest in NBK. NBK is an oil and gas company, which has a license for the exploration and production of the West Novobogatinksoye oil field located in Atyrau oblast of the Republic of Kazakhstan.

The acquired company is currently in the exploration stage and has rights to sell test production from four successful exploration wells over the period of exploration. The interest in NBK was acquired for cash consideration of 35,000 thousand US Dollars (5,162,150 thousands Tenge). The Company paid 90% of the consideration and withheld the remaining 10%, subject to the vendor completing their obligations under the sale purchase agreement. Subsequent to the acquisition, NBK's exploration license was extended to September 2012 from September 2010.

NBK's assets and liabilities, based on the allocation of the consideration over the fair values of the identifiable net assets, as at September 24, 2010 and the corresponding carrying amounts immediately before the acquisition and as at December 31, 2010 are as follows:

	Carrying values as at September 24, 2010	Fair values as at September 24, 2010	Assets and liabilities as at December 31, 2010
Cash	212	212	77,001
Current assets	11,768	11,768	53,460
Non-current assets	1,343,003	6,161,767	5,618,324
	1,354,983	6,173,747	5,748,785
Current liabilities	19,494	19,494	51,921
Non-current liabilities	28,350	992,103	992,103
	47,844	1,011,597	1,044,024
Net assets	**1,307,139**	**5,162,150**	**4,704,761**

The difference of 3,855,011 thousand Tenge between the consideration paid for and the carrying value of the net assets acquired has been wholly attributed to the value of the exploration and production license of NBK.

The results of operations of NBK for the period from the acquisition date to the year end were included into the consolidated financial statements of the Company and comprised a loss of 544,919 thousand Tenge.

ACQUISITIONS OF SAPABARLAU SERVICE LLP ("SBS")

On September 24, 2010 the Company acquired a 100% interest in SBS. SBS is an oil and gas company, which has a license for the exploration of the East Zharkamys I field located in Aktobe oblast of the Republic of Kazakhstan. The interest in SBS was acquired for cash consideration of 4,410,000 thousand Tenge. The Company paid 90% of the consideration and withheld 10%, subject to the vendor completing their obligations under the sale purchase agreement. Subsequent to acquisition, SBS's exploration license was extended to November 2012 from November 2010.

SBS's assets and liabilities, based on the allocation of the consideration over the fair values of the identifiable net assets, as at September 24, 2010 and the corresponding carrying amounts immediately before the acquisition and as at December 31, 2010 are as follows:

	Carrying values as at September 24, 2010	Fair values as at September 24, 2010	Assets and liabilities as at December 31, 2010
Cash	1,968	1,968	47,800
Current assets	2,502	2,502	1,744
Non-current assets	1,144,484	5,474,983	5,040,257
	1,148,954	5,479,453	5,089,801
Current liabilities	194,401	194,401	2,572
Non-current liabilities	8,952	875,052	875,052
	203,353	1,069,453	877,624
Net assets	**945,601**	**4,410,000**	**4,212,177**

The difference of 3,464,399 thousand Tenge between the consideration paid for and the carrying value of the net assets acquired has been wholly attributed to the value of the exploration license of SBS.

The results of operations of SBS for the period from the acquisition date to the year end were included into the consolidated financial statements of the Company and comprised a loss of 480,000 thousand Tenge.

5. PROPERTY, PLANT AND EQUIPMENT

	Oil and gas properties	Other assets	Construction work-in-progress	Total
2009				
Opening net book amount at January 1, 2009	207,361,723	28,813,068	11,446,502	247,621,293
Additions	1,014,674	1,253,022	41,296,702	43,564,398
Change in ARO estimate	(794,517)	-	-	(794,517)
Disposals	(2,468,772)	(380,150)	(1,999,246)	(4,848,168)
Transfers from work-in-progress	35,083,465	6,285,162	(41,368,627)	-
Internal transfers	483,912	(496,180)	12,268	-
Depreciation charge	(26,166,197)	(3,973,459)	-	(30,139,656)
(Impairment) / reversal	-	(791,888)	1,382,446	590,558
Closing net book amount at December 31, 2009	**214,514,288**	**30,709,575**	**10,770,045**	**255,993,908**
At December 31, 2009				
Cost	362,550,961	46,672,242	10,770,045	419,993,248
Accumulated depreciation	(148,036,673)	(15,962,667)	-	(163,999,340)
Net book amount	**214,514,288**	**30,709,575**	**10,770,045**	**255,993,908**
2010				
Opening net book amount at January 1, 2010	214,514,288	30,709,575	10,770,045	255,993,908
Additions	2,009,579	806,415	77,576,377	80,392,371
Change in ARO estimate	(542,101)	-	-	(542,101)
Disposals	(2,394,841)	(242,585)	(1,849,502)	(4,486,928)
Transfers from work-in-progress	70,757,966	4,686,423	(75,444,389)	-
Internal transfers	190,187	(191,374)	1,187	-
Depreciation charge	(29,503,722)	(4,328,781)	-	(33,832,503)
Impairment	(790)	(3,099)	(12,305)	(16,194)
Closing net book amount at December 31, 2010	**255,030,566**	**31,436,574**	**11,041,413**	**297,508,553**
At December 31, 2010				
Cost	428,871,355	51,045,927	11,041,413	490,958,695
Accumulated depreciation	(173,840,789)	(19,609,353)	-	(193,450,142)
Net book amount	**255,030,566**	**31,436,574**	**11,041,413**	**297,508,553**

6. INTANGIBLE ASSETS

	Exploration and evaluation assets	Other intangibles	Total
2009			
Opening net book amount at January 1, 2009	1,729,860	2,401,553	4,131,413
Additions	445,764	487,845	933,609
Disposals	-	(27,179)	(27,179)
Amortization charge	(430,229)	(585,474)	(1,015,703)
Closing net book amount at December 31, 2009	**1,745,395**	**2,276,745**	**4,022,140**
At December 31, 2009			
Cost	10,588,798	4,175,304	14,764,102
Accumulated amortization	(8,843,403)	(1,898,559)	(10,741,962)
Net book amount	**1,745,395**	**2,276,745**	**4,022,140**
2010			
Opening net book amount at January 1, 2010	1,745,395	2,276,745	4,022,140
Additions	13,068,275	858,857	13,927,132
Disposals	-	(6,173)	(6,173)
Deletions	(1,103,615)	-	(1,103,615)
Amortization charge	(954,694)	(698,931)	(1,653,625)
Closing net book amount at December 31, 2010	**12,755,361**	**2,430,498**	**15,185,859**
At December 31, 2010			
Cost	22,553,458	5,027,989	27,581,447
Accumulated amortization	(9,798,097)	(2,597,491)	(12,395,588)
Net book amount	**12,755,361**	**2,430,498**	**15,185,859**

Additions in 2010 relate primarily to the licenses acquired in NBK and SBS acquisitions (Note 4).

