



2019 KT&G REPORT

SUSTAINABLE SEED FOR TOMORROW

ABOUT THIS REPORT

Report Overview

KT&G annually publishes KT&G Report to share its activities, performances, and plans for sustainable growth and healthy development. In this report of 2019, we thoroughly reviewed and reflected recommendations by ESG-related global initiatives to widely communicate with various stakeholders. Through the report, we will continue to transparently share our sustainability activities and performances of the key sustainability issues and strive for harmonious development of environmental and social aspects.

Reporting Period

This report is based on the fiscal year-end between January 1 and December 31, 2019. The quantitative data of the recent 3 years (2017 - 2019) were included to compare trends. Some significant activities and performances of sustainability management until the 2Q of 2020 were also added to secure timeliness.

Reporting Scope

Financial information in this report is based on the Korean International Financial Reporting Standards (K-IFRS). The scope of social and environmental information includes domestic operations such as KT&G Head Office, R&D Headquarters, Shintanjin Plant, Gwangju Plant, Youngju Plant, Cheonan Plant, Gimcheon Plant, and domestic sales sites. For any discrepancies, annotations were added.

Reporting Standard

Reporting contents were developed in accordance with the Core Options of the Global Reporting Initiative (GRI) Standards.

Third-party Assurance

This report was verified by an independent assurer to enhance content quality and data credibility. The Independent Assurance Statement can be found on pp. 104-105.

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KT&G will endeavor
to become an upright and
righteous company based on
the advanced governance
with managerial transparency.

Chairman, Board of Directors
Baek, Jong-Soo

백종수

MESSAGE FROM THE BOD CHAIRMAN

Dear respected stakeholders,

I would like to show my sincere gratitude to all stakeholders including shareholders, customers, and employees for your concerns and affection for KT&G.

The year 2019 was difficult both internally and externally due to continued global economic stagnation, industrial environment changes, intensified market competition, and unpredicted exogenous variables. Even in the fluctuating business environment, KT&G has strived to develop into an internationally recognized company and create sustainable social values based on the best governance in Korea.

Through the Governance Enhancement Project, we have substantialized operation of the board as a partner for discussing future-oriented corporate strategy and have established a basis for improving our governance from the Korea's best to world's best by building a global-level management infrastructure. As a result, in 2019, we have received the highest standard, A+, in the ESG evaluation by the Korea Corporate Governance Service (KCGS) for 2 consecutive years, as well as the 'Grand Prize' at the Governance Evaluation. KT&G will continue to strive for becoming an upright and righteous company based on the advanced governance with managerial transparency.

KT&G's board of directors and employees believe that the company's sustainable growth can be achieved when the sharing value of shared growth is created in harmony with society and environment. As a global corporate citizen, we communicate transparently with stakeholders to cultivate sustainable and healthy business competitiveness, beyond creating economic values. Moreover, we will do our best to make the best decisions for our stakeholders including the company, shareholders, customers, suppliers, local community, and environment, with fair decision making of the board and responsibilities of the executive management.

KT&G has continued to grow by overcoming numerous crises during its history of 137 years. I ask you to kindly provide continuous concerns and supports on efforts and performances that KT&G will create in the challenging environment.



For sustainable growth into
a internationally recognized company,
KT&G strives to maximize
non-financial values of environment,
society, and governance, as well as
financial values.

CEO
Baek, Bok-In

A handwritten signature in orange ink, appearing to read 'Baek', located to the right of the CEO's name.

MESSAGE FROM THE CEO

Dear valued stakeholders,

It is genuinely regrettable that the society is going through chaos and difficulties due to the COVID-19 pandemic and prolonged stagnation in the global economy. As a corporate citizen that shares with the society, KT&G is actively engaged nationwide efforts to prevent spread of COVID-19 and will continue to actively contribute to global recovery from the crisis, thereby fulfilling social responsibility.

■ Continuously Strengthening Business Competitiveness and Systematizing Risk Management

In the difficult business environment last year, KT&G has strived to grow into an internationally recognized company based on relentless changes, innovation, and sustainability by strengthening competitive edges of main businesses and internalizing business areas with growth potential. We are enhancing competitiveness and growth potential by strengthening a balanced business portfolio between the Combustible Tobacco Product Business and Next Generation Product Business which is a new leading platform in the future market. At the same time, we are expanding our business scope into various areas including health functional food, biopharmaceuticals, and real estate that are future growth engines.

In particular, we have established infrastructure for global business by sophisticating the Business Management System for systematizing preliminary risk management. We have strengthened transparency and expertise by realizing the advanced internal control function and expanded the Controller System for efficient management of the overseas business. As a result, in 2019, we accomplished growth in both sales and operating profit from the previous year, even in the difficulties such as contraction of the global tobacco market size and intensified regulations. KT&G will continuously fortify its profit basis in the main businesses and actively cultivate developing businesses to cope with the uncertainty in the future and to turn risks into opportunities.

■ Company that Grows Together with the Society

KT&G actively promotes social responsibility activities for sustainable shared growth of the company and society. We have expanded the scope of Social Responsibility Management to all suppliers and offer various systematic assistances to create a healthy industrial ecosystem and secure sustainable competitiveness. In addition, we have complied with various principles required by the international society in the areas such as human rights, safety, and compliance, and we also have established the management system fulfilling the global standard. Through unique social contribution activities including the Youth Startup Support and Cultural Contribution Activity, KT&G will expand its role to solving social issues through social contribution, beyond sharing performance with the society.

■ Actively Fulfilling Environmental Responsibility for the Future Generation

KT&G acknowledges its environmental responsibility, and thus actively participates in the climate change response which is expected by the international society. According to the company-wide Environmental Management System, we practice the Eco-friendly Management and strive to secure health of the ecosystem for the future generation. KT&G will minimize its management's environmental impacts by transparently sharing and actively communicating its environmental responsibilities with various stakeholders.

To achieve sustainable growth as a internationally recognized company, KT&G endeavors to maximize non-financial values of environment, society, and governance, along with the financial value. KT&G will communicate with internal and external customers vigorously, share with the local community, and achieve sustainable growth, for sustainable growth.

RESPONSE TO COVID-19

KT&G, Overcoming COVID-19 Together with Society

The Coronavirus Disease (COVID-19) pandemic that broke out at the end of 2019 has made enormous impacts on safety and health of all human beings, as well as on the global economy. COVID-19 is a huge risk globally, and every area of the world is striving to find means to relieve the pandemic. KT&G, under its corporate philosophy of 'Together Company', is actively engaging in recovery from economic and health crisis caused by the protracting COVID-19. In the sustainability perspective, KT&G plans to provide physical and mental supports to the vulnerable social group and society and we allocated KRW 4.1B to do so. Based on the plan, we are reorganizing directions of social contribution activities to focus on resolving the COVID-19 issue and performing various supporting activities.



*Sig-gu Campaign: 'Sig' means 'eat', 'gu' means 'buy', and 'siggu' means 'family'. Thus, 'Sig-gu' campaign means that all members of society eat and buy products of self-employed and farmers and overcome COVID-19 together like a family.

Minimizing Business Impact

KT&G analyzed the impact of COVID-19 on the overall business to minimize it. We examined from materials sourcing, manufacturing, sales, and demand changes of domestic/overseas consumers for the Tobacco Business, and for the Real Estate Business and Health Functional Food Business, we developed response plans to flexibly cope with high volatility in the market. KT&G will continue to strive to build a foundation for sustainable growth and win the trust of stakeholders by creating opportunities and creating higher levels of value through overcoming crises.

Response System for Preventing and Suppressing COVID-19 within the Company

KT&G prioritizes health and safety of its employees and is, therefore, striving to develop plans to prevent possible infections from COVID-19 among them. We established the Status Reporting System and preventive plans, and the Chief of the Management Support Headquarters is in charge of the overall response activities. We held labor-management agreements 3 times to develop plans for protecting our employees' health and maintaining a stable managerial environment. Furthermore, we established a guideline for preventing infections and created the Corporate Culture Improvement Action Guide (The 5 Codes for 'Daily Disinfection Execution') through the idea contest, thereby enhancing employees' interest.

Flextime and Work-at-Home

- Flexible working hours: Autonomous selection of the get-to-work time between 6 am and 1 pm / 8-hour working hours
- Alternative holiday: Taking paid leave in return for working on holidays
- Selective working hours: Autonomous implementation by application and advisor's approval
- Work-at-home: Autonomous implementation after advisor's approval / Worktime selection between 6 am and 10 pm with work record submission
- Mandatory work-at-home for all pregnant employees
- Recommended work-at-home, leave, and family care leave for those who need childcare due to extended school closures

COVID-19 Medical Costs Assistance

- Full support, including diagnostic test costs
- Paid sick leaves provided for those who need time for treatment or quarantines after diagnosis

Overseas Visitors

- Recommendations for avoiding overseas travels or business trips
- Work-at-home or sick leave up to 14 days given to overseas business travelers
- Personal leaves up to 14 days recommended to overseas leisure travelers

Disinfection supplies
provision to
all employees
(masks and hand
sanitizers)

Regular company-wide
disinfection

Ginseng products
provision to
all workers in Dae-
gu-Gyeongbuk region

'Daily Disinfection Execution' Idea Contest
The 5 Codes for 'Daily Disinfection Execution'

‘코로나19’ 생활방역* 실천 아이디어 공모전
함께 극복해요 KT&G

공모 주제
· 코로나19 관련 감염 예방을 위한 생활 속 작은 아이디어
· 코로나19 관련 활력을 불어 넣을 수 있는 상생 아이디어
· 코로나19 관련 임직원에게 심리적 안정을 줄 수 있는 아이디어

공모 기간 2020.04.08 ~ 2020.04.17 [당첨자발표: 4.22(수)]

공모 방법 별도 양식 없이 댓글이나 이메일로 응모

포상 내역 참가자 중 5명 선정하여 20만원씩 증정

응모/문의처 안전관리실 김지혜 (내선1506/e-mail:20190097@ktmg.com)

* 생활방역이란 코로나19가 확산되거나 백신과 치료제가 나올 때까지, 현재는 생강에서 일한 생활방역을 바이러스 감염을 방지하는 생활방식으로 바꿔야 하는 것을 말한다

코로나-19 장기화에 따른 ‘생활방역 실천’ 5대 수칙

- 1. ‘업무환경 개선’ 알람서기**
업무공간, 회의·요청 장소 개인차와 분리하기
재택근무·화상회의시스템 적극 활용하기
손씻기 생활화를 위한 시·공간적 여건 보장하기
- 2. ‘사회적 거리두기’ 생활화**
폐쇄된 공간, 혼잡한 다중시설 이용 금지
일과 후 피싱, 모임 자제하기
유증상자, 자가격리 중환자 휴식하고 3~4일간 관찰하기
- 3. ‘초조는 물에 손씻기’ 생활화**
물과 손 씻기는 물에 손씻기
식사 직전 초조는 물에 손씻기
화장실 가는 전후 초조는 물에 손씻기
- 4. ‘마스크 착용’ 생활화**
회의 또는 다중이용시설 마스크 착용하기
엘리베이터 등 밀폐된 공간에서 마스크 착용하기
시장, 회의실, 휴게실, 엘리베이터 등 이용시에는 마스크 착용하기
- 5. ‘코로나 불확’ 극복하기**
일과후 산책, 독서, 휴식 등 취미생활 즐기기
전화, SNS 등으로 가족이나 친구들끼리 자주 소통하기
긍정적인 소통과 응원할 수 있는 취미하기

KT&G

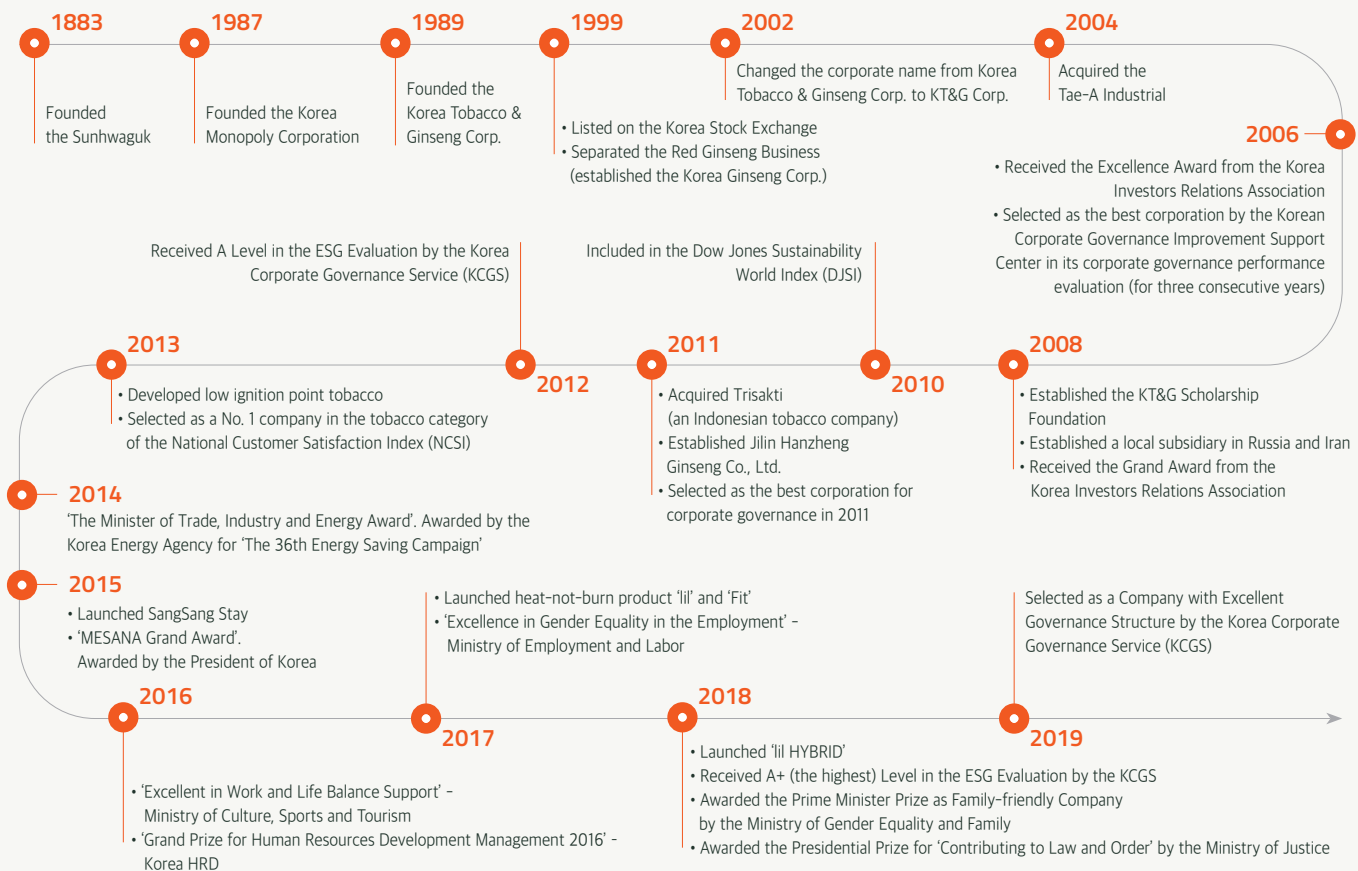
KT&G AT A GLANCE

COMPANY OVERVIEW

KT&G pursues 'Making a Better Life Together' with the society and is growing into a internationally recognized company by making changes and innovation. Based on the corporate philosophy, 'Exemplary', 'Progressive', and 'Together' company, we are creating social values and expanding sustainability activities. In addition to strengthening the global competitiveness of our major Tobacco Business, we are generating performances in various business areas including Next-generation Tobacco, Health Functional Food, Biopharmaceuticals, and Real Estate.

Company Name	KT&G Corporation
Foundation Date	April 1, 1987
Address	71, Beotkkot-gil, Daedeok-gu, Daejeon, Republic of Korea
Main Business	Manufacturing and distribution of tobacco products
CEO	Baek, Bok-In
No. of Employees	4,623 (as of Dec. 31, 2019, including contract-based employees)
Major Subsidiaries in Korea	Korea Ginseng Corporation, Tae-A Industrial, KGC Yebon, KGC Life & Gin, COSMOCOS, Yungjin Pharmaceutical, SangSang Stay
Website	http://www.ktng.com

COMPANY MILESTONES

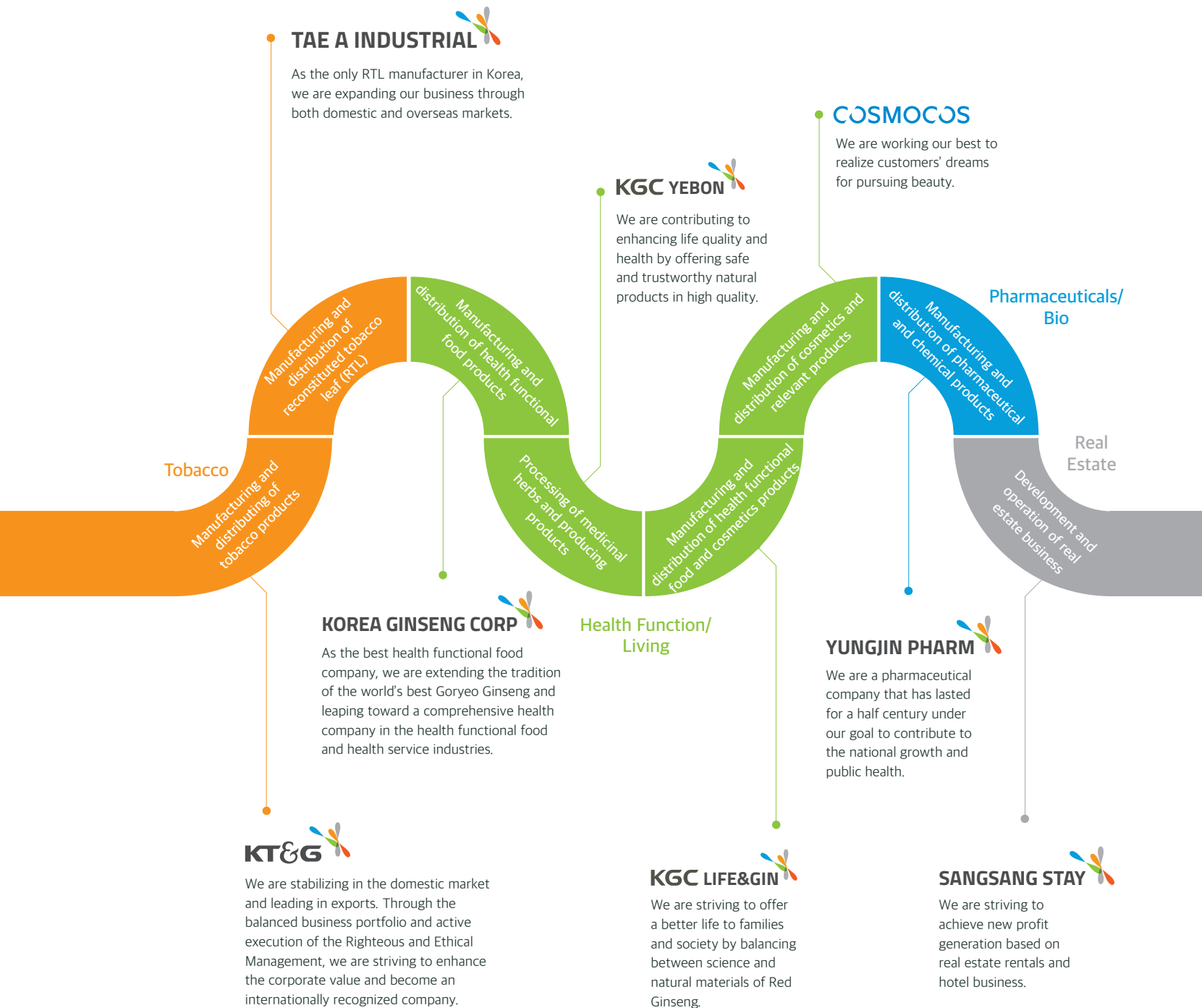


PORTFOLIO OVERVIEW

Business Areas

KT&G have developed new markets and achieved growth through the Tobacco and Health Functional Food Businesses. Moreover, we are expanding our business areas to Biopharmaceuticals, Health & Beauty, and Real Estate. We plan to fulfill our responsibility as a leader in the industrial ecosystem, broaden the global market areas, and grow continuously.

