

Focusing on the issues that matter

In defining our strategic priorities and the content of our corporate reports, we analyse the matters that are most important to the company, our value-creation processes and our stakeholders.

Continuous monitoring of our operational, financial and social activities, along with the identification of interrelated and significant material matters, gives us a better view of the impact that our business has on the world around us, and of how our future value creation may be impacted by our stakeholders.

TO DEFINE MATERIALITY IN 2018, WE:

1

Surveyed key company employees regarding the importance and priority of the relevant matters defined in 2017 for the year 2018, and added other matters they considered significant.

2

Surveyed external stakeholders regarding the importance and priority of these matters, and added other matters they considered significant.

3

Updated our Materiality Matrix based on internal and external surveys.

4

Prioritised material matters.

We define ‘material matters’ as those which are significant to the company’s value creation potential, and those which are important to our key stakeholders.

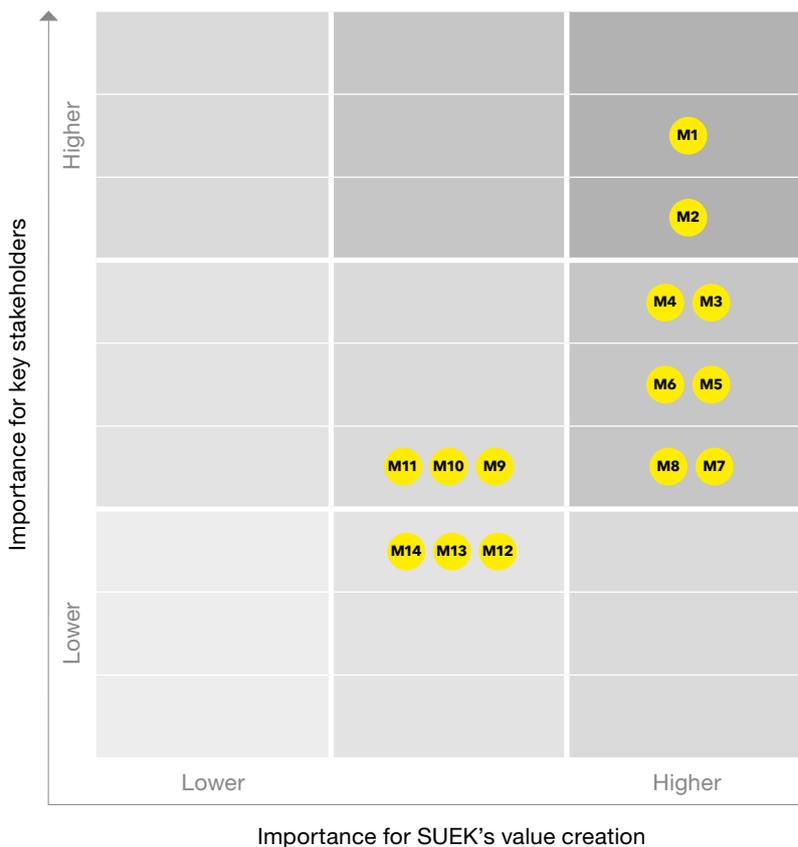
In preparing our 2018 Annual Report, we conducted a thorough analysis of the external and internal environment, carried out surveys among our employees, and interacted with a number of external

stakeholders to expand the survey scope due to the energy business consolidation. Through this process, we identified relevant matters which we believe are important for the growth, success and sustainability of our business, such as reputation, financial performance, delivery of strategy and licence to operate.

The updated Materiality Matrix was used to assess the company’s long-term goals and strategic priorities, as well as develop this Report.

In total, we identified 14 key issues, of which the first six were deemed the most material for the year:

MATERIALITY MATRIX 2018



Key material matters

- M1** Financial stability and development prospects
- M2** Product quality and high-value products
- M3** Industrial safety and emergency preparedness
- M4** Environmental impact of the company’s operations
- M5** Corporate governance and risk management
- M6** Operational efficiency

Other important matters

- M7** Fair remuneration and social support for employees
- M8** Human resources policy and labour relationships
- M9** Staff training, including training for new jobs
- M10** Contribution to urban infrastructure development
- M11** Development of local communities
- M12** Clear specifications and requirements for suppliers and support for local suppliers
- M13** Mutual adherence to business ethics
- M14** Company’s role in the development of mono-industry towns