In 2010 the Company recognized dry well expense related to three exploratory wells drilled on its R-9 block in the amount of 1,103,615 thousand Tenge.

7. FINANCIAL ASSETS

OTHER FINANCIAL ASSETS

	2010	2009
Investments in debt instruments of NC KMG	220,710,987	-
Tenge denominated term deposits	953,920	636,520
Other	160,911	161,411
Total non-current	**221,825,818**	**797,931**
US dollar denominated term deposits	264,841,437	447,254,500
Tenge denominated term deposits	57,786,248	87,033,308
Held-to-maturity financial assets	54,916,073	-
Investments in debt instrument of NC KMG	256,928	-
Other	270	270
Total current	**377,800,956**	**534,288,078**
	599,626,774	**535,086,009**

The weighted average interest rate on US dollar denominated term deposits in 2010 was 6.6% (2009: 9.3%). The weighted average interest rate on Tenge denominated term deposits in 2010 was 4.7% (2009: 7.9%).

As at December 31, 2010 the current US dollar denominated term deposits include restricted cash of 27,639,860 thousand Tenge (2009: 9,840,620), which is kept in a blocked account as security for the repayment of interest and principal on the long term debt of KazMunaiGaz PKI Finance B.V. (KMG PKI Finance), a 100% subsidiary of the Company (Notes 9 and 13).

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 221,543,183 thousand 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, 2010 the outstanding amount of the Debt Instrument and related accrued interest is 220,710,987 thousand Tenge and 256,928 thousand Tenge respectively.

The Debt Instrument contains the following key provisions:

i. 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.

ii. 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.

iii. 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.

iv. 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

	2010	2009
Trade receivables	65,367,737	49,398,083
Other	439,253	523,914
Allowance for doubtful receivables	(277,223)	(211,081)
	65,529,767	**49,710,916**

As of December 31, 2010 US dollar denominated trade and other receivables represented 93% of total receivables (2009: 90%). The remaining balances are Tenge denominated. Trade receivables are non-interest bearing and are generally on 30 days' terms.

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

	2010	2009
Current	58,298,195	49,689,150
0 – 30 days overdue	7,222,973	2,442
120 and more days overdue	8,599	19,324
	65,529,767	**49,710,916**

CASH AND CASH EQUIVALENTS

	2010	2009
US dollar denominated term deposits with banks	75,315,631	8,041,112
Tenge denominated term deposits with banks	12,982,717	71,469,368
Euro denominated term deposits with banks	394,734	641,004
US dollar denominated cash in banks and on hand	5,067,220	20,541,767
Tenge denominated cash in banks and on hand	3,880,555	6,933,117
GBP denominated cash in bank and on hand	878,823	-
	98,519,680	**107,626,368**

Cash with banks earns interest at floating rates based on daily bank deposit rates. Short-term deposits 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 short-term deposit rates.

The weighted average interest rate on Tenge denominated deposits in 2010 was 1.9% (2009: 6.2%). The weighted average interest rate on US dollar denominated deposits in 2010 was 0.2% (2009: 3.0%).

8. INVESTMENTS IN JOINT VENTURE AND RECEIVABLE FROM A JOINTLY CONTROLLED ENTITY

	2010	2009
Interest in JV Kazgermunai LLP (“Kazgermunai”)	96,737,910	122,424,309
Receivable from jointly controlled entity	20,356,923	21,351,028
	117,094,833	**143,775,337**

JV KAZGERMUNAI

On April 24, 2007 the Company acquired from NC KMG a 50% joint venture interest in Kazgermunai, which is involved in oil and natural gas production in south central Kazakhstan.

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

	2010	2009
Cash	14,503,911	28,182,715
Current assets	9,998,641	8,219,342
Non-current assets	125,855,630	127,628,947
	150,358,182	164,031,004
Current liabilities	21,808,244	16,472,625
Non-current liabilities	31,812,028	25,134,070
	53,620,272	41,606,695
Net assets	**96,737,910**	**122,424,309**

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

	2010	2009
Revenues	112,478,772	86,500,472
Operating expenses	(73,201,797)	(69,279,410)
Profit from operations	39,276,975	17,221,062
Finance cost, net	(169,169)	(2,092,941)
Profit before tax	39,107,806	15,128,121
Income tax expense	(16,550,967)	(17,525,803)
Profit (loss) for the year	**22,556,839**	**(2,397,682)**
Foreign currency translation (loss) gain recognized in other comprehensive income	**(460,988)**	**7,775,291**

Profit for the year in 2010 is net of the effect of amortization of the fair valuation of the licenses in the amount of 10,175,494 thousand Tenge (2009: 10,642,389 thousand Tenge) and related deferred tax benefit of 1,129,711 thousand Tenge (2009: deferred tax expense of 8,640,105 thousand Tenge).

During 2010 the Company received dividends from Kazgermunai in the amount of 47,782,250 thousand Tenge (2009: 3,768,250 thousand Tenge).

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 amounted to 753.2 million US dollars (111,019,849 thousand Tenge) as at December 31, 2010 (2009: 790.5 million US dollars or 117,288,512 thousand 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, 2010, amounted to 135.9 million US dollars (20,027,909 thousand Tenge) (2009: 141.7 million US dollars equivalent to 21,022,017 thousand Tenge).

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. 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:

	2010	2009
Current assets	25,459,836	27,436,006
Non-current assets	119,535,632	112,162,558
	144,995,468	139,598,564
Current liabilities	23,498,775	11,680,985
Non-current liabilities	121,496,693	127,917,579
	144,995,468	139,598,564
Net assets	-	-

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

9. INVESTMENTS IN ASSOCIATES

	2010	2009
Interest in Petrokazakhstan Inc. (“PKI”)	139,164,657	130,962,455
Other	787,785	761,154
	139,952,442	**131,723,609**

PETROKAZAKHSTAN INC.

On December 22, 2009 the Company acquired from NC KMG 100% of the common shares of KMG PKI Finance. The shares were acquired for cash consideration of 100,500 thousand US dollars (14,930,515 thousand Tenge). KMG PKI Finance holds a 33% equity interest in PKI, which is involved in exploration, development and production of hydrocarbons in south central Kazakhstan as well as sales of oil and oil products.

This acquisition of KMG PKI Finance does not represent a business combination and accordingly the Company accounted for this transaction as an acquisition of assets and liabilities. KMG PKI Finance’s investment in PKI is recognized as an investment in associate in the consolidated financial statements of the Company.