Business Portfolio & Key Subsidiaries



A full-page background image with an orange tint. It depicts a business meeting in progress. Several people are seated around a large conference table, which is highly reflective, showing clear reflections of the participants. In the background, a man stands and presents to the group. The overall atmosphere is professional and collaborative.

BUSINESS PERFORMANCE REVIEW

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GLOBAL BUSINESS OVERVIEW

Efforts and Directions for Global KT&G

Based on the quality-focused management and marketing expertise, KT&G has strengthened its market dominance in Korea and now is growing beyond the domestic market into a global tobacco company in the overseas market where competition among multinational companies are intensified. We operate local offices in various countries to supply products smoothly. We are also focusing on strengthening infrastructure and human resources (HR) capacities to grow ESSE as a global brand and develop big local brands in each market. Ultimately, KT&G plans to become a Top 4 tobacco company in the world and a global exporting company, thereby contributing to the national economy and job creation.

2020

Plan strategies for operating business models optimized for each market and expand new market countries

Establish Optimized Business Models by Nation & Explore Overseas Markets Actively

2021

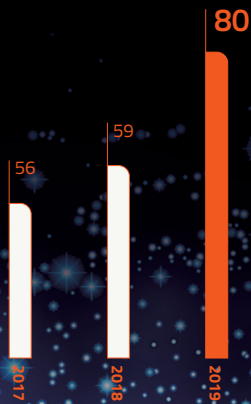
Cultivate new markets and sophisticate the business structure

2022

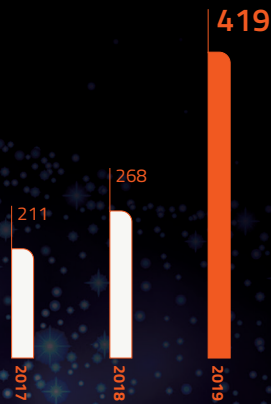
Develop overseas subsidiaries as a major player and expand the scale of organizations of each region

KT&G in the World

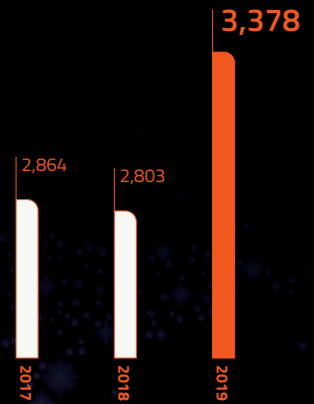
No. of Countries for Export (EA)



No. of Exported Brands (SKU*)



No. of Local Employees (persons)



*SKU: Stock Keeping Unit

Exports of ESSE
303.2
 billion sticks
 (Cumulative as of Mar. 2020)

Global performance
42.8
 billion sticks
 (in 2019)

Key Overseas Subsidiaries

- Nation: United States
- Founded in: Dec. 2004
- Main business: Distribution and wholesale of tobacco products
- Main brands: Carnival, TIME, THIS



- Nation: Indonesia
- Founded in: Feb. 2013
- Main business: Manufacturing and distribution of tobacco products
- Main brands: ESSE, BOHEM
- Annual production capacity: 10.2B cigarettes



- Nation: Russia
- Founded in: Jul. 2008
- Main business: Manufacturing and distribution of tobacco products
- Main brands: ESSE
- Annual capacity: 7.2B cigarettes



- Nation: Turkey
- Founded in: Dec. 2003
- Main business: Manufacturing and distribution of tobacco products
- Main brands: ESSE, THIS
- Annual capacity: 3.9B cigarettes

- Nation: Iran
- Founded in: Feb. 2009
- Main business: Distribution and wholesale of tobacco products
- Main brands: ESSE

FINANCIAL HIGHLIGHTS

Financial Statement Summary and Key Indicators

Consolidated				Separate			
(unit: KRW 100M)				(unit: KRW 100M)			
Items	2017	2018	2019	Items	2017	2018	2019
Current assets	65,857	64,134	64,172	Current assets	46,883	44,186	43,142
Cash and cash equivalents*	27,967	26,573	25,285	Cash and cash equivalents*	26,375	24,578	22,734
Accounts receivable and other receivables	11,243	9,759	10,234	Accounts receivable and other receivables	8,982	7,309	7,802
Inventory assets	23,178	24,613	24,472	Inventory assets	8,724	9,547	9,681
Other current assets	3,469	3,189	4,181	Other current assets	2,802	2,752	2,925
Fixed assets	33,957	37,417	42,949	Fixed assets	39,921	43,113	47,986
Property, plant, and equipment	17,753	18,188	17,534	Property, plant, and equipment	11,718	12,009	11,163
Investment properties	3,178	4,950	8,853	Investment properties	4,266	6,067	9,991
Other current assets	13,026	14,279	16,562	Other current assets	23,937	25,037	26,832
Total assets	99,814	101,551	107,121	Total assets	86,804	87,299	91,128
Current liabilities	18,164	16,407	16,001	Current liabilities	14,565	12,890	12,515
Fixed liabilities	3,352	3,813	4,061	Fixed liabilities	804	757	812
Total liabilities	21,516	20,220	20,062	Total liabilities	15,369	13,647	13,327
Total equity	78,298	81,331	87,059	Total equity	71,436	73,652	77,801
Current ratio (%)	362.57	390.89	401.05	Current ratio (%)	321.89	342.79	344.72
Debt-to-equity ratio (%)	27.48	24.86	23.04	Debt-to-equity ratio (%)	21.51	18.53	17.13
*Cash and cash equivalents, other financial assets, and fair value through profit or loss during the term				*Cash and cash equivalents, other financial assets, and fair value through profit or loss during the term			

Total equity (KRW 100M)

2017

99,814

2018

101,551

2019

107,121

Current ratio (%)

2017

362.57

2018

390.89

2019

401.05

Debt-to-equity ratio (%)

2017

27.48

2018

24.86

2019

23.04

Total equity (KRW 100M)			
2017		86,804	
2018		87,299	
2019		91,128	
Current ratio (%)			
2017		321.89	
2018		342.79	
2019		344.72	
Debt-to-equity ratio (%)			
2017		21.51	
2018		18.53	
2019		17.13	

Income Statement Summary and Key Indicators

Consolidated (unit: KRW 100M)				Separate (unit: KRW 100M)			
Items	2017	2018	2019	Items	2017	2018	2019
Sales	46,672	44,715	49,632	Sales	30,001	26,246	29,426
Cost of goods sold	19,089	18,360	20,886	Cost of goods sold	10,986	9,774	11,321
Gross profit	27,583	26,355	28,746	Gross profit	19,015	16,473	18,105
Selling and administrative expenses	13,322	13,804	14,926	Selling and administrative expenses	6,567	6,428	6,759
Operating profit	14,261	12,551	13,820	Operating profit	12,448	10,044	11,346
Other income (expense)	-1,277	-303	-38	Other income (expense)	-1,235	-77	27
Finance income (costs)	415	846	829	Finance income (costs)	1,175	1,472	883
Profit before income tax	13,456	13,187	14,627	Profit before income tax	12,389	11,439	12,255
Income tax	1,814	4,200	4,240	Income tax	2,640	3,030	3,342
Net income	11,642	8,987	10,387	Net income	9,749	8,409	8,914
Other comprehensive income	474	-447	195	Other comprehensive income	443	-471	56
Total comprehensive income	12,116	8,539	10,581	Total comprehensive income	10,192	7,939	8,970
Gross profit ratio (%)	59.10	58.94	57.92	Gross profit ratio (%)	63.38	62.76	61.53
Operating profit margin (%)	30.56	28.07	27.85	Operating profit margin (%)	41.49	38.27	38.56
Net income ratio (%)	24.94	20.10	20.93	Net income ratio (%)	32.50	32.04	30.29

Sales (KRW 100M)		
2017	<div></div>	46,672
2018	<div></div>	44,715
2019	<div></div>	49,632

Operating profit (KRW 100M)		
2017	<div></div>	14,261
2018	<div></div>	12,551
2019	<div></div>	13,820

Net income (KRW 100M)		
2017	<div></div>	11,642
2018	<div></div>	8,987
2019	<div></div>	10,387

Sales (KRW 100M)		
2017	<div></div>	30,001
2018	<div></div>	26,246
2019	<div></div>	29,426

Operating profit (KRW 100M)		
2017	<div></div>	12,448
2018	<div></div>	10,044
2019	<div></div>	11,346

Net income (KRW 100M)		
2017	<div></div>	9,749
2018	<div></div>	8,409
2019	<div></div>	8,914

Cash Flow Statement

Consolidated (unit: KRW 100M)				Separate (unit: KRW 100M)			
Items	2017	2018	2019	Items	2017	2018	2019
Cash flow from operating activities	11,431	8,217	10,425	Cash flow from operating activities	11,052	6,583	7,702
Cash generated from operating activities	15,381	11,619	14,641	Cash generated from operating activities	14,449	9,424	11,222
Income taxes paid	-3,950	-3,402	-4,216	Income taxes paid	-3,397	-2,841	-3,521
Cash flow from investing activities	-6,830	-463	-4,592	Cash flow from investing activities	-5,889	55	-3,493
Current asset earnings	-3,183	-3,533	-2,222	Current asset earnings	-2,474	-3,037	-1,676
Other cash flow from investing activities	-3,647	3,070	-2,370	Other cash flow from investing activities	-3,415	3,092	-1,817
Cash flow from financing activities	-4,386	-5,494	-6,321	Cash flow from financing activities	-4,546	-5,051	-5,111
Dividends paid	-4,546	-5,051	-5,051	Dividends paid	-4,546	-5,051	-5,051
Other cash flow from financing activities	160	-443	-1,270	Other cash flow from financing activities	0	0	-60
Net change in cash and cash equivalents	247	2,179	-417	Net change in cash and cash equivalents	614	1,584	-913
Beginning cash and cash equivalents	6,904	7,151	9,330	Beginning cash and cash equivalents	5,284	5,898	7,481
Year-end cash and cash equivalents	7,151	9,330	8,913	Year-end cash and cash equivalents	5,898	7,481	6,568

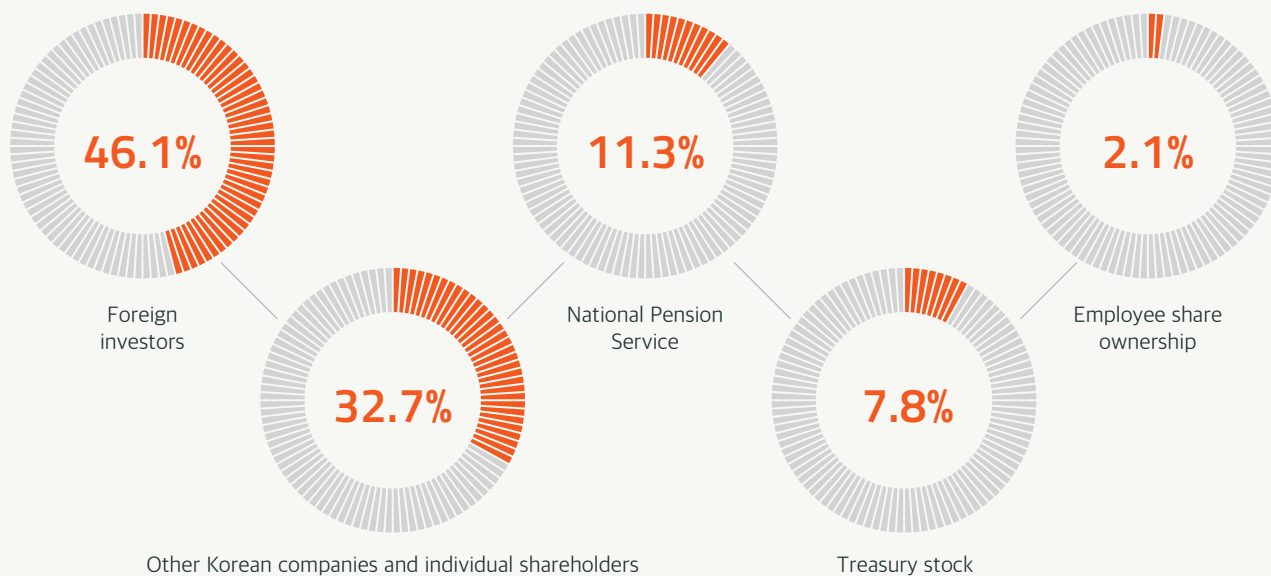
Other Financial Indices

Consolidated				Separate			
(unit: %)				(unit: %)			
Items	2017	2018	2019	Items	2017	2018	2019
ROA	11.7	8.8	9.7	ROA	11.2	9.6	9.8
ROE	14.9	11.0	11.9	ROE	13.6	11.4	11.5
Earnings per share (KRW)	9,217	7,141	8,208	Earnings per share (KRW)	7,721	6,660	7,059
ROA (%)				ROA (%)			
2017			11.7	2017			11.2
2018			8.8	2018			9.6
2019			9.7	2019			9.8
ROE (%)				ROE (%)			
2017			14.9	2017			13.6
2018			11.0	2018			11.4
2019			11.9	2019			11.5
Earnings per share (KRW)				Earnings per share (KRW)			
2017			9,217	2017			7,721
2018			7,141	2018			6,660
2019			8,208	2019			7,059

Investment Information

Shareholders Structure

(unit: %)



*As of Dec. 31, 2019

Voting Rights Status (Common Shares)

Category	No. of shares
No. of issued shares	137,292,497
No. of non-voting shares (Treasury stock)	10,712,574
No. of voting shares	126,579,923

*As of Dec. 31, 2019

Cash Dividends Paid

Total dividends (KRW 1M)

2017	505,061
2018	505,061
2019	556,952

Consolidated payout ratio (%)

2017	43.4
2018	56.0
2019	53.7

Cash dividends yield ratio (%)

2017	3.3
2018	3.7
2019	4.5

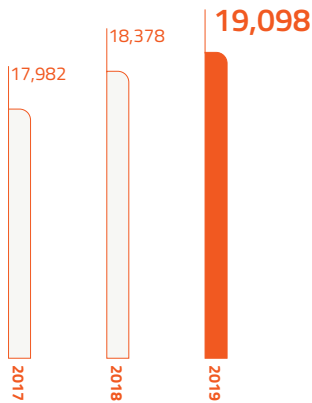
Dividends per share (KRW)

2017	4,000
2018	4,000
2019	4,400

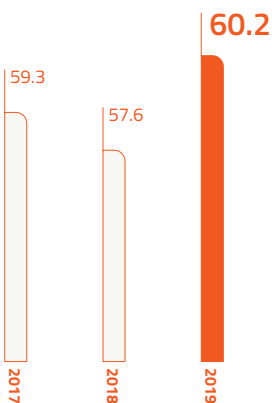
DOMESTIC TOBACCO BUSINESS

Including NGP (Next Generation Product)

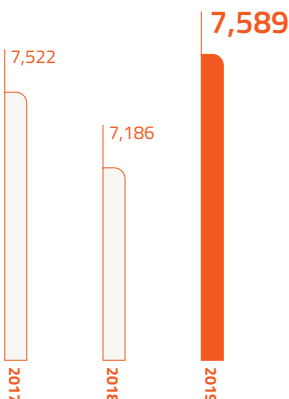
Domestic Sales of Tobacco Products
(KRW 100M)



Domestic Tobacco Market Share (%)



Domestic Operating Profits of Tobacco
Products (KRW 100M)



MARKET TREND

The tobacco industry requires a capacity for large-scale facility operations and nation-wide distribution network for managing materials and manufacturing cigarettes. Due to the industrial nature, overall manufacturing and distribution are regulated stringently and affected significantly by external factors such as the economic condition. The Korean tobacco market experienced tobacco tax increase in 2015, introduction of graphic warnings in 2016, launch of heat-not-burn products in 2017, and reinforcement of graphic warnings in 2018, thus raising volatility.

2019 BUSINESS PERFORMANCE

The Domestic Tobacco Business Sector has launched [ESSE Change Himalaya], [RAISON French Cleo] to satisfy diversified consumer needs including less smell. Based on these efforts, we recorded a domestic combustible tobacco products market dominance of 63.5%, which is an increase by 1.5% point, thereby continuing growth in market share for 5 consecutive years. In particular, we are strengthening the market position of the 3 types of “Less Smell Functional Products (ESSE Change Himalaya, Raison Hyvaa, RAISON French Cleo)” by accomplishing about 3.3% of market share as of 2019 year-end. The Next Generation Product Headquarter launched the first hybrid type of the heat-not-burn product, “lil Hybrid”, in the early 2019. This enabled us not only to fortify our portfolio of the electronic cigarette, but also to lead innovation in the tobacco industry by offering various flavors and scents of products and recording accumulated sales of 500,000 lil Hybrid devices in 2019.

OUTLOOK

The tobacco business is undergoing a drastic change of paradigm due to the emerging innovative products. KT&G aims to strengthen its No.1 position in the domestic market through differentiated high-quality products. Moreover, we plan to secure global standard of business competitiveness by developing brands to fulfill consumer needs, improving quality of products, and cultivating global talents. Furthermore, we will concentrate on expanding our market share to cope with potential decrease in demands in the mid-to long-term perspective and continuously enhancing profitability by increasing high-profit products.



OVERSEAS TOBACCO BUSINESS

MARKET TREND

The overseas tobacco market is facing intensified oligopoly due to global competitors' new market entries and M&A of local companies. Moreover, the growth and competition of the next generation tobacco market are also aggravated. Preferences of global tobacco consumers are diversifying in flavor, shape, and design, and differentiated strategies for each market are demanded.

