BRIGHTER HORIZONS

Kcell Annual Report 2017

A BETTER YEAR

Welcome to Kcell's annual report for 2017, when Kazakhstan's economy fared better following the turbulence of the previous two years, resulting in brighter horizons.

Throughout the reporting period, the Company continued to demonstrate excellence in leadership, maintaining its number one position and pursuing a pioneering network sharing agreement with another operator, a progressive move in the emerging 'network economy' of the new millennium.

There were numerous improvements in Kazakhstan's external conjuncture in 2017. Prices of oil and other commodities rose, the tenge fluctuated in a fairly narrow band and interest rates were reduced, while the competitive situation in the country's telecommunications sector stabilised.

Against this backdrop, Kcell reconfirmed its position as the leading mobile telecommunications operator in Kazakhstan in terms of both revenues and subscriber numbers*. At the year-end, we had 10.0 million subscribers, while 49% of the population had access to our 4G network and 73% to our 3G service. Over the year, we continued to focus on enhancing our offering in the B2B and B2C segments with a view to delivering exceptional quality to all customers.

* Based on the Company's calculations.

Contents

The full annual report and accounts are available online at: http://www.investors.kcell.kz/en

HIGHLIGHTS OF 2017

Financial highlights

+0.1%
Net revenues (y-o-y)

+12.1%
Data revenues (y-o-y)

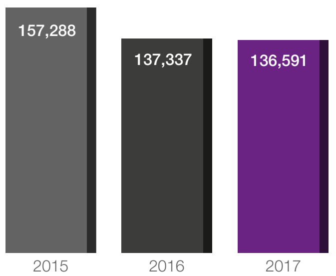
+11.3%
B2B revenues (y-o-y)

Financial highlights

Service revenues (KZT mln)

136,591

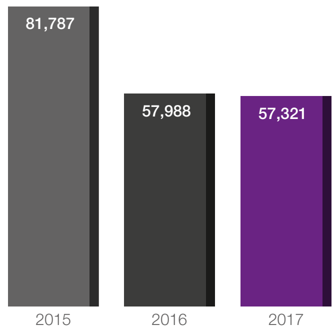
-0.5%



EBITDA excluding non-recurring items (KZT mln)

57,321

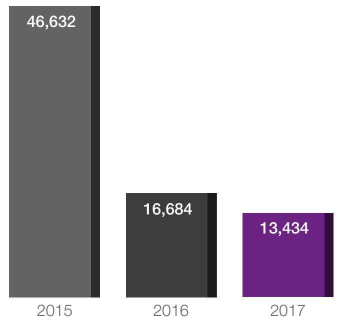
-1.2%



Net income (KZT mln)

13,434

-19.5%



FROM MOBILE OPERATOR TO SERVICE PROVIDER

Established in 1998 as a mobile operator, Kcell is now well on its way to becoming an innovative service provider.

Services

Kcell provides the full spectrum of mobile telecommunications services to both individuals and organisations. Alongside standard voice, VAS and data services, the Company offers a wide range of OTT and MFS services under the Mobi brand. It has licences to operate on 2G, 3G and 4G/LTE frequencies indefinitely.

Brands

The Company operates through two key brands that are among the best established in Kazakhstan. Activ is targeted at the mass market (B2C) and Kcell at corporate subscribers (B2B), as well as high net-worth individuals.

Activ seeks to fulfil all individual customers' mobile communication needs by offering national and international tariffs, complemented by various bundles.

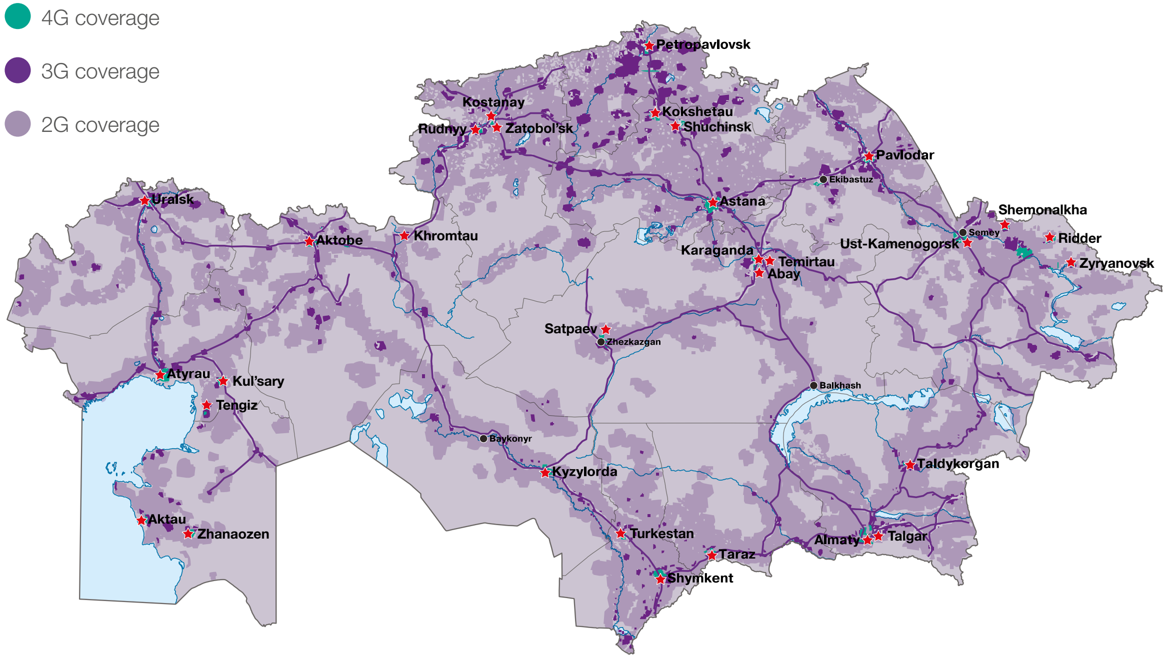
Network

In 1998, Kcell became the first company to receive a licence to provide cellular services on the GSM-900 standard in Kazakhstan. Since then, it has built one of the most modern, technologically advanced and extensive mobile telecommunication networks in the country.

The network is collocated and operates at four frequency bands – 700/800 MHz, 900 MHz, 1700/1800 MHz and 2100 MHz – providing both data and voice communications. Data transfer speeds range up to 300 kbps for 2G, 37 mbps for 3G, 73 mbps for 4G, and 140 mbps for 4G+.

Map key

- 4G coverage
- 3G coverage
- 2G coverage



History

1998

On 1 June 1998, Kcell was established as GSM Kazakhstan OAO Kazakhtelecom, a limited liability partnership, to design, construct and operate a cellular telecommunications network in Kazakhstan using the Global System for Mobile Communications (GSM) standard.

After receiving the first GSM licence in Kazakhstan, the Company officially launched its mobile communications network on 7 February 1999, operating under the Kcell trademark initially and adding the Activ brand in that September.

2003

On 18 September 2003, Kcell announced the launch of General Packet Radio Service (GPRS) technology, making it the first telecommunications operator in Kazakhstan to offer mobile internet, and unveiled Multimedia Messaging Service (MMS) technology.

The launch of GPRS marked a major step towards modernising the GSM network and paving the way for 3G technology. In September 2005, Kcell continued to build on this competitive advantage by being the first cellular operator to introduce GPRS roaming.

2010

On 1 December 2010, Kcell officially began operating dedicated 3G networks in Astana and Almaty. This heralded a new stage in the development of the country's telecommunications industry, significantly improving the quality of data transfer services in Kazakhstan.

The new technology has played a key role in enabling the country to offer high-quality mobile telecommunications while hosting major events, such as the Organisation for Security and Cooperation in Europe (OSCE) summit in December 2010 and the Seventh Asian Winter Games in January-February 2011.

2012

Before 2 February 2012, the Company was a subsidiary of Fintur Holdings B.V. (Fintur), which owned 51%, and Kazakhtelecom JSC (Kazakhtelecom), which held 49%. Fintur itself is owned jointly by Sonera Holding B.V. and Turkcell Iletisim Hizmetleri A.S., which have holdings of 58.55% and 41.45%, respectively.

On 2 February 2012, Kazakhtelecom sold its 49% to Sonera Holding B.V. (Telia), a subsidiary of TeliaSonera.

In July 2012, the Company was converted from a Limited Liability Partnership to a Joint Stock Company.

2012

On 17 December 2012, Kcell successfully completed an initial public offering of global depository receipts (GDRs) on the London Stock Exchange and ordinary shares on the Kazakhstan Stock Exchange (KASE). The offering consisted of a sale by Sonera Holding B.V. of 50 million shares, representing 25% of Kcell's share capital. The shares were priced at US$10.50 per GDR and KZT1,578.68 per ordinary share.

Following the placement, TeliaSonera Kazakhstan Holding B.V. retains 24% directly, Fintur Holdings B.V. holds 51% directly, and the remaining 25% is in free float.

2014

In May 2014, Kcell became an official distributor of the iPhone in Kazakhstan.

In September 2014, Kcell launched a major rebranding and repositioning campaign for its popular Activ brand. The objective of the campaign is to reinvigorate the brand in order to strengthen subscriber loyalty, drive growth in the mass-market segment and retain leadership in the highly competitive market.

2015

On 14 March 2015, the Company opened its first branded Kcell store in Almaty, marking the beginning of a drive to overhaul its retail business model. The aim of the new concept is to combine service and sales in a single environment, improving the experience for customers who can explore new products and applications in-store.

2016

On 5 January 2016, Kcell acquired additional spectrum rights on the 700/800 MHz and 1800 Mhz bands to boost its nationwide connectivity and prepare for advanced 4G and LTE services, which were launched later in the year.

On 22 May 2016, the Company received an award for its high level of transparency and disclosure from the KASE, 'Striving Towards Greater Transparency'.

BRIGHTER HORIZONS

Dear stakeholders,

Looking back at 2017, I am extremely pleased with how Kcell navigated the difficulties it faced at the beginning of the year. After a somewhat shaky start, our business passed an inflection point and the horizons brightened, as the Kazakh economy improved, interest rates fell and the national currency stabilised.

A 4G network-sharing agreement with Beeline signed in 2016 has proved extremely successful. While it took a full year to conclude a highly complicated contract, this important commercial decision will reduce our capital expenditure on network expansion. In addition, 4G has served as a platform for increasing revenues from digital services substantially.

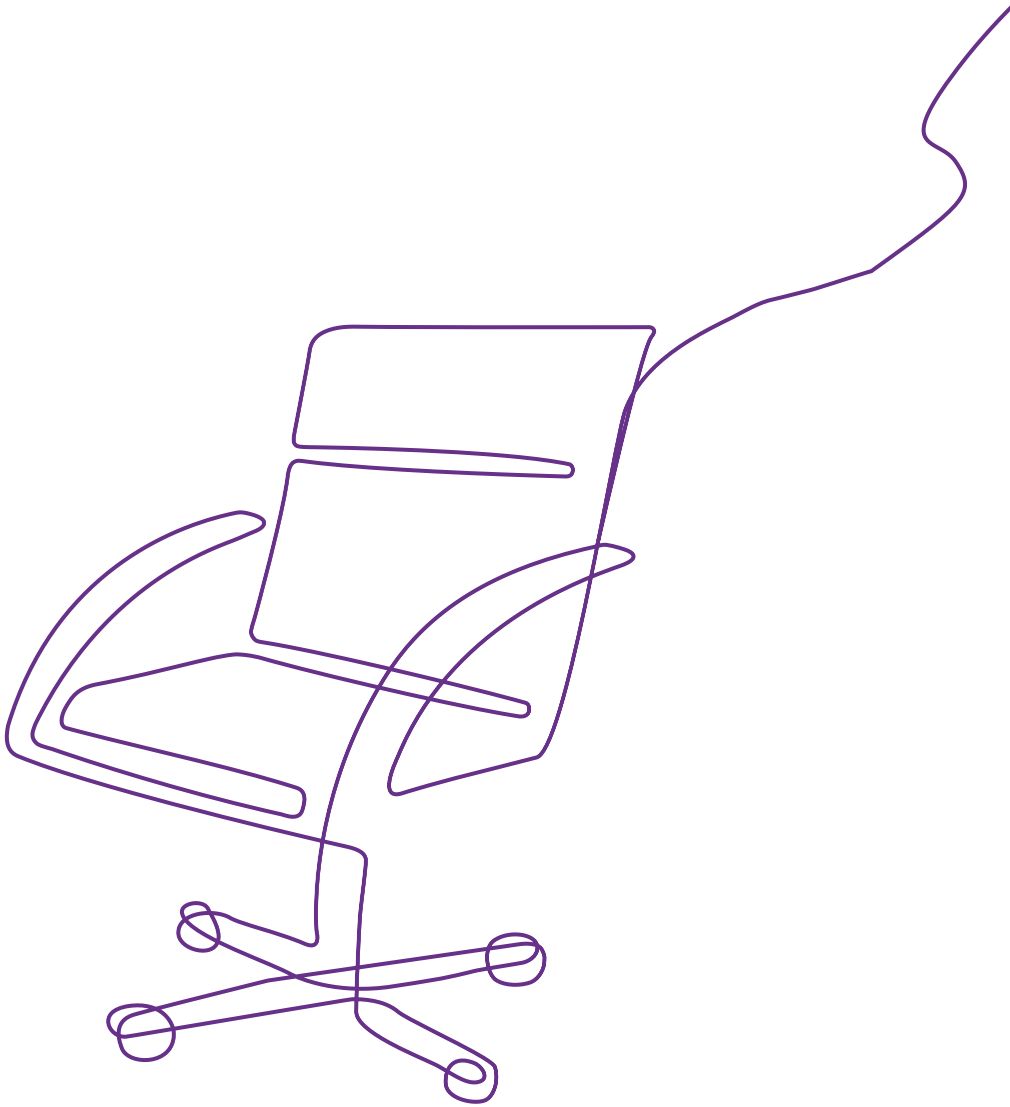
Kcell also made strong steps forward in terms of overall strategy, including by increasing the number of customers on bundles and post-paid tariffs. As of today, around 90% of all handsets sold in our retail network are contract phones. Looking ahead, we aim to work with our existing customer base to improve retention and satisfaction.

Reflecting our ability to regain ground in the second half of the year, the EBITDA margin amounted to 38.9% in 2017, virtually unchanged from 39.4% a year before. In addition, we continued to invest in the future, as indicated by the CAPEX-to-sales ratio of 14.7%, despite the still challenging macroeconomic conditions.

Kcell also maintained its pledge to return income to investors. The dividend policy undertakes to distribute at least 70% of the Company's net income for the previous financial year, together with any excess capital, after considering cash at hand, cash flow projections, medium-term investment plans and capital market conditions. In 2017, Kcell paid an annual dividend of KZT58.39 (around US$0.19), representing that 70%, for the 12 months ending 31 December 2016. In addition, in April 2018, after the reporting period, the Board of Directors recommended the same disbursement per share, KZT58.39, for 2017, representing 87% of the net income for that financial year.

Over the last few years, we have worked hard on improving our internal processes to ensure sustainable growth. During that time, items on the risk map that were near the top in terms of both probability and magnitude have moved towards the bottom. Our processes have become much more robust and we have concluded significant work internally to improve such areas as our procurement processes and anti-corruption policies.

In addition to this progress, Kcell has made definitive changes to its corporate culture, which is an integral part of sustainability. We have set ourselves the goal of being a trendsetter and role model in terms of corporate governance, and I believe we are succeeding. Fostering corporate culture takes longer and is more involved than implementing processes and



policies, which on their own can end up on the bookshelf. These must be living documents that build on a foundation of compliance and stewardship.

To conduct business over a long-term perspective, there needs to be stability. We support regulatory change paving the way for the industry, including easier access to licences and more openness. Such initiative will enable us to do a better job and make more grounded decisions. I believe that we have strengthened our executive team and placed our business on a firmer footing, providing the Company with the stability needed to drive through whatever lies ahead.

Given Telia's decision in September 2015 to exit Eurasia, further developments in Kcell's corporate history are a matter of time at this stage. As this new chapter approaches, the Company has confirmed and re-confirmed its status as the leader of Kazakhstan's mobile telecommunications sector, and it looks well positioned to capitalise on this and the inevitable additional technological developments in the industry worldwide. I would like to thank all of our stakeholders – investors, customers, suppliers, employees, local communities and public bodies – for their faith in and support of Kcell, as we move towards brighter horizons.

Jan Rudberg
Chairman of the Board of Directors

"We have set ourselves the goal of being a trendsetter and role model in terms of corporate governance, and I believe that we are succeeding."

Jan Rudberg
Chairman of the Board

Key Events in 2017

January

Kcell acts as official mobile operator for the 28th Winter Universiade, held in Almaty from 29 January to 8 February.

March

Kcell and the WikiBilim public foundation announce the launch of the first massive open online course (MOOC) in Kazakhstan: www.openu.kz. The project was supported by leading universities in the country: KBTU, AlmaU, SDU, KazNITU, and the Institute of Mathematics and Mathematical Modeling.

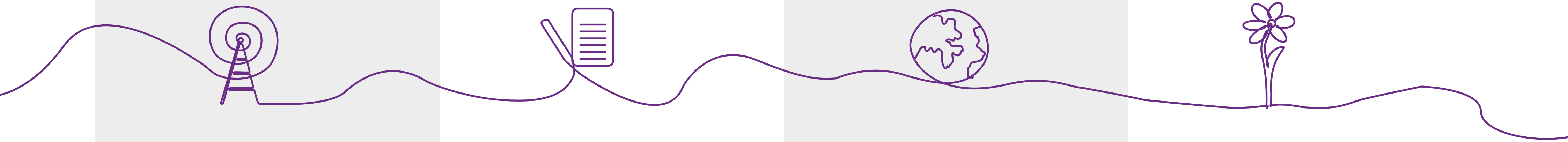
April

The Board of Directors proposes a dividend for 2016, approved in May, of 70% of net income, keeping its pledge to shareholders despite the macroeconomic conditions.

The number of citizens who have taken part in the Digital Life mobile literacy programme exceeds 6,000 over the last two years. Since 2015, over 230 free master classes on mobile media, mobile security, mobile education, mobile state and mobile business, as well as courses for elderly people, have been conducted.

June

Kcell launches a 4G+ network (LTE advanced) in Almaty and Shymkent. By the end of 2017, 4G+ becomes operational in nine cities in Kazakhstan. Almost a quarter of the Company's subscribers already use the 4G/LTE network.



July

Andis Locmelis is appointed as Finance Director.

Kcell expands the range of OTT services. The new video streaming service mobi kino, in partnership with popular online services Amediateka and MEGOGO, provides access to more than 6,800 movies and TV serials from the world’s leading studios.

October

Kcell continues to develop its mobile financial services, making cash withdrawals from mobile account balances available for activ subscribers at 3,400 Kazpost branches nationwide.

November

International ratings agency Fitch assigns Kcell a long-term issuer default rating of ‘BB’ and a Kazakhstan national long-term rating of ‘A(kaz)’, the outlook ‘stable’.

December

Kcell announces plans to place a KZT30 billion, three-year bond, its first, with a coupon of 11.5% as part of a KZT50 billion bond programme.

Bonds to the value of KZT 4.95 billion were placed in January 2018.

INFLECTION POINT

Dear stakeholders,

Following the headwinds of the past few years, 2017 brought stabilisation for Kazakhstan, the mobile telecommunications market and Kcell. While the economy remains exposed to potential external shocks, the outlook seems to have improved. Overall, Kazakhstan is setting a positive example of how a country's leadership and business community can work together productively.

Towards the end of the year, the competitive situation on the mobile telecommunications market became more favourable for all players. Kcell remains the leader in the mobile sector in terms of both revenue and subscriber market share. All indications are that the number of customers using mobiles as a central internet access point is increasing.

Our 4G capabilities play a vital role in meeting and exceeding our customers' expectations. The network sharing agreement with our competitor, Beeline, allows us to use each other's 4G infrastructure. This provides significant cost savings, given the low population density in most of the country and the increasing roll-out of 4G data services.

In terms of results, around the middle of 2017, Kcell experienced an inflection point, and the third and fourth quarters largely made up for the weakness seen in the first two. Our new business-to-business (B2B) and business-to-consumer (B2C) offerings also contributed to this.

The B2B business generated 9% of Kcell's overall revenues during the reporting period, up 11% year-on-year. The Company's expansion in that segment has been heavily supported by the success of business solutions, and I am happy to report that we are exceeding our expectations. While the contribution to revenues remains relatively small, B2B is coming into greater focus.

Our internal figures suggest that Kcell has a market share of at least 60-65% in mobile B2B services among the three main operators, placing it well ahead of competitors. Business solutions generated 53% of B2B revenues in 2017, far more than telecommunications services in the segment. With this confirmation that our digital transformation has started to pay rewards, we will continue to expand our technological efforts to bolster this trend.

Meanwhile, the more mature B2C business continued to expand, as mobile data, digital content and bundled tariffs largely drove growth. Kcell places a high priority on how many customers are using bundles. We offer popular bundled service plans alongside contracts for handsets from Apple and Samsung, with which we have direct distribution agreements. This has the potential to eliminate smartphone wholesalers and other intermediaries between us and customers.

By the end of 2017, 36% of Kcell's customers had signed up for bundles and they were contributing around 70% of B2C revenues. Our strategy is to maximise these figures and transform traditional customers into digital customers by using our digital ecosystem, which is the largest in Kazakhstan.

Looking to 2018, we aim to maintain our leadership in terms of customer experience, enhance network sharing, further expand our B2B and B2C businesses, continue to digitalise operations and begin to realise the benefits from the international licence.

I would like to thank each and every one of our employees for their contributions to the common cause in 2017. While it is perhaps premature to talk of a turnaround, we seemed to pass an inflection point in the year, and I see brighter horizons ahead for Kcell and all stakeholders.

Arti Ots
Chief Executive Officer

"Around the middle of 2017, Kcell experienced an inflection point, and the third and fourth quarters largely made up for the weakness seen in the first two."

Arti Ots
Chief Executive Officer

TRANSFORMING INTO A DIGITAL OPERATOR

Kcell's updated strategy envisions transforming the business model to that of a digital service provider by delivering value to customers through intuitive digital touchpoints and products, as well as digitalising customer interactions and core processes. Our overarching goal is to renew our focus on creating value for both customers and shareholders, while protecting market share in the new digital reality.

Strong foundations

The strength of any construction depends on its foundations. At Kcell, our overarching objective is to serve and create value for our customers, shareholders and country, and we strive to do this by ensuring that the right model underpins our business.

At our core are high-quality assets that can be divided into four main groups: people, network, brands and data-centric products and services. All of them interconnect to form a compelling proposition, with digital coming to the forefront in the new market reality.

The industry has undergone one of the most significant transitions in its history: the shift from voice to data. To remain ahead in this, Kcell's focus is on offering new tariffs to increase customer value, retaining customers by moving them from pay-as-you-go to bundles and converting traditional customers to digital with 'over the top' services.

Complete cycle

The overall result is a business model that not only generates revenues, but also contributes to sustainability. At Kcell, free cash flow is one of our key performance indicators, and our dividend policy reflects our commitment to creating value for shareholders. Equally important, however, are the funds reinvested in our asset base, which complete the cycle, further strengthening our foundations today for the generations of tomorrow.

The substantial effort and resources invested in the central foundations of the business has proved the right approach, as confirmed by the value created for both customers and shareholders.

People

By far our most important asset is our people, whose customer focus, standards and commitment have made us one of most dedicated service providers in Kazakhstan today. Without them, we simply would not exist.

Network

Another key strength is our high-quality network, through which we have led, and continue to lead, the advancement of mobile telecommunications in Kazakhstan. With the roll-out of nationwide 4G/LTE services well under way, we look forward to introducing the next generation of mobile telecommunications: 5G.

Brands

Cementing our identity in the market are our brands, Activ and Kcell, which are among the best established in Kazakhstan and synonymous with the quality of customer experience and value that we offer.

Data-centric products and services

Kcell's move to a digital operator business model is underpinned by its vast range of data-centric products and services. We aim to create the largest digital ecosystem in Kazakhstan and provide additional value for digital customers by continuing to develop high-value products in adjacent areas. In 2017, examples of these included 'over the top' platforms for accessing written content, music and films, as well as a unique mobile financial services ecosystem.

SHORT-TERM TARGETS DRIVE LONG-TERM OBJECTIVES

If our business model is the vehicle for reaching our ultimate goal, our strategy is our road map. As technology advances and the market develops, the utmost effort is required to remain the leader. To maintain its position, Kcell recognises the need for the highest standards, the greatest efficiency and maximum focus throughout its activities, and that these qualities come from within.

It is important to be able to not only define the best strategy, but also execute it effectively. This becomes more challenging when behavioural change is needed for people to become more client-oriented, which requires strong discipline and a clear focus on goals. To drive this, Kcell has created a Strategy Execution Programme and a three-person strategy team to coordinate the work.

The function is part of the CEO's office, ensuring an effective two-way transmission channel between the senior executive body and other departments. Its main responsibility is to identify strategic targets for the short term, each year, that will help to fulfil the long-term objectives and enable teams to implement the programme as effectively as possible.