Material issue	Context 2018	Impact on our value creation	How we responded
<p>M1</p> <p>Financial stability and development prospects</p>	<p>In 2018, the international debt market tightened sanctions against Russian companies due to geopolitical reasons.</p> <p>Restrictions on the financing of coal projects, imposed by a number of banks following the Paris Climate Change Agreement, continued.</p>	<p>Inability to finance our operating activities could adversely affect the company's operations and business as a whole. Limited diversification of our international debt portfolio and the necessity to attract higher-cost financing from Russian banks instead of coal-exiting European banks may impact SUEK's financial results.</p>	<p>The diversification of the international debt portfolio to include Chinese and Japanese banks helped SUEK to attract the necessary financing in the form of pre-export finance facility from a pool of international banks. Consolidation of the energy business diversified SUEK's cash flow decreasing EBITDA dependence on volatile global coal prices and ensured predictable and stable financial results, enabling the Group to upgrade its credit rating.</p>
<p>M2</p> <p>Product quality and high-value products</p>	<p>In 2018, the demand for high-CV coal remained at a consistently high level due to the growing number of new, high-efficiency coal-fired power plants consuming premium-quality coal, and because of tighter environmental standards. At the same time, the market experienced a shortage of coal with a calorific value of 6,000 kcal/kg, which led to a sharp rise in quotations and an increase in the price difference between low and high-CV coals.</p> <p>In Russia, the issue of the quality of heat energy supplies is becoming increasingly important for consumers. Due to increasing deterioration of heat networks, there are risks of interruptions in the supply of heat energy.</p>	<p>Stricter requirements from new coal-fired power stations and tighter domestic and international environmental standards of coal quality may result in a lower demand for lower-grade coal. This trend could influence the company's financial and operational performance.</p> <p>Accidents on heat networks and restrictions in the supply of heat reduce customer satisfaction with the quality of services.</p>	<p>We invest in the development of high-grade coal deposits and improve washing capacities to meet demand for higher-quality products from international markets. In 2018, SUEK increased its share of washed hard coal to 59% and began the construction of new washing plants in Buryatia and Khakassia.</p> <p>In the energy sector SUEK has developed, and proposed to local authorities, investment projects for the modernisation of heat supply systems in the cities where SUEK operates, which will significantly improve the quality of heat supply.</p>
<p>M3</p> <p>Industrial safety and emergency preparedness</p>	<p>Coal mining is associated with high production risks related to natural and man-triggered hazards, mining and geological factors, regularly changing working conditions and the human factor. Work at power plants and heat networks is also associated with high risks to human life and health.</p> <p>Despite all our efforts, in 2018 there were six fatal accidents at the company's facilities.</p>	<p>Industrial accidents and emergencies may potentially result in a number of tragic and adverse consequences: loss of life, direct property or environmental damage, temporary suspension of operations and, consequently, losses and fines, social unrest, or damage to business reputation. They may encourage partners to discontinue business relationships or lenders to demand early loan repayments.</p>	<p>We continued implementation of comprehensive programmes improving the level of industrial and labour safety, introducing the best international practices. We thoroughly investigated all accidents and incidents, analysed their causes and took actions to prevent their re-occurrence in the future, and reiterated our commitment to zero tolerance for accidents and breaches of safety requirements. The Lost Time Injury Frequency Rate (LTIFR) dropped to 0.75 for the mining and to 0.29 for the energy facilities. These figures are among the lowest for the coal and energy industries in Russia and abroad.</p>

Material issue	Context 2018	Impact on our value creation	How we responded
<p>M4</p> <p>Environmental impact of the company's operations</p>	<p>Environmental responsibility issues are becoming increasingly important for SUEK's product consumers, financial institutions and potential investors. Consolidation of the energy business brought additional attention to our environmental programmes from non-governmental, environmental, financial and other dedicated organisations.</p>	<p>In the event of environmental damage or degradation, there may be claims from supervisory bodies, as well as on the part of financial institutions and potential investors. These claims could, in turn, influence the company's production and financial performance indicators; negatively affecting our ability to raise funds through the debt market.</p>	<p>In 2018, SUEK continued the implementation of its Environmental Strategy adopted in 2017 and extended its effect on energy facilities. The fundamental principle of this strategy is to minimise our environmental impact by reducing harmful emissions and maximising the recycling of production waste.</p> <p>The company constantly monitors emissions at power plants. In 2018, an environmental programme was launched at Krasnoyarskaya CHPP-1 related to the modernisation and replacement of inefficient boilers. As in the Coal Segment, the company seeks to recycle waste and, in 2018, ash and sludge waste and from power generation began to be transformed into materials for land reclamation and construction.</p> <p>SUEK increased investment in environmental protection by 144% year-on-year.</p> <p>The company also raised coal washing rates, thereby reducing the environmental impact of our products during their transportation and use.</p> <p>The company's coal assets were certified for compliance with the requirements of the Bettercoal Code.</p>
<p>M5</p> <p>Corporate governance and risk management</p>	<p>Our key stakeholders in Russia and abroad have traditionally paid much attention to transparency, corporate governance and risk management.</p> <p>Energy business consolidation posed new integration challenges that can ensure sustainable corporate governance, including risk management.</p>	<p>Lack of transparency in corporate governance and non-compliance with national regulations can lead to additional requests from state authorities, lenders and business partners. It can also impact the company's operations as claims to the company are increased.</p>	<p>We strive to consistently develop our corporate governance, relying on the best Russian and global practices.</p> <p>The consolidation of the coal and energy businesses allowed the management of the integrated company to aggregate the best practices of both entities in various areas of management, risk management and internal control, and to extend them to the entire Group.</p>
<p>M6</p> <p>Operational efficiency</p>	<p>SUEK continued to focus on production efficiency and cost optimisation in order to maintain profitability and competitiveness in the global market.</p> <p>Furthermore, tighter environmental regulations following the Paris Agreement and an increase in the number of HELE coal-fired stations have increased demand for higher-quality coal.</p>	<p>Inefficient production processes can increase costs and decrease product quality, consequently diminishing the company's competitive advantages.</p>	<p>SUEK carries out modernisation programmes, substituting outdated equipment at mining and washing facilities and ports with more efficient and innovative items.</p> <p>We achieved record coal production levels of 110.4 Mt.</p> <p>The consolidation of the coal and energy businesses made it possible to improve the Group's operational efficiency, tighten control over all stages of the operational cycle, optimise utilisation rates at mining facilities and fuel supplies to generating companies and refine administrative functions within the consolidated company. As a result, the company's EBITDA margin remained at the target level.</p>