2019 BUSINESS PERFORMANCE

KT&G is responding to different tastes of global consumers by developing various special editions customized for local cultures including Kretek in Indonesia and slim or extra-slim products in Africa. In addition, we were able to generate overseas sales of KRW 843.5 billion (including exports of KRW 534.4 billion) in 2019 by performing active marketing activities and strengthening business competitiveness of the overseas operations. We also expanded exports from 59 countries in 2018 to 80 countries in 2019 that included about 400 brands (268 brands in 2018) and 42.8 billion cigarettes. This is a result of our efforts to enhance competitiveness based on the business strategy focused on product quality and the production capacity customized for local demands. Moreover, we are operating the Controller System for more efficient management of the overseas business and strengthened the financial transparency by realizing the advanced internal control function.

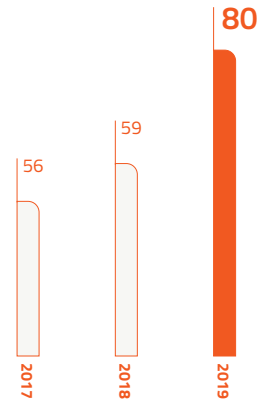
Indonesia is the 2nd largest tobacco market in the world. KT&G Indonesia initiated the localization of our signature brand, ESSE, in accordance with the high preference of Kretek in the market. Through this localization strategy, KT&G Indonesia continue to grow. The number of cigarette sales of Indonesia was increased from 4.9 billion in 2018 to 5.6 billion in 2019 (by 14%). KT&G USA restructured sales organizations and expanded the distribution coverage throughout the 6 regions of the United States. Therefore, we achieved sales of 4.1 billion cigarettes which is an increase by 64% from the previous year (2.5 billion cigarettes).

OUTLOOK

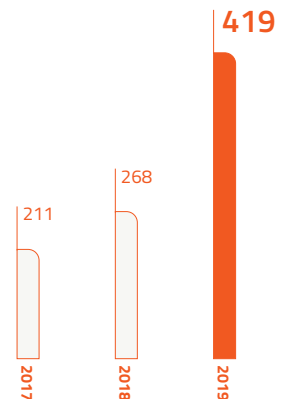
KT&G will strengthen its status as a global company by continuously expanding the overseas tobacco business. We will first focus on penetrating new markets with high potentials such as Africa, Central and South America, and Southeast Asia, and then we will move forward to other global markets. Moreover, we will enhance business competitiveness of overseas operations by expanding regional distribution and marketing and secure core technologies such as Virginia and Kretek that are required to capture local markets.

KT&G Indonesia will proactively develop and launch products that are differentiated in each brand and improve sales capacities by expanding sales organizations and personnel. KT&G USA will continue to enhance efficiency of organizations based on regional segmentation and local workforce and to expand wholesale and retail networks by systematizing the sales management. Lastly, assistance functions such as global HR and information technology (IT) will be provided to each operation to strengthen business competitiveness.

No. of Countries for Export (EA)

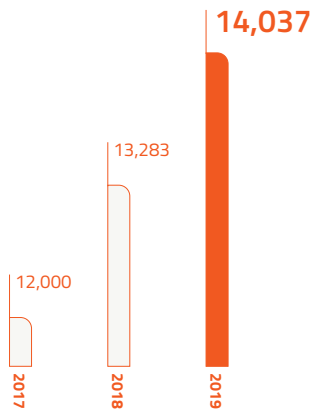


No. of Exported Brands (SKU)



HEALTH FUNCTIONAL FOOD BUSINESS

Sales of Health Functional Food (KRW 100M)



MARKET TREND

The Function Food Business is expected to grow continuously as consumers' concerns about health and well-being is growing due to the increasing life expectancy. The health functional food market recently has been led by non-Ginseng related health functional foods such as probiotics and vitamins.

2019 BUSINESS PERFORMANCE

KGC achieved sales of about KRW 1.4 trillion as of 2019 year-end with the outstanding product competitiveness even in the difficult market environment such as shrinking consumption. Based on the products produced from fresh ingredients procured from 6-year contract cultivation and cutting-edge manufacturing facilities with annual capacity of 8,000 tons, we are fortifying our dominance in the health functional food market. In 2019, KGC set a foundation for increasing consumption of non-Ginseng health functional food by nurturing the 2nd Mega Brands such as Cheon Nok, Good Base, and α Project. Moreover, the online mall for health functional foods, 'KGC Shop' started to offer products reflecting characteristics and lifestyles of different age groups through the O4O* service, and it exceeded KRW 50 billion in sales in 2019 by enhancing product quality in accordance with Cheong Kwan Jang's strict standards in health functional food and safe food.

*O4O: Online for offline

OUTLOOK

KGC plans to continuously generate demands for Red Ginseng as the World's No.1 Red Ginseng Company and foster the next generation products by focusing on non-Ginseng health functional food. By fortifying products sales customized for the major market, China through general health functional food, we will secure exporting competitiveness in the overseas market. Moreover, following the growing trend of untact consumption, we will strengthen operation of online malls and enhance the brand value of Cheong Kwan Jang globally. Based on successful online mall experiences in China, we will promote expansion in the global market. Through these efforts, Korea Ginseng Corporation (KGC) plans to become a global integrated health company in overall health functional food areas based on 110-year tradition and manufacturing expertise.



REAL ESTATE BUSINESS

MARKET TREND

Followed by the changes in generational structure and segmentation of cultures including the aging society and increasing one-person households, demand-focused development is becoming more material in the real estate business. In addition, the integrated real estate development combined with shopping and entertainment are becoming key competitiveness as lifestyle of consumers are diversifying.

2019 BUSINESS PERFORMANCE

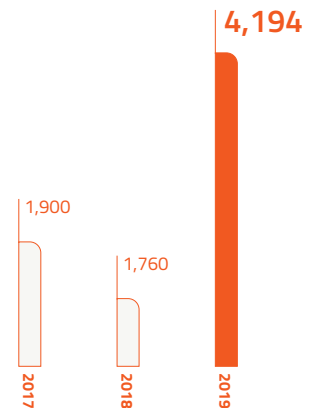
Even in the worsening market environment in 2019, KT&G recorded KRW 419.4 billion in sales, increased from KRW 243.5 billion in 2018. In the case of rental business, we accomplished 0.9% in vacancy rate, KRW 67.9 billion in sales, and KRW 17.9 billion in operating profits through active lease marketing, tenant CRM*, and cost reduction. We are also creating new demands such as the development and leasing of a premium shopping complex in Sejong City. In the Development Business, we generated the parcel-out sales of KRW 351.5 billion and operational profit of KRW 178 billion. In the Financial Investment sector, we are concentrating our resources on diversifying investment targets and identifying blue chips. With these efforts, we made KRW 17 billion of dividend income during the year from 2 new investments in offices in major cities overseas. In addition, we are assisting the Group's projects including the Youth Startup Support Center, building Busan SangSang Madang, and lil Service Centers.

*CRM: Customer Relationship Management

OUTLOOK

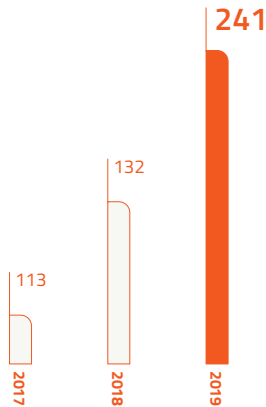
In the real estate market, instability is rising, and competition among companies are intensifying. Therefore, KT&G plans to operate business areas that can generate stable profits, including rental, real estate development, and real estate investment. In particular, we will establish balanced portfolios, sophisticate the business management process, and generate effective performance through the securing of cash flows and purchasing of tangible assets with high potentials in the Rental Business and the Building Operations Business.

Sales of Real Estates (KRW 100M)



COSMETICS BUSINESS

Sales of premium brand (Donginbi)
(KRW 100M)



MARKET TREND

The Cosmetics Business is sensitive to market changes in preferences and trends, and the life cycle of products is short, and the success of new products is very important, such as a business-wide crisis if it fails to keep up with changes in the market. The domestic cosmetics market is globally renowned, and K-Beauty is becoming popular as Hallyu (the Korean Wave) is highly recognized in various countries in the Middle East and Central and South America.

2019 BUSINESS PERFORMANCE

In alignment with the increasing global fame of K-Beauty, COSMOCOS is accelerating the overseas market entry by reinforcing its competence in the cosmetics area to grow into a global beauty company. Its outdoor dermocosmetic brand, 'VPROVE' launched products in 'Beautica' which is the biggest online beauty channel in Kuwait and 'Farmacias del Ahorro' which is the No.1 drug store in Mexico. Based on these results, we are promoting market expansion to the Middle East and Central and South America. In addition, we are also entering online shopping malls in Japan and China to expand our target markets. KGC's Donginbi brand launched products in Lounge 1899, department stores, and duty-free stores, thereby increasing customer contact points and recognition as a premium brand.

OUTLOOK

COSMOCOS plans to capture channels such as ODM* products and overseas markets using cosmetic product manufacturing technologies and expertise developed in the domestic market. We will utilize R&D and manufacturing capacities of COSMOCOS to continuously expand the ODM business following the market trends of diversified distribution channels and multi-product batch production. Furthermore, through Donginbi, KGC will strengthen brand image as a premium brand and offer solutions optimized for skin care needs of both domestic and overseas consumers.

*ODM: Original Development/Design Manufacturing. A manufacturer with design and development capacities providing products to sales companies with distribution networks.



PHARMACEUTICALS BUSINESS

MARKET TREND

The pharmaceuticals industry is a key contributor to enhancing 'health' and 'life quality' of the public. As the development of new medicines requires a vast amount of time and costs for sophisticated expertise and technologies, retaining the R&D pipeline* and infrastructure is the most important factor to secure industrial competitiveness. Moreover, the pharmaceuticals are regulated and managed more widely and delicately by the government to ensure safe production, quality management, and transparent distribution of products, as it is closely related to the national health. Recently, governmental policies and sales environment are rapidly changing, and the competition in the domestic market is intensifying.

*Pipeline: New drug project under development

2019 BUSINESS PERFORMANCE

In 2019, Pharmaceuticals Business achieved KRW 220.5 billion which is increased by 18.2% from the previous year. In the domestic market, we are focusing the sales of top 5 diseases (4 diseases + chronic diseases including circulatory system disease) and introduction of licensed products. In the overseas business, we are broadening new clients while fortifying the existing antibiotics business in Japan. Moreover, we are expanding businesses in CMO¹⁾ and CDMO²⁾ for entering markets in China and Southeast Asia. In the R&D sector, for strengthening differentiated competitiveness, we are implementing the technological transfer of 'YPL-001' which is a cure for chronic obstructive pulmonary disease (COPD) and completed the Phase 2a³⁾ clinical trial in the United States, along with the Phase 2b⁴⁾. Also, we are developing a targeted cancer drug, YPN-005, and an immunotherapy cancer drug, YPN-006, as the new task in the Anticancer sector.

Our Pharmaceuticals Business annually invests 10% of total sales in R&D and concentrates on developing new medicines such as rheumatoid arthritis treatment and next generation vaccines. In 2019, we successfully recertified for the 'innovative pharmaceutical company' for our R&D investment, innovativeness, overseas business capacities, social responsibility, and ethical standard. We will strive to become a global pharmaceuticals leader generating consistent outcomes based on core businesses.

1) CMO: Contract Manufacturing Organization

2) CDMO: Contract Development and Manufacturing Organization

3) 2a: One of the 2 clinical trial processes that checks the effect and effective dosage of medicines

4) 2b: One of the 2 clinical trial processes that verifies the effect, effective dosage, validity, and safety of medicines

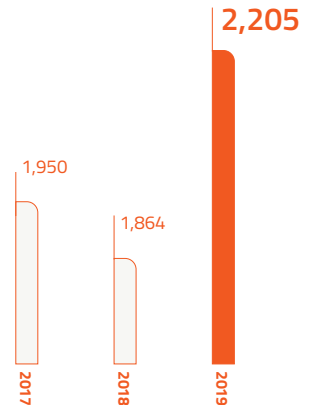
OUTLOOK

The Pharmaceuticals Business of KT&G will strengthen its product pipeline and enter new overseas markets including the United States and China by expanding in-licensing* and out-licensing** of popular products. In addition, we will develop products related to the 3 diseases (enteral nutrition, fever treatment/pain reliever/antiphlogistic/NSAIDs) to continue our growth in sales.

*In-licensing: The process of bringing in rights for technologies, substances, patents, and products from other companies

**Out-licensing: The process of granting rights for production and sales of products with technologies, know-hows, and intellectual properties to other companies

Sales of the Pharmaceuticals Business
(KRW 100M)





KT&G SUSTAINABILITY PERFORMANCE

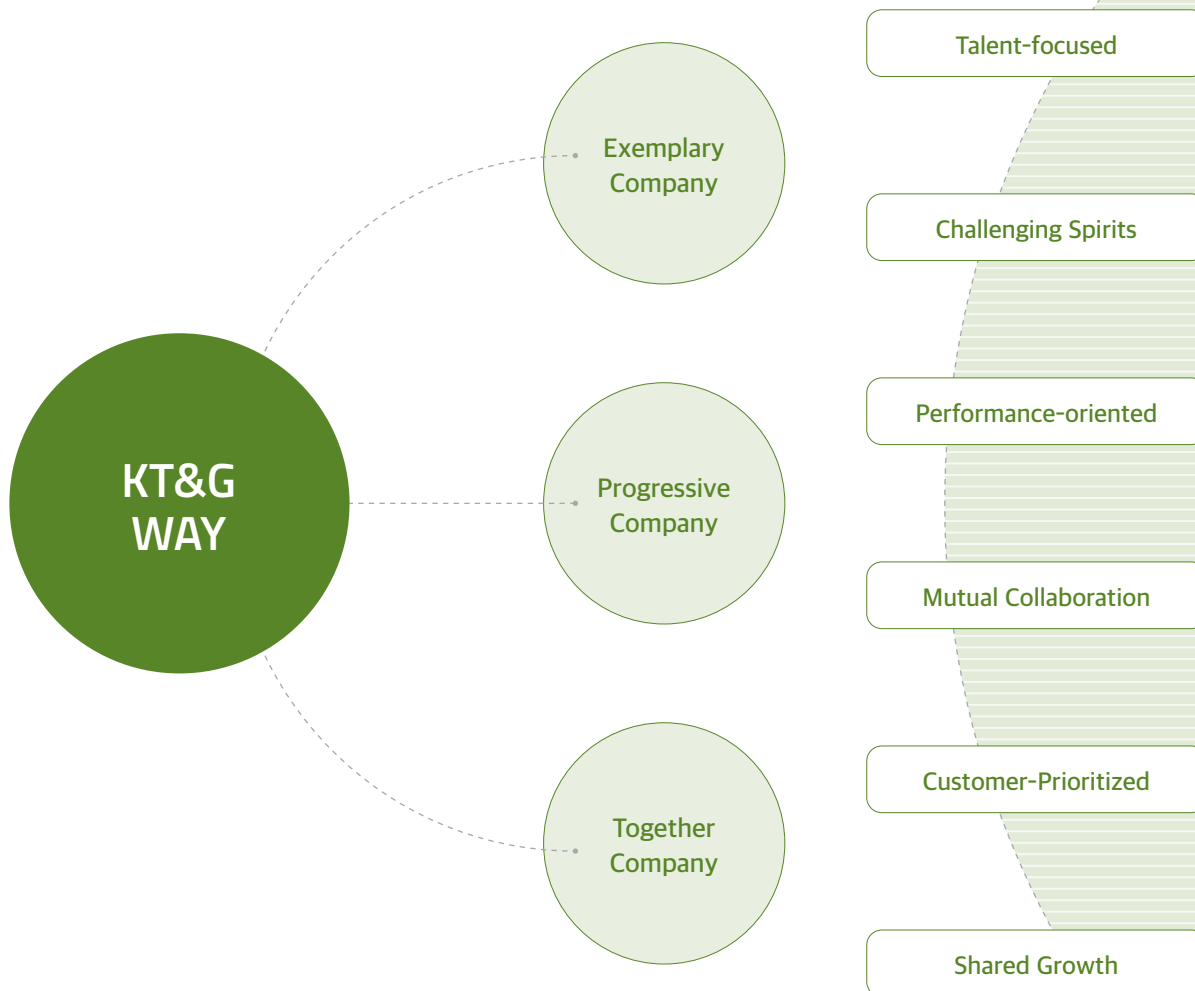
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GOVERNANCE. Advanced Governance to the Global Standard	66
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SUSTAINABILITY STRATEGY

Sustainability Commitment

KT&G endeavors to create a better life with various stakeholders.

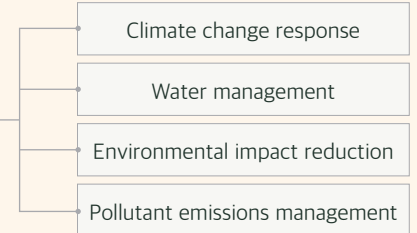
KT&G minimizes environmental impacts of its business and continues to take relentless challenges based on a sound governance to pursue a better life through embracement.





Environmental Responsibility for the Future

KT&G considers eco-friendliness from the product development phase to use phase to resolve environmental challenges faced by the world.



A Better Society through Embracement

KT&G constantly communicate with stakeholders to bring out positive changes in the society and performs shared growth to realize a better life.



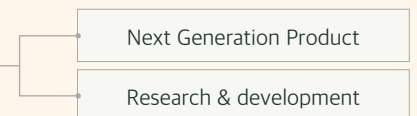
Advanced Governance to the Global Standard

KT&G enhances the corporate soundness through transparent governance and pursues a long-term, stable growth of all stakeholders by internalizing sustainability management.



New Market Creation through Innovation

KT&G strives to enhance market position by launching innovative products through relentless R&D and satisfy various customer needs.