Behind this, the achievements in such a short space of time have been tremendous. Personal goals have been set for all members of staff whose work is connected with any target. Kcell has established an intranet tool where employees can view them and the achievements of everyone openly. Each week, the strategy team meets with heads of department to discuss progress to date and next steps. The Company has adopted the 'Four Disciplines of Execution' (4DX) methodology and is educating employees about it through workshops and training sessions. Individual KPIs are aligned with the strategic targets. Together, these measures are focusing the efforts of all employees on pursuing excellence from within.

In response to the ever-changing environment, the Company refined its long-term strategic objectives, increasing their number from five to seven. They are now:

- Retain a leading position in the consumer market using strong brand positioning.
- Be a trendsetter and leader in the digital content business.
- Be a credible partner for customers in financial services.
- Strengthen customer loyalty wherever possible.
- Maintain leadership of the enterprise segment.
- Become a key player on the 'internet of things' market.
- Stay focused on the development of mobile marketing.

In 2017, the short-term strategic targets were to boost revenues, increase gross profit and optimise costs.

Our ultimate strategic goal is to strengthen customer loyalty by creating value

Strategic target 1	Strategic target 2	Strategic target 3
Boost revenues	Increase gross profit	Optimise costs

BUSINESS SOLUTIONS TAKE THE LEAD

In terms of technology and services, Kcell is far ahead of its competitors in the B2B segment, with a market share of at least 60-65% in core B2B services, based on internal figures.

Executive summary

In 2017, Kcell's B2B business generated 9% of overall revenues, up 11% year-on-year. While its revenue contribution remains relatively small, the B2B segment is coming into greater focus as the business matures. Business solutions accounted for 53% of B2B revenues in 2017 and are slated to continue growing strongly as the Company expands its technology efforts going forward. Other ways that Kcell drives revenues from its core B2B telecommunication offering include transactional and marketing bulk SMS services, which provide companies a secure and confidential way to reach customers, and toll-free short numbers, which can help businesses to increase incoming customer calls by roughly one-third.

Mobile marketing

Kcell's transactional and marketing bulk SMS business was highly successful in 2017, partly because of attractive pricing policies and a confidential and secure platform. This helped the Company to extend the useful life of the service.

Progress made

- Kcell increased bulk SMS revenue by 49.7% in 2017, partly due to outreach efforts to show B2B customers new ways to use the service.
- The Company brainstormed with a bank as a partner to develop a bulk SMS roadmap, which resulted in substantial savings for the customer.

Next steps

- Seek to attract additional bulk SMS customers by continuing outreach efforts.

Toll-free short numbers

Kcell's free-phone product, which allows businesses to set up toll-free short numbers for customers to contact them, is growing rapidly, both organically and with the market. Research shows that using this product can increase customers' internal calls by around 30%.

Progress made

- Kcell began working with customers to help them to find ways to use short numbers.
- The Company used short numbers to help more charitable fundraising and social hotlines.
- Kcell attracted 21 clients by the year-end.

Next steps

- Continue to promote short numbers for charitable fundraising and social hotlines.

Business solutions

Kcell has continued to expand its business solutions offerings, partnering with leading global internet security and graphic design names such as like Kaspersky, Symantec, Kerio, McAffee, Esed, Autodesk and Adobe. Kcell is also a 'silver' status partner of Microsoft and offers integration with the IT company's cloud platform to provide subscription-based services to corporate customers.

Progress made

- By the year-end, business solutions generated 53% of B2B revenue

Next steps

- Expand business solutions rapidly while retaining the existing core B2B client base.
- Begin offering business solutions in Kcell's regional offices to accelerate adoption.

Mobile services

Kcell is a market leader in terms of B2B mobile subscriber plans. One of its newest offerings is the Business Class tariff, which operates somewhat like a loyalty programme by giving subscribers additional benefits, such as discounts at partner businesses. This new tariff has helped to underpin the Company's B2B mobile services business.

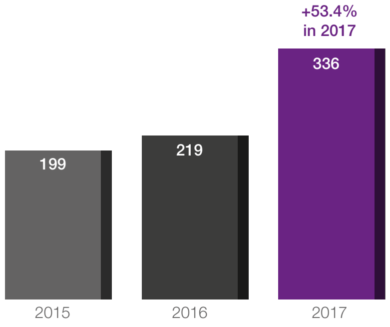
Progress made

- Kcell launched the new Business Class B2B tariff in autumn 2017, aiming to sell it at a higher price by adding value through offerings from partners.

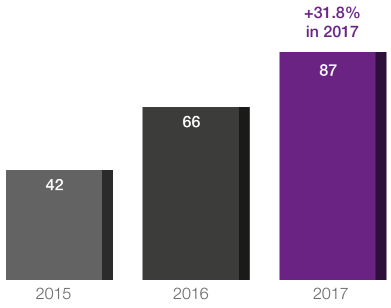
Next steps

- Expand from the initial 100 partners to around 150 for the full launch in 2018.
- Continue to bolster core B2B revenues through the Business Class tariff.

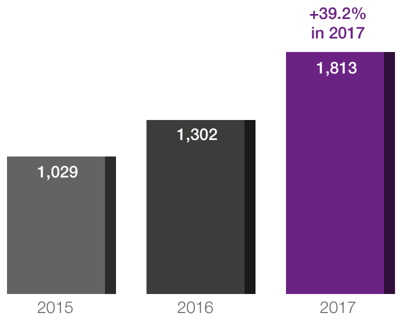
Number of bulk SMS customers



Number of short number customers



Number of business solutions customers



CUSTOMER RETENTION IS KEY

In a market like Kazakhstan, where subscriber churn is high compared with more developed economies, Kcell is aiming to retain customers by offering innovative new products and services.

Executive summary

In 2017, the B2C business generated 89% of Kcell's billed revenues. Core telecommunication services accounted for 99% of the segment's revenues and the main growth drivers were mobile data, digital content and bundled tariffs. The Company's B2C strategy is to transform traditional customers into digital customers by using its digital ecosystem, which is the largest in Kazakhstan. Kcell views digital content development as a major differentiator that will help to better serve and retain customers. It is expected to continue to drive rapid growth in data traffic, which surged from 16 PB in 2013 to 185 PB in 2017, up 1,088%.

PRODUCTS AND SERVICES

The popular new Mobi white-label service is aimed at changing habits to make subscribers used to paying for content, an important development in Kazakhstan's digital services industry. Kcell has become the country's largest digital ecosystem thanks to such content as mobile television, movies, books, music and magazines. More than 500,000 Kcell subscribers actively use Mobi digital content products.

Products

- The new Mobi music product allows users to stream hit songs from major labels including Sony and Universal.
- Kcell launched Mobi TV for streaming television content on mobile devices.
- Another new digital content product is Mobi press, which offers more than 2,200 issues of 70 popular magazines.

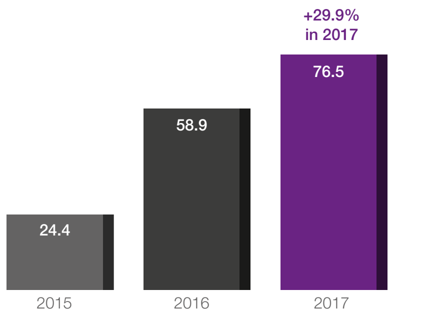
Services

- Kcell launched Mobi Kino, a new video streaming service, which provides access to movies and global TV series in partnership with MeGoGo and Amediateka.
- By the end of 2017, more than 45,000 subscribers were regularly using the new mobile finance service, which was launched in August 2017.
- By the year-end, Kcell had expanded its 4G network to cover 49.4% of the population, up 10 percentage points year-on-year.

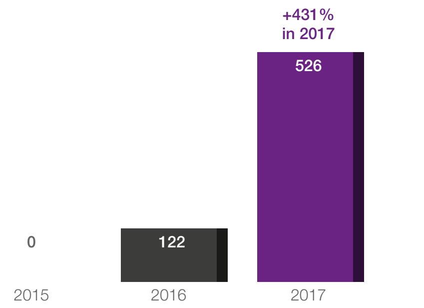
Other initiatives

- Kcell launched speech interactive voice response (IVR) technology featuring virtual assistants; it already handles 50% of all call centre volumes and has fully recouped the investment by encouraging pre-paid customers to sign up for bundles and contract phones.
- In December 2017, the Company opened an innovation lab, which has started working on 'internet of things' (IoT) services.

Contract phone sales (units '000)



OTT users ('000)



Kcell's customer retention efforts have helped it to slow down its churn rate

Kcell's digital content development is a major differentiator on the market

TARIFFS

Given Kazakhstan's high subscriber churn, which is arguably irrational economic behaviour, Kcell feels a responsibility to offer long-term value to its customers through tariffs that bundle services together at reasonable prices. This helped the Company to reverse the revenue trend from negative to positive in 2017.

Activ

- In March 2017, Kcell launched new Activ brand tariff bundles, which are highly competitive on today's market.
- Activ operates as a separate brand that uses Kcell's network and is aimed at mass-market customers.

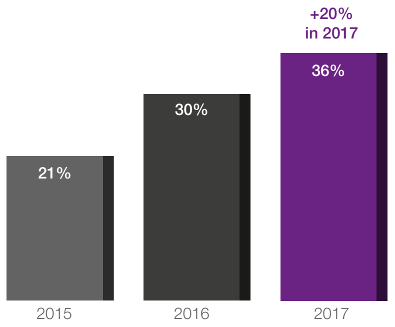
Mobile Circle

- A unique proposition on the market is Kcell's Mobile Circle tariff range, which is primarily aimed at families.
- Mobile Circle tariffs allow a group of subscribers to share bundled data, voice and other services while paying only one subscription fee.

Other

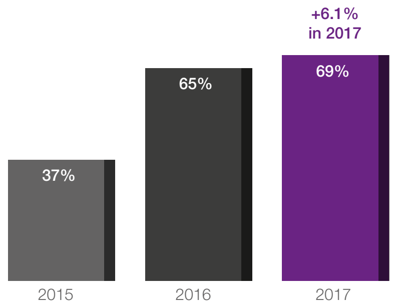
- In 2017, Kcell introduced a service that allows customers to roll over unused mobile internet data from one month to the next.

Bundled customers as share of total subs



In 2017, the B2C business generated 89% of Kcell's revenues

Bundle subs' share of revenue



Digital services are becoming an increasingly important part of Kcell's B2C business

THE FUTURE IS DIGITAL

In 2017, Kazakhstan's economy reached an inflection point. Against this backdrop, the country's telecommunications market is poised to continue growing, amid the ongoing roll-out of the nationwide 4G network and with plans under way for 5G coverage.

Macroeconomic overview

Kazakhstan's economy is the largest in Central Asia and the second largest in the Commonwealth of Independent States. It is a world leader in terms of oil and gas reserves and a major producer of other mineral resources. The country is in the global top 10 of grain exporters and has emerging consumer and service industries. Its location in the heart of Central Asia makes it a major transit route.

Since the early 1990s, Kazakhstan has witnessed a stellar rise in living standards. As measured by the World Bank, the country's gross national income (GNI) per capita, using comparable purchasing power parity (PPP) rates, has risen from US$1,430 in 1993 to US$8,810 in 2016. Today, the World Bank ranks Kazakhstan among the world's upper middle-income economies, placing it on par with countries such as China, Mexico and Turkey.

Based on World Bank statistics, following the macroeconomic headwinds of 2015 and 2016, when GDP growth in local currency terms fell to 1.2% and 1.1% respectively, Kazakhstan's economy fared much better in 2017. The latest estimate from the World Bank is that GDP grew by 3.7% year-on-year, a considerable improvement compared with 2016 and much closer to the 4.2% growth seen in 2014. This suggests that 2017 may have been an inflection point for Kazakhstan's economy.

Brent crude prices rose by 21% year-on-year in 2017, mostly in the second half of the year, and national oil output increased by 9.7% year-on-year, according to the World Bank, following the commissioning of the Kashagan offshore oilfield in late 2016. As oil production is a considerable contributor to GDP, the combined growth in prices and volumes helped to buoy Kazakhstan's economy in 2017. That said, the economy remains exposed to potential external shocks, including any fall in the prices of oil and other commodities, while disposable income will remain a consideration in the prevailing environment.

Kazakhstan's government has continued to build on its record of leading the region in terms of fiscal and market liberalisation by further lowering its policy interest rate from 12% to 10.25% in late 2017, continuing to cut its non-oil deficit, and injecting an additional US$6.5 billion, or some 4% of GDP, into the problem loans fund to help banks' balance sheets recover more rapidly. Since the end of the reporting period, in 2018, the European Bank for Reconstruction and Development and Kazakhstan renewed their partnership framework agreement, which previously covered 2014-17 and includes improving municipal infrastructure, building a green economy and renewable energy sector, making the country more competitive in the global context and preparing national companies for privatisations.

Telecommunications market

Kazakhstan's telecommunications market has certain structural features in common with those of other Central Asian economies. In terms of geographic size, the country is roughly equal to Western Europe. Coupled with its thin population density in rural areas, where nearly half the population lives, this makes it relatively costly to achieve nationwide coverage. Historically, the same factors have led to relatively low fixed-line penetration.

Despite these structural challenges, Kazakhstan has created Central Asia's most developed and competitive telecommunications market. A crucial differentiator is ongoing market liberalisation, highlighted in 2017 by the rapid roll-out of a 4G service, which the regulator opened in early 2016 to all market players. According to BMI, through the existing 3G network, 4G coverage was 60.3% of the country's population at the end of 2017.

A major driver behind the speed with which the nation's 4G networks are expanding is the decision of Kcell and its competitor, Beeline, to enter a network sharing agreement under which the two firms have effectively split the country to use each other's 4G infrastructure. This is a significant advantage given the low population density in most of the country and the rapidly increasing demand for wireless data services.

Mobile telephony has outpaced the fixed-line segment in recent years, while the preponderance of pre-paid cards, network connection charges and other factors have led to many people to having two or more SIM cards. As a result, Kazakhstan retains the highest mobile penetration rate in Central Asia, with subscriber numbers far exceeding the total population.

In 2017, according to BMI, the number of mobile phone subscribers in Kazakhstan reached an estimated 25.8 million, although growth in additions slowed due to saturation in the voice segment. At the end of 2017, mobile SIM penetration exceeded 141.5%, and saturation has depressed average revenue per user (ARPU) numbers. In response, the launch of bundled mobile phone services and contract phones has helped to underpin Kcell's ARPU growth in a highly competitive market.

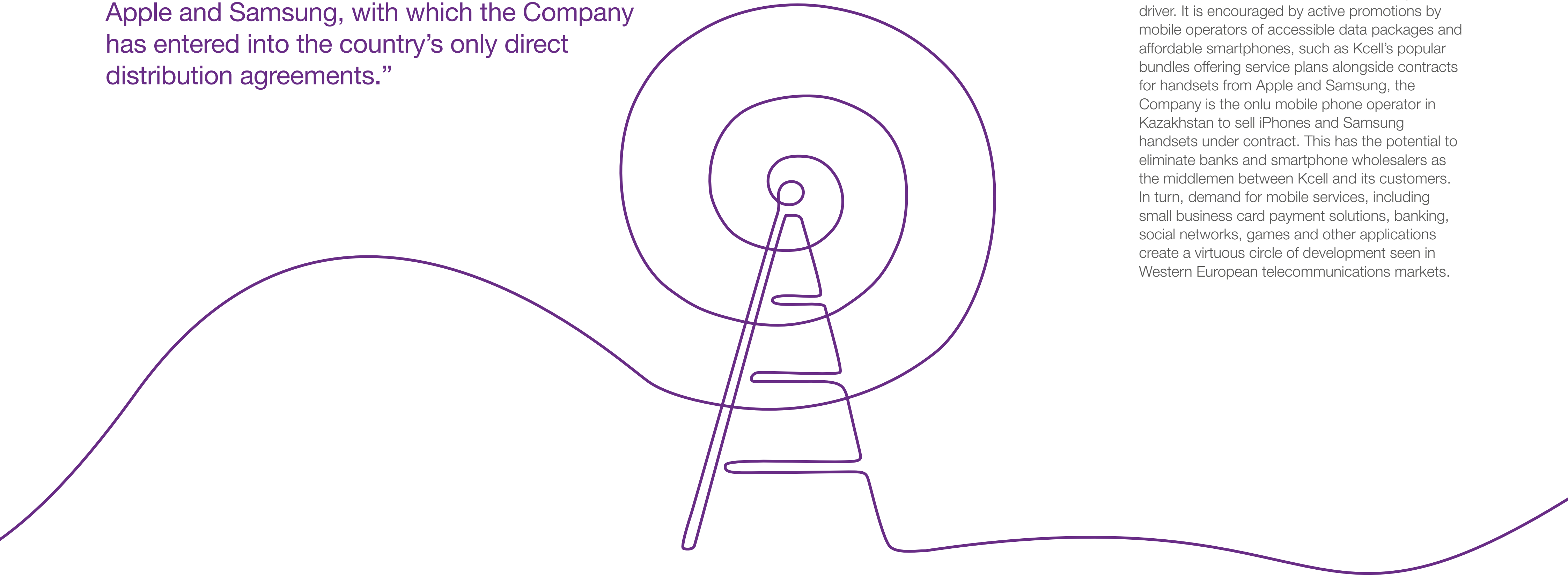
> "Despite these structural challenges, Kazakhstan has created Central Asia's most developed and competitive telecommunications market."

> "The number of handsets will remain an important driver. It is encouraged by active promotions by mobile operators of accessible data packages and affordable smartphones, such as Kcell's popular bundles offering service plans alongside contracts for handsets from Apple and Samsung, with which the Company has entered into the country's only direct distribution agreements."

Mobile internet access

Mobile data traffic growth remains one of the main drivers of overall expansion in Kazakhstan's mobile telecommunications market. A key factor supporting this was the rise in the number of smartphones in the market. According to Kcell's own figures, at the end of 2017, penetration stood at 57.4% for smartphones.

The number of handsets will remain an important driver. It is encouraged by active promotions by mobile operators of accessible data packages and affordable smartphones, such as Kcell's popular bundles offering service plans alongside contracts for handsets from Apple and Samsung, the Company is the onlu mobile phone operator in Kazakhstan to sell iPhones and Samsung handsets under contract. This has the potential to eliminate banks and smartphone wholesalers as the middlemen between Kcell and its customers. In turn, demand for mobile services, including small business card payment solutions, banking, social networks, games and other applications create a virtuous circle of development seen in Western European telecommunications markets.



Continued long-term growth in mobile data services has been assured by the rapid acceptance of 4G by the population, as can be seen in the rapid estimated 52% conversion of 3G data to the 4G network in the first 18 months of operations. Kcell has substantially reduced the capital expenditure required for the roll-out thanks to its network sharing agreement and was already well positioned due to the previous investments in its 3G and 4G network. In 2018, the 4G network is forecast to expand rapidly to cover most of Kazakhstan's regional population centres.

Competitive landscape

Based on Company estimates, Kcell remains the clear market leader in the mobile market in terms of both revenues (42.0%) and market share (37.8%). The competitive situation in the telecommunications sector has also improved following the price wars of previous years.

Kcell's internal figures suggests that it has a market share of at least 60-65% in core business-to-business (B2B) services among the three leading operators, placing it far ahead of competitors. The B2B business is an increasing focus for Kcell, particularly business solutions, which generated 53% of B2B revenues in 2017, out-earning telecom services in the segment.

Regulation

Kazakhstan's Telecommunication Committee, a part of the Ministry of Information and Communications, oversees the mobile telecommunications sector. Its remit includes licensing, the granting of radio frequencies, mobile number portability and legislation on communication.

In 2017, the dialogue between the regulators and Kcell became more open and productive. One major development is that beginning in 2018, operators with foreign capital will have the right to have an independent international licence for voice and internet connection for the first time in Kazakhstan. This should help to significantly reduce operating expenses for operators. The improved dialogue is also encouraging, as government support could be a crucial component to ensure adequate investments are made in vital areas like transmission infrastructure, which is costly to build in a country as large as Kazakhstan.

Outlook for 2018 and beyond

Kcell's customer base is changing dramatically as people become used to using more and more internet services. Kazakhstan is a young nation, generating significant demand for internet access and paving the way for a successful experience with 4G. With the 4G network quickly spreading to cover most of the country's population, partly thanks to Kcell's network sharing agreement, the market has begun to look at what is required for the next step: 5G mobile internet. One of the greatest challenges for the final roll-out of the 4G network and the eventual introduction of 5G mobile internet services is geographical in nature. Kazakhstan's population is located in 14 regions with high density in the two most important cities, Almaty and Astana. In rural areas, the country has a vast number of remote villages with just 500-1,000 inhabitants who still lack access to the mobile network.

In December 2017, Kcell agreed with Ericsson to implement Kazakhstan's first 5G network demonstration in 2018. A complete 'pre-5G roadmap' is now being developed for the full network to outline the requirements. For example, no frequency for the 5G network is currently available, there is no clear roadmap for spectrum, and operators must upgrade the backhaul infrastructure because 5G requires lower latency than the existing networks.

"In December 2017, Kcell agreed with Ericsson to implement Kazakhstan's first 5G network demonstration in 2018."

CONTINUED FOCUS ON COSTS

In 2017, Kcell's higher shares of revenues from data and value-added services, coupled with a consistent focus on reducing costs, helped to break the negative trends seen in recent years.

FINANCIAL HIGHLIGHTS

- In 2017, net revenues increased by 0.1% to KZT147,229 million (KZT147,037 million in 2016)
- Service revenues fell by 0.5% to KZT136,591 million (KZT137,337 million in 2016)
- EBITDA, excluding non-recurring items, decreased by 1.2% to KZT57,321 million (KZT57,989 million in 2016), while the EBITDA margin fell to 38.9% (39.4% in 2016)
- Operating income, excluding non-recurring items, grew by 1.3% to KZT34,174 million (KZT33,740 million in 2016)
- Net financial items totalled KZT9,419 million (KZT8,285 in 2016)
- Net income declined by 19.5% to KZT13,434 million (KZT16,684 million in 2016)
- Free cash flow climbed to KZT10,899 million (KZT -13,293 million in 2016)
- The customer base increased by 23 thousand to 10,009 thousand (9,986 thousand in 2016)

KZT in millions, except key ratios, per share data and changes	**Jan-Dec 2017**	Jan-Dec 2016	Chg (%)
Revenues	**147,229**	147,037	0.1
of which service revenues	**136,591**	137,337	(0.5)
EBITDA excl. non-recurring items	**57,321**	57,989	(1.2)
EBITDA margin (%)	**38.9**	39.4	
Operating income	**31,501**	31,041	1.5
Operating income excl. non-recurring items	**34,174**	33,740	1.3
Net income attributable to owners of the parent company	**13,434**	16,684	(19.5)
Earnings per share (KZT)	**67.2**	83.4	(19.5)
CAPEX-to-sales (%)	**14.7**	34.7	
Free cash flow	**10,899**	(13,293)	

Financial Review continued

Breakdown of revenues

KZT in millions, except %	2017	% of total	2016	% of total
Voice services	**80,400**	54.6	**86,634**	58.9
Data services	**46,358**	31.5	**41,339**	28.1
Value-added services	**9,837**	6.7	**9,351**	6.4
Other revenues	**10,633**	7.2	**9,713**	6.6
Total revenues	**147,229**	100.0	**147,037**	100.0

Net revenues
Net revenues increased by 0.1% to KZT147,229 million (KZT147,037 million in 2016). Service revenues fell by 0.5% to KZT136,591 million (KZT137,337 million in 2016).

Voice services
Revenues from voice services declined by 7.2% to KZT80,400 million (KZT86,634 million in 2016). Voice traffic decreased by 1.2% to 22,678 million minutes (22,948 million minutes in 2016), while the average revenues per minute of use (ARMU) fell to KZT2.2 (KZT2.5 in 2016).

Interconnect revenues rose by 1.0% to KZT21,549 million (KZT21,335 million in 2016).

Data services
Data revenues climbed by 12.1% to KZT46,358 million (KZT41,339 million in 2016). Data traffic increased by 58.5% to 192,691,522 GB (121,587,949 GB in 2016). Growth in data traffic was partially offset by packages with lower tariffs per MB, which resulted in a decrease in the average revenues per MB (ARMB) to KZT0.2 (KZT0.3 in 2016).

Value-added services
Revenues from value-added services increased by 5.2% to KZT9,837 million (KZT9,351 million in 2016), largely due to the introduction of new OTT services.

Other revenues
Other revenues rose by 9.5% to KZT10,633 million (KZT9,713 million in 2016), reflecting higher handset sales.

Expenses

Cost of sales

Cost of sales decreased by 1.9% to KZT90,107 million (KZT91,866 million in 2016), primarily due to lower interconnect expenses of KZT22,870 million (KZT24,283 million in 2016).

Selling and marketing expenses

Selling and marketing expenses dropped by 4.4% to KZT10,506 million (KZT10,988 million in 2016), mainly due to the digitalisation programme and lower staff costs.

General and administrative expenses

General and administrative expenses increased by 9.7% to KZT15,524 million (KZT14,150 million in 2016), mainly due to the tax provision.

Earnings, financial position and cash flow

EBITDA, excluding non-recurring items, fell by 1.2% to KZT57,321 million (KZT57,989 million in 2016). The EBITDA margin was 38.9% (39.4% in 2016).

Net financial items climbed to KZT9,419 million (KZT8,285 million in 2016).

Income tax expense increased by 42.4% to KZT8,648 million (KZT6,073 million in 2016).