The Company capitalized transaction costs of 5,675 thousand US dollars (846,066 thousand Tenge) directly attributable to this acquisition.

The consideration was allocated between the assets and liabilities using the fair values at the date of acquisition as follows:

	Fair values as at December 22, 2009
Equity interest in PKI	130,980,827
Cash and cash equivalents	3,361,953
Other assets	10,465,851
Borrowings	(128,983,948)
Other payables	(48,102)
	15,776,581

As at December 22, 2009, other assets include restricted cash of 66,329 thousand US dollars (9,855,848 thousand Tenge), which is placed on the bank term deposits in accordance with the terms of KMG PKI Finance notes (Note 13).

The Company’s share of PKI’s assets and liabilities as at December 31 are as follows:

	2010	2009
Cash	12,908,371	12,376,980
Current assets	33,467,489	51,347,630
Non-current assets	199,098,292	143,541,055
	245,474,152	207,265,665
Current liabilities	69,317,233	22,436,202
Non-current liabilities	36,992,262	53,867,008
	106,309,495	76,303,210
Net assets	**139,164,657**	**130,962,455**

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

	2010	2009
Revenue	166,399,322	3,489,068
Operating expenses	(122,656,203)	(2,851,783)
Profit from operations	43,743,119	637,285
Gain on Turgai Petroleum (TP) re-acquisition	13,242,336	-
Finance cost, net	(988,517)	(12,725)
Profit before tax	55,996,938	624,560
Income tax expense	(21,813,358)	(366,019)
Profit for the period	**34,183,580**	**258,541**
Foreign currency translation loss recognized in other comprehensive income	**(776,305)**	**(276,913)**

Profit for the year in 2010 is net of the effect of amortization of the fair valuation of the licenses in the amount of 13,638,372 thousand Tenge (from acquisition date to December 31, 2009: 349,015 thousand Tenge) and write off of the fair valuation of inventory in the amount of 4,337,420 thousand Tenge.

During 2010 the Company received dividends from PKI in the amount of 46,676,268 thousand Tenge (2009: nil).

During 2006 PKI and Lukoil Overseas Kumkol B.V. ("Lukoil") commenced arbitration claims against each other in the Stockholm Chamber of Commerce ("the Tribunal"). On October 28, 2009, the Tribunal issued an award, where Lukoil was entitled to acquire 50% of TP from PKI and to receive compensation by way of damages and accrued interest on such damages. Starting from October 28, 2009 PKI ceased consolidation of TP's results in its consolidated financial statement for the year ended December 31, 2009.

On August 16, 2010 PKI and Lukoil have entered into an Amicable Agreement (hereinafter – the Agreement) with respect to the TP dispute. According to the Agreement the ownership structure of TP remains unchanged: PKI and Lukoil will continue to jointly own TP in equal shares. Furthermore, PKI paid to Lukoil an amount of 438.4 million US Dollars as compensation for damages.

As a result of the Agreement, PKI accounted for the re-acquisition of a 50% interest in TP in its consolidated financial statements for the year ended December 31, 2010, based on the assessment of fair values of the identifiable assets, liabilities and contingent liabilities of TP as at the acquisition date. The Company accordingly reflected this in its consolidated financial statements for the year ended December 31, 2010. The resulting share of gain in the amount of 90 million US Dollars (13,242,336 thousand Tenge) was recognized by the Company in 2010.

With regard to the compensation to Lukoil, CNPC Exploration and Development Company Limited ("CNPC E&D") and the Company entered into a separate Agreement on Principles (the "AOP") on July 28, 2010. In accordance with AOP the Company's share of the compensation to Lukoil was paid by PKI after they secured a loan for this purpose. At the same time, CNPC E&D made a contribution to the share capital of PKI in the amount of 441.6 million US Dollars which is equal to the principal amount of the loan taken by PKI, inclusive of financing costs. The Company was held harmless in respect of any liability in relation to the payment of the compensation or any loss relating to such liability, and retained its 33% interest. Consequently, the Company recognized in 2010 the resulting gain of 145.7 million USD Dollars (21,471,195 thousand Tenge) within other income.

10. INVENTORIES

	2010	2009
Materials, at cost	8,881,241	7,165,606
Crude oil, at cost	9,898,695	8,360,098
	18,779,936	**15,525,704**

As at December 31, 2010 the Company had 347,685 tons (2009: 380,703 tons) of crude oil in storage and transit.

11. SHARE CAPITAL

	Shares outstanding (number of shares)				
	Common shares	Preferred shares	Common shares	Preferred shares	Total share capital
As at January 1, 2009	**69,910,396**	**4,136,107**	**258,690,820**	**1,034,027**	**259,724,847**
Reduction of treasury stock due to exercise of share options	12,528	-	203,266	-	203,266
Increase of treasury stock due to share repurchases	(1,499,180)	-	(21,381,199)	-	(21,381,199)
As at December 31, 2009	**68,423,744**	**4,136,107**	**237,512,887**	**1,034,027**	**238,546,914**
Reduction of treasury stock due to exercise of share options	5,927	-	66,258	-	66,258
Increase of treasury stock due to share repurchases	-	(1,346,213)	-	(24,531,975)	(24,531,975)
As at December 31, 2010	**68,429,671**	**2,789,894**	**237,579,145**	**(23,497,948)**	**214,081,197**

The Kazakhstan Stock Exchange has enacted on October 11, 2010 a requirement for disclosure of the total equity less other intangible assets (Note 6) per shares outstanding as at year end. As at December 31, 2010 the amount per share outstanding is 16,249 Tenge.

11.1 SHARE CAPITAL

AUTHORIZED SHARES

The total number of authorized ordinary and preferred shares is 70,220,935 (2009: 70,220,935) and 4,136,107 (2009: 4,136,107), respectively. 43,087,006 of the outstanding common shares are owned by the Parent as at December 31, 2010 (2009: 43,087,006). Ordinary and preferred 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 the period amounted to 704 Tenge per share (2009: 656 Tenge per share) for both of the outstanding ordinary and preferred shares as at June 7, 2010, the date of record.

11.2 EMPLOYEE SHARE OPTION PLANS

The expense recognized for share option plans related to employee services received during the year is 309,987 thousand Tenge (2009: 248,106 thousand 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 incentivise 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.

INITIAL PUBLIC OFFERING (“IPO”) PLAN

Following the Company’s 2006 IPO a one off award of zero exercise price GDRs was made to key employees, senior executives and directors to reward them for contributions towards a successful IPO. The grant date for the IPO award was December 29, 2006. The options vested on December 29, 2006 and the entire allotment was exercised within one month of their vesting.