KT&G 2019 SUSTAINABILITY PERFORMANCE

PERFORMANCE	APPROACH	2019 ACHIEVEMENT (QUANTITATIVE)
Environmental Responsibility for the Future	KT&G has established a company-wide environmental management system and operates a dedicated organization to faithfully implement it. The main areas of implementation are climate change response, water and waste management at worksites, reducing environmental impacts of products, and enhancing environmental awareness. We will endeavor to reduce environmental impacts, respond to relevant regulations, and recycle resources through continuous environmental investment to contribute to the circular economy. Furthermore, to proliferate the Environmental Management, we will intensify communication activities such as environmental training programs to enhance employees' awareness.	GHG emissions - 104,559tCO ₂ e _q Energy use efficiency - KRW 58M Environmental investment - KRW 561M New renewable energy power generation - 2,026,224kWh Water use reduction by repairing high-temperature water softeners - 4,730 tons Water consumption - 489,187 tons Recycled wastes - 1,283,506kg
A Better Society through Embracement	KT&G strives to analyze and respond to expectations of various stakeholders. We also try to create a safe and pleasant work environment for our employees and expect that all stakeholders can work in a sound industrial ecosystem. We are not only putting aggressive investment to satisfy product safety and liability which are the key to sustainability, but also establishing policies and system to enable partners who are the basis for business competitiveness to fulfill their social responsibilities. Moreover, we are conducting various support projects to growth with the local community.	Marketing training (Tobacco Business Act) - 128 persons Early payment to suppliers - KRW 45.9B Purchase amount from suppliers - KRW 745B Purchase amount of domestic leaf tobacco - KRW 96.5B Training hour per employee - 124 hours Training cost per employee - KRW 1.4M Labor union membership rate - 89.6% Training to future retirees - 96 persons Industrial accident rate - 0.062% VOC response rate(fourth quarter) - 98.6% No. of customer privacy breach - 0 case Social contribution investment - KRW 101B
Advanced Governance to the Global Standard	KT&G established the responsible managerial system centered on the board of directors controlled by outside directors and considers compliance with laws and ethical standards a top priority for all its businesses. We will strengthen schemes to maintain the governance that emphasizes balanced benefits of all shareholders and stakeholders. In addition, we will implement training and other programs for proactively responding to needs for compliance that are changing and becoming complicated.	Outside director attendance rate - 98.3% Rate of outside directors - 71% No. of compliance and ethics training - 26 cases No. of business-related legal reviews - 6,214 cases No. of employees participated to compliance and ethics offline training - 688 persons
New Market Creation through Innovation	KT&G is growing into a global tobacco manufacturer by developing innovative technologies and identifying new ideas. In particular, to respond to the next generation tobacco market actively, we are striving to conduct R&D in various areas such as materials, product planning, and manufacturing. KT&G will develop into the 'Global Top 4 Tobacco Company' by launching various products tailored for consumer preferences.	No. of NGP developers - 118 persons NGP sales - KRW 252.3B No. of NGP patents/trademarks/designs applied - 2,174 EA R&D investment - KRW 23.4B

2019 ACHIEVEMENT (QUALITATIVE)

SDGs

- | | |
|--------------------------------|--|
| Climate Change Response | <ul style="list-style-type: none"> Achieved energy efficiency through the introduction of high-efficiency and eco-friendly facilities Established the climate change response system Operated solar power generation facilities in Shintanjin Plant and Youngju Plant |
| Water Management | <ul style="list-style-type: none"> Reduced water use through high-temperature water softeners maintenance |
| Environmental Impact Reduction | <ul style="list-style-type: none"> Use of eco-friendly materials and reuse of resources |
| Pollutant Emissions Management | <ul style="list-style-type: none"> Established the integrated management platform for managing environmental laws and regulations Managed pollutants through monitoring system Expanded reusing of byproducts by recycling raw materials from manufacturing processes Promoted recycling through refinement of ethanol |



- | | |
|----------------------------|---|
| Product Safety and Quality | <ul style="list-style-type: none"> Conducted the safety management assessment of all chemical substances Conducted the preliminary safety assessment of all additives and materials Acquired and recertified ISO 9001 Shared the responsible marketing policy and trained employees |
| Supply Chain Partnership | <ul style="list-style-type: none"> Established the new supplier selection process that includes ESG evaluation Provided early payment to suppliers for their financial soundness Purchased all domestic tobacco leaves, raised fund, and performed support activities for tobacco farms |
| Better Work Place | <ul style="list-style-type: none"> Provided workplace harassment training to all employees Executed the 1·3·5 Campaign (5 promises to make our work and life happy) |
| Worksite Safety Health | <ul style="list-style-type: none"> Investigated harmful labor factors of muscular skeletal disease |
| Customer Satisfaction | <ul style="list-style-type: none"> Introduced the 'Visiting A/S' and 'Parcel A/S' to enhance accessibility to product A/S Introduced the trade-in purchase program for lil products |
| Social Contribution | <ul style="list-style-type: none"> Supported Coffee Lab in Indonesia |



- | | |
|-----------------------|---|
| Governance | <ul style="list-style-type: none"> Established the Governance Committee Strengthened the process for verifying director candidate |
| Compliance Management | <ul style="list-style-type: none"> Established the Compliance Guideline by task |
| Ethical Management | <ul style="list-style-type: none"> Created the Compliance Department in charge of the Compliance and Ethical Management |



- | | |
|-------------------------|---|
| Next Generation Product | <ul style="list-style-type: none"> Signed the Head of Agreement (HOA) with Philip Morris International (PMI) for overseas distribution of lil product lines Grown the size of the NGP organization (launched the NGP Business Division) |
| Research & Development | <ul style="list-style-type: none"> Implemented the research on less-smell products and applied patents for relevant technologies Awarded the Prime Minister's Award for developing the fat-soluble liquid capsule |



STAKEHOLDER COMMUNICATION

KT&G defines shareholders/investors, government, local community, employees, partners, customers, and environment as the key stakeholder group. Communication channels for each stakeholder group are operated, and we endeavor to reflect their opinions in the business activities.

STAKEHOLDERS		EXPECTATIONS
	Shareholders/Investors	<ul style="list-style-type: none"> • Maximizing shareholder values • Securing soundness of governance • Stable and long-term growth
	Government	<ul style="list-style-type: none"> • Compliance with legal/social responsibilities • Job creation • Tax payment
	Local community	<ul style="list-style-type: none"> • Collaboration for solving social issues • Win-Win Growth through development of the local community
	Employees	<ul style="list-style-type: none"> • Good work environment • Shared growth of the labor and management • Support for career development
	Partners	<ul style="list-style-type: none"> • Win-Win growth through collaboration • Support for sustainability
	Customers	<ul style="list-style-type: none"> • Products and services development to satisfy various needs • Enhancing customer satisfaction
	Environment	<ul style="list-style-type: none"> • Reducing environmental impact caused from business activities • Response to climate change

COMMUNICATION CHANNELS AND PLATFORMS	KT&G ACTIVITIES 2019
<ul style="list-style-type: none"> • General meeting of shareholders • Business evaluation • Business report • Corporate seminars 	<ul style="list-style-type: none"> • Ordinary General Meeting of Shareholders (Mar. 29, 2019) • 29 events of shareholder communication activities such as NDR, conferences, and corporate seminars • Other occasional IR activities (20 to 30 times a month)
<ul style="list-style-type: none"> • Political meetings and seminars • Opinion proposal system • Public hearing • Advisory meetings 	<ul style="list-style-type: none"> • 26 compliance and ethics training sessions to employees • 313 new employment • KRW 421.6B in corporate tax
<ul style="list-style-type: none"> • SangSang Fund • SangSang Madang • Employee volunteering • Welfare foundation/Scholarship foundation • Tobacco farm support 	<ul style="list-style-type: none"> • KRW 101B in social contribution investment
<ul style="list-style-type: none"> • Labor-management agreement • Grievance system • Intranet • SangSang Realization Committee 	<ul style="list-style-type: none"> • 89.6% of labor union membership rate • 124 hours in training per person • KRW 1.4M in training expense per person
<ul style="list-style-type: none"> • KT&G Advanced Purchasing System (KAPS) • Electronic Data Interchange (EDI) System • Grievance process • Supplier assistance programs 	<ul style="list-style-type: none"> • Regular communication through KAPS • Early payment of KRW 45.9B to partners • KRW 745B in purchasing partners' products
<ul style="list-style-type: none"> • Managerial disclosure • Sales report • Sinmungo • Factory tour • SNS/Website • CS center • New product satisfaction surveys 	<ul style="list-style-type: none"> • 188 centers for customer communication • 302,128 receptions and redressal of VOC • Improvement in VOC response rate (98.6%)
<ul style="list-style-type: none"> • Environmental organizations/NGOs • Environmental policy meetings 	<ul style="list-style-type: none"> • Training for enhancing environmental awareness • Programs for eco-friendly factory tours

MATERIALITY TEST

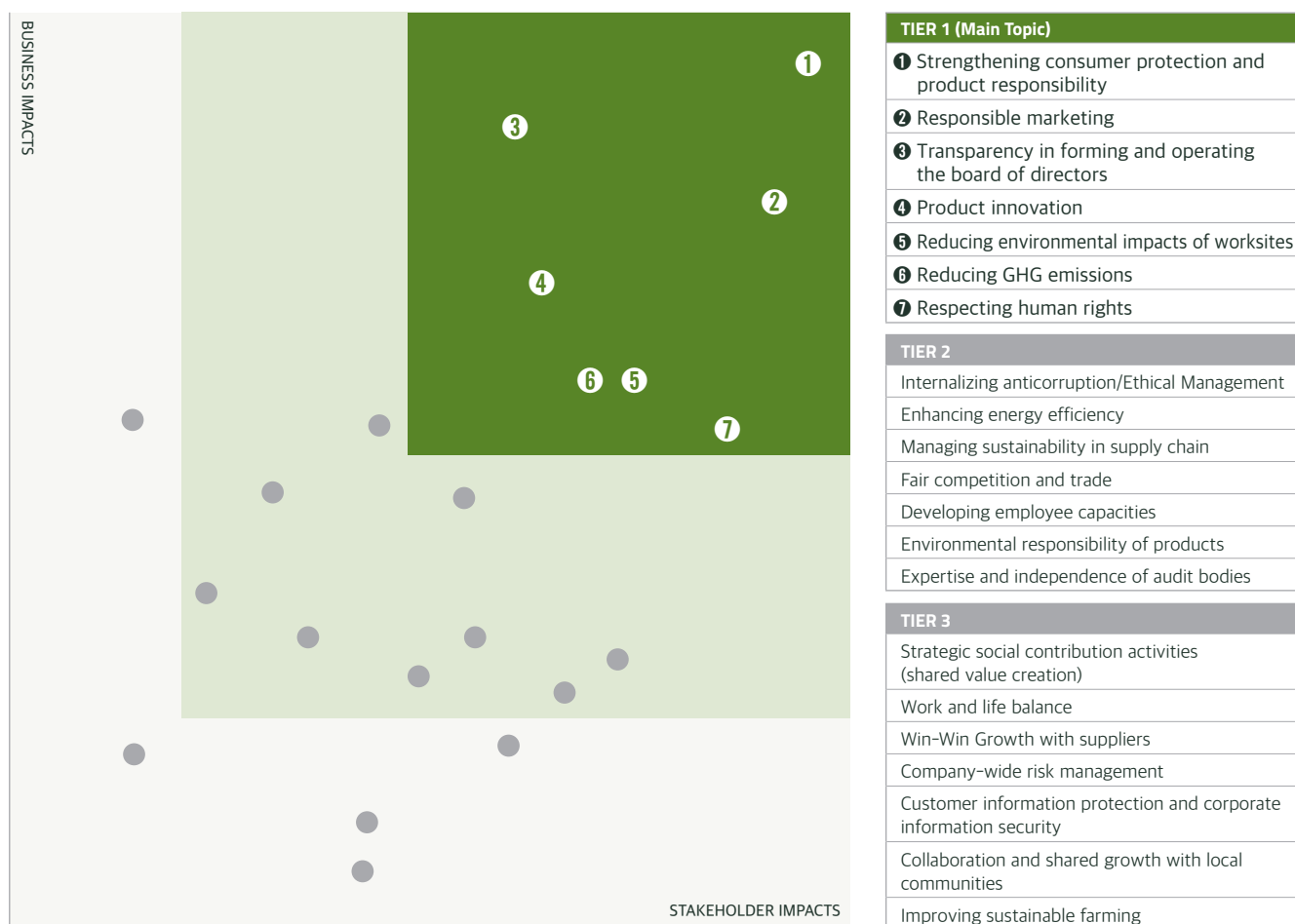
Materiality Test Process

KT&G conducted the materiality test to identify and manage key ESG issues for stakeholders and the company. We analyzed external sustainability indices, media exposures, stakeholder demands, and best practices in the industry to identify issues. Then, we investigated main implementations and employee surveys to evaluate the materiality of issues.



Materiality Test Matrix

We evaluated 21 issues to decide on the reporting content of 2019, and the top 7 issues were reported as main topics.



Materiality Test Results

7 main topics were selected through the materiality test in 2019. The main topics include: reducing environmental impacts of worksites and reducing GHG emissions in the environmental aspect; strengthening consumer protection and product responsibility, responsible marketing, and respecting human rights in the social aspect; transparency in forming and operating the board of directors in the governance aspect; and product innovation in the innovation aspect. Each topic is intimately reported in the Priority Area sections of the report.

Main Topic	Priority Area	Stakeholders	GRI Standards	Page
Reducing GHG emissions	Climate Change Response	Environment, Government, Local community	305-1,2,4	36~38
Reducing environmental impacts of worksites	Water Management	Environment, Government, Local community	306-1	39~40
Strengthening consumer protection and product responsibility	Product Safety and Quality	Customers	416-1,2	44~45
Responsible marketing	Product Safety and Quality	Customers, Government	417-1~3	46~47
Respecting human rights	Supply Chain Partnership Better Work Place	Employees, Partners, Local community	412-2	48~49, 53
Transparency in forming and operating the board of directors	Governance	Shareholders, Investors	102-18	68~73
Product innovation	Next Generation Product	Customers, Employees	-	82~85

Environmental Responsibility for the Future

ENVIRONMENT





GLOBAL MEGATREND

Global warming caused by greenhouse gas (GHG) emissions has a significant impact on the global economy. Companies, therefore, need to identify opportunity factors as a foundation for new value creation while fulfilling social and environmental responsibilities by minimizing their impacts on climate change. Water resource is an area essential for careful management in the tobacco industry, and the industry sources materials from farms that constitutes 70% of total water intake and 90% of total water consumption in the world.

RISKS

Issues related to climate change are stressed due to the tightened environmental laws and regulations.

Brand values are damaged due to environmental and social impacts.

Procurement costs of materials are changing due to the changes in farming environment.

Investment costs in introducing eco-friendly facilities are increasing.

OPPORTUNITIES

Securing eco-friendly competitiveness through proactive response to environmental laws and regulations

Enhancing brand values by enhancing eco-friendliness of the manufacturing process

Satisfying consumer demands by developing eco-friendly products

Reducing costs through efficiency improvement of facilities

APPROACH

KT&G has established a company-wide environmental management system and operates a dedicated organization to faithfully implement it. The main areas of implementation are climate change response, water and waste management at worksites, reducing environmental impacts of products, and enhancing environmental awareness. We will endeavor to reduce environmental impacts, respond to relevant regulations, and recycle resources through continuous environmental investment to contribute to the circular economy. Furthermore, to proliferate the Environmental Management, we will intensify communication activities such as environmental training programs to enhance employees' awareness.

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PRIORITY AREA

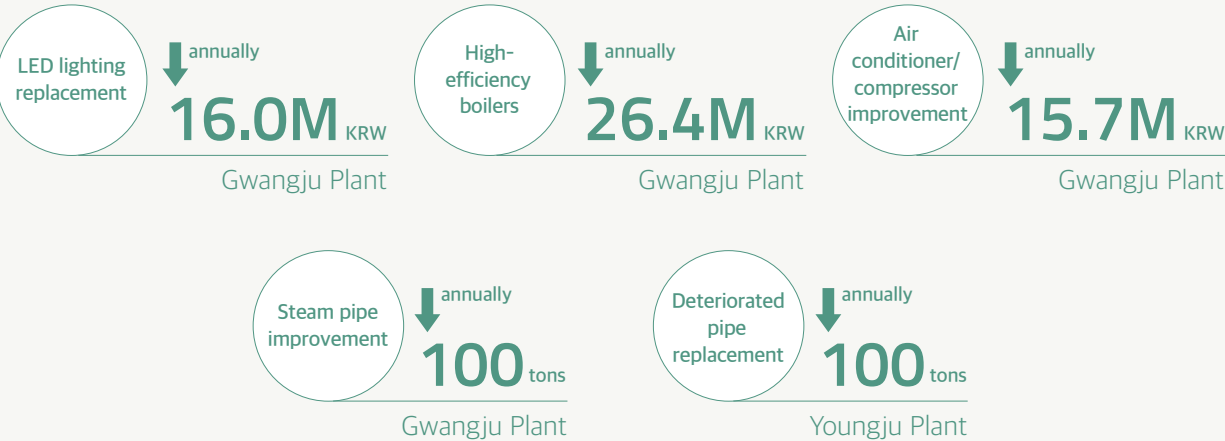
Climate Change Response

2019 CASE STUDY

Introduction of High-efficiency, Eco-friendly Facilities

KT&G reduces GHG emissions by expanding high-efficiency, eco-friendly facilities as a part of the Eco-friendly Business for energy efficiency. In the 5 plants (Shintanjin, Youngju, Gwangju, Gimcheon, and Cheonan), we are implementing various activities including the establishment of the maximized power monitoring system for efficient use of energy.

In Gwangju Plant, we replaced all lighting to LED to reduce electricity consumption. Moreover, we introduced high-efficiency eco-friendly boilers and improved steam pipes, air conditioners, and compressors to increase the energy efficiency of the facility. In Youngju Plant, we replaced deteriorated steam pipes and repaired leakage to reduce steam consumption. To summarize, we are conserving energy use through the energy efficiency and eco-friendly facilities and plan to realize reduction of energy consumption by discovering various activities at each plant.



LED Lighting at Gwangju Plant



Eco-friendly Boiler at Gwangju Plant

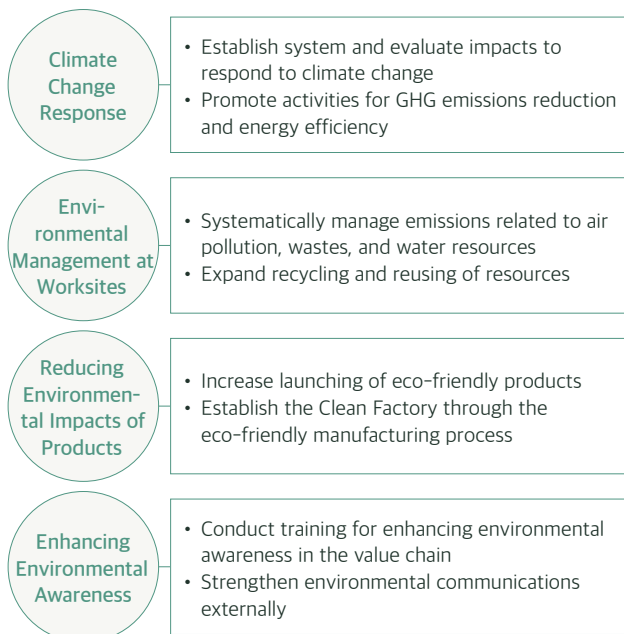
1. Governance

KT&G executives and employees share the seriousness of climate change and consider the impact of climate change in decision making and management activities. For this, we implement the company-wide systematic Environmental Management and operates the Green Safety Department exclusive for energy and environmental management. The Green Safety Department oversees the energy efficiency of KT&G plants nationwide and the planning and management of GHG emissions reduction projects. Moreover, the department conducts climate change response activities such as energy consumption and GHG emissions control, and performs responses to environmental policies and regulations of the government.

2. Strategy

KT&G performs the company-wide Environmental Management based on the Environmental Management Implementation System as described below. The selected implementation activities are climate change response, environmental management at worksites, reducing environmental impacts of products, and enhancing environmental awareness, and we are expanding the scope of the activities. In particular, we are not only responding to climate change-related international initiatives proactively, but also promoting GHG reduction activities and energy consumption efficiency to abide by the governmental policies and regulations. Moreover, we are actively engaging in the climate change response by developing products that can mediate environmental impacts.