Net income attributable to owners of the parent company decreased by 19.5% to KZT13,434 million (KZT16,684 million in 2016), while earnings per share declined to KZT67.2 (KZT83.4 in 2016).

CAPEX was lower at KZT21,648 million (KZT51,017 million in 2016) and the CAPEX-to-sales ratio fell to 14.7% (34.7% in 2016). In 2016, CAPEX included the acquisition of LTE frequencies for KZT26 billion.

Free cash flow increased to KZT10,899 million (KZT13,293 million in 2016).

Financial key ratios

KZT in millions, except %	**2017**	2016
Return on equity (%, rolling 12 months)	**18.0**	23.0
Return on capital employed (%, rolling 12 months)	**23.8**	25.9
Equity/assets ratio (%)	**41.4**	40.1
Net debt/equity ratio (%)	**77.6**	78.3
Net debt/EBITDA ratio (multiple, rolling 12 months)	**1.06**	1.03
Owners' equity per share (KZT)	**372.2**	363.4

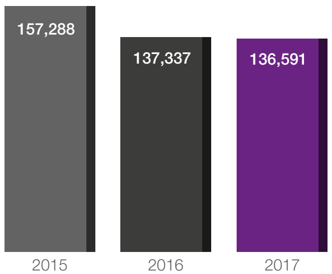
WHAT IS MEASURED IMPROVES

Kcell believes that setting measurable key performance indicators helps to maintain focus on continuous improvement. Our performance on these in 2017 suggests that the Company passed an inflection point in the period.

Financial indicators

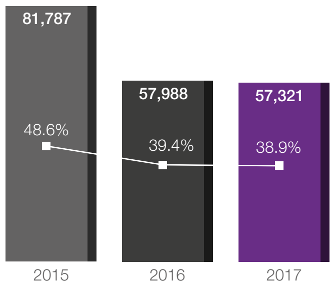
Revenues (KZT mln)

136,591



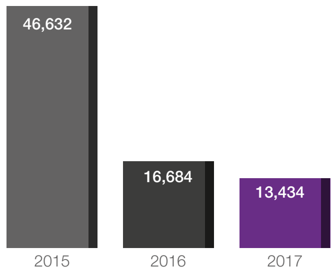
EBITDA, excl. non-recurring items (KZT mln) and EBITDA margin

57,321



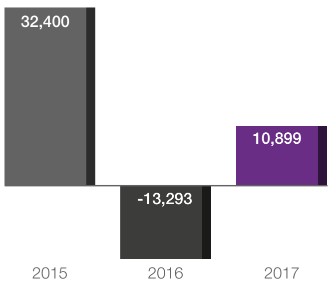
Net income (KZT mln) and net margin

13,434



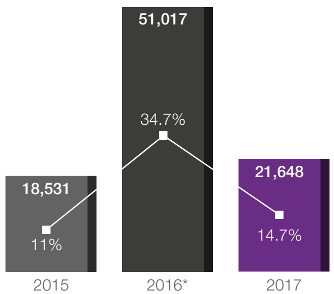
Free cash flow (KZT mln)

10,899



Capital expenditures to sales (CAPEX; KZT mln) and CAPEX to sales ratio

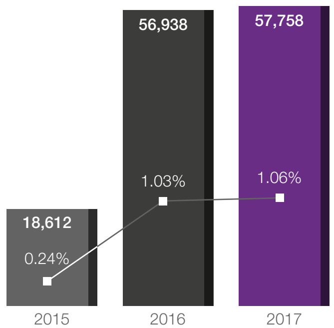
21,648



* Including KZT26 bln for LTE

Net debt (KZT mln) and net debt to EBITDA ratio

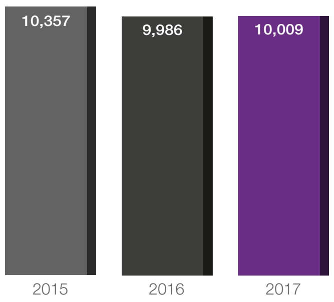
57,758



Operational indicators

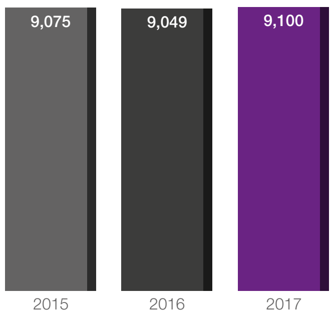
Total subscribers ('000)

10,009



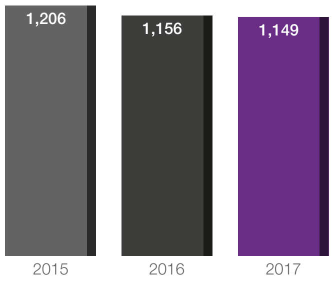
Activ brand subscribers ('000)

9,100



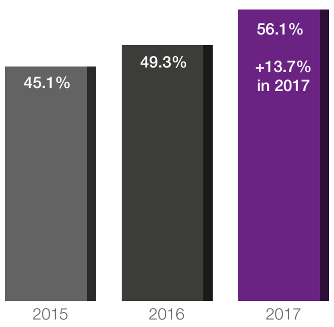
Average revenues per user (ARPU; KZT)

1,149



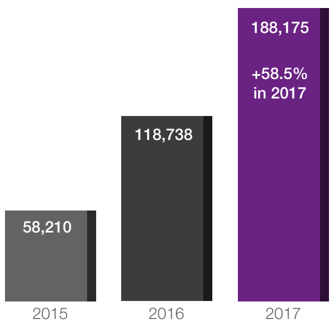
Subscriber churn

56.1%



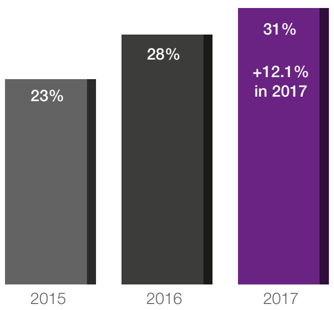
Data traffic (PT)

188,175



Share of data revenues

31%



BE THE CHANGE YOU WISH TO SEE

With a principled and systematic 'zero-tolerance' approach to ethics and compliance, Kcell strives to be a role model for responsible business by eliminating questionable practices and rooting out corruption from every part of its activities.

Responsibility

As one of Kazakhstan's leading companies, Kcell has a high degree of visibility. We understand that this is a privileged position and are committed to being a role model for responsible business. We firmly believe that in steadfastly adhering to the highest standards of ethical conduct in every interaction, we are setting the best example for all stakeholders: investors, customers, employees, partners, suppliers, public organisations and society in general. In doing so, we seek to contribute to and promote an enduring culture of responsible business.

Platform

At the Company, sustainability covers all efforts relating to how we account for our long-term effect on society and the environment. Our responsibility extends along the entire value chain. We believe that when we do good, it strengthens not only our business, but also the communities in which we operate, creating long-term shared value for society and shareholders. Sustainability is a vital part of our business model, strategy and philosophy: through it, we mitigate negative impact and create a positive effect on society.

Kcell channels its responsible business efforts into the following focus areas:

- Anti-bribery and corruption
- Responsible procurement
- Human rights
- Customer privacy
- Freedom of expression
- Environmental responsibility
- Occupational health and safety

These areas are governed by an ethics and compliance framework, the purpose of which is to ensure that the Company has a systematic approach for implementation, monitoring and compliance. As part of the regular risk self-assessment process, all gaps identified in the assessment in 2016 were closed during 2017. To further improve the sustainability of our business practices, the plan is to conduct another self-assessment in 2018.

In 2017, Kcell added a three-person internal due diligence team to its compliance function, which now totals five employees. Four of the five current ethics and compliance staff have TRACE anti-bribery specialist accreditation, also known by the acronym TASA, a renowned international certification programme for compliance professionals. In addition, the fifth member is in the process of obtaining such certification and due to complete the programme in 2018.

“In 2017, Kcell placed a major emphasis on further developing its face-to-face anti-bribery and corruption training programme.”

The new internal due diligence team allows us to perform our own due diligence checks, for both new vendors and existing suppliers. This significant investment in the compliance function confirms our commitment to responsible business. In 2017, the compliance framework was further strengthened by introducing and revising internal guiding documents.

Also in the year, Kcell held a further four governance, risk, ethics and compliance (GREC) meetings. Their purpose is to integrate risk areas and further embed risk management into the decision-making process. Bringing together the executive management, heads of departments and other key employees quarterly, they help to coordinate GREC efforts across the organisation.

Anti-bribery and corruption

Kcell takes a ‘zero-tolerance’ approach to corruption: it is committed to implementing effective measures to prevent, monitor and eliminate questionable business practices in any form. To this end, our efforts to root out corruption from every aspect of our activities are ongoing. In 2017, the internal audit function, an independent body that reports to the Board of Directors, conducted an anti-bribery and corruption programme audit. While it found some room for improvement, overall, no major risk areas in need of critical improvement were identified.

In 2017, Kcell placed a major emphasis on further developing its face-to-face anti-bribery and corruption training programme. Our HR platform enables us to store all policies and instructions in one place and track compliance training of employees, allowing the ethics and compliance team to work with policy owners to identify which employees need training on which policy.

To date, 97% of current employees have successfully completed the foundation anti-bribery and corruption training. The programme is mandatory for all new recruits, who represent the outstanding 3%. During the reporting period, 253 new hires and 32 interns attended the bi-weekly foundation training sessions. In addition, more than 200 other employees underwent an advanced e-learning anti-bribery and corruption programme that teaches practical applications: that’s namely, ‘what not to do”.

The Company is also conducting another course, ‘Ethical Blindness Training’, which covers the reasons why good people sometimes make bad decisions. In 2017, more than 300 employees completed the programme, which focuses on obtaining a broader perspective of ethics and compliance. It helps employees to make better decisions by learning to identify and manage the types of professional pressures that can cause good people to suffer from ‘tunnel vision’ and make bad decisions.

Kcell also provided a more focused course, ‘Ethical Compass Training’, for around 30 members of the due diligence, sourcing, internal buying and procurement teams. These employees, who are at the forefront of our ethics and compliance efforts, received guidance on how to understand and report findings, identify risk and implement mitigation activities.

Another key part of Kcell’s anti-bribery and corruption work was a responsible business survey conducted in 2017. The survey aimed to determine:

- employees’ perception of whether the Company is conducting business in a responsible way in its day-to-day operations;
- how employees view the ‘tone from the top’;
- how ethically the management team behaves;
- whether employees know whom to contact if they have an ethical dilemma in their workplace; and
- whether employees know how/when to report ethical issues.

Responsible Business continued

As part of the survey, employees were also asked to identify which compliance issues they would like to receive additional training on. The three most frequent requests were:

- how to correctly deal with confidentiality and privacy of customers and colleagues;
- how to minimise fraud risk in their work; and
- how to relate to competitors.

Overall, the responsible business survey showed that Kcell employees have a high degree of awareness of ethical standards, the code of conduct and other compliance matters. Interestingly, respondents who had attended our anti-bribery and corruption training were twice as aware of proper compliance practices as the new hires who had not yet done so. This underscores the positive effect of the programme.

Speak-Up line and disciplinary action

Alongside anti-bribery and corruption instruction, another major part of Kcell's mandatory compliance training is the Speak-Up line. This is a secure channel through which all stakeholders can report potential unethical business practices or misconduct. An independent third party manages the system to ensure the utmost impartiality and confidentiality. The portal is available on the intranet for employees and on an external web site for third parties. Messages can be left online and the interface is user-friendly.

To ensure accessibility to and the effectiveness of the Speak-Up line, the service is offered in 19 languages, including Kazakh, Russian and English. There is also a direct link in the 'Responsible business' section on Kcell's external website. To promote the Speak-Up line as widely as possible, we maintain a high-visibility employee communications campaign in our offices. We also have a separate internal reporting line for managers wishing to raise concerns about conduct.

In 2017 a total of 30 whistleblowing reports came via the Speak-Up line from or about Kcell. The types of issues raised related to leadership, violation of policy, conflict of interest, embezzlement, fraud and retaliation. Some 33% of the reports were filed anonymously, while 67% specified the whistleblower's name. All cases reported in 2017 were reviewed or investigated and closed apart from one, which remains ongoing.

Kcell highly values the feedback that it receives via whistleblowing reports. They are seen not as negative, but rather as a positive indication that employees and managers are engaged and support our ethics and compliance approach, and that they have the confidence to speak up without fear of retaliation.

Responsible procurement

With the new internal due diligence team in place, Kcell has now conducted due diligence checks on most local suppliers. In 2017, the team reviewed more than 600 new procurement cases.

Another important part of the responsible procurement approach during the reporting period was the work done on reviewing Kcell's site leases. The project team used the knowledge of relevant risks and local business practices to identify the highest-risk group among more than 7,000 leased sites. The review includes auditing payments and revenue generated at each site in the identified group, as well as comparing with the average market price for each location.

Another risk area that the Company is addressing is transactions with dealers. We have developed a plan to gradually check all dealers who sell our services to ensure that they comply with our responsible procurement requirements.

> "The Company has undertaken meaningful proactive measures to respect human rights, led by a management team with a strong commitment to international standards of business conduct."

Human rights

In 2016, BSR, an independent not-for-profit organisation commissioned by Telia, undertook a human rights impact assessment at Kcell using a methodology based on the UN Guiding Principles on Business and Human Rights. Its report found that the Company has undertaken meaningful proactive measures to respect human rights, led by a management team with a strong commitment to international standards of business conduct. There were also some recommendations – regarding customer privacy, freedom of expression, anti-discrimination, vulnerable groups and labour rights – based on which an action plan was developed. In 2017, Kcell pursued this by focusing on all of the areas highlighted, and there were progress reviews at each GREC meeting.

Customer privacy

Kcell is committed to respecting and safeguarding its customers' privacy. Our aim is to integrate privacy as a natural part of our services, processes, infrastructure and daily activities. We strive to operate highly secure communication networks and take action to prevent unauthorised access to customers' personal data.

The Company's work in this area is guided by the Kcell privacy policy, which sets a consistent standard with regard to respecting customer privacy. Among other matters, the policy defines principles regarding the collection, processing and retention of personal data, transparency, data accuracy, risk assessments, supplier requirements, and technical and organisational measures to protect integrity and confidentiality.

Kcell pursues its customer privacy objectives in accordance with a dedicated road map.
In 2017, 99% of employees completed a mandatory e-learning course regarding the road map.
Overall progress in the area is monitored by a specially appointed officer, a privacy governance organisation and GREC meetings.

Freedom of expression

Kcell believes that its services contribute to social development by enabling information and ideas to be shared openly.

To this end, we have a dedicated policy on freedom of expression in telecommunications. Its primary purposes are to reduce human rights risks relating to government surveillance of communications, and to give customers confidence that we will, wherever possible, respect and safeguard their freedom of expression.

The policy's principles apply to requests, demands and legislative initiatives by governments or national authorities relating to the surveillance of communications, including restrictions on access to networks and internet websites, and signals intelligence.

Environmental responsibility

Kcell cares about the environment in which it exists and operates. We contribute to local and global environmental sustainability by developing, promoting and utilising resource-efficient and environmentally friendly services and by seeking to reduce our environmental footprint. We constantly look for opportunities to maximise the use of best practices and synergies between our businesses.

Kcell's environmental policy follows a structured approach to managing key environmental impacts. We contribute data about our energy and resource consumption for inclusion in Telia's sustainability report, in accordance with Global Reporting Initiative requirements. The consolidated information can be found at https://www.teliacompany.com/en/sustainability/reporting/.

Occupational health and safety

For Kcell, the health and safety of employees is of paramount importance. We implement all measures in this area in accordance with the Labour Code of Kazakhstan and other corresponding regulations.

The Company has a policy and an instruction on occupational health and safety, which define its commitments aimed at safeguarding employees in the workplace. These include: providing safety training and protective clothing and equipment; guaranteeing optimal labour conditions; standardising sanitary labour conditions; making health care services available; and monitoring compliance with occupational safety and health standards.

In 2015, Kcell received the international OHSAS 18001 certification, which has since been renewed annually following independent audits conducted by the BSI (British Standard Institution). In addition, based on risk assessments, the Company developed and implemented safety instructions covering offices, transport, warehouses and field maintenance. Twice a year, Kcell conducts review of OHS risks and implements necessary corrective actions. In the reporting period, around 200 employees underwent safety trainings.

Employees

As a people-centric organisation, Kcell believes that its employees are the lifeblood of its business. As such, we aim to hire, develop and retain talented people and to be an employer of choice in Kazakhstan.

Kcell supports the international human rights and dignity of all employees as outlined by the UN declaration and core International Labour Organisation's conventions.

All employees have a remuneration package that reflects internal equity and external local market conditions. We work with two different international HR consultants to monitor salaries in the local market. Based on the results of research conducted, we make suggestions to the management about shifting pay bands. We also conduct an annual review of employees' fixed pay, based on individual overall performance and differentiated within acceptable salary ranges.

In an effort to create a positive and motivating work environment as well as improve the quality of life of employees and their family members, the Company provides numerous benefits over and above those required by law in Kazakhstan. Our comprehensive benefits package includes: voluntary medical insurance; transportation; mobile communications; a meal allowance and financial aid in the case of sickness of an employee and close relative; or death of a close relative.

As of 31 December 2017, Kcell had 1,921 employees, up 5.5% year-on-year. We support equality and diversity in the workforce. At the year-end, the Company employed 788 male and 1,133 female staff representing more than 30 nationalities.

INVESTING IN A BRIGHTER TOMORROW

Helping people in need and investing in a brighter tomorrow become especially critical in more challenging times. In 2017, Kcell was involved in 17 CSR projects, some of which have been under way for years.

Every business has a symbiotic relationship with the society in which it operates: their success is interdependent. Kcell demonstrated its commitment to pursuing the highest principles of corporate social responsibility (CSR) alongside market leadership almost a decade ago. In 2007, it was the first telecommunications company in Kazakhstan to sign the United Nations Global Compact, which seeks to create a sustainable and inclusive global economy by encouraging businesses to follow key principles regarding human rights, labour, environment and anti-corruption.

Even before then, since its very creation, Kcell has been actively involved in dozens of initiatives aimed at improving life for people where possible. With a view to maximising the benefit of its efforts and organising its approach most effectively, the Company has identified three key areas in which to target support: education, sport and healthy lifestyle, and society.

When evaluating potential projects, Kcell seeks to engage with established partners committed to making a difference over the long term and for as many individuals as possible. Of particular interest are initiatives that strengthen the fabric of society, by contributing to sustainable development, helping those less fortunate and creating equal opportunities for self-improvement, as well as those that drive progress through innovation, integrity and inspiration.

Helping people in need and investing in a brighter tomorrow become especially critical in more challenging times. In 2017, Kcell was involved in 17 CSR projects, some of which have been under way for years, and the Company would like to thank every one of its partners for their support.

Education

In 2017, Kcell received guidance from the Board of Directors to maintain the primary focus of its CSR efforts on its ‘Education for All’ strategy. As education is one of the main drivers of personal, social and national development, making learning accessible to as many people as possible is an overriding priority. The Company seeks to provide ongoing support to both individuals dedicated to self-improvement through education and organisations established to help them, and its work in this area often receives authoritative acclaim.

Situational Kazakh

One such example is an award that Kcell won in 2017 from the American Chamber of Commerce in Kazakhstan for supporting local culture with Situational Kazakh, a mobile application for Kazakh language education. As part of its education-oriented strategy, the Company supported the development of Situational Kazakh, which is an official electronic version of the first volume of the eponymous book written by Kanat Tassibekov.

The application supports smartphones using both the iOS and Android mobile platforms, has a user-friendly interface and, most importantly, is always at hand. Situational Kazakh provides important details of the correct situational and contextual application of idioms, set expressions and word forms in the Kazakh language. The application’s text content is enriched with illustrations and audio.

Open University
One of Kcell's most prominent CSR initiatives of 2017 was the launch of Kazakhstan's Open University (OpenU.kz), which allows anyone interested in self-development to study courses taught in the Kazakh and Russian languages by professors from the country's best state and private universities. The online educational programme is based on the Open edX platform developed by specialists at Harvard University and Massachusetts Institute of Technology.

In the first nine months of operation, more than 1,000 students registered on OpenU.kz. The project allows people in Kazakhstan to study scientific and technical fields and other popular disciplines. The programme offers lectures on mathematics, physics, IT and such specialised narrow areas as business planning and administration, web-programming, developing automated devices and modelling in difficult programming languages. Basics of programming using the Java language, basics of web-programming and robotics have become the most popular lectures among students. Almost 80% of the platform's unique online content is presented in the Kazakh language.

Digital Life
For the past three years, as part of its Activ brand, Kcell's 'Digital Life' mobile literacy programme has aimed to raise awareness about the opportunities and benefits that smartphones and mobile applications offer to society. To date, more than 7,000 people have taken part in over 230 free master classes, which have been conducted in 16 cities nationwide and cover such topics as mobile media, mobile security, mobile education, mobile government and mobile business, among others. Participants in the master classes include schoolchildren and their parents, students, representatives of small and medium-sized businesses, journalists and bloggers.

The organisers of 'Digital Life' are particularly proud of an initiative called 'Grandmas, Grandpas and Smartphones', which was held in 16 cities for the second year in 2017. Its aim is to teach people aged 50 and over to use smartphones and overcome the so-called 'digital barriers', enabling them to enjoy all the benefits of modern mobile technology. Through the course, around 200 people aged 50 and over began to use smartphones for the first time, getting help with installing messaging applications and learning to use social media.

The 'Digital Life' initiative fits with Kcell's drive to increase smartphone penetration and help people to maximise their benefits. The programme continued in 2018, including in February, when nine free training sessions were held throughout Kazakhstan for a total of 253 participants.

Open Championship
Over 29-30 April 2017, the IV Annual Open Championship of Almaty on scientific and technical creativity and robotics among schoolchildren and students was held in Almaty. The Company supported the competition as part of the Kcell Academy project. Overall, 209 teams from all over Kazakhstan took part in the championship, which included engineering, programming and creative projects, as well as fighting robots.

One of the most interesting projects was from students of Nazarbayev Intellectual School of Almaty, who designed a machine for sowing and harvesting that works on solar batteries. Another fascinating project was presented by a team of young engineers from Aktau, whose robot can solve a Rubik's cube in a minute and half. After two days of competition, a total of 42 teams won certificates and prizes from the championship's sponsors and partners.

Purple Breakthrough
In 2017, Kcell supported the 15th international 'Purple Breakthrough' student conference, which was held at Almaty's University of International Business. The theme of the conference, which included students from six universities of Kazakhstan, was 'PR Social Boom'.

In the 'Business Promotion' section, the best team was from KIMEP university with the 'KIMEP Day Care' project, an unusual idea to establish a childcare centre at the university to help young mothers avoid having to take academic leave due to the birth of a child. In the 'PR Networks' section, the winners were students from International IT University with an innovative informational portal about PR in Kazakhstan. In the 'Proper Strategies' section, the best work was presented by a team of four female students from Kazakh-German University with the 'I Am a Citizen of Almaty' project, which allows every visitor to the city to feel like they are a true citizen of Almaty.

Corporate Social Responsibility continued

Sport and healthy lifestyle

Like education, sport is central to the development of individuals, communities and nations. It stimulates health, energy and spirit and encourages teamwork and friendly competition. Kcell provides financial, technological and other assistance to numerous sporting endeavours at the local, national and international level.

28th World Winter Universiade

Kcell was the official mobile operator of the 28th Winter Universiade, which was held in Almaty from 29 January to 8 February 2017. A total of 2,000 athletes from 58 countries took part in the Universiade, which featured competitions in 12 sports at eight sports facilities.

Kcell provided high-quality mobile communication signal within the sports facilities and launched a contact centre that operated using a single short number, 7117, for subscribers of all local mobile operators. The contact centre, which operated 24 hours a day, fielded 4,883 calls from participants and guests of the Universiade mostly regarding the competition schedule, location of sports facilities and how to purchase tickets.

To provide high-quality internet and voice services, Kcell's engineers installed base stations supporting 4G/LTE at 12 facilities, as well as Almaty international airport and the Almaty-1 railway station. In addition, four new base stations supporting 2G/3G/4G were installed within the Shymbulak ski resort, Athletic Village, Halyk Arena and Almaty Arena. Kcell also opened a special service centre for athletes and foreign delegations in the Athletic Village, which provided convenient and comfortable service in English.

During the competitions, Kcell and Activ subscribers talked for 6.4 million minutes, the equivalent of almost 4,400 days of non-stop conversation, and used 69,515 GB of internet traffic at the sports facilities in Almaty.

Camp Shriver

In summer 2017, the Special Olympics in Kazakhstan, with which Kcell has been a partner for more than a decade, organised a Camp Shriver summer sports event with help from the Company. The camp gives young athletes with intellectual disabilities the chance to take part in individual and team competitions, learn new sports and meet like-minded people. The 2017 event was held in Almaty during 20-30 June and some 70 young athletes, 10 coaches and 20 volunteers took part.

Camp Shriver, which began in the US in 1962, is now an international movement, as is the Special Olympics, which was established in 1968. Kcell is especially proud of its work with both organisations, which enable people with intellectual disabilities of all ages to train and compete in sporting events worldwide. Today, the Special Olympics brings together more than 4.9 million athletes with intellectual disabilities.