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:

	2010		2009	
	No.	WAEP	No.	WAEP
Outstanding at January 1	1,384,542	17.41	808,701	14.82
Granted during the year	1,028,436	19.27	746,805	13.42
Exercised during the year	(35,561)	15.71	(109,093)	14.99
Forfeited during the year	(131,222)	19.11	(61,871)	21.18
Outstanding at December 31	2,246,195	18.15	1,384,542	17.41
Exercisable at December 31	543,641	21.83	257,823	15.25

The weighted average remaining contractual life for share options outstanding as at December 31, 2010 is 6.24 years (2009: 6.12 years). The range of exercise price for options outstanding at December 31, 2010 was 13.00 US Dollars -26.47 US dollars per GDR (2009: 13.00 US Dollars -26.47 US Dollars).

The EOP 1, EOP 2 and IPO plan are equity settled plans and the fair value is measured at the grant date.

12. EARNINGS PER SHARE

	2010	2009
Weighted average number of all shares outstanding	72,561,873	73,057,697
Profit for the year	234,501,890	209,726,900
Basic and diluted earnings per share	3.23	2.87

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

13. BORROWINGS

	2010	2009
Fixed interest rate borrowings	8,146,065	8,690,190
Weighted average effective interest rate	7.42%	7.45%
Floating interest rate borrowings	114,334,798	128,982,970
Weighted average effective interest rates	4.74%	5.41%
Total borrowings	**122,480,863**	**137,673,160**
Non-current	62,286,045	92,023,143
Current	60,194,818	45,650,017

The Company's borrowings are denominated in US dollars. The fixed rate borrowings (2010: 6,795,238 thousand Tenge, 2009: 7,330,565 thousand Tenge), primarily relate to an obligation to reimburse historical costs incurred by the Government prior to the acquisition of licenses by the Company, which will expire on December 31, 2025. The Company has discounted this obligation at an interest rate of 7.93% and accounts for these borrowings at amortized cost.

The Company's floating interest rate borrowings relate to KMG PKI Finance notes, which were issued in 2006 relating to the acquisition of 33% equity interest in PKI (Note 9). On July 5, 2006 KMG PKI Finance issued floating rate notes in the amount of 1,374,500 thousand US dollars. As at December 31, 2010 the outstanding amounts of the notes and related accrued interest are 760,034 thousand US dollars and 15,643 thousand US dollars, respectively (112,029,012 thousand Tenge and 2,305,786 thousand Tenge, respectively) (2009: 850,010 thousands US dollars and 19,382 thousands US dollars respectively or 126,107,460 thousand Tenge and 2,875,510 thousand Tenge, respectively). There is no recourse to the Company or its assets, except for:

i) a share pledge over all KMG PKI Finance rights, benefits and title in the 33% of the equity interest in PKI

ii) 80% of any dividend or distribution made from PKI is restricted for further redemption of principal and accrued interest on notes

The notes bear interest at twelve months LIBOR plus a margin of 2.9073%. The notes are redeemed at one seventh of the principal and accrued interest on the first Monday of July every year to the extent of the restricted cash balance. As this loan is non-recourse, any outstanding annual principal and interest of the notes will be deferred to be due and payable on the next payment date and bear interest at the rate applicable for the interest period concerned. If KMG PKI Finance fails to repay the aggregate of any deferred principal and interest outstanding at the expiry of the initial period in July 2013, KMG PKI Finance may seek to redeem the outstanding amount on each of the eighth, ninth and tenth years after the issuance date. Whether KMG PKI Finance will be permitted to redeem the outstanding amount in eighth, ninth and tenth years after the issuance date will be at the discretion of the trustee. As at December 31, 2010 the deferred principal comprises 183,558 thousand US dollars (27,056,450 thousand Tenge) (2009: 79,463 thousand US dollars or 11,789,187 thousand Tenge).

14. PROVISIONS

	Environmental remediation	Taxes	Asset retirement obligation	Other	Total
At January 1, 2009	**25,505,339**	**18,840,500**	**15,183,703**	**4,284,363**	**63,813,905**
Additional provisions	-	12,714,474	50,660	629,190	13,394,324
Unused amounts reversed	-	(10,544,242)	-	-	(10,544,242)
Unwinding of discount	-	-	1,204,068	-	1,204,068
Changes in estimate	(93,363)	-	(794,517)	-	(887,880)
Used during the year	(3,403,119)	-	(914,886)	(245,648)	(4,563,653)
Current portion	4,823,769	21,010,732	999,735	262,843	27,097,079
Non-current portion	17,185,088	-	13,729,293	4,405,062	35,319,443
At December 31, 2009	**22,008,857**	**21,010,732**	**14,729,028**	**4,667,905**	**62,416,522**
Additional provisions	-	2,795,918	223,432	998,919	4,018,269
Unused amounts reversed	-	(4,835,885)	-	-	(4,835,885)
Unwinding of discount	-	-	1,168,011	-	1,168,011
Changes in estimate	-	-	(542,100)	-	(542,100)
Used during the year	(2,207,597)	(7,285,707)	(956,735)	(287,899)	(10,737,938)
Current portion	3,170,070	11,685,058	695,421	311,083	15,861,632
Non-current portion	16,631,190	-	13,926,215	5,067,842	35,625,247
At December 31, 2010	**19,801,260**	**11,685,058**	**14,621,636**	**5,378,925**	**51,486,879**

15. REVENUE

	2010	2009
Export:		
Crude oil	556,566,299	435,815,380
Domestic (Note 22):		
Crude oil	34,603,268	31,964,447
Gas products	6,452,132	4,826,049
Refined products	6,104,431	4,897,497
Other sales and services	5,516,268	7,990,106
	609,242,398	**485,493,479**

16. OPERATING EXPENSES

	2010	2009
Rent tax	97,484,646	58,673,500
Mineral Extraction Tax	70,932,591	55,087,266
Employee benefits	66,241,795	50,876,767
Transportation	57,794,777	53,793,843
Depreciation, depletion and amortization	35,486,128	31,155,360
Repairs, maintenance and other services	28,857,572	21,178,039
Materials and supplies	12,007,713	10,135,010
Energy	10,987,439	10,429,959
Management fees and sales commissions (Note 19)	8,281,574	7,648,453
Export customs duty	6,477,735	-
Other taxes	4,815,027	5,031,000
Social projects	4,137,051	2,239,845
Fines and penalties	2,805,102	8,132,702
Loss on disposal of fixed assets	2,200,613	2,547,437
Dry well expense	1,103,615	-
Geological and geophysical expense	968,648	390,950
Change in crude oil balance	(1,538,597)	213,835
Other	13,449,630	13,071,663
	422,493,059	**330,605,629**