Environmental Management Implementation System



*Certified ISO 14001 since 2005

3. Risk Management

KT&G identifies and manages key risks of climate change that can affect the company. The key risks are categorized into the transitional risks that occur when the economic system changes to climate change-oriented and the physical risks that are directly influenced by the real climate change. We plan to sophisticate and implement mid- to long-term strategies according to these risks.

Category	Risks
Transitional risks (regulatory, technological, market, and reputational risks)	<ul style="list-style-type: none"> Intensified environmental laws/regulations Potential damage to brand values due to environmental impacts occurred in the process Increased consumer demands for developing eco-friendly products
Physical risks (short-term, mid- to long-term)	<ul style="list-style-type: none"> Risks in procurement of main materials such as tobacco leaf due to changes in cultivation environment

4. Index Management

KT&G performs activities for reducing energy consumption and GHG emissions. Both direct and indirect emissions of GHG are recorded in the 5 plants and about 100 sales branches nationwide. In 2018, the emissions data were temporarily increased due to the expansion and installation of facilities (air conditioner and water/power facilities) for producing next generation products. But we are accomplishing high efficiency in both existing and new supplies to realize reduction of GHG emissions and energy consumption.

Intensity of GHG Intensity

Category	Unit	2017	2018	2019
Intensity of GHG emissions (separate)	tCO ₂ eq/ KRW 100M	3.30	3.95	3.55

Intensity of Energy Consumption

Category	Unit	2017	2018	2019
Intensity of energy consumption (separate)	TJ/KRW 100M	0.06	0.08	0.07

5. Climate Change Response Activities

Establishing the GHG Inventory

Followed to the Emissions Trading Scheme in 2015, GHG management has become extremely important. Therefore, KT&G established the GHG Inventory and manages the emission amounts by source systematically.

New Renewable Energy Production and Consumption

KT&G operated solar power generators in Shintanjin Plant and Youngju Plant. Through the 1,715kWp power generation facility, we produce eco-friendly energy, and the total amount of electricity generated from both plants in 2019 was 2,026,224kWh. We plan to continue contributing to energy transition of the global society by expanding production of eco-friendly energy.

6. Environmental Communication

KT&G transparently shares environmental data including GHG emissions, energy and water consumption, and wastes emissions generated from its business on the website, KT&G Report, and ENV-INFO. In addition, Shintanjin and Youngju Plants run the factory tour programs to show the status of eco-friendly facilities operation to external stakeholders. Through the active communication, we are informing all stakeholders about the status of our Environmental Management Implementation, while also triggering attention to the climate change issues.

1	2
3	

Factory Tour Program 1, 2
Solar Panel Facility at Shintanjin Plant



PRIORITY AREA

Water Management

2019 CASE STUDY

Reducing Water Consumption by Repairing HT Water Softener

Youngju Plant softens hard water using the high-temperature (HT) water softener* equipment to supply soft water to boilers. Putting HT condensate water** into boilers diminishes the function of water softener and increases use of waterworks to control temperature, and it may generate water quality issues in the wastewater treatment facility. So, we introduced the condensate water recovery system and HT water softener drain system to lower the temperature of condensate water.

These improvements enabled us to save about 4,730 tons of water annually, which is about 6.3% of total water consumption at Youngju Plant. Therefore, we expect to conserve costs in both water use and wastewater treatment.

*Water softener: An equipment that softens hard water by eliminating positive ions such as calcium and magnesium

**Condensate water: Water vapor comes into contact and changed from gas to liquid



HT Water Softener

Before Improvement

- Increase in water consumption due to additional use of waterworks
- Functional decline of water softeners due to parts corrosion and difficulties in boiler operation
- Water quality issues in the wastewater treatment facility

After Improvement

- 4,730 tons of water saved annually (about 6.3% of total water consumption at Youngju Plant)
- Solution through lower-temperature management of condensate water tanks
- Reduction in wastewater treatment costs

1. Governance

KT&G manages water resources based on the Environmental Management Implementation System, and the Green Safety Department manages the amount of water resources usage. We record the amount water used in the manufacturing process and implement corrective actions by plant for the eco-friendly worksite management.

2. Index and Program

For stable supply of water resources, KT&G regularly monitors potential risks such as droughts, floods, and nearby infrastructural damages. Moreover, we record water consumption amount at each plant to identify and manage trends of the water usage. The scope of data collection includes Singtanjin, Youngju, Gwangju, Gimcheon, and Cheonan Plants. In 2018, the data was temporarily increased due to the expansion and installation of facilities for producing next generation products. We will save water consumption by continuously improving facilities and operational efficiency.

Intensity of Water Consumption



Category	Unit	2017	2018	2019
Intensity of water consumption (separate)	Tons/ KRW 100M	15.49	17.90	16.62

Environmental Impact Reduction

2019 CASE STUDY

Eco-friendly Products

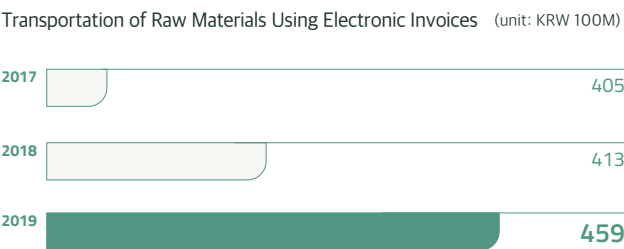
KT&G considers eco-friendliness from product development, manufacturing, packaging, to disposal to execute the Eco-friendly Management. We are striving to reduce environmental impacts of products by using eco-friendly materials, minimizing use of resources, and expanding recycling.

Use of Eco-friendly Materials		Expanding Resource Recycling	
Improved packaging materials of cigarette carton	<ul style="list-style-type: none">Details - We stopped using vinyl cases made of crude oil and changed paper materials with low pulpEffects - Reduced about 1,500 tons of annual pulp consumption	Use of recycled pulps	<ul style="list-style-type: none">Details - We made collected paper into pulp and produced hemp packaging and cardboard paper.Effects - Reduced about 400 tons of annual pulp consumption
Improved inner paper of cigarette packs	<ul style="list-style-type: none">Details - We replaced aluminum inner paper with self-developed, eco-friendly paper that can be recycledEffects - Reduced about 850 tons of annual aluminum consumption	Improvement of cigarette carton wrapper	Improvement of wrapping paper in cigarette packs
Oxo-biodegradable films	<ul style="list-style-type: none">Details - We developed eco-friendly films that reduce degradation speedEffects - Accelerated degradation of products from 100 years to 10 years		

1. Realizing Eco-friendly Purchase




Purchasing Eco-friendly Materials

KT&G only uses packaging paper made of Forest Stewardship Council (FSC)-certified pulps to practice the Eco-friendly Green Purchase. Moreover, as efforts for accomplishing the Eco-friendly Quality Management, we use papers made of wastepaper and recycled paper, harmless and eco-friendly adhesives, and bio-degradable films, as well as accelerating biodegradation of paper filters. KT&G plans to further promote the Green Purchase by establishing the Green Purchase System that defines targets, scope, and procedures of Green Purchase.



Transportation of Raw Materials Using Electronic Invoices

KT&G transitioned to electronic invoicing for the Eco-friendly Management of distribution. In the past, about 90,000 pages of paper invoices were consumed annually, but our electronic invoicing enabled us to conserve resources. Until the 2nd half of 2020, we plan to complete the Transportation Information Sharing System which will facilitate access to invoice details such as departure and arrival time, items, and quantity using a mobile application, as well as driver's signature management. The electronic invoicing will contribute to not only saving resources but also work efficiency.

		Point of departure	Carrier	Destination
Electronic invoicing	IMPROVED Invoice	 Sign electronic invoice	 Confirm electronic invoice	 Sign electronic invoice
	Tracking	Message alerts for estimated time to arrival or tracking through mobile apps/system		
Paper invoicing	EXISTING Invoice	Print 3 pages and sign	Keep 1 copy at carrier	Keep 1 copy after loading
	Tracking	Call drivers by phone or ask relevant department		

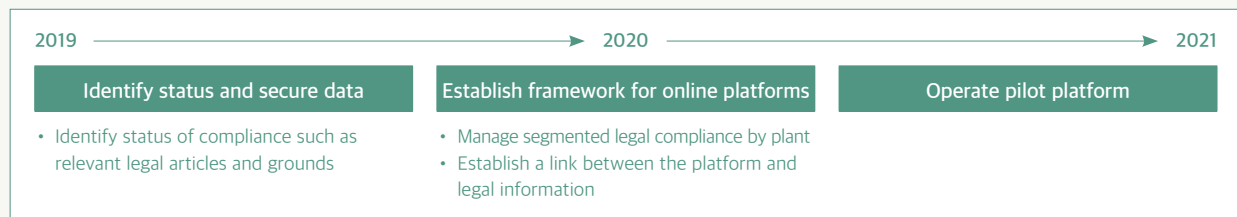
Pollutant Emissions Management

2019 CASE STUDY

Reinforcing Integrated Management of Laws/Regulations

KT&G operates the Integrated Management Platform to proactively respond to environmental laws and regulations. By 2020, we will complete collecting data and establishing a platform, and we plan to sophisticate the system by applying segmented legal contents. In addition, we perform regular training for the Environmental Management to enhance employees' awareness of environment.

Process of establishing the Integrated Management System for laws and regulations



1. Air and Water Pollutants Management

KT&G takes proactive responses to control pollutant emissions below the regulated standard. So, eco-friendly high-efficiency facilities were introduced at Shintanjin, Gwangju, and Cheonan Plants, and we measured and analyzed emission amounts at all plants to comply with the strengthened air pollutant emissions standard. For water pollutants, we changed our management index from the chemical oxygen demand (COD) to total organic carbon (TOC) for more systematic organism management. The change was made in the 1st half of 2020, and we plan to extend the scope gradually.

2. Wastes Management

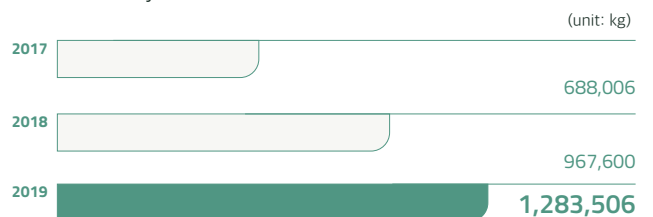
Waste Emissions Management

KT&G is reducing the amount of materials used by developing a technology for decreasing byproducts from the manufacturing process, and it is monitoring emission amounts at the 5 plants. In 2018, the data was temporarily increased due to the expansion and installation of facilities for producing next generation products. Moreover, we are developing plans to check and annually inspect waste management companies to strengthen our environmental responsibility for waste emissions. The inspection will evaluate their compliance with the standards in waste treatment process and treatment capacity based on the governmental guideline and ISO 14001.

Wastes Recycling

Ethanol loses purity after used in the manufacturing process and is treated as designated waste. KT&G refines and recycles ethanol to minimize generation of designated wastes. The rate of recycled ethanol at Shintanjin Plant 2 is about 81.0% which is equivalent to annual recycling amount of 3,000L. Moreover, we are expanding recycling of byproducts and also recycling metals, plastics, and wastepaper.

Amount of Recycled Wastes



Intensity of Waste Emissions

Category	Unit	2017	2018	2019
Intensity of waste emissions (separate)	kg/KRW 100M	84.80	111.45	98.97

A group of people, mostly wearing light blue t-shirts, are holding hands in a circle. The image is warm and slightly blurred, with a soft orange glow in the background, suggesting a sunset or sunrise. The text 'A Better Society through Embracement' is overlaid on the image in a teal color, with horizontal lines underlining each word.

A Better Society through Embracement

SOCIAL



GLOBAL MEGATREND

KT&G is affected by various laws and regulations due to the nature of tobacco-related business, and its impacts on the value chain must be controlled. As our products vary in different tastes of consumers, we need to conduct stringent screening of chemicals to provide safe products and perform responsible marketing based on laws of each country. In addition, supplier-related issues influence our business competitiveness and credibility as we source materials from diverse suppliers. Thus, we need to create a sound industrial ecosystem by leading partners to fulfill their social and environmental responsibilities.

RISKS

Increase in issues of responses to intensified laws and regulations in chemical substances and marketing

Decrease in consumer trust and generation of costs due to safety-related issues

Loss of stability of procurement system followed by falling competitiveness of supply chain

OPPORTUNITIES

Eliminating legal risks of product liability through proactive responses to laws and regulations in chemical substances and marketing

Enhancing customer satisfaction and retaining new customers by improving quality of products and services

Contributing to creation of a shared growth ecosystem by enhancing competitiveness of supply chain

APPROACH

KT&G strives to satisfy expectations of stakeholders. We are forming safe and pleasant workplace for the employees with the expectation that all stakeholders can work in a sound industry. Moreover, we are not only investing aggressively to guarantee product safety and liability which are the key to sustainability, but also establishing system to enable partners, who are the basis for business competitiveness, to fulfill their social responsibilities. Moreover, we are conducting various projects to grow with the local community.

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PRIORITY AREA

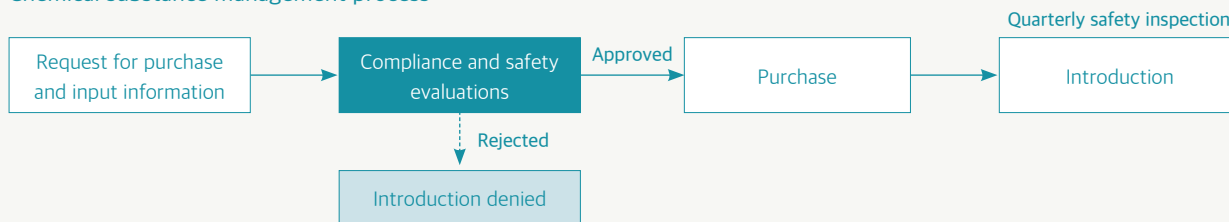
Product Safety & Quality

2019 CASE STUDY

Chemical Substance Safety Management

KT&G manages all chemical substances to pursue unconditional compliance with environmental safety regulations and voluntary reduction of hazardous risks. According to the Chemical Substances Control Act (K-Toxic Act), all chemical products and used in all operations are biennially investigated, reported, and disclosed on the National Chemicals Information System (NCIS). Moreover, we are passionately preventing accidents through the work safety evaluation and facility improvements as our chemical safety management activities. When new chemical substances are introduced, we conduct preliminary legal reviews and chemical safety evaluations to prohibit any in-coming hazardous materials. Safety inspections are performed once or more every quarter to maintain the standard of storage, transportation, and management, and we are advancing the existing management system to enable real-time review of regulated substances that are getting diversified lately. We plan to introduce the advanced management system in overseas operations and subsidiaries.

Chemical substance management process



1. Consumer Safety

KT&G prioritizes safety of consumers who use products. We abide by relevant regulations to secure product safety and strengthen safety from materials to final products. We will continue to thoroughly analyze impacts on consumer safety and health and provide safe products to consumers.

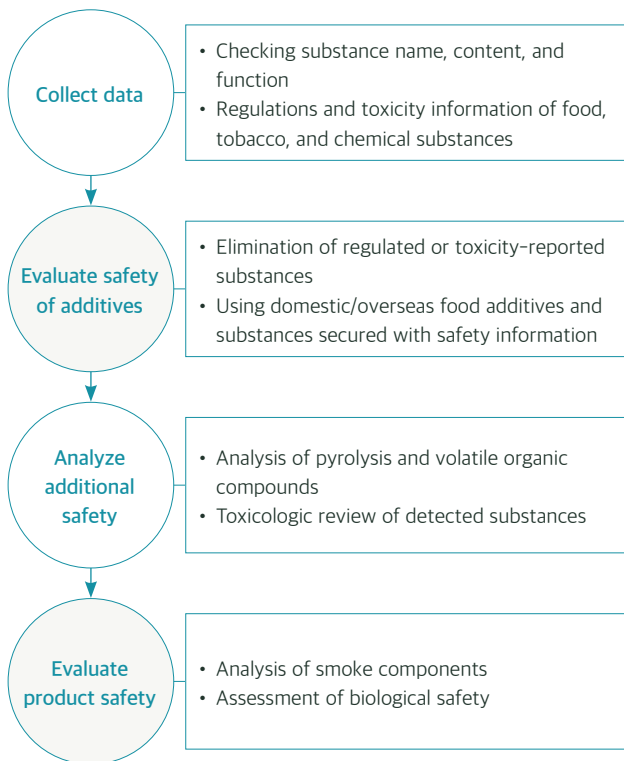
Certifications for Strengthening Consumer Safety

Category	Institutions	Type	Details	Initial Certification
Materials	Cooperation Centre for Scientific Research Relative to Tobacco (CORESTA)	International standard	Tobacco leaf that satisfies 118 safety standards	-
Materials	KT&G	Self-regulatory standard	Preliminary safety evaluation and quality system suitability test for additives and ingredients	-
Tobacco substances	Korea Laboratory Accreditation Scheme (KOLAS)	Certification	Quarterly assessment of tobacco substance suitability	Mar. 2000
Tobacco products	Korea Fire Institute (KFI)	Certification	Quarterly accreditation and renewal of anti-fire performance certification	Jun. 2015
lil products	Korea Certification (KC) Mark	Certification	Attach to safety devices and temperature control devices that prevent overvoltage, overcharge, and overdischarge in accordance with the Electrical Appliances and Consumer Products Safety Control Act	Oct. 2017
Worksite	International Organization for Standardization (ISO)	Certification	Maintain the Quality and Environmental Management System at worksites based on ISO 9001	Apr. 2000

2. Chemical Safety of Products

In accordance with the principle of product liability, KT&G develops trustworthy products and verifies safety from the early stage of product development. We check conformity of all chemical substances to the domestic/international regulations and only use of safety-ensured substances by conducting review and study on relevant toxicological data. In this process, concerned chemicals known to be Carcinogenicity/Mutability/Reproduction toxicity/Respiratory toxicity are excluded first. Moreover, we perform the smoke component analysis and biological safety evaluations after applying new materials into products.

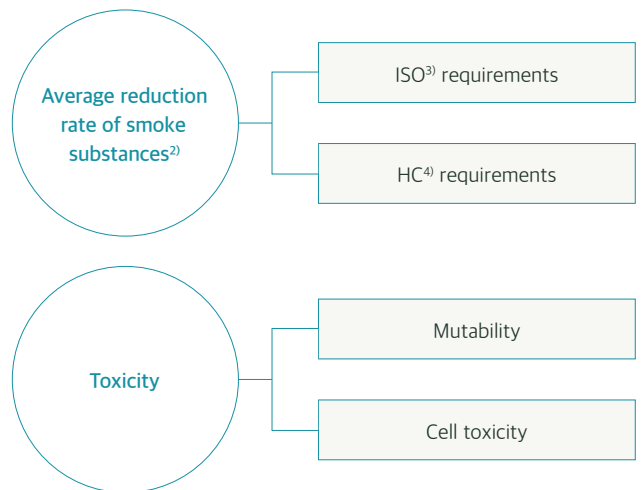
Procedure for Preliminary Safety Evaluation of Additives and Materials



KT&G will provide consumers accurate information about products through the impact analysis from development to user phase and prioritize consumers' safety by using only permitted chemical substances.