Short charity numbers

Kcell also puts its technology to good use as part of its charitable fundraising and awareness initiatives to promote a healthy lifestyle. This can be seen in the Company's use of short charity numbers as ways to help improve the outreach and fundraising for its own charitable efforts, as well as those of its customers and partners. In 2017, Kcell helped to support the following charitable campaigns using short numbers:

- Number 6486 – the 'We Will Overcome Autism' campaign aims to raise the awareness of autism among Kazakhstan's society and to help children with this diagnosis.
- Number 9099 – the 'Make a Gift of Life' campaign's purpose is to collect money for children's medical treatment that is not provided in Kazakhstan.
- Number 9962 – the 'Breathe Life' campaign seeks to provide medical equipment for rehabilitation rooms in children's hospitals to decrease fatality rates among children.
- Number 9191 – the 'Helping Hand' campaign collects money for Shugyla Foundation's social projects, which are targeted at low-income families.
- Number 9777 – the 'Humanitarian Help' campaign, in cooperation with Red Crescent International, is a fundraising project for humanitarian activities at different emergency sites that provides food and basic necessities.

Society

Society is the sphere in which we interact: it shapes our lives, meaning that we all have a vested interest in it flourishing. As the leading provider of telecommunications in Kazakhstan, Kcell is at the heart of daily life and strives to use this position to support social development where possible. Some of the key social events that the Company supported in 2017 included the PR Days in Kazakhstan, the Boztorgai Children's Talent Festival and the Media Kuryltai Summit.

Media Kuryltai

For the past four years, Kcell has supported the Media Kuryltai conference, a unique forum that furthers the development of Kazakhstan's media market by fostering the exchange of opinions between representatives of the media, government and business. In total, about 200 delegates from all over Kazakhstan took part in the conference in 2017. In honour of the forum's anniversary, the organisers recognised their long-standing partners, including Kcell, which received the honorary title 'Communication agent of Media Kuryltai'.

Part of what makes the forum unique is that its organisers try to represent the whole spectrum of Kazakhstan's media, gathering in the same hall heads of state and private publishing houses, national and regional media, and highly placed public servants. This year, the conference's main theme was 'Media market: systemic changes and search for new meanings'. Attendees discussed the media's influence on the country's general economic and political system and trends in the media market's development, as well as rising media costs and involvement of investors, and the role of education in the media industry. As part of the conference, master classes were organised for participants on explanatory journalism, how to make news successfully and journalistic standards in the 'fake news' era.

PR Days in Kazakhstan

On 18-19 May 2017, the traditional PR Days in Kazakhstan forum was held at the Intercontinental Hotel in Almaty. Kcell was once again an official partner of the event, which featured more than 220 leading PR specialists, opinion leaders, top managers of the state and business institutions and senior editors of the country's leading publications.

The forum's theme was 'PR Leap Year' in recognition both of the recent leap year and of the difficult year that the market has experienced. Representatives of Telia and Kcell shared their experience and vision of PR communications in the difficult modern realities. During her speech, Irina Stradzhesku, head of Telia's Eurasia Communication Division, spoke about trusting business with a human face. Natalya Eskova, head of communications at Kcell, shared the Company's experience on how to respond to crises.

It is important to note that in addition to the general discussion of crisis communications, the topic of government relations, which receives scant attention in the country, was thoroughly discussed.

TEDx Almaty

Kcell was pleased to partner for the seventh year in a row with TEDx Almaty 2017, which sought to explore what is hidden 'On the far side of the moon'. This slogan alludes to the gaps that exist in society – the misunderstandings and hidden aspects that we do not understand – that can provoke fear in people, causing them to close off from society.

In the past seven years, more than 3,000 people have come to TEDx Almaty to be inspired by the ideas of speakers from Kazakhstan and around the world. Thousands more have watched the videos from these events online. At the 2017 conference, around 500 participants heard 12 lectures that covered such varied fields as the basic sciences and music.

Social hotlines

Another aspect of Kcell's short charity number initiative is social hotlines, including for the protection of children's rights, a new focus after Telia's human rights assessment. The short number hotlines introduced in 2017 include:

- Number 150 – the 'Psychological Helpline for Children and Teens' is a new joint project with Crisis Union Centres that provides an easy number for children, teenagers, parents and friends to call for psychological consultations on protection from violence.
- Number 1422 – the 'Mothers' House' adoption support hotline.

ACCOUNTABILITY, TRANSPARENCY, RESPONSIBILITY

Kcell is committed to international best practice in corporate governance, as reinforced by its listing on the London Stock Exchange. The Company has established a rigorous corporate governance system, underpinned by strong institutions, to ensure accountability, transparency and responsibility throughout every area of the business.

The Kcell Corporate Governance Code has been adopted by the General Meeting of Shareholders. It is based on the Kazakh Model Code, Telia's Code of Ethics and Conduct and the UK Corporate Governance Code, and complies with the regulations of the Kazakhstan Stock Exchange concerning joint stock companies and securities.

Corporate governance at Kcell is based on the principles of fairness, honesty, responsibility, transparency, professionalism and expertise. The Company's system of corporate governance: requires respect and protection for the rights and interests of all stakeholders; increases Kcell's efficiency and market value; and promotes financial stability and profitability.

Kazakhstan Model Code

Corporate governance guidelines for Kazakh companies are set out in the Kazakh Model Code, which is based on international best practice in corporate governance. The Model Code contains certain general rules and recommendations regarding corporate governance that may be applied on a voluntary basis.

UK Corporate Governance Code

In keeping with Kcell's GDR listing on the London Stock Exchange, the Company is aiming to move towards compliance on a voluntary basis with the UK Corporate Governance Code.

Corporate governance principles

Protecting the rights and interests of shareholders	The Company guarantees fair and equitable treatment of all shareholders, assists shareholders in participating effectively in key decisions and provides detailed information relevant to their interests.
Effective management of the Company by the Board of Directors and Chief Executive Officer (CEO)	The Board of Directors aims to increase the Company's market value and provide shareholders with a balanced and accurate assessment of progress and prospects. The CEO manages the Company's daily operations in accordance with the established business plan and development strategy.
Transparency and objectivity in disclosure of information on Company operations	The Company aims to ensure maximum transparency through the timely and accurate disclosure of information.
Legality and ethics	The Company operates in strict accordance with the law, its Corporate Governance Code and generally accepted standards of business ethics.
Effective dividend policies	The Company pays dividends in accordance with the law, the Charter and the relevant resolutions of the General Meeting of Shareholders. Net income is distributed in accordance with the decision of the General Meeting of Shareholders on payment of dividends, taking into account the Company's development goals and the ratio of long-term net debt to EBITDA.
Effective human resources policies	The Company guarantees its employees' rights under the law and the Kcell Code of Ethics and Conduct, developed based on Telia's Code of Ethics and Conduct. The Company develops partnership relations with staff to address social issues and the regulation of working conditions.
Environmental protection	The Company considers the need for environmental preservation in conducting its operations and complies with environmental safety standards established by the law and its Code of Ethics and Conduct.
Settlement of corporate disputes	In the event of a corporate dispute, participants can seek resolution through negotiation, in order to effectively protect the rights of all shareholders and the Company's reputation.

Corporate governance policies

Kcell has adopted a range of policies in support of its commitment to establishing a strong corporate governance framework. They include the following:

- Corporate Governance Code
- Instruction on Allocation of Work Between the Board and CEO
- Procurement Policy
- Financial Management Policy (second version)
- Insurance Policy
- Risk Management Policy
- Communication Policy
- Recruitment Policy
- Remuneration Policy
- Insider Information Policy
- Insider Trading Policy
- Security Policy (second version)
- Code of Ethics and Conduct
- Anti-Corruption Policy
- Privacy Policy
- Freedom of Expression in Telecommunications Policy
- Occupational Health and Safety Policy
- Supplier Code of Conduct
- People Policy
- Sponsorship and Donations Instruction
- Environmental Policy
- Competition Policy

Corporate Governance continued

Board of Directors

Kcell's Charter sets out the duties of the Board and the CEO. Under the Charter, the Board is responsible for the general management of Kcell's activities. Besides formulating strategies and approving plans for the Company's development, the Board is responsible for taking: decisions on establishing Kcell branches and representative offices; on the Company acquiring or disposing of 10% or more of third-party shares; on concluding major transactions and transactions with related parties; on approving annual budgets; and on deciding other issues that belong to the exclusive competence of the Board of Directors according to the Company's Charter and the Joint-Stock Company Law of the Republic of Kazakhstan.

The CEO and executive management of Kcell are a highly professional team of experts with experience spanning telecommunications, finance, marketing and information technology. The Company's Charter details the CEO's responsibilities in managing daily operations. These include all matters not within the exclusive jurisdiction of the Board of Directors or the Annual General Meeting (AGM) of Shareholders. In addition, the CEO is responsible for executing decisions taken by the General Meeting (GM) of Shareholders and the Board of Directors.

Membership of the Board of Directors

Members of the Board of Directors are elected at the GM, where their terms of office are also decided. The current members of the Board of Directors have been elected for the term until the next AGM, the agenda of which will include the issue of re-election of the Board of Directors.

The Board is chaired by Jan Rudberg*. The CEO, Arti Ots, is not a member of the Board. The other members of the Board are:

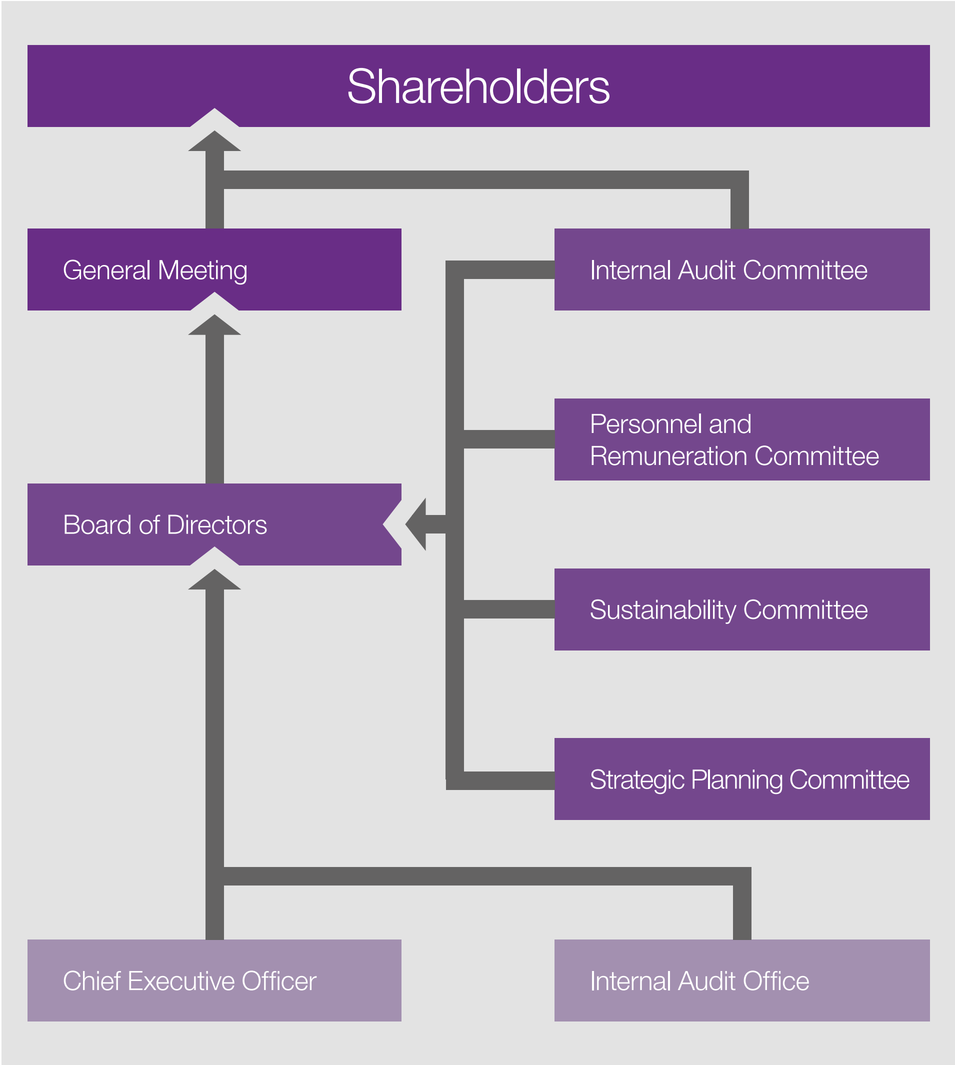
William H R Aylward*
Vladimir Smirnov*
Ingrid Stenmark
Douglas Lubbe
Emil Nilsson
Peter Lav

* The Company Charter and the law require that at least 30% of the members of the Board be independent Directors. UK legal advice has confirmed that Mr Rudberg, Mr Aylward and Mr Smirnov are independent in accordance with the UK Corporate Governance Code (section B.1.1).

The Directors' biographies are on pages 49-50.

In 2017, no members of the Board of Directors held shares in Kcell.

Corporate structure



Committees of the Board of Directors

In line with the legislation on joint stock companies in Kazakhstan, Kcell has established the following committees to consider important issues and prepare recommendations for the Board of Directors: Strategic Planning Committee, Personnel and Remuneration Committee, Internal Audit Committee and Sustainability Committee (previously the Social Matters Committee, it was renamed in 2014 as part of the Company's increasing focus on sustainability).

The Board may create other committees at its discretion. The chairperson of each committee is an independent Director. The law also requires that committees be drawn from members of the Board of Directors who have the necessary expertise to serve on the given committee. All committees are advisory bodies of the Board of Directors.

Committee name	Role	Chairman and members
Strategic Planning Committee	Makes recommendations to the Board of Directors on the Company's strategic development. At least one meeting is held each year.	William H R Aylward (Chairman) Jan Rudberg Vladimir Smirnov Douglas Lubbe Emil Nilsson Peter Lav Ingrid Stenmark
Personnel and Remuneration Committee	Makes recommendations to the Company's Board of Directors on qualification requirements for employees, appointment and dismissal of certain employees, bonuses and salary for management bodies and internal documents evaluating staff fitness, training and motivation of employees. Minimum of two meetings are held each year.	William H R Aylward (Chairman) Emil Nilsson Ingrid Stenmark
Internal Audit Committee	Makes recommendations to the Company's Board of Directors on financial statements, internal controls and risk management, and internal and external audits. Four meetings are held each year.	Jan Rudberg (Chairman) Douglas Lubbe Peter Lav
Sustainability Committee	Makes recommendations to the Company's Board of Directors on internal documents related to: social accountability and sustainable development; improvement of the sustainability strategy; development and implementation of the Company's policies and procedures relating to environmental and social sustainability, including but not limited to, respecting human rights, environmental safety, social responsibility, compliance with business ethics requirements in accordance with the Company's internal documents and applicable legislation. Two meetings are held each year.	Vladimir Smirnov (Chairman) Ingrid Stenmark Jan Rudberg

Board activities

Kcell uses specialist software that is designed to improve Board communications and effectiveness. This provides end-to-end security for its governance and workflow management. The Board of Directors held eight meetings in total during 2017: five were conducted in person and three via conference calls, and more than 48 decisions were adopted by voting in absentia.

The Board's activities during 2017 included:

- Updates on business, commercial, operational and legal matters, and approvals arising from these
- The 2017 annual operating plan and budget
- Approvals of major contracts, agreements and purchases
- Approval of the appointment and terms of employment of the members of the senior management and executive bodies of Kcell subsidiaries
- Approval of voluntary liquidation of AR-TELECOM LLP, a subsidiary wholly owned by Kcell
- Preliminary approval of the 2017 annual financial report and approval of quarterly financial reports
- Convocation of the 2017 AGM, including dividend proposals
- Interested-party transactions approval
- Approval of revisions to policies, including the updated Financial Management Policy and Security Policy
- Approval of changes to the terms and conditions of loan agreements
- Approval of the registration of the local bond programme totaling KZT50 billion and the subsequent placement of the first issue, totaling KZT30 billion

The Board's agenda for 2018 is as follows:

There are five Board meetings scheduled for 2018. As well as regular items covering financial results, risks reviews and reports from the CEO and Board committees, the Board's schedule includes: a review of the Company's policies; business development projects; public affairs; year-end matters, including the external audit report, annual report and GM; strategy; sustainability approach; and the annual operating plan. In addition, ad hoc meetings or conference calls will be held as and when required for approvals when there is no scheduled meeting planned.

Accountability and viability

The Board of Directors is responsible for preparing the annual report and accounts. They consider that the 2017 annual report and accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the Company's position and performance, business model and strategy. A description of the basis on which Kcell generates value over the longer term, its business model, and the strategy for delivering the objectives of the Company are explained in the Strategic Report on pages 13-16.

The Board has assessed the Company's prospects over the next year, being the period over which the key risks facing the Company can be accurately assessed and mitigated. Based on this assessment, the Board has a reasonable expectation that the Company will be able to continue to operate and meet its liabilities as they fall due over the period of their assessment.

The Board has carried out a robust assessment of the principal risks facing the Company, including those that would threaten Kcell's business model, future performance, solvency or liquidity. These risks and an explanation of how they are being managed or mitigated are described in the Risk Management section on pages 53-56. The Board monitors the Company's risk management and internal control systems, and has reviewed their effectiveness during the year. This review has covered all material controls, including financial, operational and compliance controls.

Internal Audit

The Internal Audit function is responsible for evaluating how exposed Kcell's governance, operations and information systems are to risks that could affect the:

- Achievement of strategic objectives
- Reliability and integrity of financial and operational information
- Effectiveness and efficiency of operations and programmes
- Safety of assets
- Compliance with laws, regulations, policies, procedures and contracts
- Potential for fraud occurring

The function consists of the Internal Audit Committee, which reports to the Board of Directors, and an Internal Audit Unit, which was established in 2013 and reports to the Committee.

The Committee met five times during 2017. It considered significant issues in relation to financial statements and the findings of an internal audit.

The Committee also has primary responsibility for making recommendations on the appointment, reappointment and removal of the external auditor to the General Meeting of Shareholders. Deloitte has been the Company's auditor since 2014. To protect its independence, Kcell does not engage Deloitte for any non-audit services for Kcell.

Remuneration of the Board of Directors

In accordance with Kcell's regulations on the amount and terms of remuneration and compensation of expenses paid to members of the Board of Directors for the fulfilment of their duties, remuneration is paid to independent Directors and to Directors who are not employed at Telia. The amount of remuneration paid to the Board of Directors consists of two parts: a fixed annual remuneration, which depends on Board members' attendance at meetings, and an auxiliary annual remuneration for participation in Board committees. The regulation also provides for the compensation of expenses that the Board members incur when fulfilling their duties.

The General Meeting of Shareholders held in 2012 approved the following pre-tax annual remuneration for those independent Directors and Directors who are not employed at TeliaSonera: fixed annual remuneration of US$75,000; auxiliary annual remuneration for chairing the Board of Directors of US$25,000; US$15,000 for participating in the Internal Audit Committee; and US$6,000 for participating in any other Board committee. These payments remained unchanged in 2016 and 2017.

According to the payment terms, 50% of the fixed annual remuneration fee and annual additional remuneration for committee membership is paid six months after a Director takes office; and the remaining 50% and additional annual remuneration for committee membership is paid one year after a Director takes office.

The total remuneration paid to the Board of Directors in 2017 was US$270,900 (after tax).

Relations with shareholders

The Board is in regular dialogue with Kcell's major shareholders.

Board of Directors

Jan Rudberg

Chairman, Independent Non-executive Director

Jan Rudberg has been the chairman of the Board of Directors and an independent Director at Kcell since 20 November 2012.

Mr Rudberg is the chairman of the board of directors at Hogia AB and served as an independent director and the chairman of the Audit Committee at PJSC MegaFon. He is a member of the board of directors at Turkcell Iletisim Hizmetleri A.S. and the chairman of the board of directors at CJSC Belarusian Telecommunications Network.

From 1994 to 2003, Mr Rudberg held various managerial positions with Telia AB. He previously served as CEO of Tele2 AB, executive vice president of Nordbanken AB and CEO of Enator AB.

Mr Rudberg holds a degree from the Gothenburg School of Business Administration, Sweden.

William H R Aylward

Independent Non-Executive Director

William H R Aylward has been an independent member of the Board of Directors at Kcell since 24 May 2013 and has been Chairman of the Strategic Planning and Personnel and Remuneration Committees.

Mr Aylward has extensive experience working as the chairman, CEO and non-executive director of both private and public companies across various sectors, including telecommunications, media and technology (TMT), energy, software and services, and manufacturing. He is currently the executive chairman of ABCO Holdings Limited, which is involved in intelligent metering systems, software and data analytics, as well as the design and manufacturing of sophisticated electronic avionics systems. From 2011 to 2016, he served as the chairman and CEO of Alchemy Group, which primarily focused on TMT and energy.

Mr Aylward has been a strategic investment adviser at Redwave Technology Ltd since 2006. From 2008 to 2011, he was CEO of Belvedere Media Santa Monica, CA. Before that, he held senior management positions in numerous companies. He has extensive M&A experience.

Mr Aylward graduated from the University of London with a BSc in Mechanical and Production Engineering.

Vladimir Smirnov

Independent Non-executive Director

Vladimir Smirnov has been an independent member of the Board of Directors at Kcell since 21 May 2014.

Mr Smirnov's background is in competitive sport at the international level. A professional cross-country skier since 1976, he won a gold medal at the 1994 Winter Olympics in Lillehammer, was the world champion four times, won the World Cup 30 times and has held the World Cup General twice. He was also a member of the International Olympic Committee (2000-02), its Athletes' Commission (1998-02) and vice president of the International Biathlon Union (2006-10). In 1991, he moved to Sweden as a professional athlete.

From 1999 to 2004, Mr Smirnov ran his own company, Vladimir SMIRRE Smirnov AB, working in cooperation with Veidekke AS in Norway. From 2004 to 2006, he was the managing director for Almaty's application to host the 2014 Winter Olympics. From 2005 to 2007, he consulted for Scania in Kazakhstan, before becoming managing director of Scania Central Asia. In August 2014, he became the general director of the Astana Presidential Professional Sports Club.

Mr Smirnov graduated from the Kazakhstan Institute of Physical Culture and Sport in 1985. In September 2014, he became the Honorary Consul of the Republic of Kazakhstan to the Kingdom of Sweden, having also held the position from 2001-04.

Ingrid Stenmark

Non-Executive Director (representative of the shareholder Fintur Holdings B.V.)

Ingrid Stenmark has been a member of the Board of Directors at Kcell since 21 May 2014.

Since joining TeliaSonera in 1994, Ms Stenmark has held several managerial positions in the Group. Currently, she is a senior vice president, overseeing strategy and responsible business, and head of the CEO's office. Her responsibilities include Group strategy, risk management and the Internal Audit department, which reports to the Audit Committee. Previously, she was acting general counsel and head of regulatory affairs, and she remains responsible for Turkcell and other Telia group companies. She was also a member of the board of directors at MegaFon.

Ms Stenmark holds a master's in Law from Stockholm University.

Douglas Lubbe

Non-Executive Director (representative of the shareholder Fintur Holdings B.V.)

Douglas Lubbe became a member of the Board of Directors at Kcell on 3 February 2015.

Mr Lubbe joined TeliaSonera as CFO for Eurasia, based in Istanbul, in July 2014. Before that, he had been working at Vodacom Group in various senior managerial positions since 1997. During his tenure there, he served on numerous boards and board sub-committees at subsidiaries. Between April 2012 and September 2012, he served as interim managing director at Vodacom Mozambique, successfully seeing off the launch of a third operator shortly after his arrival. He also started a project to overhaul the sales and distribution network. In 2013, he was transferred to the Mergers and Acquisitions division in Vodacom Group and was responsible for the integration of a pending acquisition that would combine a fixed-line operation with the South African business.

Mr Lubbe is a qualified chartered accountant and a registered member of the South African Institute of Chartered Accountants. He also holds an MBA from the University of Southern Queensland in Australia and an executive management diploma from the University of South Africa.

Emil Nilsson

Non-Executive Director (representative of the shareholder Fintur Holdings B.V.)

Emil Nilsson became a member of the Board of Directors at Kcell on 6 January 2016.

Mr Nilsson joined TeliaSonera as vice president and senior adviser in early 2015 and was appointed as senior vice president and head of the Eurasia region in October 2015. Since August 2013, he has been a board member of the Swedish national team for European handball.

Mr Nilsson started his career at Ericsson in 1996 and held various positions in Sweden, Brazil, the US and Austria. His roles included CFO and acting president of Ericsson Brazil, CFO and COO of the North America region, and president of the Central Europe region. He left Ericsson in August 2012 to become the executive vice president and CFO of Sandvik Group in Sweden, a publicly listed company with 50,000 employees. He worked there for just over a year and then decided to fully dedicate himself to his family business, which was founded earlier in February 2012.

Mr Nilsson holds a degree in Finance from the University of Stockholm.

Peter Lav

Non-Executive Director (representative of the shareholder TeliaSonera Kazakhstan Holding B.V.)

Peter Lav became a member of the Board of Directors at Kcell on 6 January 2016.