17. FINANCE INCOME / COSTS

17.1 FINANCE INCOME

	2010	2009
Interest income on term deposits with banks	27,613,518	42,880,748
Interest income on Debt Instrument of NC KMG	7,061,243	-
Interest income on receivable from jointly controlled entity	3,101,386	3,216,660
Interest income on held-to-maturity financial assets	239,628	404,288
Other	24,010	257,209
	38,039,785	**46,758,905**

17.2 FINANCE COSTS

	2010	2009
Interest expense	6,192,140	958,917
Unwinding of discount on asset retirement obligation	1,168,012	1,204,068
Impairment of held-to maturity financial assets	16,449	570,928
Realised loss on crude oil derivative instruments	-	246,132
Other	118,954	261,244
	7,495,555	**3,241,289**

18. INCOME TAXES

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

	2010	2009
Corporate income tax	45,298,691	63,934,177
Excess profit tax	10,276,747	20,648,241
Current income tax	**55,575,438**	**84,582,418**
Corporate income tax	1,683,946	(7,015,624)
Excess profit tax	185,879	(1,820,965)
Deferred income tax	**1,869,825**	**(8,836,589)**
Income tax expense	**57,445,263**	**75,745,829**

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

	2010	2009
Profit before tax	291,947,153	285,472,729
Income tax	57,445,263	75,745,829
Effective tax rate	**20%**	**27%**
Statutory income tax	20	20
Increase (decrease) resulting from		
Excess profit tax	4	8
Corporate income tax of prior years	-	(1)
Share of result of associates and joint ventures	(4)	-
Non-taxable income	(2)	-
Movement of provisions	-	(1)
Non-deductible expenses	2	1
Effective tax rate	**20**	**27**

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

	Fixed assets	Provisions	Taxes	Other	Total
At January 1, 2009	**2,855,336**	**(1,284,424)**	**(279,765)**	**(2,720,095)**	**(1,428,948)**
Recognized in profit and loss	1,273,534	162,153	(8,551,971)	(1,720,305)	(8,836,589)
At December 31, 2009	**4,128,870**	**(1,122,271)**	**(8,831,736)**	**(4,440,400)**	**(10,265,537)**
Deferred taxes acquired in business combinations	1,816,597	-	-	-	1,816,597
Recognized in profit and loss	4,878,318	(346,980)	(2,914,487)	252,974	1,869,825
At December 31, 2010	**10,823,785**	**(1,469,251)**	**(11,746,223)**	**(4,187,426)**	**(6,579,115)**

19. 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 NWF, except for banks, controlled by Samruk-Kazyna NWF. Halyk Bank of Kazakhstan is a related party due to the bank being controlled by a member of the management board of Samruk-Kazyna NWF. BTA Bank is a related party since it is controlled by Samruk-Kazyna NWF and Kazkommertsbank is a related party due to Samruk Kazyna NWF holding 21.2% of the bank”s ordinary shares.

Sales and purchases with related parties during the years ended December 31, 2010 and 2009 and the balances with related parties at December 31, 2010 and 2009 are as follows:

	2010	2009
Sales of goods and services (Note 15)		
Entities under common control	594,059,556	386,384,246
Other state-controlled entities	986,698	1,106,860
Joint ventures	328,627	398,864
Associates	34,332	9,416
Halyk Bank of Kazakhstan affiliates	23,955	778
Purchases of goods and services (Note 16)		
Entities under common control	25,597,155	25,084,989
Parent Company	7,775,474	7,212,870
Other state-controlled entities	12,434,270	12,651,588
Associates	995,559	267,312
Halyk Bank of Kazakhstan affiliates	1,190,601	1,278,380
Interest earned on financial assets		
Interest earned on Debt Instrument	7,061,243	-
Effective interest rate on Debt Instrument – indexed USD/KZT	6.87%	-
Halyk Bank of Kazakhstan	12,854,310	17,857,881
Average interest rate on deposits	7.31%	8.30%
Kazkommertsbank	9,489,680	10,621,306
Average interest rate on deposits	8.54%	8.34%
BTA Bank	112,906	2,347,620
Average interest rate on deposits	12.00%	11.48%
Impairment loss on held-to-maturity financial assets		
BTA Bank	16,449	570,928
Salaries and other short-term benefits		
Members of the Board of Directors	115,197	109,729
Members of the Management Board	325,066	196,930
Share-based payments		
Members of the Board of Directors	5,248	5,698
Members of the Management Board	33,917	37,687

	December 31, 2010	December 31, 2009
Cash and cash equivalents (Note 7)		
Halyk Bank of Kazakhstan	13,141,643	51,232,052
Kazkommertsbank	997,391	14,572,711
BTA Bank	10,381	19,085,560
Financial assets (Note 7)		
Halyk Bank of Kazakhstan	99,583,042	232,974,000
Kazkommertsbank	37,873,202	182,825,420
BTA Bank (net of impairment)	-	5,222,040
Debt Instrument – indexed USD/KZT	220,967,915	-
Trade and other receivables (Note 7)		
Entities under common control	66,981,677	51,319,746
Other state-controlled entities	606,068	785,946
Joint ventures	20,432,051	21,399,372
Associates	7,540	-
Halyk Bank of Kazakhstan affiliates	98,300	-
Trade payables		
Entities under common control	543,559	523,423
Parent Company	2,591,825	1,009,802
Other state-controlled entities	282,844	389,600
Associates	631,987	180,151
Halyk Bank of Kazakhstan affiliates	48,609	82,162

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 6,860,318 tons of crude oil in 2010 (2009: 5,320,931 tons). The sales of crude oil are priced by reference to Platt's index quotations and adjusted for freight, insurance and quality differentials. For these exports of crude oil the Company received an average price per ton of approximately 83,890 Tenge in 2010 (2009: 66,462 Tenge). In addition, the Company supplies oil and oil products to the local market at the directive of the Kazakhstan government, the ultimate controlling shareholder of the Parent Company. Those supplies to the domestic market represented 1,604,458 tons of crude oil production in 2010 (2009: 1,717,488 tons). Prices for the local market sales are determined by agreement with NC KMG. For deliveries to the local market in 2010 the Company received an average price per produced crude oil ton of around 21,531 Tenge (2009: 18,579 Tenge). 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 7,775,474 thousand Tenge in 2010 (2009: 7,212,870 thousand Tenge). Agency commissions for crude oil sales amounted to 506,100 thousand Tenge in 2010 (2009: 435,583 thousand Tenge). Transportation services related to the shipment of 6,128,082 tons of crude oil in 2010 (2009: 6,967,200 tons) were purchased from a subsidiary of NC KMG for 20,656,793 thousand Tenge in 2010 (2009: 21,064,331 thousand Tenge). The remaining services purchased from subsidiaries of NC KMG include primarily payments for demurrage, sales commissions and electricity.