In 2018, through the service of external official analytic institutions, we performed substance analysis and safety assessment of aerosol from heat-not-burn products. This study was presented at an overseas academic conference¹⁾.

Aerosol Substance Analysis and Safety Evaluation



1) Overseas academic conference study related to reduction of aerosol of heat-not-burn products

- Comparison of in vitro toxicity of heated tobacco products and combustible cigarette (CORESTA 2019)

- Comparison of Selected smoke components in Mainstream Smoke According to Reuse of Consumable of Hybrid Heated Tobacco Product (ACS 2019)

- Determination of Carbonyl Compounds in Mainstream Smoke of Hybrid Heated Tobacco Product Using High Performance Liquid Chromatography (ACS 2019)

2) Average reduction rate of smoke substances: Individual reduction rate of analyzed substances

3) ISO smoke requirement: Analysis of cigarette filters by opening the perforation

4) Health Canada (HC) smoke requirement: An intensified smoking requirement of the Canadian Health Authority that analyzes cigarette filters by closing the perforation

3. Responsible Marketing and Labeling

Tobacco products are regulated by various regulatory policies based on the WHO(World Health Organization) Framework Convention on Tobacco Control (FCTC). KT&G complies with international standards and relevant regulations of marketing and labeling. In addition, we established the internal control procedure or responsible communication with consumers and prevention of teenager smoking. Based on the procedure, we are striving to perform responsible marketing activities.

KT&G Responsible Marketing Policy

To enhance the global brand value, we perform responsible and sustainable marketing in accordance with the designated tobacco-related policies and regulations. We also formed the Internal Control Department to monitor whether product marketing and sales activities are conducted in accordance with the marketing policy, thereby enhancing effectiveness of the policy.

Our Tobacco Business targets only adults as consumers and prevents minors to access our products rigorously through the ‘Teenager Smoking Prevention Campaign’. We deliver information of product characteristics and directions for use clearly and transparently to secure reasonable selection rights of consumers, and we strive to provide consumer rights by receiving VOC (Voice of Customer) and building trust through various channels.

In addition, we are conducting regulatory activities for illegal tobacco products in collaboration with external institutions in order to establish sound distribution and marketing order. As the tobacco industry has various stakes in tobacco farm protection, exports, taxation, employment, and distribution, we pursue support the regulatory authority to establish balanced and reasonable regulatory policies for marketing.

[Applied Scope]

The marketing policy is applied to all products of KT&G, and every worksite where the products are sold comply with marketing regulations.

Responsible Marketing	KT&G abides by the National Health Promotion Act and Tobacco Business Act that were amended based on the FCTC of WHO, and overseas operations also strive to perform marketing activities in accordance with the local tobacco-related regulations. Moreover, we formed the Internal Control Department to monitor whether product marketing and sales activities are conducted in accordance with the marketing policy, thereby enhancing effectiveness of the policy.
Consumer Rights Protection	KT&G contributes to adult consumers' reasonable choices of products by delivering information about product characteristics and use directions transparently and clearly, while diversifying the product portfolio. By complying with regulations, we indicate product information, warning texts and images on all products for domestic and overseas sales and prevent marketing that can bring out misunderstanding by consumers. In addition, we strive to build trust by communicating with consumers through various channels such as CS centers and company website and to secure basic rights of consumers.
Minor Protection	KT&G's business targets adult consumers only and prevents minors' accessibility. To prohibit smoking by minors, we are conducting the 'Teenager Smoking Prevention Campaign' annually. Moreover, we are continuously striving to reduce smoking rate of minors by creating a social trend of checking identifications when purchasing cigarettes in retail stores.
Creation of Environment for Sound Industrial Regulation	We support the regulatory authority to establish balanced and reasonable regulatory policies for marketing as the tobacco industry has various stakes in tobacco farm protection, exports, taxation, employment, and distribution. Moreover, we are constantly cooperating with external institutions to build a structure of sound distribution and marketing such as preventive regulation activities for illegal tobacco products.

Activities for Responsible Marketing

Protecting Minors

KT&G strictly prohibits minors to access its products and conducts various campaigns and education to protect them. We also led nationwide retail stores to attach stickers indicating 'ARS (1382) for Checking IDs and forged IDs to stop minors to access our distribution channels. Moreover, we provide various educational and research programs to mental health centers throughout Korea to prevent minors' smoking.

Offering Responsible Product Information

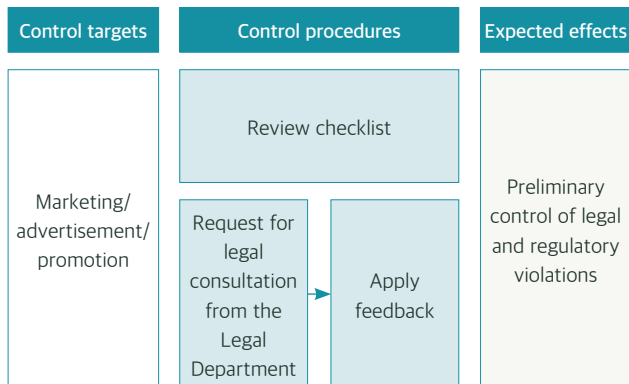
KT&G fulfills its responsibilities in product promotions and marketing. In all product packaging and advertisements, we put written and graphic warnings and comply with international standards not to use warnings with potential misunderstanding.

Category	Compliance
Domestic sales products	<ul style="list-style-type: none"> Indicate text and graphic warnings and level of tar and nicotine in accordance with the National Health Promotion Act and Tobacco Business Act Disclosure of tar and nicotine levels
Overseas exported products	<ul style="list-style-type: none"> Comply with local regulations such as text and graphic warnings and tar level indication

In addition, we collect VOCs through various channels including CS centers and corporate website and take responses actively according to manuals.

Internal Control Procedures for Marketing, Advertising, and Promotion

KT&G prevents violations of laws and regulations related to marketing, advertising, and promotions using the internal control procedure.



Marketing/Advertising/Promotion Training

KT&G trains all employees from new recruits to managers on the Tobacco Business Act. In 2019, we provided training on the Tobacco Business Act to a total of 128 employees including new and experienced employees and new managers.

Training of the Tobacco Business Act 2019

Category	Details	Targets
Understanding of the Tobacco Business Act	<ul style="list-style-type: none"> System related to tobacco manufacturing/sales such as manufacturing business permission and retailer specification Business compliances such as product information and advertising limitation 	New and experienced employees
Understanding of the Tobacco Business Act and regulation trends	<ul style="list-style-type: none"> Overall regulation about manufacturing and sales of tobacco products Regulation trends such as flavor regulations, advertisement, and promotions 	Experienced employees (2018 - 2019)
Understanding of the Tobacco Business Act and Fair-Trade Act	<ul style="list-style-type: none"> Overall regulation about manufacturing and sales of tobacco products Compliance with Fair-Trade Act such as unfair trades 	New managers

Lawsuits Regarding Marketing·Advertisement·Promotion

Lawsuit by National Health Insurance Service (NHIS) - Seoul Central District Court 2014-Ga-Hap-525054

Category	Details
Filed date	April 14, 2014
Interested parties	Plaintiff: NHIS Defendant: KT&G and 2 others*
Lawsuit contents	NHIS requested for KRW 53.7 billion of compensation to the defendant for expenses used by the institution to treat illness caused by smoking between 2003 and 2012.
Compensation amount	KRW 53,741,768,930 won
Progress	First hearing
Future hearing	September 11, 2020 (due date of pleading)

*Philip Morris Korea and British American Tobacco Korea
(Including British American Tobacco Korea Manufacturing Limited.)

PRIORITY AREA

Supply Chain Partnership

2019 CASE STUDY

Supplier Quality Evaluation including ESG

KT&G considers environment, social, and governance (ESG) factors such as human rights, labor condition, environment, and ethics when selecting new suppliers. So, we conduct the Supplier Quality (SQ) Evaluation including ESG-related items on main suppliers who wish to have trade relations. In particular, to assess the work environment respecting human rights of labors, we check their policy and programs for each item. More specific evaluation items include prohibition of forced and child labors, working hours and overtime payment, basic wages, collective bargaining, and health and safety activities. The portion of ESG-related items in the SQ Evaluation is 40%, and the evaluation team composed of experienced employees engaged in the relevant field or those who have relevant certificates perform evaluation by visiting the suppliers.

Items for Supplier ESG Evaluation

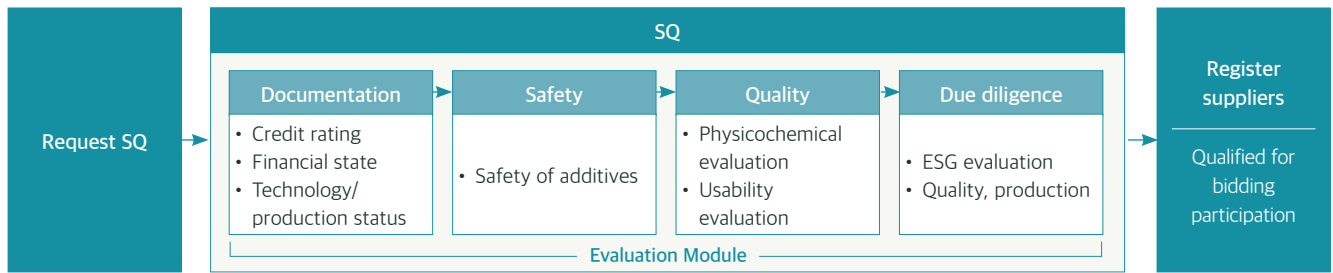
Evaluation Items		Definition	Questionnaires
Human rights and labor conditions	Human rights	Evaluation of the control system that respects human rights and provide fair labor conditions	<ul style="list-style-type: none">• Relevant policies• Relevant programs
	Labor conditions		
	Safety & Health		
	Grievance treatment		
Environment	Pollution prevention	Evaluation of the environmental control system that identifies/reduces pollution sources and uses resources efficiently	
	Resources use		
	Chemical substances		
Ethics	Business ethics	Evaluation of the control system for prohibiting corruptions such as bribery and inflict of interests	
	Pre-/Post-management		
Business management	Human resources	Evaluation of the overall business management system for sustainable management	
	Supply chain management		
	Products & services		
	Local community		

1. Supply Chain Evaluation

Materials Supplier Qualification System

KT&G runs the Materials Supplier Qualification System to fairly select new suppliers and secure stable supply by establishing cooperative relationship with the existing suppliers. The qualification period is 3 years, and we reevaluate suppliers after 3 years to verify their competence and encourage them to take corrective actions. Since 2011, a total of 75 suppliers were evaluated, and 74 of them were qualified. When the suppliers are not qualified, we provide them reasons and give them time to take corrective actions until the requalification process. Only those who had completely corrected any deficiencies can receive qualifications. Through this qualification system, suppliers can check their production and R&D capacities, and KT&G can create the value of shared growth with stable partners. In the overseas operation, we prioritize tobacco leaf suppliers who comply with requirements of the Sustainable Tobacco Programme (STP) for selection.

Certification Process



Infrastructure for Suppliers' Social/Environmental Responsibility

KT&G developed the Supplier Code of Conduct to transfer its culture of social/environmental responsibility and reduce relevant risks of suppliers. The supplier code is used as a guideline for suppliers to self-check social/environmental responsibility during the supplier selection and comprehensive evaluation processes. In the future, we plan to conduct due diligence to check if suppliers comply with the Supplier Code of Conduct. We will endeavor to improve sustainability in the supply chain by requiring suppliers to correct deficiencies in social, environmental, and governance checklist, as well as their capacities for fulfilling contracts.

NTM Suppliers

Category	Unit	2017	2018	2019
No. of suppliers	Domestic EA	69	71	69
	Overseas EA	9	9	12
	Total EA	78	80	81
Purchase amount	Domestic KRW 100M	3,364	4,258	4,122
	Overseas KRW 100M	237	293	440
	Total KRW 100M	3,601	4,551	4,562

2. Win-Win Growth in Supply Chain

Supply Chain Management

KT&G sources tobacco leaves, filters, and packaging from supply chain. The suppliers in the supply chain are divided into tobacco material suppliers and non-tobacco material (NTM*) suppliers. When signing a contract, suppliers need to sign the Charter of Ethics to enhance the ethical standard of supply chain.

*NTM: Non-tobacco materials such as filters and packaging materials

Tobacco Material Suppliers

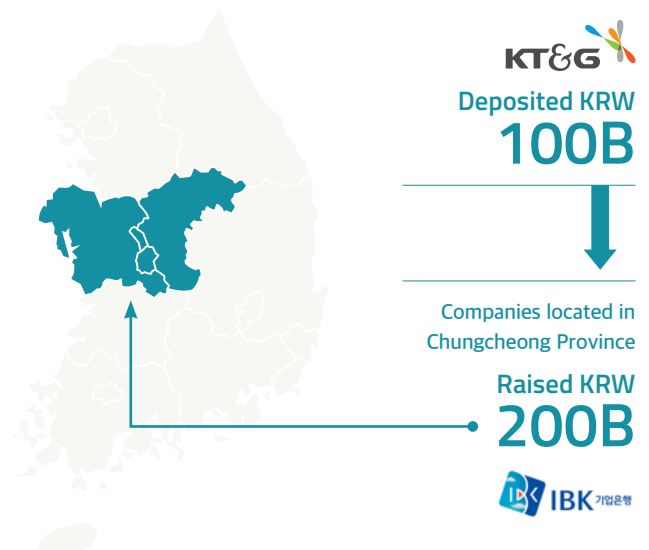
Category	Unit	2017	2018	2019
No. of suppliers	Domestic Persons	3,365	3,144	2,880
	Overseas EA	16	17	19
Purchase amount	Domestic* KRW 100M	951	947	1,175
	Overseas KRW 100M	2,172	1,881	1,713
	Total KRW 100M	3,123	2,828	2,888

*Domestic purchase amount includes the amount purchased from KT&G's subsidiary, Tae-A Industrial (RTL manufacturer)

Low-interest Loan Assistance

In order to facilitate the local economy and job creation in Chungcheong Province where the head office is located, KT&G signed a memorandum of understanding (MOU) with Industrial Bank of Korea (IBK) to provide low-interest loans to local businesses.

Low-Income Loan Assistance Process



Financial Assistance

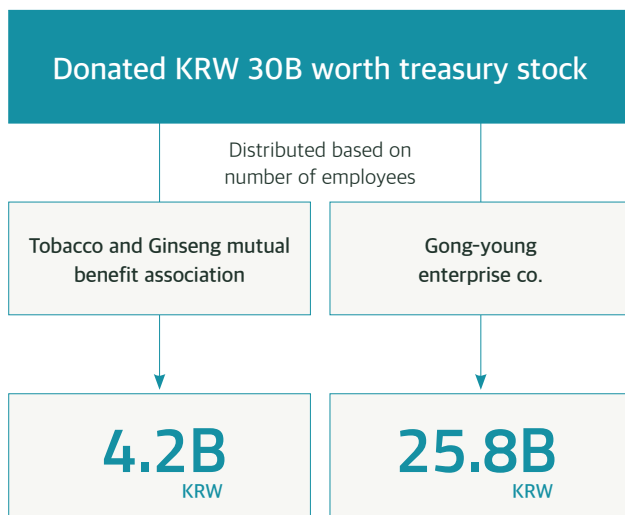
KT&G operates various financial assistance programs for farmers or other suppliers.

We settle invoices by cash payment within 5 business days of the next month, and we also encourage our primary suppliers to pay secondary suppliers by 25th of the next month. In 2019, we aided suppliers by providing KRW 45.9 billion of early payment. In addition, we endeavor to relief suppliers' financial burden by increasing purchase order amount when they suffer from changes in product costs such as raw materials.

Welfare Supports to Cooperative Small Enterprises

In 2019, we donated treasury stock and performed Win-Win Growth activities for the Tobacco and Ginseng mutual benefit association and Gong-young enterprise co., operating partners of our main business.

Cooperative Small Enterprises Supports



3. Shared Value Creation

Purchase of Tobacco Leaves from Farms

Since 2001, the manufacturing monopoly of tobacco companies has been prohibited and obligation to purchase tobacco materials from domestic suppliers has been discontinued. However, KT&G purchases entire amount of tobacco leaves from domestic suppliers. The annual amount is about 10,000 tons which is equivalent to KRW 80 billion to 90 billion, and this is contributing to domestic farmers to cultivate tobacco stably.

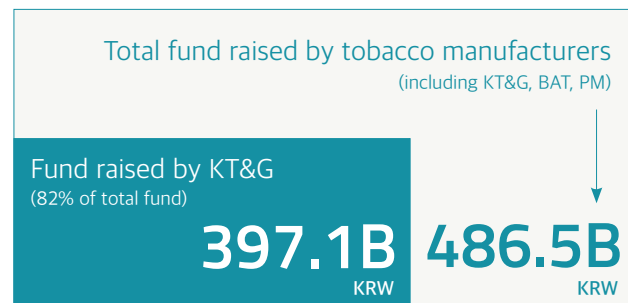
2019 Purchase

Farmers	Tobacco	Payment
2,880 persons	10,214 tons	96.5B KRW

Supporting Stability of Tobacco Production

KT&G contributes to fundraising of the 'Tobacco Production Stabilizing Foundation' to enhance productivity and economic/social status of farmers. One of KT&G's directors is nominated as a director of the foundation to engage in fund operation. Therefore, we are helping the stabilizing of the domestic tobacco production.

Fundraising Performance (2002 - 2019 Cumulative)



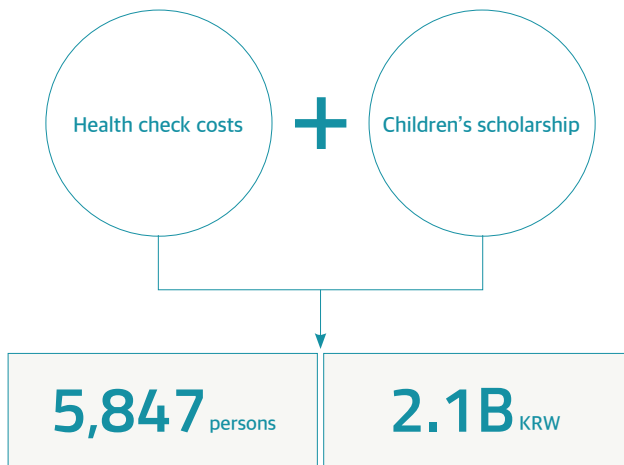
Promoting Two-way Communication with Tobacco Farms

KT&G identifies and improves issues found through the two-way communication with tobacco farms. In 2018 and 2019, we purchased tobacco materials from farms to relieve their issues of insufficient storage space for tobacco. In 2020, we resolved lack of workforce in tobacco farms by enhancing production efficiency of the hand-packaging process. Moreover, we are implementing profit increase for farmers and reduction of packaging materials.