Mr Lav has been employed by TeliaSonera since 2000 and has held several managerial positions in various legal departments within the Group. These include acting general counsel for the Eurasia region (December 2013-April 2014), general counsel for TeliaSonera International Carrier (February 2011-December 2013), general counsel for broadband wholesale (January 2007-February 2011), vice president and general counsel for TeliaSonera International Carrier (February 2004-January 2007), legal counsel for TeliaSonera International Carrier and network sales within Telia AB (September 2000-February 2004). Prior to joining TeliaSonera, he worked at the Lindskog Malmström Advokatfirma law firm and Stockholm City Court.

Mr Lav holds a master's in European and Comparative Law from the University of Limburg, the Netherlands, and a master's in Law from the University of Uppsala, Sweden.

Executive Management

Arti Ots
CEO

Arti Ots became CEO on 19 December 2014. After receiving regulatory approval, he began in the role on 9 February 2015.

Before his appointment, Mr Ots was vice president for commercial and business development at TeliaSonera Eurasia from May 2014. Between February 2012 and May 2014, he was CEO of Elion, TeliaSonera's broadband services division in Estonia. Prior to becoming CEO, he spent 10 years at Elion, working as the director of marketing between 2004 and 2012.

Mr Ots holds an MBA from Henley Business School, UK.

Andis Locmelis
Finance Director

Andis Locmelis became Director of the Finance department at Kcell on 21 November 2017.

Mr Locmelis brings over 17 years of CFO experience in the telecoms, media and technology sector, including in the mobile and fixed telecoms, internet and cable TV segments, as well as in the fast-moving consumer goods sector.

Prior to joining Kcell, Mr Locmelis served as the CFO of MegaFon in Russia, CFO of Lattelecom in Latvia, and CFO and supply chain director at Mobilink in Pakistan.

Mr Locmelis holds an EMBA and MBA (Finance) from RTU Riga Business School, Latvia.

Sasa Lekovic
Technology Director

Sasa Lekovic has been Director of the Technology department since 1 July 2016.

Mr Lekovic has more than 19 years' experience in the IT and telecommunication industry. He joined Kcell on 1 September 2015 as network and infrastructure manager in the Technology department and became acting Technology Director on 1 March 2016. He continues to lead the business area in transforming and implementing strategic Company-wide projects. Prior to joining Kcell, he was chief technical officer and a board member at Telecom Serbia Group.

Mr Lekovic has an MSc in Electrical Engineering from the University of Belgrade, Serbia.

Irina Savina
Consumer Director

Irina Savina has been Director of the Consumer department since 2 March 2016.

Ms Savina has more than 15 years' international experience in executive positions in sales and marketing in various companies, including MTS, Velcom, ASBIS and Procter and Gamble. Prior to joining Kcell, she was chief commercial officer at Altel.

Ms Savina holds a degree in Accounting, Analysis and Audit from Belarus State Economical University and in Robots and Robotics from Belarus Polytechnic Institute. She also holds a certificate from INSEAD for a programme that included a focus on business marketing and sales strategy in telecommunications and was specially developed for talented managers at Telecom Austria.

Aliaksandr Prakapovich
Centralised Procurement Director

Aliaksandr Prakapovich has been Director of the Centralised Procurement department since 18 December 2014.

Mr Prakapovich joined Kcell in August 2014 as Deputy Procurement and Administration Director and led the drive to centralise the procurement function. Before that, he spent eight years in procurement at Velcom, the first GSM operator in Belarus, ultimately heading a department.

Mr Prakapovich holds a degree in International Economic Relations from the Institute of Parliamentarism and Entrepreneurship, Belarus.

Assya Kalinkina
HR Director

Assya Kalinkina has been Director of the Human Resources department since 5 January 2016.

Ms Kalinkina has more than 15 years' experience in human resources in various companies, including Danone Kazakhstan, Derbes Brewery and Halyk Bank. Prior to joining Kcell, she was HR director at Sandoz CIS.

Ms Kalinkina has a professional degree in Human Resource Management from Robert Gordon University, UK.

Damir Zhanbakiyev
Legal Affairs and Government Relations Director

Damir Zhanbakiyev joined Kcell in May 2014 and has been Director of the Legal Affairs and Government Relations department since 1 September 2016.

Mr Zhanbakiyev has 11 years of experience in jurisprudence. He previously worked as a chief expert at ATF Bank, head of legal support at Kazkommertsbank (now Qazqom Bank) and head of litigation at a law firm.

Mr Zhanbakiyev holds a degree in Jurisprudence from Kazakh State Law University, Kazakhstan.

Vadim Lyu
Enterprise Director

Vadim Lyu has been Director of the Enterprise department since 17 March 2017.

Mr Lyu has 14 years of experience in IT and business consulting. He previously worked as a senior consultant at Deloitte Belgium and Deloitte in Kazakhstan, and was the founder of iBEC Systems.

Mr Lyu holds a degree in Jurisprudence from Almaty State University, Kazakhstan.

Kazbek Shaimov
Customer Channels Director

Kazbek Shaimov joined Kcell in November 2008 and has been Director of the Customer Channels department since 1 September 2016.

Mr Shaimov has 11 years of experience in telecommunications. He previously worked as an executive director for JTI, an FMCG company in Pavlodar Region, Kazakhstan.

Mr Shaimov holds a degree in Physics and Computer Engineering from Pavlodar State University, Kazakhstan.

COMMITTED TO CONTINUOUS IMPROVEMENT

Like any business, Kcell encounters various potential and actual risks while conducting its activities. To identify and mitigate these, it has created a robust risk management system. The Company is committed to continuously improving its risk management methods and process to ensure that its business functions without disruption.

Responsibility

In 2013, Kcell adopted a risk management policy based on the principles contained in Telia's Group policy. Overall responsibility for the Company's risk profile lies with the Board of Directors, which is supported in this area by the Internal Audit Committee. At the same time, Kcell's aim is to foster a culture of risk awareness, management and accountability throughout the Company. The ultimate objective is to identify risks rapidly and ensure that all employees take responsibility in their work.

Risk management is fully integrated into the business planning and control processes, with established procedures, clear lines of reporting and regular reviews.

On an operational level, within each business area, departmental heads and dedicated risk coordinators are responsible for:

- Identifying, assessing, managing and mitigating risks.
- Making relevant and reasonable efforts to safeguard business continuity.
- Reporting risks in a timely and clear manner.
- Recruiting staff to oversee effective risk evaluation, mitigation and reporting processes.
- Maintaining and promoting overall risk awareness in their area of responsibility.
- Ensuring that the department's risk management activities are adequately documented.

Framework

Kcell's risk management framework has been developed in line with the Committee of Sponsoring Organisations of the Treadway Commission's Enterprise Risk Management framework.

Kcell's risk management process identifies and evaluates potential threats to the business and implements plans to ensure its continuity. It enshrines risk management as part of daily operations: for example, all business units are tasked with continuously identifying, assessing and monitoring risks across all activities.

Process

The main principles of the risk management process are:

- Integrity: Kcell considers the elements of its overall risk in the context of a corporate risk management system.
- Openness: the risk management system is easily accessible and understandable.
- Structuring: the risk management system has a clear structure.
- Awareness: the risk management system necessitates objective, accurate and timely information.
- Continuity: the risk management process is ongoing.
- Cyclicity: the risk management process is a constantly recurring cycle consisting of main components.

Risk identification

Kcell uses risk identification to categorise its exposure to uncertainty. This requires an intimate knowledge of the Company, the market in which it operates and the legal, social, political and cultural environment in which it exists. It also involves a sound understanding of its strategic and operational objectives, including factors critical to its success, as well as related threats and opportunities.

Through the risk management framework, Kcell has identified several principal risks and uncertainties that are key to its day-to-day operations: strategic, operational, financial, legal and natural disaster/catastrophe.

Strategic risk

Strategic risks represent the potential for losses due to changes or errors in defining and implementing the business strategy, the Company's development, competition, changes in the political or regional environment and customer or industry changes. Most are considered high-risk, requiring the attention of the management.

Strategic risks include increased price competition caused by the activities of other mobile operators or changes in legislation. Kcell seeks to mitigate these risks by protecting its leadership in 'strong' regions and increasing market share by launching competitive tariffs and products.

Operational risk

Operational risks are defined as the potential for losses due to defects or errors in internal processes, the supply chain, recruitment, culture, regulations, the Board's composition and information systems and technologies. Most of them have a low-risk rating and mitigating actions are already in place as part of the daily risk management procedures.

Financial risk

Kcell's activities involve various financial risks. The Company's risk management framework seeks to minimise potential adverse effects on performance from fluctuations on financial markets and other macro and microeconomic factors. Kcell does not use derivative financial instruments to hedge risk exposure.

Alongside its principles for overall risk management, Kcell has written policies covering specific areas of financial risk, including credit, foreign exchange and interest rate risk.

Credit risk

Kcell has introduced policies to ensure that sales of products and services are made to customers and distributors with an appropriate credit history. If corporate customers have independent ratings, they are used. If not, risk control assesses a customer's credit quality based on financial position, past experience and other factors. The Company's management reviews ageing analysis of outstanding trade receivables and follows up on overdue balances. Customers that fail to settle their liabilities for mobile services provided are disconnected until the debt is paid.

Kcell has no significant concentration of credit risk, as its customer portfolio is highly diversified, with a large number of both individuals and companies. While the collection of receivables could be influenced by economic factors, the management sees no significant risk of loss.

Risk Management continued

Kcell has established relationships with numerous banks, which were considered at the time of deposit to have minimal risk of default. The Company works only with the banks in Kazakhstan that have the highest credit ratings.

Kcell reviews the credit ratings of these banks periodically to reduce its credit risk exposure. As Kazakhstan continues to display some characteristics of an emerging market, certain risks inherent to the country are also inherent to the banks where the Company has placed its cash and cash equivalents and term deposits at the end of the reporting period.

Foreign exchange risk

The majority of Kcell's purchases of property, plant and equipment and inventories, as well as certain services such as roaming, are denominated in US dollars.

Overall, most of the Company's foreign exchange risk relates to the movement of the tenge against the US dollar, although profit is less sensitive to this. Due to the undeveloped market for financial instruments in Kazakhstan, the Company does not hedge its foreign exchange risk.

Interest rate risk

Kcell's income and operating cash flow are largely independent of changes in market interest rates. As of 31 December 2017, the Company had no assets or liabilities with floating interest rates.

Legal risk

Legal risks are defined as the potential for uncertainty due to legal action or ambiguity in the applicability or interpretation of contracts, laws or regulations. Kcell's legal department checks queries and orders for compliance with legislation, monitors amendments to legislation and participates, whenever possible, in draft law debates.

Natural disaster/catastrophe risk

Natural disasters or catastrophes are defined as natural phenomena or processes that provoke catastrophic situations characterised by a sudden reduction in the population, the destruction of infrastructure and property and/or death. Kcell has implemented measures for dealing with disasters such as fires, accidents and incidents arising from human neglect. These include fire drills, fire alarm systems, regular vehicle servicing, preventive measures against seasonal illnesses, medical insurance, annual medical examinations, diesel generators for use during power failures, deliveries of reserve water supplies to employees and preventive work.

Statement of Management's Responsibilities

For the preparation and approval of the Consolidated Financial Statements for the year ended 31 December 2017

Management is responsible for the preparation of the consolidated financial statements that present fairly the financial position of Kcell JSC ("the Company") and its subsidiaries (together referred to as "the Group") as at 31 December 2017, the results of its operations, cash flows and changes in equity for the year then ended, in compliance with International Financial Reporting Standards ('IFRS') as issued by the International Accounting Standards Board ('IASB').

In preparing the consolidated financial statements, management is responsible for:

– properly selecting and applying accounting policies;
– presenting information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
– providing additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the Group's financial position and financial performance; and
– making an assessment of the Group's ability to continue as a going concern.

Management is also responsible for:

– designing, implementing and maintaining an effective and sound system of internal controls throughout the Group;
– maintaining adequate accounting records that are sufficient to show and explain the Group's transactions and disclose with reasonable accuracy at any time financial position of the Group, and which enable them to ensure that the consolidated financial statements of the Group comply with IFRS;
– maintaining statutory accounting records in compliance with the legislation of Kazakhstan and accounting standards;
– taking such steps as are reasonably available to them to safeguard the assets of the Group; and
– preventing and detecting fraud and other irregularities.

The consolidated financial statements of the Group for the year ended 31 December 2017 were approved by management on 15 February 2018.

Approved for issue and signed on behalf of the management

Arti Ots
Chief Executive Officer

Andis Locmelis
Chief Financial Officer

Independent Auditor's Report

To the shareholders and Board of Directors of Kcell JSC

Opinion

We have audited the consolidated financial statements of Kcell JSC ("the Company") and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2017, 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 notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ('IFRSs').

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing ('ISAs'). Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (the "IESBA Code") together with the ethical requirements that are relevant to our audit of the consolidated financial statements in the Republic of Kazakhstan, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Independent Auditor's Report continued

Why the matter was determined to be a key audit matter	How the matter was addressed in the audit and the outcome of the procedures
Provisions and contingent liabilities In July 2017, the Kazakhstan tax authority completed its comprehensive tax audit for the period 2012 to 2015. Upon finalisation of the tax audit, the total claim by the tax authority amounted to KZT9 billion. Currently, the Group is in the process of disputing the claim. Refer to Note 19 – Contingencies, Commitments and Operating Risks. As a result of this dispute and the ongoing discussions and negotiations, there is a high level of judgement required in estimating the level of provisioning required as of 31 December 2017.	Our procedures included the following: – enquiring of management and independently analysing the Group's correspondence with tax authorities; – analysing the opinions of external tax consultants obtained by management in respect of the tax audit and claims made; – enquiring of the Group legal team about the actions planned upon receipt of the tax audit conclusion; and – assessing and challenging management's conclusions through understanding precedents set in similar cases with the assistance of our internal experts in order to come up with an independent estimate of the level of provisioning required. We also validated the completeness and appropriateness of the related disclosures in Note 19 of the consolidated financial statements. Based on the evidence obtained, whilst noting the inherent uncertainty with such in process legal, regulatory and tax matters, we concluded that the level of provisioning as at 31 December 2017 is appropriate.
Impairment of assets (assets under construction and plant and machinery) In prior years, based on management estimates of usage, the Group has written off a significant amount of plant and machinery and assets under construction. Given the pace of technological advancements in the sector, we consider asset impairment to continue to be a significant area of judgement for 2017.	We tested the operating effectiveness of controls over the impairment assessment process. Our procedures included reviewing plant and machinery for the existence of impairment indicators, as well as auditing the impairment model used for purposes of the value in use calculation, including reviewing the future cash flow projections and assessing the methodology used in the determination of related input assumptions, such as the growth rate and discount rate applied in the model; no significant issues were noted. In addition, we have reviewed the ageing of the assets under construction balance for indicators of impairment and the timeliness of the transfer from assets under construction. Based on our procedures, we noted no significant issues and consider management's key assumptions applied in the impairment test to be within a reasonable range.

Capital expenditure (assets under construction)

As discussed in Note 9 to the consolidated financial statements, there is a material amount of assets in the course of construction and advances given pertaining to such assets, which are transferred to other groups of property, plant and equipment as such assets start being used.

There is a number of areas where management judgements impact the carrying value of assets under construction. These include:

- identifying whether costs qualify for recognitions as an asset; and
- the timeliness of the transfer from assets in the course of construction to the appropriate classes of property.

We tested the operating effectiveness of controls in place over the fixed asset cycle, evaluated the appropriateness of the Group's capitalisation policies, performed tests of details on costs capitalised and assessed the nature of costs incurred in capital expenditure through testing the amounts recorded and assessing whether the expenditure met the capitalisation criteria.

In performing these procedures, we challenged the judgements made by management including the nature of underlying costs capitalised as part of the cost of the network roll-out through reviewing third-party supporting documentation in relation to the costs incurred.

Further, we substantively tested the transfer of assets in the course of construction to the appropriate property class through reviewing, on a sample basis, supporting documentation detailing the type of asset being constructed and the related asset class in which it had been transferred to on completion, along with the timeliness of the transfer. No significant issues were noted from our testing.

Revenue recognition

There is an inherent risk around the accuracy and cut-off of revenue recorded given the complexity of systems and the impact of multiple-element arrangements to revenue recognition (tariff structures, the appropriateness of the allocation of the total transaction value between multiple elements in a bundled transaction, etc.).

The application of revenue recognition accounting standards is complex and involves a number of key judgements and estimates.

We involved our IT specialists to test the operating effectiveness of controls over the customer billing systems. Our tests assessed the controls in place to ensure all services supplied to customers are input into and processed through the billing systems, allowing us to rely on the controls in place within the billing system.

We applied a combination of substantive analytical procedures and tests of detail to obtain assurance over the validity and completeness of the reported output of these systems.

We tested the basis of allocation of total transaction value between multiple elements in bundled transactions.

We also considered the application of the Group's accounting policies to amounts billed and the accounting implications of allocation of the total transaction value between multiple elements in a bundled transaction to ensure that the Group accounting policies were determined appropriately and applied consistently.

Based on our work, we noted no significant issues related to the accuracy and cut-off of revenue recorded in the year.

Other information

Management is responsible for the other information. The other information comprises the information included in the annual report, but does not include the consolidated financial statements and our auditor's report thereon. The annual report is expected to be made available to us after the date of this auditor's report.

Our opinion on the consolidated financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

When we read the annual report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs, 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.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.

- Obtain an understanding of internal control relevant to the audit 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 Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters.

Mark Smith
Engagement Partner
Chartered Accountant
Institute of Chartered Accountant of Scotland
License Nº M21857
Glasgow, Scotland

Ivan Mudrichenko
Auditor-performer
Qualification certificate
Nº MF-0000415
dated 13 January 2017

Deloitte, LLP State license for audit activities
in the Republic of Kazakhstan Nº 0000015,
type MFU-2, issued by the Ministry of Finance
of the Republic of Kazakhstan dated 13 September 2006

Nurlan Bekenov
General Director
Deloitte, LLP

15 February 2018
Almaty, the Republic of Kazakhstan

Consolidated Statement of Financial Position

(in thousand of Kazakhstani tenge)

	Note	**31 December 2017**	31 December 2016
Assets			
Non-current assets			
Property, plant and equipment	9	**93,680,082**	95,321,606
Intangible assets	10	**43,060,675**	42,842,480
Long-term trade receivables	11	**1,437,480**	1,162,961
Restricted cash		**38,733**	86,419
Total non-current assets		**138,216,970**	139,413,466
Current assets			
Inventories		**3,424,664**	3,587,082
Trade and other receivables	11	**19,672,722**	18,238,920
Prepaid current income tax		**5,064,001**	10,575,846
Due from related parties	8	**810,492**	738,983
Cash and cash equivalents		**12,659,844**	8,476,653
Total current assets		**41,631,723**	41,617,484
TOTAL ASSETS		**179,848,693**	181,030,950
EQUITY			
Share capital	12	**33,800,000**	33,800,000
Retained earnings		**40,636,532**	38,880,286
TOTAL EQUITY		**74,436,532**	72,680,286

	Note	31 December 2017	31 December 2016
LIABILITIES			
Non-current liabilities			
Deferred income tax liability	18	**4,817,503**	6,012,214
Other non-current liabilities		**1,354,594**	1,285,482
Borrowings	14	**12,000,000**	8,000,000
Total non-current liabilities		**18,172,097**	**15,297,696**
Current liabilities			
Borrowings	14	**58,417,722**	57,414,639
Trade and other payables	13	**21,228,218**	26,952,614
Due to related parties	8	**1,177,333**	1,525,559
Deferred revenue		**6,007,580**	6,759,535
Taxes payable		**409,211**	400,621
Total current liabilities		**87,240,064**	93,052,968
TOTAL LIABILITIES		**105,412,161**	108,350,664
TOTAL EQUITY AND LIABILITIES		**179,848,693**	181,030,950

Approved for issue and signed on behalf of the management on 15 February 2018

Arti Ots
Chief Executive Officer

Andis Locmelis
Chief Financial Officer

The accompanying notes on pages 13 to 45 are an integral part of these consolidated financial statements.

Consolidated Statement of Comprehensive Income

(in thousand of Kazakhstani tenge, unless otherwise stated)

	Note	2017	2016
Revenues	15	**147,228,988**	147,037,004
Cost of sales	16	**(90,107,393)**	(91,865,727)
Gross profit		**57,121,595**	55,171,277
Selling and marketing expenses	16	**(10,505,832)**	(10,988,346)
General and administrative expenses	16	**(15,523,936)**	(14,149,534)
Other operating income		**1,027,660**	2,871,658
Other operating expenses	16	**(618,051)**	(1,863,772)
Operating profit		**31,501,436**	31,041,283
Finance income	17	**957,314**	2,650,545
Finance costs	17	**(10,376,680)**	(10,935,593)
Profit before income tax		**22,082,070**	22,756,235
Income tax expense	18	**(8,647,824)**	(6,072,619)
Profit and total comprehensive income for the year		**13,434,246**	16,683,616
Earnings per share (Kazakhstani tenge), basic and diluted	12	**67.17**	83.42

Profit and total comprehensive income for both periods are fully attributable to the Group's shareholders.

Approved for issue and signed on behalf of the management on 15 February 2018

Arti Ots
Chief Executive Officer

Andis Locmelis
Chief Financial Officer

The accompanying notes on pages 13 to 45 are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

(in thousand of Kazakhstani tenge)

	Share capital	Retained earnings	Total equity
Balance at 1 January 2016	**33,800,000**	**46,646,103**	**80,446,103**
Profit and total comprehensive income for the year	–	16,683,616	16,683,616
Business combination under common control (Note 3)	–	(1,133,433)	(1,133,433)
Dividends declared (Note 12)	–	(23,316,000)	(23,316,000)
Balance at 31 December 2016	**33,800,000**	**38,880,286**	**72,680,286**
Profit and total comprehensive income for the year	–	13,434,246	13,434,246
Dividends declared (Note 12)	–	(11,678,000)	(11,678,000)
Balance at 31 December 2017	**33,800,000**	**40,636,532**	**74,436,532**

Approved for issue and signed on behalf of the Management on 15 February 2018

Arti Ots
Chief Executive Officer

Andis Locmelis
Chief Financial Officer

The accompanying notes on pages 13 to 45 are an integral part of these consolidated financial statements.

Consolidated Statement of Cash Flows

(in thousand of Kazakhstani tenge)

	Note	2017	2016
Cash flows from operating activities			
Profit for the year		**13,434,246**	16,683,616
Adjustments for:			
Depreciation of property, plant and equipment	9	**17,384,246**	17,192,050
Amortisation of intangible assets	10	**5,762,324**	7,036,978
Income tax		**4,317,134**	(4,474,443)
Net foreign exchange loss/(gain)		**108,305**	(1,206,903)
Interest income		**(722,764)**	(1,316,560)
Interest expense		**10,104,293**	10,283,135
Impairment of trade receivables		**966,405**	1,090,968
Impairment and loss on disposal of property, plant and equipment	9	**–**	9,666
Operating cash flows before working capital changes		**51,354,189**	45,298,507
Change in working capital and other balances:			
Trade and other receivables		**(4,303,005)**	(4,679,352)
Long-term trade receivables		**(274,519)**	(765,850)
Due from related parties		**(71,509)**	41,071
Inventories		**162,418**	(528,205)
Taxes payable		**8,590**	(533,544)
Trade and other payables		**(2,593,947)**	2,030,961
Due to related parties		**(348,226)**	310,021
Deferred revenue		**(751,955)**	(1,637,693)
Other		**47,686**	59,413
Cash generated from operations		**43,229,722**	39,595,329
Interest paid		**(10,469,528)**	(10,364,306)
Interest received		**722,764**	1,316,475
Net cash generated from operating activities		**33,482,958**	30,547,498

	Note	2017	2016
Cash flows from investing activities			
Purchase of property, plant and equipment		**(18,951,198)**	(15,091,050)
Purchase of intangible assets		**(3,632,732)**	(28,857,944)
Cash inflow as a result of acquisition of a subsidiary		**–**	108,615
Net cash used in investing activities		**(22,583,930)**	(43,840,379)
Cash flows from financing activities			
Proceeds from bank borrowings	14	**48,000,000**	33,000,000
Repayment of borrowings	14	**(43,000,000)**	(18,000,000)
Dividends paid	12	**(11,678,000)**	(23,316,000)
Purchase of investments in subsidiaries	3	**–**	(2,185,000)
Net cash used in financing activities		**(6,678,000)**	(10,501,000)
Net increase/(decrease) in cash and cash equivalents		**4,221,028**	(23,793,881)
Effects of exchange rate changes on the balance of cash held in foreign currencies		**(37,837)**	681,527
Cash and cash equivalents at the beginning of the year		**8,476,653**	31,589,007
Cash and cash equivalents at the end of the year		**12,659,844**	8,476,653

Approved for issue and signed on behalf of the management on 15 February 2018

Arti Ots
Chief Executive Officer

Andis Locmelis
Chief Financial Officer

The accompanying notes on pages 13 to 45 are an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

(in thousand of Kazakhstani tenge, unless otherwise stated)

1. THE GROUP AND ITS OPERATIONS

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board for the year ended 31 December 2017 for Kcell JSC ("the Company") and its subsidiaries (together referred to as "the Group").

The Company was established as a limited liability partnership (GSM Kazakhstan OAO Kazakhtelecom LLP) on 1 June 1998 to design, construct and operate a cellular telecommunications network in the Republic of Kazakhstan, using the GSM (Global System for Mobile Communications) standard.

