

Strengthening our position as a leader

“ In 2014, we continued to demonstrate marked progress in the implementation of our strategic objectives, despite the difficult economic and market environment. We are consistently strengthening our position as a leader of the Russian coal mining industry and one of the leading players in international coal markets. ”

ANDREY MELNICHENKO
CHAIRMAN OF THE BOARD
OF DIRECTORS, JSC SUEK



Leader of the coal industry

The coal mining industry experienced a difficult year in 2014. The sharp drop in global coal prices due to excessive supply in several key markets was exacerbated by deterioration in the Russian economic climate and increased geopolitical tension. Nonetheless, our position as the largest coal producer in Russia and supplier in both Russian and international markets remains strong. As a result of recent investment in the modernisation of our production assets and logistics chain and an extensive programme to improve operational efficiency, we continue to show sustainable growth in key operational indicators and to follow the same growth strategy.

In 2014, we produced 2.4 million tonnes (+2%) more coal than in 2013. A number of our mines in Kuzbass, Khakasia and eastern Siberia achieved extraordinary results in terms of productivity and efficiency of operations.

In 2014, we managed to further strengthen our position in the global coal market – our international sales increased by 8% to 45.6 million tonnes, which is about 5% of total internationally traded thermal coal. The Group consistently ranks among the top ten global coal mining companies in terms of coal reserves and amongst the six largest international coal exporters.

Growth strategy

Our central strategy provides a firm basis for growth and for sustainable long-term competitiveness based on efficient, vertically integrated coal production, transportation and sales.

We have been systematically building direct relationships with important customers in our target markets, as evidenced by the expansion of our sales network. Since demand for our coal continues to grow, mainly in the Asia-Pacific region, we are focused on developing relationships with customers in these markets. At the same time, we intend to retain our position as the preferred supplier for our clients in Russia and Europe. Our competitive position in the international market was boosted at the end of 2014 as the Russian Rouble's exchange rate weakened.

The strategy for achieving our growth objectives in target international markets includes large-scale projects to increase coal production in regions situated closer to Asian markets. In particular, we are expanding production from the Urgal deposit in Khabarovsk region and from the Apsatsky open pit in north Zabaikalye. At the same time, we are modernising and enlarging our production facilities in Kuzbass, Khakasia, Buryatia and at Zabaikalye. Our investment programme and comprehensive set of measures to improve operational efficiency at our production units should ensure we maintain high productivity levels while continuing to achieve one of the lowest production costs within the coal mining industry in Russia.

Of special note is our programme for developing coal processing capabilities, which has enabled an increase in coal washing capacity from 28.1 to 32.1 million tonnes. We aim to increase this capacity by further development of washing plants at Urgal, Buryatia and Kuzbass.

An important aspect of our strategy is building optimal logistic chains and developing our own transport infrastructure. We have been steadily increasing coal shipments through Vanino Bulk Terminal and Murmansk Commercial Seaport. In 2014, both ports achieved the highest performance in their history based on their statistics, and our shipments through these ports are expected to increase further. At the same time, we are working to increase the capacity of our own rail infrastructure which provides us entry to the national Russian rail network.

One of the top priorities within our strategy is to achieve further progress in safety. The large-scale integrated programme we have been running for several years, including investment in emergency response provision, modern safety equipment and organisational and motivational measures, has allowed us to reduce injury rates and the number of production-related accidents. Despite all these efforts, and to our deepest regret, we had eight fatal accidents in 2014. The causes and details of each accident have been studied closely and discussed at all management levels – from meetings of mine personnel to Board members. In each case we have developed a specific action list to prevent similar accidents occurring, and we are implementing broader programmes to change behaviour and reduce risk taking throughout the workforce. We intend to reduce the number of fatal and severe injuries to zero.

Our approach to sustainable development

A major focus for the Board and the management team is sustainable development and corporate social responsibility. In this regard, we play a crucial social role in the cities and towns where our production units operate. We also seek to improve the environment and quality of life in these areas. Many of these are single-industry towns so our role is of major importance to the community.

We actively engage with the regional governments, municipal authorities and local communities to help create high-quality, modern social environments for our employees and their families. Dozens of social programmes and projects financed by the 'SUEK to the Regions' fund support this goal. The effectiveness and importance of our social and charitable work, even in a tough economic climate, was reflected in the multiple awards and top rankings for corporate social responsibility received in 2014.

Prospects

The difficult economic environment and poor global coal market conditions may persist in the medium term. The surplus of coal production and transport capacity in the major coal-exporting countries, compounded by weakening of demand, has resulted in increased competition between suppliers and the most significant drop in coal prices in recent years. Additional complications for coal mining companies in Russia include volatility in the financial markets, the geopolitical situation, and increased inflation of capital expenditure and operational costs.

Despite these headwinds, coal continues to be one of the most important energy sources and remains essential to the power industry. Global coal consumption continues to grow and new projects are being implemented to ensure coal usage is more efficient and friendlier to the environment. These are the fundamentals of the future cyclical growth of the coal market.

In these circumstances, it is crucial for us to continue to implement the main principles of our strategy by consistently fulfilling targets for increased production capacity, building long-term relationships with key customers, improving our management approaches and upgrading our employees' skills. We continue to commit ourselves to the most effective investment projects with the highest payback in areas such as production, processing and logistics, as well as improving our operational efficiency and safety. In addition, allowing for the challenges imposed by the current business environment, we are focused on ensuring sustainability of our cash flow and liquidity.

We have ambitious objectives. If we pursue them aggressively and systematically we will get through the current market situation intact and remain a global leader in the coal mining industry for the long term.

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