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. Additionally during 2010 the Company granted 122,434 options (2009: 117,942 options) at average exercise prices of, US dollars 19.84 or 2,929 Tenge (2009: US dollars 15.13 or 1,971 Tenge).

20. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Company's principal financial liabilities comprise loans, payables to Government for geological information, trade and other payables. The main purpose of these financial liabilities is to raise finance for the Company's operations and to support the Company's mergers and acquisition activities. The Company has various financial assets such as trade receivables, short and long-term deposits and cash and cash equivalents.

The main risks arising from the Company's financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. The Company's management reviews and agrees policies for managing each of these risks which are summarized below.

INTEREST RATE RISK

The Company's exposure to the risk of changes in market interest rates relates primarily to the Company's long-term borrowings with floating interest rates.

The Company's policy is to manage its interest cost by closely monitoring the debt markets and using a mix of fixed and floating rate debts. To manage this, the Company has previously entered into fixed interest rate swaps on a portion of its debt, in which the Company agrees to exchange, at specified intervals, the difference between fixed and floating rate interest amounts calculated by reference to an agreed-upon notional principal amount.

At December 31, 2010 the Company has floating rate debt of 114,334,798 thousand Tenge (2009: 128,982,970 thousand Tenge).

FOREIGN CURRENCY RISK

As a result of investments and borrowings denominated in US dollars the Company's consolidated statement of financial position can be affected by movements in the US exchange rates. The Company seeks to mitigate the effect of its currency exposure by reducing or increasing exposure to the US dollar in its investment portfolio based on the management expectations on movements in the short and medium term US dollar to Tenge exchange rates.

The Company also has transactional currency exposures. Such exposure arises from sales of crude oil in currencies other than the Company's functional currency. Approximately 91% of the Company's sales are denominated in US dollars, whilst almost all of costs are denominated in Tenge. The majority of the sales receipts are received within thirty days of sale. Therefore, exposure to movement in the exchange rate on these amounts is limited at any one time to one month of sales. Management monitors but historically has not mitigated this exposure.

When determining the composition of the investment portfolio, with respect to settlement currency, management takes into consideration the next three to six months of budgeted Tenge cash outflows and ensures that minimum Tenge assets are held to settle these amounts as they materialize or come due.

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).

	Increase / decrease in Tenge to US dollar exchange rate	Effect on profit before tax
2010		
US dollar	+ 10%	75,147,053
US dollar	- 15%	(112,720,579)
2009		
US dollar	+ 10%	49,142,464
US dollar	- 15%	(73,713,695)

CREDIT RISK

The Company's vast majority of sales is made to affiliate of the Parent and has a significant concentration risk of the receivable from this affiliate (Note 7, 19). 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.

With respect to credit risk arising from the other financial assets of the Company, which comprise cash and cash equivalents and held-to-maturity financial investments, the Company's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

The Company is exposed to credit risk from its operating activities and certain investing activities. With regard to investing activities, the Company places deposits with Kazakhstan and foreign banks as well as purchases held-to-maturity Government bonds. In addition, the Company purchased Debt Instruments issued by its Parent (Note 7).

The Company's treasury policy limits the amount of financial assets held at any one bank to the lower of a stipulated maximum threshold or a percentage of the bank's Tier I capital, which is linked to the banks long term counterparty credit rating, as measured by Standard and Poor's rating agency, (e.g. not greater than 40% for a BB rated bank at December 31, 2010). In 2010 the Company's Board of directors approved a transition plan whose intent was to allow the Company to better manage its credit risks and more closely comply with its amended treasury policy. The amended policy stipulates that local and foreign banks, which are the residents of Kazakhstan, with credit ratings less than two levels below that of the Kazakhstan government's sovereign credit rating, cannot be used to deposit financial assets. If the foreign subsidiary banks do not have their standalone credit ratings, than the credit ratings of their parent banks can be used. The treasury policy defines a foreign subsidiary bank as a bank with at least 50% ownership by the foreign parent bank. In that case, the credit rating of the foreign parent bank should be at least 'A–' as measured by Standard and Poor's rating agency. When the Company deposits financial assets in overseas foreign banks, the rating of the bank should also be at least 'A–'. The transition plan allows the Company to keep financial assets in Halyk Bank and Kazkommertsbank, irrespective of their credit ratings, given that Samruk Kazyna NWF holds stakes in the above banks.

Maximum exposure to Kazkommertsbank and Halyk Bank is targeted at 250 million US Dollars and 750 million US Dollars as at December 31, 2010 and 250 million US Dollars and 500 million US Dollars as at December 31, 2011, respectively.

As at December 31, 2010 the Company has greatly reduced its year on year exposure to the Kazakh banking system primarily through the purchase of the Parent's Debt Instuments and increasing deposits with foreign banks. As a result the Company's compliance with its treasury policy has greatly increased and amounts of the financial assets in non-compliant instruments or institutions are not material as at December 31, 2010.

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.

Banks	Location	Rating[1]		2010	2009
		2010	2009		
Investment in Debt Instruments of NC KMG	Kazakhstan	BBB- (stable)	BB+ (stable)	220,967,915	-
Halyk Bank	Kazakhstan	B+ (stable)	B+ (negative)	112,724,685	284,204,891
ATF Bank[2]	Kazakhstan	BBB (positive)	Rating recalled	86,746,032	43,506,484
Citi Bank	Kazakhstan / UK	A+ (negative)	A (stable)	75,505,810	17,254,342
HSBC	Kazakhstan / Hong Kong / UK	AA (stable)	AA (negative)	70,384,415	25,679,952
National Bank of Republic of Kazakhstan	Kazakhstan	Baa2 (stable)	Baa2 (negative)	54,916,073	-
Kazkommertsbank	Kazakhstan	B (negative)	B (negative)	38,870,593	197,375,592
RBS Kazakhstan	Kazakhstan	A (stable)	A (stable)	21,412,244	38,916,400
Deutsche Bank	Germany	A+ (stable)	A+ (stable)	8,816,125	4,626,872
Credit Suisse	British Virgin Islands	A+ (stable)	A+	4,971,970	4,573,579
BankCenterCredit	Kazakhstan	Ba3 (negative)	Ba3 (negative)	1,840,538	2,144
ING Bank	Netherlands	A+	A+	668,737	1,997,796
BTA Bank	Kazakhstan	B- (stable)	D/no forecast	10,381	24,307,599
Other				149,540	105,045
				697,985,058	**642,550,696**

[1] Source: Interfax – Kazakhstan, Factivia, official sites of the banks as at December 31 of the respective year.

[2] ATF Bank is a member of UniCredit Group.