Activities for Supporting Shared Growth of Tobacco Farms

KT&G performs various assistances to enhance life quality of tobacco farms. We pay 30% of payment earlier between April and May to reduce their financial burden. The rest will be paid from September to December after the tobacco leaves harvest. In addition, we provide costs for health check and scholarship for farmers' children to enhance welfare of the tobacco farmers. Along with the financial support, we help tobacco farms through employees' volunteering in harvesting tobacco leaves.

Financial Assistance to Tobacco Farms



Health check assistance and children's scholarship



Tobacco leaf harvest volunteering

Assisting Extra Income of Tobacco Farms

KT&G operates the Haearin Project of assisting cultivation and harvest of peppers for tobacco farms as a means to create extra income using the existing farmlands and technologies. In 2019, we signed a contract with 20 farmers and helped sales of KRW 158 million worth dried peppers. We plan to continue the extra income creation projects to diversify income sources of tobacco farms.

Extra Income Sales Support (Haearin Project) in 2019

Farmers	Amount of dried red pepper purchased	Purchase amount
20 persons	10,488 kg	158M KRW

4. Supplier Communication

KT&G runs the KT&G Advanced Procurement System (KAPS) which is an information sharing system with suppliers in order to enhance transparency and efficiency in the purchase process.

Supplier Communication through KAPS

Category	Details
Approach to purchase	• Access the overall purchase process (bidding, contracting and purchase order, product examination and service, payment request, and stock management)
Communication	• Send notices through the message board of KAPS • Report any unethical actions of KT&G employees through the whistleblowing channel, Sinnungo
Transfer of Ethics Management	• Share the 'KT&G Ethical Management Directions' • Encourage execution of the 'KT&G Ethical Practice Special Clause' when signing contracts • Post the 'KT&G Purchasing Principles'

PRIORITY AREA

Better Work Place

2019 CASE STUDY

SangSang Realization Committee



Since 2015, KT&G has operated the 'SangSang Realization Committee' composed of the CEO and younger employees to enhance the organizational culture based on voices of employees. The committee constitutes CEO as the chairman, 10 members representing employees, and 19 insitutional committees including sales organizations and tobacco plants. The committee identifies and realizes ideas for improving organizational and communicational cultures. The implemented ideas include an employee lifecycle and family care program, 'Gah-wamansasung', a group-wide teamwork improvement program, 'In-company Athletic Club Competition', and a sharing office for business travelers, 'Station Room'. Moreover, the committee provides business proposals for strengthening

business competitiveness. To improve the organizational culture and facilitate communication, KT&G will continuously apply innovative plans derived from the committee which has become a unique corporate culture platform for communication.

1. Talent Management

Talent Principle

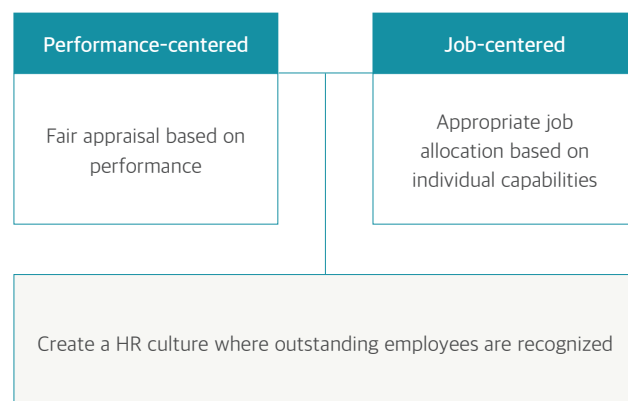
Employees are a valuable asset and future of KT&G, and value creation and capacity building of the employees enhance competitiveness of KT&G. We value potentials of talents rather than the current state and foster the right people for our talent principle, 'I am C.E.O.'.

CHALLENGE - A talent who do not give up	
A person who challenges relentlessly with passion and tenacity for the company's growth and change	<ul style="list-style-type: none"> • Strong passion and tenacity for growth • Create thinking and relentless challenge • Leader of changes and innovations
EXECUTE - A talent who strives to generate performance	
A person who finds the most effective method to achieve the goal through the correct acknowledgement of issues	<ul style="list-style-type: none"> • Decision making based on facts • Swift execution and outcome creation • Attitude to be responsible
OPTIMIZE - A talent who cooperates mutually	
A person who communicates and cooperates with every coworker with the gratitude to everyone	<ul style="list-style-type: none"> • Consideration of us than myself • Collaborate with all members • Respect diversity with open communication

HR Philosophy

KT&G operates the Talent Development and Management System based on the HR Management System focused on performance and duty. In particular, we evaluate employees' performance centered on duties according to the Career Development Plan (CDP). This enables employees to enhance their values and have job satisfaction. Moreover, we prohibit discrimination based on gender, education, origin, and disability and strive to employ a wide variety of employees. So, we are diversifying the recruitment methods and channels and running job creation systems such as additional points for the disabled and open recruitment for high school graduates.

HR Philosophy Process



2. Human Rights Protection

Respecting Employees' Human Rights

KT&G supports international initiatives such as the Universal Declaration of Human Rights, ILO Declaration, and UN Global Compact, in order to respect human rights and prohibit any human rights violations in the business activities, and established regulations to comply with relevant laws and regulations in local countries. In particular, we declared prevention of abusing human rights such as respecting basic rights, offering fair opportunities, and prohibiting discrimination in the Chapter 6, 'Company's Ethics on Employees' of the 'KT&G Charter of Ethics'. We also conduct training for all employees annually to create a culture of complying with the charter. In 2019, we provided training on preventing workplace harassment and improving awareness of disability, thereby enhancing the awareness standard of human rights. In the future, we will strengthen the company-wide screening of human rights impacts and establish relevant management process.

Scope of KT&G Human Rights Policy

Prohibition of Forced and Child Labors
Compliance with Working Hours
Providing Freedom of Association
Humanitarian treatment

Employee Human Rights Impact Management System

Issues	Impact Management and Prevention Program
Guaranteeing freedom of association and collective bargaining	<ul style="list-style-type: none"> Conduct collective bargaining annually Hold the Labor-Management Agreement quarterly Notify the result of collective bargaining through intranet
Prohibiting discrimination in employment and work	<ul style="list-style-type: none"> Diversify employment methods and channels and monitor discriminant factors in the employment process Conduct meeting individually after appraisal and operate dissent procedures
Enhancing working condition	<ul style="list-style-type: none"> Manage through network shut-off and PC-off system Operate the job-sharing model 1·3·5 Campaign
Preventing workplace harassment	<ul style="list-style-type: none"> Establish the workplace harassment treatment process and request employees' pledge Conduct training on all employees In-company campaigns

Responding to the Prohibition against Workplace Harassment

The Labor Standards Act amended in 2019 stipulates companies to perform annual training to prevent any behaviors that harasses physically and mentally and aggravates work environment by abusing authority or relationship. Therefore, KT&G provided online training for prevention of workplace harassment to every employee in 2019. Moreover, we established the guideline for 'Preventing and Treating Workplace Sexual and Other Harassment' and enforced employees to sign pledges to enhance their consciousness of the issue. Starting in 2020, we will constantly receive voices of employees and facilitate internal campaigns by developing surveys in order to prevent workplace harassment.

Reducing Working Hours

KT&G have established the suitable work system according to the changes in business environment and strived to reduce worktime for employees. In 2017, we began establishing the infrastructure for the 52-hour workweek scheme and created the fixed worktime culture by introducing the network shut-off and PC-off system.

In addition, we introduced the flextime and new leave of absence system considering business areas based on the labor collective agreement.

In the sales and manufacturing fields, we established the job-sharing model reflecting the characteristic of business to realize the reduction of working hours. In the sales area, we placed substitute workforce for holidays, and in the manufacturing plants, we fostered multi-functional workforce to invigorate annual leave system. Moreover, we are actively executing activities for enhancing work efficiency and engagement in order to reduce worktime. In 2019, we executed the '1·3·5 Campaign (5 promises to make our work and life happy)' that encourages clear work orders and enhanced work engagement to improve working method.

KT&G endeavors to increase job efficiency and achieve work-life balance by operating system related to working hours and compensation.



1·3·5 Campaign Posters

3. Labor Union

KT&G respects employees' freedom of association indicated in the International Labor Organization (ILO) Declaration and domestic labor law, thus assuring free activities of the Labor Union. KT&G Labor Union was founded in 1958 followed by the standard of the Monopoly Bureau Labor Union Federation. As of 2019 year-end, 3,604 members (89.6%) out of 4,023 qualified members are registered in the Labor Union. We conduct collective bargaining every year and hold the Labor-Management Agreement every quarter to discuss about various agenda including HR and wage, welfare system, industrial safety, and social contribution. In accordance with the Article 94 (Employment Stabilizing Committee) of the collective bargaining, we assign same number of members between 5 and 10 in the Employment Stabilizing Committee. In addition, as the two pillars for business management, the labor-management of KT&G is building a collaborative culture based on mutual understanding and trust. Through this culture, we have continued bargaining agreement without dispute since 1989, and both parties strive to achieve stable employment and welfare expansion for employees.

Labor Union

No. of Members	3,604
Membership Rate	89.6%

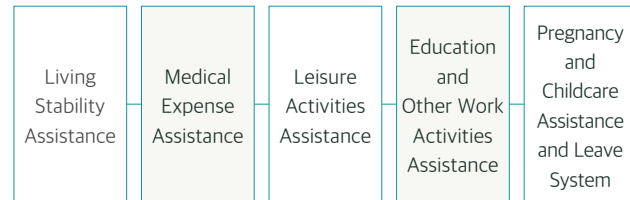
4. Appraisal and Compensation

KT&G performs systematic appraisals and reasonable compensation based on performance appraisal so that employees are encouraged. The appraisal is conducted according to the process standardized from the HR Management Regulation for transparent and fair evaluation of performance and capacity. Moreover, we offer tailored coaching and mentoring system for performance. We share the appraisal results transparently and operate the dissent system to enhance fairness. The compensation is provided based on the appraisal results, and new recruits receive equal compensation regardless of gender or job type. In 2019, the basic pay of college graduates was set as 191% of the legal minimum wage of Korea.

5. Welfare System

KT&G runs the welfare system to assist employees to enhance quality of life and achieve work-life balance. We established the welfare system customized for employees' life cycles depending on their age and work experience, as well as for employees' families.

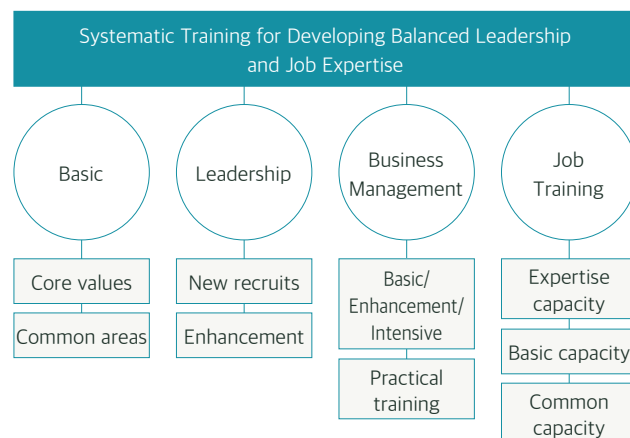
Welfare System by Area



6. Employee Training

KT&G pursues job experts and global talents who lead changes and innovation and creates new values in order to realize the corporate vision of an internationally recognized company. Therefore, we established the capacity building roadmap and offer systematic training to nurture talents. Employees of KT&G are growing into leaders creating performance based on understanding of job expertise in various areas.

Company-wide Training System



Core Value Training

We operate various training courses to understand the core value of KT&G Way and apply in the way of working for employees. Ultimately, KT&G Way is a standard for all employees' thinking and actions to propose directions for sustainable growth.

Leadership Training

This program aids employees to acknowledge roles of each position and design visions and to cultivate knowledge for understanding strategies and business management. It establishes the leadership model and internalize the leadership development process to foster future leaders systematically.

Business Management Training

Based on the theoretical learning of MBA, the program is operated in each level to strengthen strategic project management competences. Moreover, we operate practical working courses to fortify design capacity of employees.

Job Training

This program is designed to self-inspect job capacities and set and execute capacity building plans, and it offers intensive training courses in each area for nurturing job experts. We developed the microlearning¹⁾ contents to enable employees to learn about field work at any time.

2019 training hours per employee	124 hours
2019 training costs per employee	KRW 1.39M

1) Short and concise contents that are effective in learning core contents

Supporting Voluntary Capacity Building

KT&G creates spaces and operates various programs for employees to voluntarily strengthen their competences. We offer e-learning-based reading and established the 'SangSang Maru' which is a mini library for employees. Moreover, we run various cultural programs to expand opportunities for enjoying cultural activities at work. The programs include book concerts, exhibitions, and engaged arts programs, and these are offered quarterly.

7. Training and Assistance for Retirees

KT&G runs a system to support employees' 2nd life after retirement and offer tailored information. We reemploy outstanding retirees with experience techniques and experiences in the manufacturing, and we reemployed 31 retirees in 2019. Some of these reemployed employees are dispatched overseas plants to facilitate operation and assist capacity building of local employees. In addition, we conduct training on expected retirees each year. This training is provided quarterly, and a total of 96 employees were trained in 2019. The training includes lectures from retirement experts about planning post-retirement and relevant information. We believe that retirees can plan their post-retirement life systematically through these programs.

8. Communication Channels between Employees and Company

In 2015, KT&G established the Cooperative Department in charge of the corporate culture and internal communication. This department facilitates communication among employees and between employees and the company. Moreover, we operate the 'SangSang Realization Committee' composed of young employees for improving the corporate culture. Through the committee, we are creating a corporate culture that reflects voices of employees.

In addition, we also conduct online communication actively. The 'Idea of KT&G' page on the intranet is a board to post various opinions of employees anonymously. We reflect employees' opinions in the business management and also provide answers to their inquiries. We utilize other channels to share key issues and internal information to employees.



In-company Library, 'SangSang Maru'



Book Concert

Worksite Safety & Health

2019 CASE STUDY

Investigating Causes of Musculoskeletal System Disorder

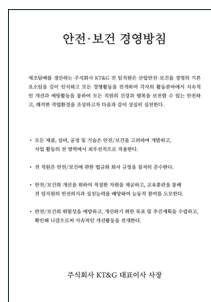
KT&G conducts investigation of musculoskeletal system disorder causes every 3 years to enhance health of employees. The investigation has been continued since 2004, and we promote activities to reduce risk factors of burdened work based on the investigation results.

In 2019, we received consulting from external hospitals and implemented corrective actions in the 2 worksites (flavoring and unpacking process) with high risk factors of musculoskeletal system disorders. The flavoring process is improving methods for transporting favor materials, and the unpacking process improvement will commence after the flavoring process is corrected. In addition, we arranged shifts for high-risk workers from repetitive musculoskeletal burden labor, as well as break time, stretching exercises, and safety training.

1. Worksite Safety Management

Safety & Health Management Guideline

KT&G established the 'Safety & Health Management Guideline' to enable employees to work in a safe and pleasant environment. The guideline is used to spread the awareness of industrial safety and health as a basic factor of the business management, and it also encourages constant improvement and prevention of safety and health factors.



Safety & Health Management Guideline

Disaster and Accident Management

KT&G manages disasters and accidents of workers by monthly, daily, hourly, job position, work experience, and age. Under the goal of 'Zero Accident', we are preparing disaster and accident prevention plans and conducting prevention activities. In particular, we shared the 3 general accidents (According to Korean Occupational Safety and Health Act, accidents are divided into major accidents and general accidents. The accidents occurred in 2019 were all general accidents.) cases occurred at manufacturing plants in 2019 to all worksites, and we are implementing the Safety Activity Plan for preventing recurrences. Starting in 2020, we will secure fundamental stability by eliminating risk factors through facilities improvement and continuously strengthen disaster preventive activities through relevant education and training. Furthermore, we will not only fortify preventive measures for periodic vulnerable disasters such as fire that has high occurrence rate in winter and spring seasons and traffic accidents when getting to or leaving workplace, but also expand rewards for worksite with outstanding performance of disaster reduction and employees excellent in preventing disasters to actively motivate them toward disaster-free environment.

Status of Disasters and Incidents Occurrences

Category	Unit	2017	2018	2019
Industrial accident rate (No. of industrial accidents / No. of workers X 100)	%	0.021	0.042	0.062
Operation hold rate (No. of industrial accidents / Total working hours X 1,000,000)	%	0.101	0.206	0.299
Total working hours	hours	9,806,070	9,454,656	9,828,048
Lost time days	days	272	130	390
Lost time day rate (Lost time days / Total working hours X 1,000)	%	0.028	0.014	0.040

*Including laborers and temporary employees

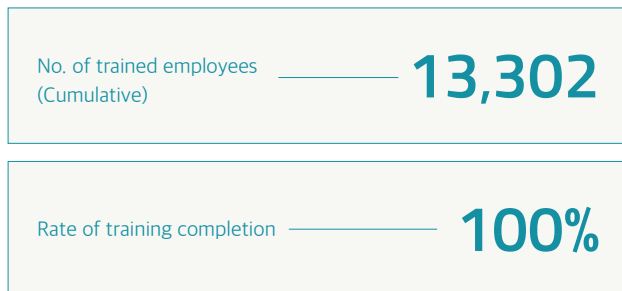
Industrial Safety & Health Committee

KT&G holds the Industrial Safety & Health Committee composed of equal number of persons from labor and management at each manufacturing plant. The committee deliberates key items about safety and health and take corrective actions for any harmful or risk factors at worksites. In 2019, we held 1 ad-hoc meeting and 4 regular meetings, and the results of committee meetings were shared to all employees. The main agenda included establishing the industrial safety and health management plans, reviewing plans for improving lighting at worksites, and investigating risk factors of musculoskeletal system disorder. In the future, we will utilize the safety & health suggestion box to apply opinions of workers related to industrial safety and health.

Employee Safety & Health Training

KT&G conducts safety & health training on employees quarterly. In 2020, we will avoid group training due to COVID-19 but provide online training for high-risk processes.

Safety & Health Training in 2019



2. Enhancing Employee Health

Healthcare Office

KT&G runs the in-company Healthcare Office. In accordance with the Occupational Safety and Health Act, the Healthcare Office is located in a easily accessible, well-ventilated, and well-lighted place. The office is equipped with emergency medicines that can be purchased without prescriptions and records any allergies or side effects before and after the medication. Moreover, the relevant administrators are in place to manage medicine stocks and patient status. A nurse is stationed in the Healthcare Office to conduct health checks, consultations, emergency first aids, medication, health training, and work environment improvement.

Health Checks

KT&G performs complete medical examinations on employees in addition to the regular health checks provided by the NHIS, in accordance with the welfare system. Moreover, we also provide special health examinations for plant workers due to risk factors. After the examination, we analyze individual results and perform post-management including chronic disease prevention, diet, and exercise.

Health Improvement Program

KT&G conducts activities to enhance physical and mental health of employees. In 2019, we evaluate cardiovascular disease risk factors in lifestyle and health conditions. This enabled us to predict potential cardiovascular diseases and take post-management. In addition, we collaborate with health centers and relevant institutions to assist sound drinking habits and mental health consultations.