The Company began its commercial operations in 1999 through direct sales and a network of distributors. Prior to 2 February 2012, the Company was owned 51% by Fintur Holdings B.V. ("Fintur" or "Parent Company") and 49% by Kazakhtelecom JSC ("Kazakhtelecom"). Fintur itself is owned jointly by Sonera Holding B.V. ("Sonera") and Turkcell Iletisim Hizmetleri A.S., with holdings of 58.55% and 41.45%, respectively.

On 2 February 2012, the 49% stake in the Company owned by Kazakhtelecom was sold directly to Sonera, a subsidiary of Telia Company.

On 1 July 2012, the General Meeting of the participants of GSM Kazakhstan approved a conversion of the Company from Limited Liability Partnership to Joint Stock Company ("the Conversion"), with 200,000,000 common shares to be transferred to Fintur and Sonera in proportion to their ownership percentage. The General Meeting also approved the Company's change of name to Kcell JSC.

On 27 August 2012, the Ministry of Justice registered the Company as a Joint Stock Company. Under Kazakhstani law, upon the Conversion, retained earnings as of the date of the Conversion became share capital of the Company and ceased to be available for distribution to shareholders.

On 13 December 2012, the Company successfully completed its offering of Global Depositary Receipts on the London Stock Exchange and common shares on the Kazakhstan Stock Exchange. The offering consisted of a sale by Sonera of 50 million shares, which represented 25% of the Company's share capital (Note 12).

On 4 May 2016, the 24% stake in the Company owned by Sonera was sold directly to TeliaSonera Kazakhstan Holding B.V. ("TeliaSonera Kazakhstan"), a subsidiary of Telia Company. The Company's ultimate parent and controlling party is Telia Company.

The Company owns the following subsidiaries:

	Ownership interest		Voting power	
	2017	2016	**2017**	2016
KazNet Media LLP (Note 3)	**100%**	100%	**100%**	100%
KT-Telecom LLP	**100%**	100%	**100%**	100%
AR-Telecom LLP	**100%**	100%	**100%**	100%

1. THE GROUP AND ITS OPERATIONS CONTINUED

Operations

On 25 December 2010, the competent authority signed an addendum to the existing GSM license, which provided the Company with a right to operate a 3G network. In December 2010, the Company launched 3G services in Astana and Almaty. As of 1 January 2015, the Group provided all locations with a population of over 10,000 people with mobile services using UMTS/WCDMA based on the terms of the addendum.

In January 2016, the Group paid KZT14 billion as the first tranche for LTE radio frequencies. In accordance with the decision made by Kazakhstan's Ministry of Investments and Development ("the MID") in January 2016, the Group had to pay a one-time fee of KZT4 billion by 1 February 2016 for 10/10 MHz radio frequency within the 1700/1800 MHz band, and the first tranche of KZT10 billion by 1 March 2016 to gain access to 10/10 MHz radio frequency within the 700/800 MHz band. The second tranche for 10/10 MHz radio frequencies within the 700/800 MHz band in the amount of KZT12 billion is to be paid by 1 December 2016. The Group paid the second tranche on 30 November 2016. On 1 March 2016, the Group launched LTE in its network on the previously granted frequencies.

The Company's registered address is 100, Samal-2, Almaty, the Republic of Kazakhstan.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB') on the historical cost basis.

Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Group takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date. Fair value for measurement and/or disclosure purposes in the financial statements is determined on such a basis, except for leasing transactions that are within the scope of International Accounting Standard ('IAS') 17, and measurements that have some similarities to fair value but are not fair value, such as net realisable value in IAS 2 or value in use in IAS 36.

In addition, for financial reporting purposes, fair value measurements are categorised into levels based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES CONTINUED

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These consolidated financial statements have been prepared in accordance with IFRSs and International Financial Reporting Interpretations Committee ('IFRIC') interpretations issued and effective.

The preparation of consolidated financial statements in conformity with IFRSs requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Note 4. Actual results could differ from those estimates.

Foreign currency translation

(i) Functional and presentation currency

All amounts in these consolidated financial statements are presented in thousands of Kazakhstani tenge ('tenge'), unless otherwise stated. The functional currency of the Group entities is also tenge, the currency of the primary economic environment in which they operate.

(ii) Transactions and balances

Foreign currency transactions are accounted for at the exchange rate prevailing at the date of the transaction established by the National Bank of the Republic of Kazakhstan. Gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currency are recognised in the profit or loss for the year.

As at 31 December 2017, the principal rate of exchange used for translating foreign currency balances was US dollar ('USD') 1 = KZT332.33 (31 December 2016: USD 1 = KZT333.29). Exchange restrictions and currency controls exist relating to converting Tenge into other currencies. At present, the tenge is not a freely convertible currency in most countries outside of the Republic of Kazakhstan.

Consolidated financial statements

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company and its subsidiaries. Control is achieved when the Company:

- has power over the investee;
- is exposed, or has rights, to variable returns from its involvement with the investee; and
- has the ability to use its power to affect its returns.

The Company reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are deconsolidated from the date that control ceases. Intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Company and all of its subsidiaries use uniform accounting policies consistent with the Group's policies.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Property, plant and equipment

(i) Recognition and subsequent measurement

Property, plant and equipment are stated at cost, less accumulated depreciation and provision for impairment. Cost comprises construction cost or purchase price, including import duties and non-refundable taxes, and any directly attributable costs of bringing the asset to working condition for its intended use. Any trade discounts and rebates are deducted in arriving at the construction cost or purchase price.

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components of property, plant and equipment items are capitalised and the replaced part is retired. Construction in progress is carried at cost. Upon completion, assets are transferred to plant and machinery at their carrying amount. Construction in progress is not depreciated until the asset is available for use.

Advances for property, plant and equipment are presented within property, plant and equipment financial statement line.

(ii) Depreciation

Land is not depreciated. Depreciation on other items of property, plant and equipment is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives:

	Useful lives in years
Property	10 to 50
Plant and machinery	3 to 10
Equipment tools and installations	2 to 8

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset, less the estimated costs of disposal, if the asset was already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in the profit or loss for the year when the asset is retired.

(iii) Impairment

At each reporting date, management assesses whether there is any indication of impairment of property, plant and equipment. If any such indication exists, management estimates the recoverable amount of the asset to determine the extent, if any, of the impairment loss. The recoverable amount is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognised in the profit or loss for the year. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's value in use or fair value less costs to sell.

(in thousand of Kazakhstani tenge, unless otherwise stated)

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Intangible assets

The Group's operating licenses (GSM-900, GSM-1800 and 3G), as disclosed in Notes 1 and 10, are recorded at cost and are amortised on a straight-line basis over the estimated economic useful life of the license/right. The economic useful life of the original GSM license and 3G license is estimated by management at 15 years based on their terms. The useful life of the initial license term is in line with management's assessment of the development of communication technology. The economic useful life of the right for the radio frequencies (GSM-1800) was estimated by management to expire in line with the GSM-900 license. On 1 March 2016, the Group launched LTE in its network on the previously granted frequencies. The economic useful life of the 4G license is also estimated by management at 15 years based on its terms. The useful life of the initial license term is in line with management's assessment of the development of communication technology. The economic useful life of the right for the radio frequencies (GSM-1700/1800) was estimated by management to expire in line with the GSM-700/800 license.

Other intangible assets are amortised over their estimated useful lives as follows:

	Useful lives in years
Computer software and software license rights	3 to 8
Other telecom licenses	10
Other	8 to 10

If impaired, the carrying amount of intangible assets is written down to the higher of value in use or fair value less costs to sell.

Advances for intangible assets are presented within intangible assets financial statement line.

Operating leases

Where the Group is a lessee in a lease which does not transfer substantially all the risks and rewards incidental to ownership from the lessor to the Group, the total lease payments are charged to profit or loss on a straight-line basis over the period of the lease.

The lease term is the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option.

Inventories

Inventories primarily include handsets and other goods for resale. Inventories are recorded at the lower of cost and net realisable value. The cost of inventory is determined on the weighted average basis. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses.

Trade and other receivables

Trade and other receivables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest method, less allowance for impairment.

An allowance for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. When a trade receivable is deemed to be uncollectible, it is written off. Subsequent recoveries of amounts previously written off are credited to the profit or loss for the year. The primary factors that the Group considers whether a receivable is impaired is its overdue status and collection history.

Prepaid taxes, deferred expenses and advances to suppliers are stated at actual amounts paid less allowance for impairment.

Prepayments

Prepayments are carried at cost less any allowance for impairment. A prepayment is classified as non-current when the goods or services relating to the prepayment are expected to be obtained after one year, or when the prepayment relates to an asset which will itself be classified as non-current upon initial recognition. Prepayments to acquire assets are transferred to the carrying amount of the asset once the Group has obtained control of the asset and it is probable that future economic benefits associated with the asset will flow to the Group. Other prepayments are written off to profit or loss when the goods or services relating to the prepayments are received. If there is an indication that the assets, goods or services relating to a prepayment will not be received, the carrying value of the prepayment is written down accordingly and a corresponding impairment loss is recognised in profit or loss for the year.

Cash and cash equivalents

Cash and cash equivalents include cash on hand and deposits held at call with banks with original maturities of three months or less and are subject to insignificant risk of change in value. Balances restricted from being exchanged or used to settle a liability for at least 12 months after the reporting date are included in restricted cash.

Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares are expensed to the consolidated statement of comprehensive income. Any excess of the fair value of consideration received over the par value of shares issued is recorded as share premium in equity.

Dividends

Dividends are recorded as a liability and deducted from equity in the period in which they are declared. Any dividends declared after the end of the reporting period and before the consolidated financial statements are authorised for issue are disclosed in the subsequent events note.

Value added tax

Value added tax (VAT) related to sales is payable to the government when goods are shipped or services are rendered. Input VAT is reclaimable against output VAT upon receipt of a tax invoice from a supplier. The tax legislation permits the settlement of VAT on a net basis. Accordingly, VAT related to sales and purchases unsettled at the reporting date is stated in the statements of financial position on a net basis.

Trade and other payables

Trade and other payables are accrued when the counterparty performed its obligations under the contract. The Group recognises trade payables initially at fair value. Subsequently, trade payables are carried at amortised cost using the effective interest method.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Provisions for liabilities and charges

Provisions for liabilities and charges are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. In such circumstances, a provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Revenue recognition

Revenue is recorded on an accruals basis measured at the fair value of the consideration received or receivable, being the sales value, net of discounts granted and VAT.

Revenue is categorised as follows: voice services, data services, value added services and sale of handsets.

Voice service includes call out revenue, interconnect fees, roaming revenues charged to the Group's subscribers for roaming in other wireless operators' network and roaming revenues charged to other wireless operators for non-Group subscribers using the Group's network.

Data services include revenues from GPRS, WAP services and other data services.

Value added services consists of SMS, MMS, info services and providing content of third parties, fax and voice mail services.

The Group may bundle services and products into one customer offering. Offerings may involve the delivery or performance of multiple products, services or rights to use assets (multiple deliverables). In some cases, the arrangements include initial installation, initiation or activation services and involve consideration in the form of a fixed fee or a fixed fee coupled with a continuing payment stream. Telecom equipment is accounted for separately from service where a market for each deliverable exist and if title to the equipment passes to the end-customer. Costs associated with the equipment are recognised at the time of revenue recognised. The revenue is allocated to equipment and services in proportion to the fair value of the individual items. Services invoiced based on usage are not included in the allocation. Customised equipment that can be used only in connection with services or products provided by the Group is not accounted for separately and revenue is deferred over the total service arrangement period.

In revenue arrangements where more than one good or service is provided to the customer, customer consideration is allocated between the goods and services using relative fair value principles. Determining the fair value of each deliverable can require complex estimates. The Group generally determines the fair value of individual elements based on prices at which the deliverable is regularly sold on a stand-alone basis after considering volume discounts where appropriate.

(i) Call out revenue

Call out revenue is recognised based on the actual airtime used by the subscribers. Prepayments received for call out revenue are not recognised as revenue until the related service has been provided to the subscriber. Revenue is recognised based on the actual traffic time elapsed, at the customer selected calling plan rates.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(ii) Interconnect revenues and costs
The Group charges interconnect per minute fees and fixed monthly payments to other local wireless and fixed line operators for calls originated outside and terminated within the Group's network. The Group recognises such revenues when the services are provided. The Group is charged interconnect fees per minute and fixed monthly payments by other local wireless and fixed line operators for calls originated within the Group's network and terminated outside of the network. The Company recognises such costs when the services are provided.

(iii) Data revenue
The data service is recognised when a service is used by a subscriber based on actual data volume traffic or over the contract term, as applicable.

(iv) Roaming revenues charged to the Group's subscribers
Roaming revenue from the Group's subscribers for roaming in other operators' network is charged based on information provided by other operators to the Group.

(v) Roaming fees charged to other wireless operators
The Group charges roaming per minute fees to other wireless operators for non-Group subscribers utilising the Group's network. The Group recognises such revenues when the services are provided.

(vi) Value added services
Value added services mainly consists of content provided by third parties, different info services, fax and voice mail. When invoicing the end-customer for third-party content service, amounts collected on behalf of the principal are excluded from revenue.

(vii) Deferred revenue
Prepayments received for communication services are recorded as deferred revenue. The Group recognises revenue when the related service has been provided to the subscriber.

Roaming discounts

The Group enters into roaming discount agreements with a number of wireless operators. According to the terms of the agreements the Group is obliged to provide and entitled to receive a discount that is generally dependent on the volume of inter operator roaming traffic. The Group uses various estimates and assumptions, based on historical data and adjusted for known changes, to determine the amount of discount to be received or granted. Such estimates are adjusted monthly to reflect newly-available information.

The Group accounts for discounts received as a reduction of roaming expenses and discounts granted as reduction of roaming revenue. The Group considers terms of the various roaming discount agreements in order to determine the appropriate presentation of the amounts receivable from and payable to its roaming partners in its consolidated statements of financial position.

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES CONTINUED

Sales commission to dealers

The Company sells part of payment scratch cards, sim cards, and handsets using dealers. The Company pays a certain commission to dealers depending on the number of payment scratch cards, sim cards or handset sold. The commission is recognised when the item is sold to the subscriber.

Payroll expenses and related contributions

Wages, salaries, contributions to pension funds, paid annual leave and sick leave, bonuses and other benefits are accrued in the period in which the associated services are rendered by the employees of the Group.

Pension payments

The Group does not incur any expenses in relation to provision of pensions or other post-employment benefits to its employees. In accordance with the legal requirements of the Republic of Kazakhstan, the Group withholds pension contributions from employee salaries and transfers them into state or private pension funds on behalf of its employees. Pension contributions are the responsibility of employees, and the Group has no current or future obligations to make payments to employees following their retirement. Upon retirement of employees, all pension payments are administered by the pension funds directly.

Income taxes

Income taxes have been provided for in these consolidated financial statements in accordance with Kazakhstani legislation enacted or substantively enacted by the end of the reporting period. The income tax charge comprises current tax and deferred tax and is recognised in profit or loss for the period.

Current tax is the amount expected to be paid to or recovered in respect of taxable profits or losses for the current and prior periods. Taxable income or losses are based on estimates where the consolidated financial statements are authorised prior to the filling of the relevant tax return. Taxes, other than on income, are recorded within operating expenses.

Deferred income tax is provided using the balance sheet liability method for temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the reporting date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets for deductible temporary differences are recorded only to the extent that it is probable that future taxable profit, including deferred tax liabilities, will be available against which the deductions can be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group.

Earnings per share

Earnings per share are determined by dividing the profit or loss attributable to owners of the Group by the weighted average number of participating shares outstanding during the reporting year. The Group has no dilutive or potentially dilutive securities outstanding.

Segment reporting

Segments are reported in a manner consistent with the internal reporting provided to the Group's chief operating decision-maker. Segments whose revenue, result or assets are ten percent or more of all the segments are reported separately. The chief operating decision-maker has been identified as the Group's Chief Executive Officer. The Group determined the Group's operations as a single reporting segment.

Financial instruments

(i) Key measurement terms

Depending on their classification financial instruments are carried at fair value or amortised cost as described below.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair value is the current bid price for financial assets and the current asking price for financial liabilities which are quoted in an active market. For assets and liabilities with offsetting market risks, the Group may use mid-market prices as a basis for establishing fair values for the offsetting risk positions and apply the bid or asking price to the net open position as appropriate.

Valuation techniques such as discounted cash flow models or models based on recent arm's length transactions or consideration of financial data of the investees are used to measure at fair value certain financial instruments for which external market pricing information is not available. Valuation techniques may require assumptions not supported by observable market data.

Amortised cost is the amount at which the financial instrument was recognised at initial recognition less any principal repayments, plus accrued interest, and for financial assets less any write-down for incurred impairment losses. Accrued interest includes amortisation of transaction costs deferred at initial recognition and of any premium or discount to maturity amount using the effective interest method. Accrued interest income and accrued interest expense, including both accrued coupon and amortised discount or premium (including fees deferred at origination, if any), are not presented separately and are included in the carrying values of related items in the statement of financial position.

The effective interest method is a method of allocating interest income or interest expense over the relevant period, so as to achieve a constant periodic rate of interest (effective interest rate) on the carrying amount. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts (excluding future credit losses) through the expected life of the financial instrument or a shorter period, if appropriate, to the net carrying amount of the financial instrument. The effective interest rate discounts cash flows of variable interest instruments to the next interest repricing date, except for the premium or discount which reflects the credit spread over the floating rate specified in the instrument, or other variables that are not reset to market rates. Such premiums or discounts are amortised over the whole expected life of the instrument. The present value calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate.

Notes to the Consolidated Financial Statements continued

(in thousand of Kazakhstani tenge, unless otherwise stated)

2. BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES CONTINUED

(ii) Classification of financial assets
Financial assets of the Group include loans and receivables. The management determines the classification of its financial assets at initial recognition.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period. These are classified as non-current assets. The Group's loans and receivables comprise trade receivables (Note 11), due from related parties (Note 8) in the consolidated statements of financial position.

(iii) Classification of financial liabilities
Financial liabilities of the Group include financial liabilities carried at amortised cost. The Group's financial liabilities comprise trade and other payables (Note 13) and due to related parties (Note 8).

(iv) Initial recognition of financial instruments
Derivatives are initially recorded at fair value. All other financial assets and liabilities are initially recorded at fair value plus transaction costs. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

(v) Derecognition of financial assets
The Group derecognises financial assets when: (a) the assets are redeemed or the rights to cash flows from the assets otherwise expired; or (b) the Group has transferred the rights to the cash flows from the financial assets or entered into a qualifying pass-through arrangement while (i) also transferring substantially all the risks and rewards of ownership of the assets or (ii) neither transferring nor retaining substantially all risks and rewards of ownership but not retaining control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

3. BUSINESS COMBINATION UNDER COMMON CONTROL

On 26 August 2012, Sonera and the Company entered into a memorandum of understanding ("the MoU"), under which the Company had the right to require Sonera to sell to it, and Sonera had the right to require the Company to acquire from it:

- all participatory interests owned by Sonera in KazNet Media LLP (KazNet) together with all rights and obligations of Sonera under a framework agreement to buy all the participatory interests in the charter capital of KazNet; and
- all the participatory interests owned by Sonera in Rodnik Inc LLP (Rodnik) together with all rights and obligations of Sonera under the agreements to buy participatory interests in the charter capital of Rodnik (refer to 'Investment in Rodnik by Sonera' in Note 19).

3. BUSINESS COMBINATION UNDER COMMON CONTROL CONTINUED

On 20 October 2015, the Company and KT-Telecom (100% subsidiary of the Company) signed an agreement ("the Agreement") for the purchase of 100% of the participatory interest in KazNet where Sonera is the seller. KazNet holds 100% of the participatory interest in Kcell Solutions (formerly Aksoran LLP) and 100% of the participatory interest in Instaphone – companies holding frequencies that are capable of being deployed for 4G/LTE. On 31 March 2017, Aksoran LLP was re-registered as Kcell Solutions LLP (further – "Kcell Solutions").

In accordance with the Agreement, the amount of the transaction is divided into two tranches. The first tranche comprises a nominal price of US$5 million; the second tranche is equal to the fair market value of the frequencies. If the parties of the Agreement cannot agree on the fair value of the frequencies, then the fair value shall be determined by independent appraiser appointed by the parties. The total amount of the transaction shall not exceed US$70 million.

In accordance with the Agreement, the second tranche shall be paid by the Company within 60 calendar days from the date at which the frequencies are permitted to be used by the Company for 4G/LTE services in Kazakhstan. The Company shall receive the relevant authorisation for the use of the frequencies by 31 December 2025. The second tranche shall not be due and payable if the Company is not authorised to provide 4G/LTE services in Kazakhstan by 31 December 2025. As at 31 December 2017, the Company did not apply for permission to use the frequencies.

In accordance with the Agreement, the completion of the deal is subject to the satisfaction of a list of conditions, including but not limited to, signing of waiver-letters and execution of an amendment to the MoU.

On 15 January 2016, all parties of the Agreement signed waiver-letters according to which all parties confirmed no need for execution of the amendment to the MoU and corresponding satisfaction of all the conditions precedent set forth in the Agreement.

On 4 May 2016, the Company and KT-Telecom signed an amendment to the Agreement for the purchase of a 100% participatory interest in KazNet from Telia Company for US$1 (the revised first tranche following the amendment). The parties agreed that the control over KazNet is transferred to the Group and thereafter the Group would consolidate KazNet, including its subsidiaries Kcell Solutions and Instaphone, starting from the month after Kcell Solutions repays the US$5 million of loan principal plus US$369 thousand of accrued interest on that loan to Sonera.

On 5 May 2016, KazNet repaid a loan due to Sonera in full, thus the Group obtained control over the activity of KazNet, including Kcell Solutions and Instaphone, and consolidated its financial information since June 2016. Since the transfer of ownership in KazNet represents a business combination under common control (with Telia Company being the ultimate parent), the assets and liabilities of the transferred subsidiary were recognised at their historical carrying values per the predecessor owner's financial statements. The financial statements of these companies are not significant for understanding of the consolidated financial statements; as such, the Group consolidated them from the date of control transfer.

(in thousand of Kazakhstani tenge, unless otherwise stated)

3. BUSINESS COMBINATION UNDER COMMON CONTROL CONTINUED

The following statement of financial position of KazNet was presented in these consolidated financial statements at the date of receipt of control:

	Combination of the financial statements of KazNet as of consolidation date
Property, plant and equipment	184,562
Intangible assets	61
Total non-current assets	**184,623**
Inventories	257,275
Trade and other receivables	755,076
Prepaid income tax	11,522
Cash and cash equivalents	108,615
Total current assets	**1,132,488**
Total assets	**1,317,111**
Accumulated loss	(1,133,433)
Additional paid-in capital*	946,823
Net loss for the period	(204,032)
Total equity	**(390,642)**
Borrowings*	1,538,177
Trade and other payables	169,576
Total liabilities	**1,707,753**
Total liabilities and equity	**1,317,111**

* Borrowings comprise interest free financial aid received from the Company in the nominal amount of KZT2,485,000 thousand. KZT300,000 thousand were issued in 2015 and KZT2,185,000 thousand were issued during the year ended 31 December 2016. The difference between the nominal amount and fair value was recognised as additional paid-in capital in KazNet separate financial statements. These transactions were eliminated in these consolidated financial statements.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial period. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in these consolidated financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial period include:

Useful lives of property, plant and equipment and intangible assets

Management determines the estimated useful lives and related depreciation and amortisation charges for its property, plant and equipment and intangible assets. This estimate is based on projected period over which the Group expects to consume economic benefits from the asset. It could change significantly as a result of technical innovations and competitor actions in a high-tech and competitive mobile industry. The carrying amount of assets most affected by judgements (switches and transmission devices) amounted to KZT53,685,373 thousand (Note 9) as of 31 December 2017 (2016: KZT56,402,691 thousand). Management will increase the depreciation charge where useful lives are less than previously assessed estimated lives, or it will write down technically obsolete assets that have been abandoned.

Management assesses the useful life of telecommunication licenses based on technological development and the legal terms of the license agreements. The useful life of each of GSM, the 3G license and the 4G license is assessed as estimated by the management as 15 years. The useful lives are reviewed at least at each reporting date.

Provisions and contingencies, including tax contingencies

For each event management makes separate assessment of probable outcome and its effect on the Group's operations. Provisions are recognised when negative outcome is anticipated to be probable. For those events, with possible negative outcome on the Group's operations related contingency is disclosed.

In July 2017, the Kazakhstan tax authority completed its comprehensive tax audit for the period 2012 to 2015. Upon finalisation of the tax audit, the total claim by the tax authority amounted to KZT9 billion. Currently, the Group is in the process of disputing the claim (Note 19). As a result of this dispute and the ongoing discussions and negotiations, there is a high level of judgement required in estimating the level of provisioning required.

Deferred tax assets and liabilities

As at each reporting date, management determines the amount of deferred income tax by comparing the carrying amounts of assets and liabilities and the corresponding tax bases. Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantially enacted at the date of the corresponding consolidated statements of financial position. Management makes certain assumptions in determining future taxable income sufficient for compensation of deferred tax assets reflected in the consolidated statement of financial position. The carrying amount of net deferred tax liability as at 31 December 2017 amounted to KZT4,817,503 thousand (as at 31 December 2016: KZT6,012,214 thousand) (Note 18).