LIQUIDITY RISK

The Company monitors its liquidity risk using a recurring 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, 2010 based on contractual undiscounted payments:

Year ended December 31, 2010	On demand	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
Borrowings	-	253,358	60,419,794	63,362,092	3,348,200	127,383,444
Trade and other payables	47,304,799	-	-	-	-	47,304,799
	47,304,799	**253,358**	**60,419,794**	**63,362,092**	**3,348,200**	**174,688,243**

Year ended December 31, 2009	On demand	Less than 3 months	3-12 months	1-5 years	More than 5 years	Total
Borrowings	-	254,991	45,920,835	92,751,802	4,454,030	143,381,658
Trade and other payables	34,402,259	-	-	-	-	34,402,259
	34,402,259	**254,991**	**45,920,835**	**92,751,802**	**4,454,030**	**177,783,917**

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.

The Company is not planning to hedge its exposure to the risk of fluctuations in the price of crude oil in the nearest 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, 2010 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, 2010 and 2009.

21. 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	
	2010	2009	2010	2009
Current financial assets				
Cash and cash equivalents	98,519,465	107,626,368	98,519,465	107,626,368
Held-to-maturity financial assets	54,916,073	-	54,916,073	-
US dollar-denominated term deposits	264,841,437	447,254,500	264,841,437	447,254,500
Tenge-denominated term deposits	57,786,248	87,033,308	57,786,248	87,033,308
Receivable from jointly controlled entity	1,203,834	1,082,100	1,203,834	1,082,100
Investment in Debt Instrument	256,928	-	256,928	-
Other financial assets	270	270	270	270
Non-current financial assets				
Investment in Debt Instrument	220,710,987	-	220,710,987	-
Receivable from jointly controlled entity	19,153,089	20,268,928	19,153,089	20,268,928
Tenge-denominated term deposits	953,920	636,520	953,920	636,520
Other financial assets	160,911	161,411	160,911	161,411
Financial liabilities				
Borrowings floating rate interest	114,334,798	128,982,970	114,334,798	128,982,970
Borrowings fixed rate interest	8,146,065	8,690,190	8,146,065	8,690,190

The fair value of borrowings has been calculated by discounting the expected future cash flows at prevailing interest rates. The Company's borrowings are at market rates of interest specific to those instruments and as such are stated at fair value. The fair value of other financial assets has been calculated using market interest rates.

22. 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 Kazakhstani economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. While the Government has introduced a range of stabilization measures aimed at providing liquidity and supporting refinancing of foreign debt for Kazakhstan banks and companies, there continues to be uncertainty regarding the access to capital and cost of capital for the Company and its counterparties, which could affect the Company's 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 Company's Parent, this price may be materially below international market prices and may even be set at the cost of production. 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 1,811,481 tons of oil (2009: 2,017,488 tons) and joint venture Kazgermunai have delivered 784,000 tons of oil (2009: 615,000 tons) on the domestic market.

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, 2010.

The Company's management believes its interpretations of the tax legislation are appropriate and that the Company has justifiable arguments for its tax positions and will dispute the tax assessment to the fullest extent possible under the law of the Republic of Kazakhstan.

CUSTOMS CLAIM

On August 18, 2009 the customs committee of the Republic of Kazakhstan presented a claim to the Company of 17,574,728 thousand Tenge for underpaid export customs duty (including the principal of 15,260,014 thousand Tenge and the late payment interest of 2,314,714 thousand Tenge). This claim relates to January 2009 export shipments of crude oil, on which rent tax was fully paid per the regulations of the Republic of Kazakhstan, declared for customs clearance in December 2008.

On September 23, 2009 the Company filed an appeal with the court of first instance. On December 1, 2009 the court of first instance ruled in favor of the Company. However, on January 20, 2010 the appeal filed by the customs committee was satisfied by the court of second instance. On February 8, 2010 the Company filed the further appeal with the third instance court. On March 9, 2010 the third instance court also ruled in favor of the customs authorities. The Company is planning to appeal this matter to the Supreme Court of Kazakhstan.

Management of the Company believes that they will ultimately prevail in this matter and therefore no amounts have been accrued in the consolidated financial statements for the year ended December 31, 2010.

ENVIRONMENT

Environmental regulation in Kazakhstan is evolving and subject to ongoing changes. Penalties for violations of Kazakhstan's environmental laws can be severe. Potential liabilities which may arise as a result of civil litigation or changes in legislation cannot be reasonably estimated. Other than those amounts provided for in provisions (Note 14) management believes that there are no probable or possible 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 Energy and Mineral Resources of Kazakhstan and the Company pays royalties 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:

Field	Contract	Expiry date
Uzen (8 fields)	No. 40	2021
Emba (1 field)	No. 37	2021
Emba (1 field)	No. 61	2016
Emba (23 fields)	No. 211	2018
Emba (15 fields)	No. 413	2020

COMMITMENTS ARISING FROM OILFIELD AND EXPLORATION LICENSES AND CONTRACTS

Year	Capital expenditures	Operational expenditures
2011	98,326,086	5,539,151
2012	7,260,231	4,240,970
2013	-	4,006,987
2014	-	4,006,987
2014-2021	-	18,823,598
Total	**105,586,317**	**36,617,693**

CRUDE OIL SUPPLY COMMITMENTS

The Company has obligations to supply oil and oil products to the local market under government directives (Note 22).

COMMITMENTS OF KAZGERMUNAI

The Company's share in the commitments of Kazgermunai is as follows as at December 31, 2010:

Year	Capital expenditures	Operational expenditures
2011	4,575,950	2,545,941

23. SUBSEQUENT EVENT

ACQUISITION OF PREFERRED SHARES ON KASE

As part of its buy back program, on February 3, 2011 the Company purchased 236,430 preferred shares at an aggregate purchase price of 4,552,046 thousand Tenge via a specialized trade of its preferred shares on KASE. As at February 3, 2011, the Company has purchased 1,582,643 preferred shares from the start of the buy back program for an aggregate price of 28,909,971 thousand Tenge.

These consolidated financial statements have been signed below by the following persons on behalf of the Company and in the capacities indicated on February 11, 2011:

Chief Executive Officer	Ibrashev K.N.
Chief Financial Officer	Bekezhanova Zh.
Financial Controller	Drader Sh., CA

INFORMATION FOR SHAREHOLDERS

ANNUAL GENERAL MEETING OF SHAREHOLDERS

The AGM will be held at 10:00 am on 5 May 2011 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 including details of activities, press releases and annual and interim reports.