Going concern

These consolidated financial statements have been prepared in accordance with IFRSs on a going concern basis, which assumes the realisation of assets and discharge of liabilities in the normal course of business within the foreseeable future.

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES CONTINUED

As at 31 December 2017, the Group's net current liabilities are KZT45,608,341 thousand. On 14 December 2017, the Group announced a programme to place bonds in the amount of KZT30,000,000 thousand on the Kazakhstan Stock Exchange (Note 22). Management has considered the Group's future plans, and in light of these plans and the current and expected profitability of the Group, positive cash flows from operations, available financing, management believes that the Group will continue to operate as a going concern for the foreseeable future.

Business combinations under common control

Also, as described in Note 3, during the year ended 31 December 2016, the Group carried out a business combination under common control. Business combinations involving entities under common control are outside of the scope of IFRS 3, *Business Combinations*, and there is no other specific IFRS guidance. Accordingly, management has to apply significant judgement to develop an accounting policy that is relevant and reliable in accordance with IAS 8, *Accounting Policies, Changes in Accounting Estimates and Errors*. The Group accounted for this business combination on a carry over basis, which results in the historical carrying value of assets and liabilities of the acquired entities being combined with that of the Group. The Group consolidates the financial statements of the companies under common control from the date of obtaining control, if the financial statements of these companies do not have a significant impact on the consolidated financial statements, and, respectively, do not affect the users of the consolidated financial statements, otherwise the consolidated financial statements of the Group reflect the effect of the combination, as if it occurred, at the beginning of the earliest period presented. Any difference between the amount recorded as share capital issued and the amount recorded for the share capital acquired is adjusted against retained earnings in the consolidated statement of changes in equity.

5. AMENDMENTS TO IFRS AND THE NEW INTERPRETATION THAT ARE MANDATORILY EFFECTIVE FOR THE CURRENT YEAR

In the current year, the following new and revised Standards and Interpretations have been adopted and have affected the amounts reported in these consolidated financial statements:

- Amendments to IAS 7 *Disclosure Initiative*;
- Amendments to IAS 12 *Recognition of Deferred Tax Assets for Unrealised Losses*; and
- Annual Improvements to IFRSs 2014-2016 Cycle – amendments to IFRS 12.

The adoption of the above mentioned Standards and Interpretations has not led to any changes in the Group's accounting policies. The amendments did not materially affect the consolidated financial statements of the Group, except Amendments to IAS 7 Disclosure Initiative as follows.

Amendments to IAS 7 Disclosure Initiative

The Group has applied these amendments for the first time in the current year. The amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both cash and non-cash changes.

The Group's liabilities arising from financing activities consist of borrowings, and a reconciliation between the opening and closing balances of these items is provided in Note 14. Consistent with the transition provisions of the amendments, the Group has not disclosed comparative information for the prior period. Apart from the additional disclosure in Note 14, the application of these amendments has had no other impact on the Group's consolidated financial statements.

6. NEW AND REVISED IFRS IN ISSUE BUT NOT YET EFFECTIVE

The Group has not applied the following new and revised IFRSs that have been issued but are not yet effective:

	Effective for annual periods beginning on or after
IFRS 16 Leases	1 January 2019*
IFRS 15 Revenue from Contracts with Customers	1 January 2018*
IFRS 9 Financial Instruments	1 January 2018*
IFRS 17 Insurance Contracts	1 January 2021*
IFRIC 22 Foreign Currency Transactions and Advance Consideration	1 January 2018*
IFRIC 23 Uncertainty Over Income Tax Treatments	1 January 2019*
Amendments to IFRS 2 – Classification and Measurement of Share-based Payment Transactions	1 January 2018*
Amendments to IFRS 10 and IAS 28 – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	Date to be determined*
Amendments to IAS 40 – Transfers of Investment Property	1 January 2018*
Amendments to IFRS 4 – Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts	1 January 2018*
Amendments to IFRS 9 – Prepayment Features With Negative Compensation	1 January 2019*
Amendments to IAS 28 – Long-Term Interests in Associates and Joint Ventures	1 January 2019*
Annual Improvements to IFRSs 2014-2016 Cycle	1 January 2018*
Annual Improvements to IFRSs 2015-2017 Cycle	1 January 2019*

* With earlier application permitted.

IFRS 9 *Financial Instruments*

IFRS 9 issued in November 2009 introduced new requirements for the classification and measurement of financial assets. IFRS 9 was subsequently amended in October 2010 to include requirements for the classification and measurement of financial liabilities and for derecognition, and in November 2013 to include the new requirements for general hedge accounting. Another revised version of IFRS 9 was issued in July 2014 mainly to include: a) impairment requirements for financial assets; and b) limited amendments to the classification and measurement requirements by introducing a 'fair value through other comprehensive income' (FVTOCI) measurement category for certain simple debt instruments.

6. NEW AND REVISED IFRS IN ISSUE BUT NOT YET EFFECTIVE CONTINUED

The key requirements of IFRS 9 are:

- **Classification and measurement of financial assets.** All recognised financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortised cost or fair value. Specifically, debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost at the end of subsequent accounting periods. Debt instruments that are held within a business model whose objective is achieved both by collecting contractual cash flows and selling financial assets, and that have contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding, are generally measured at FVTOCI. All other debt investments and equity investments are measured at their fair value at the end of subsequent accounting periods. In addition, under IFRS 9, entities may make an irrevocable election to present subsequent changes in the fair value of an equity investment (that is not held for trading nor contingent consideration recognised by an acquirer in a business combination) in other comprehensive income, with only dividend income generally recognised in profit or loss.
- **Classification and measurement of financial liabilities.** With regard to the measurement of financial liabilities designated as at fair value through profit or loss, IFRS 9 requires that the amount of change in the fair value of a financial liability that is attributable to changes in the credit risk of that liability is presented in other comprehensive income, unless the recognition of such changes in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss. Under IAS 39, the entire amount of the change in the fair value of the financial liability designated as fair value through profit or loss is presented in profit or loss.
- **Impairment.** In relation to the impairment of financial assets, IFRS 9 requires an expected credit loss model, as opposed to an incurred credit loss model under IAS 39. The expected credit loss model requires an entity to account for expected credit losses and changes in those expected credit losses at each reporting date to reflect changes in credit risk since initial recognition. In other words, it is no longer necessary for a credit event to have occurred before credit losses are recognised.
- **Hedge accounting.** The new general hedge accounting requirements retain the three types of hedge accounting mechanisms currently available in IAS 39. Under IFRS 9, greater flexibility has been introduced to the types of transactions eligible for hedge accounting, specifically broadening the types of instruments that qualify for hedging instruments and the types of risk components of non-financial items that are eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principle of an 'economic relationship'. Retrospective assessment of hedge effectiveness is also no longer required. Enhanced disclosure requirements about an entity's risk management activities have also been introduced.

Overall, the Group expects no significant impact on its balance sheet and equity, except for the effect of applying the impairment requirements of IFRS 9. The Group expects changes in the loss allowance methodology and is in the process of performing a detailed assessment to determine the extent. The Group is reviewing their debt and equity arrangements, processes for calculating impairment of receivables and cash and cash equivalents and evaluating the disclosure requirements of the new guidance, and will design and implement any identified necessary controls.

IFRS 16 *Leases*

IFRS 16 introduces a comprehensive model for the identification of lease arrangements and accounting treatments for both lessors and lessees. IFRS 16 will supersede the current lease guidance including IAS 17 Leases and the related interpretations when it becomes effective.

IFRS 16 distinguishes leases and service contracts on the basis of whether an identified asset is controlled by a customer. Distinctions of operating leases (off balance sheet) and finance leases (on balance sheet) are removed for lessee accounting, and is replaced by a model where a right-of-use asset and a corresponding liability have to be recognised for all leases by lessees (i.e. all on balance sheet) except for short-term leases and leases of low value assets.

6. NEW AND REVISED IFRS IN ISSUE BUT NOT YET EFFECTIVE CONTINUED

The right-of-use asset is initially measured at cost and subsequently measured at cost (subject to certain exceptions) less accumulated depreciation and impairment losses, adjusted for any remeasurement of the lease liability. The lease liability is initially measured at the present value of the lease payments that are not paid at that date. Subsequently, the lease liability is adjusted for interest and lease payments, as well as the impact of lease modifications, amongst others. Furthermore, the classification of cash flows will also be affected as operating lease payments under IAS 17 are presented as operating cash flows; whereas under the IFRS 16 model, the lease payments will be split into a principal and an interest portion which will be presented as financing and operating cash flows respectively.

In contrast to lessee accounting, IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17, and continues to require a lessor to classify a lease either as an operating lease or a finance lease.

Furthermore, extensive disclosures are required by IFRS 16.

The management of the Group anticipates that the application of this standard may have an impact on the Group's consolidated financial statements. The Group is currently assessing an impact of the new standard on the financial results. The Group is reviewing their agreements that may contain lease and evaluating the disclosure requirements of the new guidance, and will design and implement any identified necessary controls.

IFRS 15 *Revenue from Contracts with Customers*

IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. IFRS 15 will supersede the current revenue recognition guidance including IAS 18 Revenue, IAS 11 Construction Contracts and the related Interpretations when it becomes effective.

The core principle of IFRS 15 is that an entity should recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Specifically, the Standard introduces a five-step approach to revenue recognition:

- identify the contract with the customer;
- identify the performance obligations in the contract;
- determine the transaction price;
- allocate the transaction price to the performance obligations in the contracts; and
- recognise revenue when (or as) the entity satisfies a performance obligation.

Under IFRS 15, an entity recognises revenue when or as a performance obligation is satisfied, i.e. when 'control' of the goods or services underlying the particular performance obligation is transferred to the customer. Far more prescriptive guidance has been added in IFRS 15 to deal with specific scenarios. Furthermore, extensive disclosures are required by IFRS 15.

In April 2016, the IASB issued Clarifications to IFRS 15 in relation to the identification of performance obligations, principal versus agent considerations, as well as licensing application guidance.

6. NEW AND REVISED IFRS IN ISSUE BUT NOT YET EFFECTIVE CONTINUED

The management of the Group has performed an assessment of the impact of the adoption of IFRS 15. The management of the Group does not anticipate that the application of IFRS 15 will have a significant impact on the financial position and financial performance of the Group, but it anticipates extended disclosures required by IFRS 15.

Management anticipates that the adoption of other standards will not have a material impact on the consolidated financial statements of the Group in the period of initial application.

7. SEGMENT INFORMATION

The Group's operations are a single reportable segment.

The Group provides mobile communication services in the Republic of Kazakhstan. The Group identifies the segment in accordance with the criteria set in IFRS 8, *Operating Segments*, and based on the way the operations of the Group are regularly reviewed by the chief operating decision-maker to analyse performance and allocate resources among business units of the Group.

The chief operating decision-maker (CODM) has been determined as the Group's Chief Executive Officer. The CODM reviews the Group's internal reporting in order to assess performance and allocate resources. Management has determined a single operating segment being mobile communication services based on these internal reports.

8. BALANCES AND TRANSACTIONS WITH RELATED PARTIES

Parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence or joint control over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. The Group's ultimate controlling party is Telia Company. Telia Company group includes entities under common control and associates of Telia Company. Immediate shareholders are disclosed in the Note 12.

8. BALANCES AND TRANSACTIONS WITH RELATED PARTIES CONTINUED

The Group's primary transactions with related parties are consulting services, technical assistance and operational support, roaming and interconnect. The Group's transactions with its related parties during the years ended 31 December and related amounts due as of the year-end were as follows:

		2017	2016
Due from related parties	Entities of Telia Company group	**810,492**	738,983
Due to related parties	Entities of Telia Company group	**135,926**	522,766
Due to related parties	Immediate and ultimate parent	**1,041,407**	1,002,793
Revenue	Entities of Telia Company group	**897,529**	1,415,936
Expense	Entities of Telia Company group	**3,807,743**	5,253,027
Expense	Immediate and ultimate parent	**103,977**	39,095

Amounts due from related parties are neither past due nor impaired. They represent receivables from related parties for roaming services. These entities do not have credit ratings assigned but their reliability is determined by the Group on the basis of long-term cooperation and which have a good credit history. The Group's management believes that amounts due from related parties will be fully repaid within one year.

Memorandum of Understanding (MoU)

On 26 August 2012, Sonera and the Company entered into a memorandum of understanding, details of which are disclosed further in Note 19.

Compensation of key management personnel

Compensation paid to key management personnel for their services in full time executive management positions and to the members of the Board of Directors consists of a contractual salary, performance bonus depending on financial performance of the Group, and other compensation in the form of reimbursement of apartment rent expenses from the Group. Total compensation included in staff costs in the statement of comprehensive income is equal to KZT236,408 thousand for the year ended 31 December 2017 (2016: KZT245,522 thousand). The compensation scheme does not include share-based payments, post-employment or other long-term benefits, which were nil for all years presented.

(in thousand of Kazakhstani tenge, unless otherwise stated)

9. PROPERTY, PLANT AND EQUIPMENT

	Property	Plant and machinery	Equipment tools and installations	Assets under construction and advances given	Total
As at 1 January 2016					
Cost	21,048,276	183,391,835	25,182,608	10,676,412	240,299,131
Accumulated depreciation and impairment losses	(4,627,370)	(122,654,933)	(18,515,383)	–	(145,797,686)
Carrying amount as at 1 January 2016	16,420,906	60,736,902	6,667,225	10,676,412	94,501,445
Additions	168,635	–	1,014,372	16,654,308	17,837,315
Business combination (Note 3)	–	–	184,562	–	184,562
Transfers	–	10,361,061	257,975	(10,619,036)	–
Disposals (net)	–	–	(9,666)	–	(9,666)
Depreciation charge	(686,233)	(14,695,272)	(1,810,545)	–	(17,192,050)
As at 31 December 2016					
Cost	21,216,911	193,752,896	26,553,990	16,711,684	258,235,481
Accumulated depreciation and impairment losses	(5,313,603)	(137,350,205)	(20,250,067)	–	(162,913,875)
Carrying amount as at 31 December 2016	15,903,308	56,402,691	6,303,923	16,711,684	95,321,606
Additions	59,459	–	1,480,694	14,202,569	15,742,722
Transfers	–	11,887,139	2,062,191	(13,949,330)	–
Depreciation charge	(579,066)	(14,604,457)	(2,200,723)	–	(17,384,246)
As at 31 December 2017					
Cost	21,276,370	205,640,035	30,096,875	16,964,923	273,978,203
Accumulated depreciation and impairment losses	(5,892,669)	(151,954,662)	(22,450,790)	–	(180,298,121)
Carrying amount as at 31 December 2017	15,383,701	53,685,373	7,646,085	16,964,923	93,680,082

As at 31 December 2017, the gross carrying value of property, plant and equipment, which had been fully depreciated and were still in use, was KZT105,879,825 thousand (31 December 2016: KZT95,704,126 thousand).

10. INTANGIBLE ASSETS

	Software and licenses	Intangible assets in progress	Advances given	Total
As at 1 January 2016				
Cost	41,605,939	3,886,778	382,504	45,875,221
Accumulated amortisation	(28,919,033)	–	–	(28,919,033)
Carrying amount as at 1 January 2016	**12,686,906**	**3,886,778**	**382,504**	**16,956,188**
Additions	15,762,033	3,161,176	14,000,000	32,923,209
Business combination (Note 3)	61	–	–	61
Transfers	15,783,873	(1,409,591)	(14,374,282)	–
Amortisation charge	(7,036,978)	–	–	(7,036,978)
As at 31 December 2016				
Cost	73,151,906	5,638,363	8,222	78,798,491
Accumulated amortisation	(35,956,011)	–	–	(35,956,011)
Carrying amount as at 31 December 2016	**37,195,895**	**5,638,363**	**8,222**	**42,842,480**
Additions	4,480,056	456,750	1,043,713	5,980,519
Transfers	6,133,204	(5,638,363)	(494,841)	–
Amortisation charge	(5,762,324)	–	–	(5,762,324)
As at 31 December 2017				
Cost	83,765,166	456,750	557,094	84,779,010
Accumulated amortisation	(41,718,335)	–	–	(41,718,335)
Carrying amount as at 31 December 2017	**42,046,831**	**456,750**	**557,094**	**43,060,675**

Initially, a new billing system, Amdocs, was classified as intangible assets in progress. As of 31 December 2017, Amdocs was transferred to software and licenses.

As at 31 December 2017, the carrying amount of the 3G license was KZT2,666,667 thousand (31 December 2016: KZT3,000,000 thousand) and its remaining amortisation period was eight years. As at 31 December 2017, the carrying amount of the 4G license was KZT22,677,777 thousand (31 December 2016: KZT24,411,111 thousand) and its remaining amortisation period was 13 years. As at 31 December 2017, the gross carrying value of intangible assets, which had been fully amortised and were still in use, was KZT19,275,605 thousand (31 December 2016: KZT16,668,784 thousand).

(in thousand of Kazakhstani tenge, unless otherwise stated)

11. TRADE AND OTHER RECEIVABLES

	31 December 2017	31 December 2016
Trade receivables from subscribers	**15,422,256**	12,955,810
Trade receivables for interconnect services	**900,299**	452,276
Trade and other receivables from dealers and distributors	**326,613**	1,280,359
Trade receivables from roaming operators	**259,550**	1,895,114
Less: allowance for impairment of trade receivables	**(5,494,150)**	(2,839,931)
Total financial assets	**11,414,568**	13,743,628
Less: long-term trade receivables from subscribers	**(1,437,480)**	(1,162,961)
Total current financial assets	**9,977,088**	12,580,667
VAT recoverable	**5,516,033**	2,330,281
Advances to suppliers	**2,556,276**	1,456,953
Prepaid other taxes	**497,818**	454,778
Deferred expenses	**446,512**	544,379
Other receivables	**678,995**	871,862
Total trade and other receivables	**19,672,722**	18,238,920

Total financial assets are denominated in currencies as follows:

	31 December 2017	31 December 2016
Tenge	**11,155,018**	11,848,514
US dollar	**259,550**	1,895,114
Total financial assets	**11,414,568**	13,743,628

11. TRADE AND OTHER RECEIVABLES CONTINUED

The allowance for impairment of trade receivables relates to trade receivables from subscribers, dealers and distributors. The ageing analysis of trade receivables is as follows:

	31 December 2017	31 December 2016
Total neither past due nor impaired	**8,509,690**	11,978,871
Past due but not impaired		
due for 1 month	**110,333**	77,591
due for 2 months	**822,516**	61,162
due for 3 months	**538,588**	213,468
due for 4 to 6 months	**649,269**	941,068
due for more than 6 months	**784,172**	471,468
Total past due but not impaired	**2,904,878**	1,764,757
Impaired		
30 to 60 days	**71,049**	56,860
60 to 90 days	**22,154**	69,496
90 to 120 days	**107,377**	82,514
120 to 200 days	**166,578**	232,627
Over 200 days	**5,126,992**	2,398,434
Total impaired	**5,494,150**	2,839,931
Allowance for impairment of trade receivables	**(5,494,150)**	(2,839,931)
Total financial assets	**11,414,568**	13,743,628

The main factors, which the Group takes into account when considering whether receivables are impaired, are their past due status and historical experience of collectability. Impairment of receivables was assessed based on the past due status of such receivables.

There are no customers who represent more than 10% of the total balance of receivables. The concentration of credit risk is limited due to the customer base being large and unrelated.

Notes to the Consolidated Financial Statements continued

(in thousand of Kazakhstani tenge, unless otherwise stated)

11. TRADE AND OTHER RECEIVABLES CONTINUED

Neither past due nor impaired receivables represent receivables from companies and subscribers with no credit ratings assigned but their reliability is determined by the Group on the basis of long-term cooperation representing those companies which have a good credit history. The Group's management believes that neither past due nor impaired receivables in the amount of KZT8,509,690 thousand will be fully repaid in 2018.

A reconciliation of movements in the financial assets impairment allowance is as follows:

	2017	2016
As at 1 January	**2,839,931**	2,467,799
Charge for the year	**2,716,419**	1,090,968
Receivables written off during the year as uncollectible	**(62,200)**	(718,836)
As at 31 December	**5,494,150**	2,839,931

The Group considers that the carrying amount of receivables is approximately equal to their fair value.

12. SHARE CAPITAL AND EARNINGS PER SHARE

Share capital of the Group at 31 December is as follows:

	31 December 2017		31 December 2016	
	Share	Number of shares	Share	Number of shares
Fintur	**51.00 percent**	**102,000,000**	51.00 percent	102,000,000
TeliaSonera Kazakhstan	**24.00 percent**	**48,000,000**	24.00 percent	48,000,000
JSC Central Securities Depositary	**13.24 percent**	**26,472,717**	23.32 percent	46,636,793
JSC Freedom Finance	**9.08 percent**	**18,153,541**	–	–
Single Accumulative Pension Fund	**1.14 percent**	**2,270,950**	1.14 percent	2,270,950
Other	**1.54 percent**	**3,102,792**	0.54 percent	1,092,257

The total authorised number of ordinary shares is 200,000,000 shares with a par value of KZT169 per share, all of which are issued and fully paid.

12. SHARE CAPITAL AND EARNINGS PER SHARE CONTINUED

The calculation of basic and diluted earnings per share is based on the following data:

	2017	2016
Profit for the period attributable to equity shareholders	**13,434,246**	16,683,616
Weighted average number of common shares	**200,000,000**	200,000,000
Earnings per share (Kazakhstani tenge), basic and diluted	**67.17**	83.42

The Group has no dilutive or potentially dilutive securities outstanding.

According to the requirements of the Kazakhstan Stock Exchange (KASE), the Group has calculated its book value per share, which was calculated based on the number of common shares outstanding as at the reporting date. The book value per share as at 31 December 2017 and 31 December 2016 is presented below.

	31 December 2017	31 December 2016
Net assets, excluding intangible assets	**31,375,857**	29,837,806
Number of common shares in issue	**200,000,000**	200,000,000
Book value per share (Kazakhstani tenge)	**156.88**	149.19

Dividends declared and paid during the years ended 31 December were as follows:

	2017	2016
Dividends payable as at 1 January	**–**	–
Dividends declared during the year	**11,678,000**	23,316,000
Dividends paid during the year	**(11,678,000)**	(23,316,000)
Dividends payable as at 31 December	**–**	–

Notes to the Consolidated Financial Statements continued

(in thousand of Kazakhstani tenge, unless otherwise stated)

13. TRADE AND OTHER PAYABLES

	31 December 2017	31 December 2016
Trade payables	**15,099,016**	21,605,956
Total financial liabilities	**15,099,016**	21,605,956
Accrued salaries and bonuses to employees	**1,334,003**	1,276,596
Other payables	**4,795,199**	4,070,062
Total trade and other payables	**21,228,218**	26,952,614

Trade and other payables are denominated in currencies as follows:

	31 December 2017	31 December 2016
Tenge	**10,997,974**	9,512,408
US dollar	**4,099,843**	11,624,078
Euro	**–**	433,373
Other	**1,199**	36,097
Total financial liabilities	**15,099,016**	21,605,956

14. BORROWINGS

	31 December 2017	31 December 2016
Halyk Bank of Kazakhstan JSC	**34,209,722**	42,221,389
Eurasian Development Bank	**26,103,278**	–
Alfabank JSC	**10,104,722**	10,124,500
Kazkommertsbank JSC	**–**	10,035,000
Altyn Bank JSC (previously – SB HSBC Kazakhstan JSC)	**–**	3,033,750
Total borrowings	**70,417,722**	65,414,639
Including		
Long-term loans	**12,000,000**	8,000,000
Short-term loans – principal amount	**58,000,000**	57,000,000
Short-term loans – accrued interest	**417,722**	414,639

14. BORROWINGS CONTINUED

The Group's borrowings are denominated in Kazakhstani tenge. The Group has not entered into any hedging arrangements in respect of its interest rate exposures.

The carrying amount of the Group's borrowings approximates their fair value.

The details of the Group's borrowings as at 31 December 2017 are as follows:

Bank name	Date of issue	Maturity date	Nominal interest rate	Principal amount	Outstanding balance
Eurasian Development Bank	10/02/2017	20/06/2018	13.00%	26,000,000	26,103,278
Halyk Bank of Kazakhstan JSC	05/06/2017	04/12/2018	12.50%	22,000,000	22,198,611
Halyk Bank of Kazakhstan JSC	23/09/2016	20/09/2019	12.50%	4,000,000	4,002,778
Halyk Bank of Kazakhstan JSC	28/11/2016	02/12/2019	12.50%	8,000,000	8,008,333
Alfabank JSC	01/06/2017	08/06/2018	14.50%	6,000,000	6,062,833
Alfabank JSC	01/06/2017	10/07/2018	14.50%	4,000,000	4,041,889
Total				**70,000,000**	**70,417,722**

As at 31 December 2017 and 2016, no assets were pledged under borrowing agreements.

As at 31 December 2017 and 2016, the Group was in compliance with its financial covenants.

The table below details changes in the Group's liabilities arising from financing activities. Liabilities arising from financing activities are those for which cash flows were, or future cash flows will be, classified in the Group's consolidated statement of cash flows as cash flows from financing activities.

	1 January 2017	Financing cash flows	31 December 2017
Borrowings, principal amount	65,000,000	5,000,000	**70,000,000**

The cash flows from borrowings make up the net amount of proceeds from borrowings and repayments of borrowings in the consolidated statement of cash flows.