SHAREHOLDERS' ENQUIRIES

For information about proxy voting, dividends and to report changes in personal details, shareholders should contact the Company's registrar/ depositary:

- Holders of ordinary and preferred shares: JSC Fondovyi Tsentr, 79 "A", Zheltoksan Street, Almaty, Republic of Kazakhstan, Tel.: +7 (727) 250-89-61, 250-89-60, Fax: +7 (727) 250-16-96.
- Holders of GDRs: The Bank of New York Mellon,. Shareholder Services, PO Box 358516, Pittsburgh PA 15252-8516, United States of America, Telephone +1 888 269 23 77 (toll free within the USA), Telephone +1 201 680 68 25 (outside USA), Email: shrrelations@bnymellon.com, www.adrbnymellon.com.

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www.adrbnymellon.com

REFERENCE INFORMATION

- 1P

  Proved Reserves
- 2P

  Proved and Probable Reserves
- 3P

  Proved, Probable and Possible Reserves
- bbl

  Barrel
- British Gas Group plc (BG Group)

  BG Group is a world leader in natural gas, with a strategy focused on connecting competitively priced resources to specific, high-value markets. Active in more than 25 countries on five continents, BG Group has a broad portfolio of exploration and production, Liquefied Natural Gas (LNG), transmission and distribution and power generation business interests. It combines a deep understanding of gas markets with a proven track record in finding and commercialising reserves.
- British Gas Kazakhstan (BG Kazakhstan)

  BG Kazakhstan is a part of BG Group, which has been active in Kazakhstan for 18 years. BG Group holds a 32.5 per cent interest in the giant Karachaganak oil and gas condensate field and, along with its partner, ENI, is a joint operator of this field. It is also a 2 per cent shareholder in the Caspian Pipeline Consortium (CPC), which links Kazakhstan's oil reserves to world markets.
- 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 94% 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
- Conversion factors

  KMG EP -7.36 bbl/ton; KGM - 7.7; Karazhanbasmunai - 6.68; PKI – 7.75; others - 7.33.
- CPC

  Caspian Pipeline Consortium
- ED/CED

  Export Duty/Customs Export Duty
- Embamunaigas (EMG)

  One of two production branches of KMG EP, operating in 37 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.

- Karazhanbasmunai (KBM)

  JSC Karazhanbasmunai owns 100% of the rights to develop the Karazhanbas oil and gas field in Western Kazakhstan till 2020. The proved and probable (2P) reserves of the KBM as at the end of 2010, according to preliminary data, were 67 million tonnes (449 million barrels).

- KASE

  Kazakhstan Stock Exchange

- Kazakhoil Aktobe LLP (KOA)

  KOA owns the contract for subsurface resources development and use of Alibekmola and Kozhasai deposits, located in Aktobe region. The overall production in 2010 was 0.98mmt (20kbopd) of crude oil and the 2P reserves are estimated at 30mmt (217m barrels of oil equivalent). The second shareholder of KOA is Caspian Investments Resources.

- KazakhTurkMunai Ltd. (KTM)

  KTM owns 2 contracts for subsurface resources development and use of Western Elemes, Northeast Saztobe, Southeast Saztobe deposits, located in Mangistau region, and Laktybay and Karatobe deposits, located in Aktobe region. The overall production in 2010 was 0.23mmt (4.6kbopd) of crude oil, the 2P reserves are estimated at 5.6mmt (41m barrels of oil equivalent). The second shareholder of KTM is Turkish Petroleum Corporation (TPAO).

- Kazgermunai (KGM)

  Kazakhstani oil company, sixth largest in terms of production volume based on 2010 results. Proved and probable reserves (2P) of KGM as at the end of 2010 were about 24 million tonnes (180 million barrels), production in 2010 was about 3.1 million tonnes (65 kbopd). The second member of KGM is PKI (through PetroKazakhstan Kumkol Resources).

- kbopd

  Thousand barrels per day

- KCGP

  Kazakhstan-China gas pipeline

- KCP

  Kazakhstan-China pipeline

- Korea Gas Corporation (KOGAS)

  KOGAS is the world's largest LNG importer and the nation's sole LNG provider. KOGAS currently operates three LNG terminals and a nationwide pipeline network spanning over 2,739km.

- LSE

  London Stock Exchange

- Mangistaumunaigaz (MMG)

  MMG is one of the largest oil and gas companies in Kazakhstan. MMG's operations include exploration and crude oil production. Annual production of MMG was around 5.7mmt in 2010. The volume of proved and probable reserves (2P) of MMG as at the end of 2009 was around 75,9mmt (556m barrels). Its major assets are the Kalamkas and Zhetybai oil fields in Western Kazakhstan. In total MMG owns 15 licenses to explore and produce oil.

- MET

  Mineral Extraction Tax

- National Company KazMunayGas (NC KMG)

  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 Samruk-Kazyna National Wealth Fund.

- NBK

  NBK holds the license rights, under Subsoil Use Contract Number 992 (issued in September 2002) for hydrocarbon exploration and production at the "West Novobogatinskoe field" in the Atyrau region. Recoverable reserves (2P) of this field are estimated to be 13 million barrels of oil equivalent (according to KMG EP's technical experts' evaluation). Cost of acquired barrel of this asset is $2.7/bbl. According to independent evaluation recoverable volumes are estimated at 12.9 million barrels.

- PetroKazakhstan Inc. (PKI)

  The PetroKazakhstan Inc. group of companies is involved in hydrocarbon exploration and production as well as in sales of oil and petroleum products. PetroKazakhstan has a share in 16 fields, 11 of which are in various development stages.

- PKOP

  PetroKazakhstan Oil Products

- Samruk-Kazyna Fund

  National Prosperity Fund, managing state assets, shares of national companies and financial institutions for Kazakhstan development.

- SapaBarlau Service (SBS)

  SBS 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. Extension of the contract is a condition precedent to closing. Prospective resources of this block considering risks are estimated at 123-146 million barrels of oil equivalent (according to KMG EP’s evaluation) and at 232 million barrels according to independent evaluation. Cost of acquired barrel of this asset in a conservative scenario is $0.24/bbl.

- Standard & Poor’s

  International rating agency that awards short-term and long-term credit ratings.

- Turgai Petroleum (TP)

  TP owns licenses to explore and produce hydrocarbons from the Kumkol North and East Kumkol oil fields. In 2010 TP produced 3 mmt (an average of 62kbopd). As at 31 March 2009 the total volume of TP’s proved and probable reserves was 104.4 mmbbl (KMG EP’s acquired interest is 17.2 mmbbl).

- Uzen – Atyrau – Samara (UAS)

  An oil pipeline, a 1,500lm-long link over the territory of Atyrau and Mangistau Regions to Russia.

- Uzenmunaigas (UMG)

  One of two production branches of KMG EP, operating in 2 main fields in Mangistau Region.