(in thousand of Kazakhstani tenge, unless otherwise stated)

15. REVENUES

	2017	2016
Voice service	**80,400,456**	86,443,705
Data service	**46,358,118**	41,529,225
Sale of handsets	**10,633,243**	9,713,475
Value added services	**9,837,171**	9,350,599
Total revenues	**147,228,988**	147,037,004

16. EXPENSES BY NATURE

Operating expenses are presented on the face of the statement of comprehensive income using a classification based on the functions ‘Cost of sales’, ‘Selling and marketing expenses’ and ‘General and administrative expenses’. Total expenses by function were distributed by nature as follows:

	2017	2016
Interconnect fees and expenses	**23,803,220**	25,663,407
Depreciation and amortisation	**23,146,570**	24,229,028
Network maintenance expenses	**16,126,531**	15,315,438
Frequency usage charges and taxes other than on income	**11,388,790**	10,614,327
Cost of SIM card, scratch card, start package sales and handsets	**11,004,649**	10,118,847
Staff costs	**10,949,404**	11,148,947
Transmission rent	**9,803,504**	9,909,019
Sales commissions to dealers and advertising expenses	**2,723,711**	3,274,185
Other	**7,190,782**	6,730,409
Total expenses	**116,137,161**	117,003,607

Amortisation and depreciation by function were as follows:

	2017	2016
Cost of sales	**20,361,235**	21,826,610
General and administrative expenses	**2,785,335**	2,402,418
Total depreciation of property, plant and equipment and amortisation of intangible assets	**23,146,570**	24,229,028

16. EXPENSES BY NATURE CONTINUED

Other operating expense for the year ended 31 December comprised the following:

	2017	2016
Operational foreign exchange loss	**415,968**	1,349,460
Property, plant and equipment write-off	**–**	29,310
Other	**202,083**	485,002
Total other operating expenses	**618,051**	1,863,772

17. FINANCE INCOME AND FINANCE EXPENSE

Finance income for the year ended 31 December comprised the following:

	2017	2016
Interest income	**722,764**	1,316,560
Foreign exchange gains	**234,550**	1,333,985
Total finance income	**957,314**	2,650,545

Finance expense for the year ended 31 December comprised the following:

	2017	2016
Interest expense	**10,104,293**	10,283,135
Foreign exchange losses	**272,387**	652,458
Total finance expense	**10,376,680**	10,935,593

Notes to the Consolidated Financial Statements continued

(in thousand of Kazakhstani tenge, unless otherwise stated)

18. TAXES

Income tax expense comprised the following:

	2017	2016
Current income tax	**7,267,496**	4,352,334
Deferred income tax	**(1,194,711)**	975,193
Current income tax in respect of prior years	**2,575,039**	745,092
Total income tax expense	**8,647,824**	6,072,619

A reconciliation of income tax expense applicable to profit before taxation at the statutory income tax rate to income tax expense reported in the consolidated financial statements was as follows:

	2017	2016
Profit before income tax	**22,082,070**	22,756,235
Theoretical tax charge at the statutory rate of 20%	**4,416,414**	4,551,247
Non-deductible expenses	**1,656,371**	776,280
	6,072,785	5,327,527
Adjustments recognised in the current year in relation to the current tax of prior years	**2,575,039**	745,092
Income tax expense	**8,647,824**	6,072,619

The Group paid income tax in the amount of KZT5,012,000 thousand for the year ended 31 December 2017 (2016: KZT10,505,520 thousand).

Differences between IFRS and Kazakhstani statutory taxation regulations give rise to temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and their tax bases. The tax effect of the movements in these temporary differences is detailed below and is recorded at the rates which are expected to be applied to the periods when the temporary difference will reverse.

	31 December 2016	Credited to profit or loss	31 December 2017
Tax effects of deductible temporary differences			
Other	1,158,353	1,170,773	2,329,126
Gross deferred tax asset	**1,158,353**	**1,170,773**	**2,329,126**
Tax effect of taxable temporary differences			
Property, plant and equipment and Intangible assets	7,170,567	(23,938)	7,146,629
Gross deferred tax liability	**7,170,567**	**(23,938)**	**7,146,629**
Less offsetting with deferred tax assets	(1,158,353)	(1,170,773)	(2,329,126)
Recognised deferred tax liability, net	**6,012,214**	**(1,194,711)**	**4,817,503**

18. TAXES CONTINUED

Comparative movements for year ended 31 December 2016 is detailed below:

	1 January 2016	Debited/ Credited to profit or loss	31 December 2016
Tax effects of deductible temporary differences			
Other	889,811	268,542	1,158,353
Gross deferred tax asset	**889,811**	**268,542**	**1,158,353**
Tax effect of taxable temporary differences			
Property, plant and equipment and Intangible assets	5,926,832	1,243,735	7,170,567
Gross deferred tax liability	**5,926,832**	**1,243,735**	**7,170,567**
Less offsetting with deferred tax assets	(889,811)	(268,542)	(1,158,353)
Recognised deferred tax liability, net	**5,037,021**	**975,193**	**6,012,214**

19. CONTINGENCIES, COMMITMENTS AND OPERATING RISKS

Political and economic conditions in the Republic of Kazakhstan

Emerging markets such as the Republic of Kazakhstan are subject to different risks than more developed markets, including economic, political and social, and legal and legislative risks. Laws and regulations affecting businesses in the Republic of Kazakhstan continue to change rapidly, tax and regulatory frameworks are subject to varying interpretations. The future economic direction of the Republic of Kazakhstan is heavily influenced by the fiscal and monetary policies adopted by the government, together with developments in the legal, regulatory and political environment.

Because the Republic of Kazakhstan produces and exports large volumes of oil and gas, its economy is particularly sensitive to the price of oil and gas on the world market. During 2014-16, the oil price decreased significantly, which led to a significant decrease in the national export revenue. On 20 August 2015, the Government and the National Bank of the Republic of Kazakhstan announced a transition to a new monetary policy based on a free-floating tenge exchange rate, and cancelled the currency corridor. In 2015 and in the first quarter of 2016, the tenge depreciated significantly against major foreign currencies.

Management of the Group is monitoring developments in the current environment and taking measures it considered necessary in order to support the sustainability and development of the Group's business in the foreseeable future. However, the impact of further economic developments on future operations and financial position of the Group might be significant.

Taxation

Kazakhstani tax legislation and practice is in a state of continuous development and therefore is subject to varying interpretations and frequent changes, which may be retroactive. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activities of the Group may not coincide with that of management. As a result, transactions may be challenged by tax authorities and the Group may be assessed additional taxes, penalties and interest. Tax periods remain open to retroactive review by the tax authorities for five years.

19. CONTINGENCIES, COMMITMENTS AND OPERATING RISKS CONTINUED

In July 2017, the Kazakhstan tax authority completed its comprehensive tax audit for the period 2012 to 2015. Following the completion of the tax audit, the tax authority made a total claim of KZT9 billion, of which KZT5.8 billion is for unpaid taxes and KZT3.2 billion represents fines and penalties for the late payment of unpaid taxes. Currently, the Group disputes certain elements of this claim with respect to those issues on which the Group does not agree. Such dispute is ongoing through the available mechanisms, which include court litigation. The Group considers it unlikely that the full amount of the claim will become payable following the appeal process.

The Kazakhstan tax authority's claim relates to various issues including VAT, corporate income tax and other taxes. The Group disputes several of the individual findings, including a claim that withholding tax should have been paid in relation to the IPO in 2012, when retained earnings were reinvested in the newly formed Joint Stock Company.

The Group has recorded the reserves and contingent liabilities for the tax audit, but does not disclose the amount pertaining to each claim, because it believes that disclosure of this information may adversely affect the outcome of tax audit results disputes.

Capital expenditure commitments

As at 31 December 2017, the Group has contractual capital expenditure commitments in respect of property, plant and equipment and intangible assets totaling KZT6,873,547 thousand (31 December 2016: KZT4,514,284 thousand).

Acquisitions and investments

(i) Memorandum of understanding with Sonera

On 26 August 2012, Sonera and the Company entered into a memorandum of understanding ("the Buy and Sell MoU"), under which the Company had the right to require Sonera to sell to it, and Sonera had the right to require the Company to acquire from it, all participatory interests owned by Sonera in KazNet Media LLP (KazNet) together with all rights and obligations of Sonera under a framework agreement to buy all the participatory interests in the charter capital of KazNet and all the participatory interests owned by Sonera in Rodnik Inc LLP (Rodnik) together with all rights and obligations of Sonera under the agreements to buy participatory interests in the charter capital of Rodnik (refer to "Investment in Rodnik by Sonera").

Subject to satisfaction of the applicable conditions, each of Sonera and the Company was entitled to exercise its option at any time starting from nine months after the date of the offering of global depositary receipts and listing on local stock exchange, which took place on 13 December 2012. The purchase price that the Company was supposed to pay to Sonera for the acquisition resulting from the exercise of the option would be the amount of net cost incurred by Sonera in connection with the corresponding investments and acquisition transactions plus interest accrued on such amount.

The contractual right of Sonera to sell the underlying assets (debt and equity interests and related rights and obligations) to the Company is a financial instrument (derivative) within the scope of IAS 39, *Financial Instruments: Recognition and Measurement*. The derivative instrument should be measured at fair value, with the changes in fair value recognised in the statement of comprehensive income. The Group did not have an unconditional right to avoid the settlement.

Sonera had the right to terminate the Buy and Sell MoU at any time by serving a written notice to the Company.

19. CONTINGENCIES, COMMITMENTS AND OPERATING RISKS CONTINUED

The exercise of these options was conditional upon Fintur having consented to, authorised or voted in favour of the acquisition to be made by the Company as a result of the exercise of such right. In addition, completion of the acquisition contemplated by the exercise of options is subject to law, regulation and any requisite approvals. Sonera had the option to sell ("the Put Option") and the Company had the option to buy ("the Call Option") the participatory interest. The strike price of the both options equals the net costs incurred by Sonera, annually compounded using the interest rate (interest accruals begins when the costs are incurred or the receipts are cashed and ends when the participatory interest are transferred).

Neither the Put Option nor the Call Option could be exercised without the authorisation of Fintur. In addition there is uncertainty in the timing of required changes in 4G/LTE regulation. Accordingly, there is an uncertainty regarding whether the option will be exercised. On this basis, the Company measured the derivative at the original cost of zero.

On 4 May 2016, the Company obtained control over the activity of KazNet (Note 3).

(ii) Investment in Rodnik by Sonera

Sonera negotiated an agreement with a third party to acquire 25% of the participatory interests in the charter capital of Rodnik. Rodnik owns 79.92% of the total share capital of KazTransCom JSC (KTC).

The purchase price for acquisition is US$20 million, subject to adjustments to be made based on the amount of net debt of Rodnik and KTC at the time the acquisition is completed.

On 13 August 2012, Sonera entered into a call option agreement with a third party, under which Sonera has a call option to acquire another 75% participatory interest in Rodnik. Pursuant to the terms of that call option agreement, the call option exercise price will be calculated based on fair market value of the participatory interest in Rodnik.

The acquisition of 25% of the participatory interests in the charter capital of Rodnik was completed on 14 January 2013.

Execution of the KazNet option had no effect on the option related to Rodnik.

The standby letter of credit

The standby letter of credit for US$10 million, within the framework of the general agreement between the Group and Citibank Kazakhstan JSC, was issued on 23 September 2015. As at 31 December 2017, the credit limit has been decreased to US$5.5 million. This instrument has been issued in favour of Apple Distribution International (Ireland) to allow the Group to extend the term of payment for goods purchased from the company, and will have a positive impact on the Group's working capital. As at 31 December 2017, the instrument has been used, the outstanding balance is KZT542 thousand.

The 'Daytime Unlimited' and failure to disconnect calls on Kcell network

During 2013, an investigation was initiated by the Agency for Competition Protection of the Republic of Kazakhstan ("the ACP"), in relation to the 'Daytime Unlimited' service under the Activ brand and non-interruption of services when a customer's balance reaches zero under the Kcell brand. On conclusion of the initial investigations, the Antimonopoly Inspectorate issued an administrative offence report with a potential fine on the Company of KZT16 billion. During the following court process the Company was able to reduce the penalty to KZT325 million and subsequently made payment in full in May 2014.

Notes to the Consolidated Financial Statements continued

(in thousand of Kazakhstani tenge, unless otherwise stated)

19. CONTINGENCIES, COMMITMENTS AND OPERATING RISKS CONTINUED

The ACP ordered that the Company should comply with the following on or before 21 April 2014:

1. to stop collection of the subscription fees under the tariff plan ‘Daytime Unlimited’ in case of insufficiency of funds on a subscriber’s account;
2. to ensure interruption of connection (voice or Internet access) when a subscriber’s balance reaches zero; and
3. to ensure a refund to subscribers, any fees received as a result of failure to interrupt the connection when a subscriber’s balance reaches zero (“the Order”).

The Company complied with point 1, however, due to technical limitations of the billing system, the Company is currently unable to implement point 2. However, the Company is in the process of introducing a new billing system that will enable the interruption of the connection.

The Company has challenged the ACP findings and decision through the courts system in the Republic of Kazakhstan, culminating in an appeal to the Supreme Court. On 30 June 2015, the Supreme Court of the Republic of Kazakhstan dismissed the Company’s supervisory appeal. On 15 June 2015, the ACP filed a claim in court seeking for enforcement of the order. On 9 July 2015, the court issued a resolution on satisfying the ACP claim to enforce the order, and as a result the Company must now enforce points 2 and 3 in the above ACP order.

As at 31 December 2017, the total amount returned to subscribers is KZT2,618,045 thousand. As at 31 December 2017, the Company accrued a provision in the amount of KZT116,640 thousand (31 December 2016: KZT116,640 thousand). The Company expects further refunding the subscription of fees until point 2 above is enforced.

20. FINANCIAL RISK MANAGEMENT

Financial risk factors

The Group’s activities expose it to a variety of financial risks: market risk (including foreign exchange risk), liquidity risk and credit risk. The Group’s overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group’s financial performance. The Group does not use derivative financial instruments to hedge risk exposures.

Credit risk

The Group takes on exposure to credit risk, which is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. Exposure to credit risk arises as a result of the Group’s sales on credit terms and other transactions with counterparties giving rise to financial assets.

20. FINANCIAL RISK MANAGEMENT CONTINUED

The Group's maximum exposure to credit risk by class of assets is as follows:

	Note	31 December 2017	31 December 2016
Cash and cash equivalents		**12,659,844**	8,476,653
Trade receivables	11	**9,977,088**	12,580,667
Long-term trade receivables		**1,437,480**	1,162,961
Due from related parties	8	**810,492**	738,983
Restricted cash		**38,733**	86,419
Total maximum exposure to credit risk		**24,923,637**	23,045,683

Credit risk from balances with cash and cash equivalents is managed by the Group's treasury department in accordance with the Group's policy. Investments of surplus funds are made only with approved financial institutions and within credit limits assigned to each bank or financial institution. Financial institutions' credit limits are reviewed by the Group's Treasury department on a monthly basis. The limits are set to minimise the concentration of risks and therefore mitigate financial loss through a financial institution's potential failure to make payments.

The Group has policies in place to ensure that sales of products and services are made to customers and distributors with an appropriate credit history. If corporate customers are independently rated, these ratings are used. Otherwise, if there is no independent rating, risk control assesses the credit quality of the customer taking into account its financial position, past experience and other factors. The Group's management reviews ageing analysis of outstanding trade receivables and follows up on past due balances. Customers that fail to settle their liabilities for mobile services provided are disconnected until the debt is paid. Management provides ageing and other information about credit risk (Note 11). The carrying amount of accounts receivable, net of provision for impairment of receivables, represents the maximum amount of trade receivables exposed to credit risk. The Group has no significant concentrations of credit risk since the customers portfolio is diversified among a large number of customers, both individuals and companies. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provisions already recorded.

Foreign exchange risk

The majority of the Group's purchases of property, plant and equipment and inventories, as well as certain services such as roaming are denominated in US dollars. Hence, the major concentration of foreign exchange risk arises from the movement of the US dollar against the tenge. Due to the undeveloped market for financial instruments in Kazakhstan, the management does not hedge the Group's foreign exchange risk.

The carrying amounts of the Group's foreign currency denominated monetary assets and monetary liabilities at the end of the reporting period are as follows.

	Liabilities		Assets	
	31 December 2017	31 December 2016	31 December 2017	31 December 2016
US dollar	**4,099,843**	11,624,078	**2,472,071**	5,116,232
Euro	**–**	433,373	**212,019**	174,072
Others	**1,199**	36,097	**4,280**	50,033

(in thousand of Kazakhstani tenge, unless otherwise stated)

20. FINANCIAL RISK MANAGEMENT CONTINUED

As at 31 December 2017, if the US dollar had weakened/strengthened by 10% against the tenge with all other variables held constant, after-tax profit for year ended 31 December 2017 would have been KZT113,014 thousand lower/higher (2016: KZT540,257 thousand lower/higher), mainly as a result of foreign exchange gains/losses on translation of US dollar-denominated bank balances, receivables and payables. Profit is less sensitive to movement in tenge/US dollar exchange rates at 31 December 2017 than at 31 December 2016 because of the increased amount of US dollar-denominated cash and cash equivalents at 31 December 2017 offsets exposure to US dollar denominated accounts payable.

Cash flow and fair value interest rate risk

The Group does not have floating interest-bearing assets or liabilities as of 31 December 2017, and as such, management has not presented interest rate sensitivity analysis.

Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash. Due to the dynamic nature of the underlying businesses, the Group's treasury aims to maintain flexibility in funding by keeping sufficient cash available.

The table below shows financial liabilities as at 31 December 2017 by their remaining contractual maturity. The amounts disclosed in the maturity table are the contractual undiscounted cash flows. When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the reporting date. Foreign currency payments are translated using the spot exchange rate at the reporting date.

The maturity analysis of financial liabilities as at 31 December 2017 is as follows:

	Demand and less than 3 months	From 3 to 12 months	More than 12 months	Total
Liabilities				
Borrowings	2,687,722	62,109,417	13,319,444	78,116,583
Trade payables	15,099,016	–	–	15,099,016
Due to related parties	1,177,333	–	–	1,177,333
Total future payments	**18,964,071**	**62,109,417**	**13,319,444**	**94,392,932**

The comparative maturity analysis of financial liabilities as at 31 December 2016 is detailed below:

	Demand and less than 3 months	From 3 to 12 months	More than 12 months	Total
Liabilities				
Borrowings	2,942,139	57,683,278	10,624,500	71,249,917
Trade payables	21,605,956	–	–	21,605,956
Due to related parties	1,525,559	–	–	1,525,559
Total future payments	**26,073,654**	**57,683,278**	**10,624,500**	**94,381,432**

20. FINANCIAL RISK MANAGEMENT CONTINUED

Management believes that the payments of the borrowings and other financial liabilities will be financed by cash flows from operating activities and that the Group will be able to meet its obligations as they fall due. The Group can extend borrowings up to an additional 12 months, subject to consent of the lenders (Note 14).

Fair value of financial instruments

The Group does not carry any financial assets or liabilities at fair value. Management of the Group considers that the carrying amount of financial assets and financial liabilities recorded at amortised cost in the consolidated financial statements approximate their fair values due to their short-term maturities.

Capital management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for owners and benefits to other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to owners, return capital to owners, issue new capital and sell assets to reduce debt.

Offsetting a financial asset and a financial liability

Financial instruments subject to offsetting, enforceable master netting and similar arrangements are as follows as at 31 December 2017:

	Gross amounts before offsetting in the statement of financial position (a)	Gross amounts set off in the statement of financial position (b)	Net amount after offsetting in the statement of financial position and net amount of exposure (c) = (a) – (b)
ASSETS			
Trade receivables from interconnect services	3,240,121	2,625,399	614,722
Trade receivables from roaming services	1,449,632	1,190,082	259,550
Total assets subject to offsetting, master netting and similar arrangement	**4,689,753**	**3,815,481**	**874,272**
LIABILITIES			
Trade payables for interconnect services	3,319,596	2,625,399	694,197
Trade payables for roaming services	1,190,082	1,190,082	–
Total liabilities subject to offsetting, master netting and similar arrangement	**4,509,678**	**3,815,481**	**694,197**

Financial instruments represented by trade receivables from interconnect services in the amount of KZT285,577 thousand and corresponding trade payables in the amount of KZT4,944 thousand are not eligible for offsetting. Services include testing, monitoring, analysing and optimisation of international SMS traffic routes that are provided by various number of counterparties and the Group has no intention to process payables and receivables on a net basis.

(in thousand of Kazakhstani tenge, unless otherwise stated)

20. FINANCIAL RISK MANAGEMENT CONTINUED

Financial instruments subject to offsetting, enforceable master netting and similar arrangements are as follows as at 31 December 2016:

	Gross amounts before offsetting in the statement of financial position (a)	Gross amounts set off in the statement of financial position (b)	Net amount after offsetting in the statement of financial position and net amount of exposure (c) = (a) – (b)
ASSETS			
Trade receivables from interconnect services	4,938,459	4,486,183	452,276
Trade receivables from roaming services	4,548,493	2,653,379	1,895,114
Total assets subject to offsetting, master netting and similar arrangement	**9,486,952**	**7,139,562**	**2,347,390**
LIABILITIES			
Trade payables for interconnect services	5,235,844	4,486,183	749,661
Trade payables for roaming services	2,653,379	2,653,379	–
Total liabilities subject to offsetting, master netting and similar arrangement	**7,889,223**	**7,139,562**	**749,661**

The amount set off in the statement of financial position reported in column (b) is the lower of: (i) the gross amount before offsetting reported in column; (a) and (ii) the amount of the related instrument that is eligible for offsetting.

The Group has master netting arrangements with telecom operators, which are enforceable in case of default. In addition, applicable legislation allows an entity to unilaterally set off trade receivables and payables that are due for payment, denominated in the same currency and outstanding with the same counterparty. These fall in the scope of the disclosure as they were set off in the consolidated statement of financial position.

21. FAIR VALUE OF FINANCIAL INSTRUMENTS

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Republic of Kazakhstan continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments. For the purpose of fair value disclosures the Group determines below described instruments' fair value hierarchy as level 2 (significant observable inputs).

21. FAIR VALUE OF FINANCIAL INSTRUMENTS CONTINUED

Financial assets carried at amortised cost

The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Discount rates used depend on credit risk of the counterparty. Carrying amounts of cash and cash equivalents, trade receivables and due from related parties approximate fair values due to their short-term maturities. As at 31 December 2017 and 31 December 2016, the fair value of financial assets was not significantly different from their carrying value.

Financial liabilities carried at amortised cost

The estimated fair value of fixed interest rate instruments with stated maturity, for which a quoted market price is not available, was estimated based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Carrying amounts of trade payables, dividends payable and due to related parties approximate fair values due to their short-term maturities. As at 31 December 2017 and 31 December 2016, the fair value of financial liabilities was not significantly different from their carrying value.

22. SUBSEQUENT EVENTS

Order N° 403 of the Minister of Information and Communications of the Republic of Kazakhstan dated 21 November 2017 on Amendments and Additions to the Order N° 171 of the Acting Minister for Investment and Development of the Republic of Kazakhstan dated 24 February 2015 'On Approval of the Rules for the Provision of Communication Services' was officially published on 16 January 2018, and came into force on 26 January 2018. Rules state that mobile operators will be obliged:

(i) to inform subscribers when bonus allowances are fully consumed and charge from the main balance only after receiving respective consent from subscriber. In case subscriber did not give the consent, operator should postpone services (paragraph 26); and
(ii) potentially it will not be allowed to operators to allow debt of subscribers in roaming (which contradicts to the Rules).

The violations of new rules can be recognized as an abuse of dominant position that entails a penalty of 5% of the total income of the Group or 10% in case if repeated within a year with monopoly revenue confiscation.

Management is currently assessing the risks associated with the introduction of new rules in order to comply with the amendments and additions to the 'Rules for the Provision of Communication services'.

Order N° 91 of the Committee of the National Security dated 20 December 2016 on approval of Technical Regulations 'General requirements to the telecommunication equipment in ensuring conducting of operative search measures, collection and storage of subscribers' information' was published on 7 February 2017 and came into force on 8 February 2018. According to the new regulations, there are additional requirements to the telecommunication equipment that include expansion of technical capabilities of equipment to conduct operative search activities, collection and storage of subscribers' information (ORA). Management is currently implementing the action plan in order to comply with the requirements of Technical Regulations.

Notes to the Consolidated Financial Statements continued

(in thousand of Kazakhstani tenge, unless otherwise stated)

22. SUBSEQUENT EVENTS CONTINUED

On 16 January 2018, the Group undertook a bond placement on the Kazakhstan Stock Exchange, in which bonds to the value of KZT4.95 billion were placed with investors at a yield of 11.5%. This was the first placement in the programme which the Group had announced on 14 December 2017, aimed at expanding and diversifying the Group's funding sources, increasing the average term of Kcell's financial liabilities and decreasing its funding costs. The programme details are as follows:

Type of bonds:	**Unsecured coupon bonds**
Amount of bonds	30,000,000 (30 million) bonds
Nominal price of a bond	1,000 (one thousand) tenge
Total volume of the bond issue	30,000,000,000 (30 billion) tenge

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