Health Check Types

Category	General check	Complete check	Special check
Frequency	<ul style="list-style-type: none"> Non-office workers: Annually Office workers: Biennially 	<ul style="list-style-type: none"> All employees: Annually 	<ul style="list-style-type: none"> Noise, dusts: Within a year after dispatch Organic solvents: Within 6 months after dispatch
Targets	<ul style="list-style-type: none"> All employees Spouses aged 40 or older 	<ul style="list-style-type: none"> All employees One family member 	<ul style="list-style-type: none"> Field workers (each plant, R&D center)
Details	<ul style="list-style-type: none"> 14 items including chest X-ray 	<ul style="list-style-type: none"> 41 items including abdominal ultrasound 	<ul style="list-style-type: none"> By risk factor

Customer Satisfaction

2019 CASE STUDY

Operating customer sympathy services



KT&G introduced the Visiting A/S as the first in-visit consultation and treatment in the industry to enhance service quality and customer satisfaction. Moreover, we introduced the parcel service for customers residing in the isolated region to execute customer service. Furthermore, we extended NGP-related communication channels including 'lil Minimalium' and 'lil Station' according to the increase in Voice of Customer(VOC) about NGP. In 2019, customers most frequently used 'Visiting A/S (38.6%)' and 'lil Station (35.7%)', and we were able to confirm customers' preferences to new channels.

We plan to enhance customer convenience and service quality continuously through differentiated customer services. Based on these efforts, we will realize customer sympathy service.

1. Customer Communication

Communication Channels

KT&G operates the CS center (call center) for general consultations and claims, lil website for brand introduction and 1 on 1 consultation, and lil Minimalium for product inquiry and purchase. Customers can visit A/S centers and lil stations to get services without running through CS centers.

Customer Communication Channel

Category	Role	No. of Stations
CS center (call center)*	General consultation and claims receipts, A/S parcel service (isolated areas only)	1
Online	Website	1
Offline	lil Minimalium	8
	A/S center	17
	lil Station**	40
	Visiting A/S	121
Total		188

*Including ARS, 30 call center representatives

** Mobile A/S centers at convenience stores

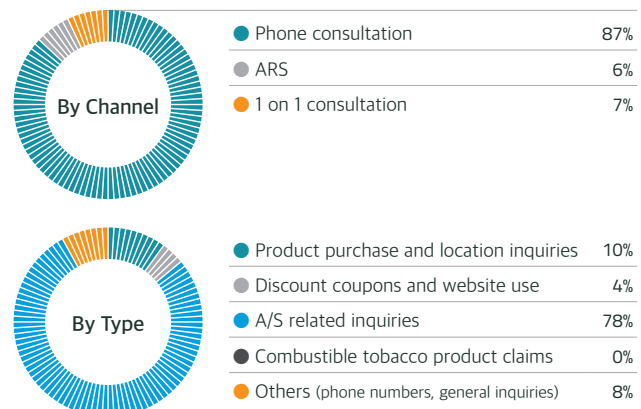
VOC Management Process

Customers' general inquiries and consultations are initially responded through the CS center, and if A/S is needed, we direct them to separate channels such as A/S center, lil Station, and Visiting A/S. A/S center and lil Station can be accessed for services without going through the CS center.

VOC Status

KT&G receives VOC through various channels and manages them by type. We reflect VOC into our managerial activities to improve product competitiveness and enhance customer satisfaction through follow-up actions.

VOC Receipt Status



2. Customer Satisfaction Improvement

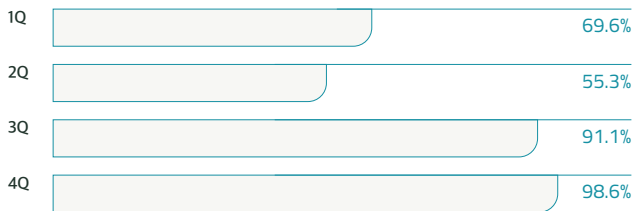
Customer Satisfaction-related Awards

KT&G collaborates with the Marketing headquarters, R&D headquarters and Manufacturing headquarters to enhance quality and customer satisfaction continuously. As a result, we were awarded the 'This Year's Electronic Award 2019' hosted by the Korea Consumer Brand Committee.

Strengthening Customer Inquiry Response Capacity

Since the launch of lil in 2017, customer inquiries and consultations have increased vastly. Therefore, we increased number of CS representatives, introduced ARS, and improved the response-to-CS representatives rate from 69.6% (1Q 2019) to 98.6% (4Q 2019), thereby enhancing customer satisfaction.

2019 VOC Response Rate



*Response rate: No. of response calls (No. of representatives' calls) / No. of received calls (No. of customer calls to call centers)

Trade-in Sales Service

As a CS program, we have introduced the Trade-in Sales Program since 2018 to allow customers to return old editions of lil products to get discounts for the new versions. Moreover, we also offer product cleaning service to visitors to service centers.

Infrastructure of CS Management

KT&G plans to start conducting regular consultation survey in July 2020 to enhance quality of the customer consultation service, as a part of the CS Management. The survey will be provided quarterly to 10,000 respondents in regard to consultants' hospitality and issue solving, and we will use the survey results to take corrective action plan and develop customer services.

Consumer Damage Compensation

KT&G regulates the consumer damage compensation procedure for products and services. The claims are categorized into emergency and priority levels to decide on treatment method after discussing them with relevant departments.

3. Customer Privacy Protection

Personal Information Protection Policy

KT&G complies with the Act on Promotion of Information and Communications Network Utilization and Information Protection, etc. and the Personal Information Protection Act and acquired the Personal Information & Information Security Management System (ISMS-P) and ISO 27001 certifications. Moreover, we share details about collection, storage, use, and discard of all personal information collected by us through the Personal Information Treatment Method.

Enhancing Personal Information Protection Capacity

KT&G recognizes cybercrimes and personal information breaches as the risks of information protection. Therefore, we established the Information Security Regulations and Operational Guidelines, as well as the response manual to breaches, to define the reporting system by incident type and incident response manuals. Moreover, we operate various programs to strengthen employees' competences in personal information protection.

In addition, we established the Information Protection System and operate the Security Monitoring Center to prevent breaches personal privacy caused by external invasions and internal leaks.

Based on the company-wide efforts for protecting personal information, we have not had any breaches in personal privacy in the past 5 years.

Information Protection Programs

Category	Details
Education and training	<ul style="list-style-type: none"> Amend information security policies and procedures (annually) Security training on new recruits (regularly) Legally obligated training on employee information security and personal privacy protection (more than once a year) Mock hacking training for employees (more than once a year)
Monitoring	<ul style="list-style-type: none"> Monitoring of information protection compliance (regularly) Operation of information protection system and security monitoring for external invasion and internal breach (regularly)
Campaign	<ul style="list-style-type: none"> Strengthening employee security awareness by operating 'Information Protection Inspection Day' (monthly)

Social Contribution

2019 CASE STUDY

Assistance to Coffee Lab Indonesia



Indonesia is the world's 4th largest coffee producer followed by Brazil, Vietnam, and Columbia. More than 650,000 tons of coffee is produced annually, and it is considered the most important industry in the country. Indonesian Government has been implementing the 'Coffee Industry Nurturing Project' since 2018 to develop the industry. Since 2012, KT&G has performed global corporate social responsibility (CSR) activities in Indonesia through the overseas volunteer group and SangSang Univ. ('SangSang' is Korean pronunciation which means 'imagination' in English). In 2019, we decided to support the Indonesian Government in the 'Coffee Industry Nurturing Project', and we signed the 3rd MOU with the government and an international relief development NGO for funding the Indonesian coffee vocational training school, 'Coffee Lab' on August 27, 2019 to further expand CSR activities in Indonesia. According to the MOU, we plan to create jobs for the youth in the coffee industry of Indonesia by developing relative training, hosting workshops for vocational school teachers and workers, and assisting the youth to acquire international barista certificates. KT&G will perform differentiated social contribution activities by expanding global CSR activities that can enhance sustainability of beneficiary countries.

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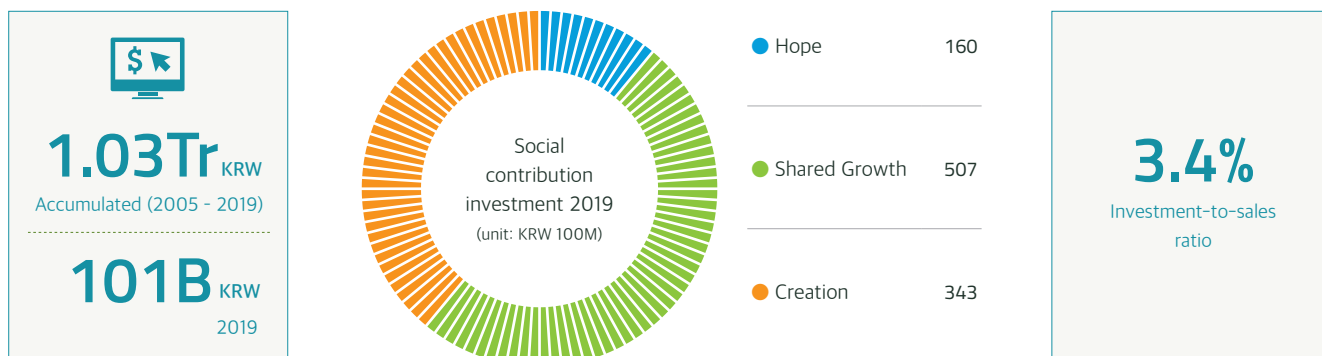
1. Social Contribution Strategy

Social Contribution Activities

KT&G actively promotes social contribution activities based on the SangSang Platform* to realize the business philosophy of 'Together Company'. We fulfill our responsibility as a corporate citizen, lead shared value creation, and pursue sustainable growth of the company and society. KT&G, under the slogan of 'We imagine (SangSang) a better tomorrow' and based on the 3 core values, 'Hope', 'Shared growth', and 'Creation', conducts various social contribution activities. We strive to build a happy society by actively implementing activities such as social welfare, scholarship, youth startup assistance, employee donation and volunteering, social responsibility project, and cultural arts support projects.

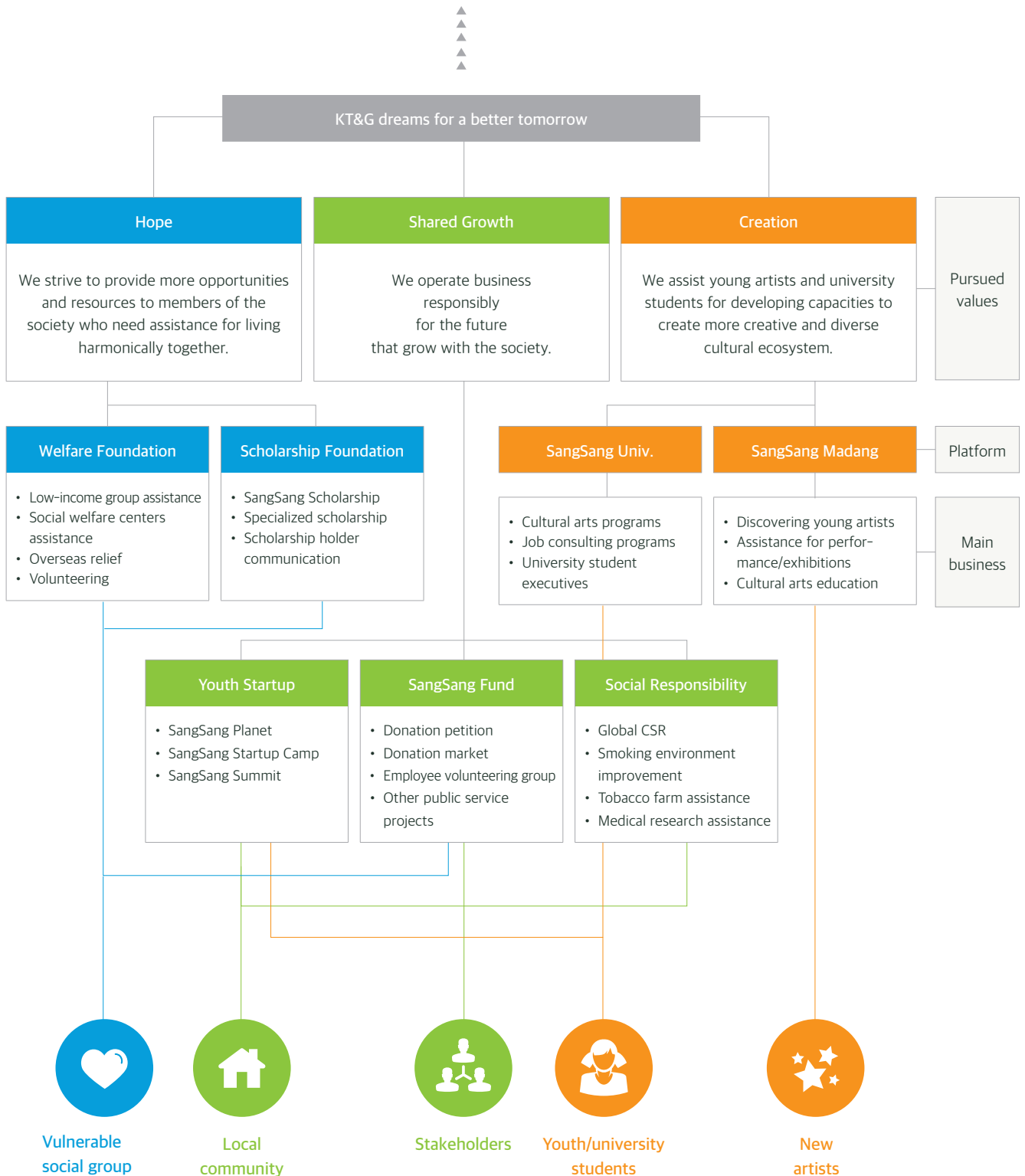
*SangSang Platform: Facilities and organizations including SangSang Madang, SangSang Univ., and SangSang Fund established by KT&G to conduct social contribution business

Social Contribution Investment 2019



The Way of Social Contribution

Sustainable Growth of the Company and Society



2. Hope

KT&G runs the social welfare business and scholarship business to deliver the value of 'Hope' to the society. We established the Welfare Foundation in 2003 to support the vulnerable social group financially and emotionally. The Scholarship Foundation created in 2008 operates the total-care system from middle and high schools to university to relive the inequality in educational opportunities.

Welfare Foundation

KT&G Welfare Foundation aims to 'realize the advanced welfare to share happiness with everyone'. Thus, we are providing financial aids and welfare institution assistance to the vulnerable social group such as children, elderly, and disabled persons, as well as the emotional support projects such as music, arts, and education for enhancing life quality and standard. In addition, we are participating in solving social issues through the overseas relief projects to fulfill our responsibility as a global corporate citizen.

Business Type	
Low-income group assistance	Living assistance to the vulnerable social group including children of low-income family and elderly
Social welfare center assistance	Vehicle assistance to nationwide welfare centers
Overseas relief	Improvement of educational environment such as establishing elementary schools and libraries
Domestic volunteering	Facilitating volunteering such as domestic/overseas talent sharing and environmental activities

Scholarship Foundation

KT&G Scholarship Foundation conducts various businesses to offer stable educational opportunities to the educationally neglected group.

We provide scholarships to middle and high school and university students, as well as those in special educational environment such

as arts and athletics, overseas students, and juvenile released from jail. Through these activities, we expect outstanding talents to continue pursuing their hope even in the difficult environment.

Business Type	
SangSang Scholarship	Educational assistance to the vulnerable social group with outstanding academic performance
Specialized scholarship	Support to students in special educational environment including arts and athletics
Scholarship holder communication	A community platform among scholarship holders such as SangSang Scholarship Camp

3. Shared Growth

KT&G considers 'shared growth' with the society as an important value and strives to create social values by developing with the local community. The 'Youth Startup Support Business' provides a foundation for the youth to dream the future and provides funds raised from the 'SangSang Fund' which is created by employees' engagement to where needed. Moreover, we also conduct various global CSR activities related to our business to take a role as a global corporate citizen.

Youth Startup

The 'SangSang Startup Camp', one of the representative KT&G Youth Startup Business programs, is a program that assists start-up of young generation who aim to become a socially innovative entrepreneur. By discovering and fostering passionate social innovation startups who strive to solve various social issues, we pursue creating social impacts for a better world while contributing to job creation.

'SangSang Startup Camp' is a 14-week program including 8 weeks of beginner's track and 6 weeks of development track. Through the mentoring by coaches composed of former and current entrepre-



Ceremony for Donating Cars to Social Welfare Centers



SangSang Scholarship Camp

neurs, we aid their fast growth. We offer financial assistance, office spaces, and benchmark opportunities to the outstanding teams and plan to provide more systematic assistances including 'SangSang Summit' which is a forum of social innovation experts and 'SangSang Planet' which an exclusive space for youth startup opened in the Social Venture Valley in Seongsu-dong in 2020.

Business Type	
SangSang Planet	Space exclusive for youth startup
SangSang Startup Camp	Program for launching social innovation startups
SangSang Summit	Social innovation expert forum

SangSang Fund

SangSang Fund is raised through a matching grant* with KT&G employees' engagement. Employees voluntarily donate partial wages, and KT&G matches the same amount of donation. SangSang fund has been in place since 2011, and the fund is executed after the decision made by the 'SangSang Fund Operational Committee' composed of employees. The fund is used to support the vulnerable social group and to solve social issues. In particular, employees are able to propose where to donate the fund in order to encourage their active engagement.

*Matching grant: A fund that a company matches the amount raised by employees

Business Type	
Donation petition	Employee proposal donation program
Donation Market	Employee engaged donation program
SangSang Together	Employee volunteering

Social Responsibility

Global CSR

As the global business size has expanded, KT&G set mid- to long-term strategies and conducts business by stage to fulfill social responsibility as a global corporate citizen.

In particular to solve issues in developing countries such as poverty, living residence, education, and environmental issues suggested by the UN Sustainable Development Goals (SDGs), we are assisting to improve living environment and independence of the poor in developing countries and implementing various global social contribution projects by dispatching the overseas volunteering group. KT&G conducts global CSR activities in Indonesia, Vietnam, Myanmar, and Cambodia and plan to expand the scope continuously to the target countries.

Countries	Main CSR Activities
Indonesia	<ul style="list-style-type: none"> SangSang Univ. Coffee Lab assistance
Cambodia	<ul style="list-style-type: none"> Establishment of elementary school libraries Improving educational environment
Vietnam	<ul style="list-style-type: none"> Establishment of elementary schools Improving medical facilities
Mongolia	<ul style="list-style-type: none"> Ecosystem rehabilitation activities such as planting trees Cultural exchange activities

Indonesia CSR Activities

In Indonesia, KT&G has created about 900 new jobs annually since 2016 and contributed to the Indonesian economy by purchasing tobacco leaves and materials. Moreover, we conduct various social contribution activities to fulfill our responsibility as a member of the local community.

In particular, we operate the 'SangSang Univ.' program at major universities in Jakarta and Surabaya to develop competence of the youth and enhance cultural exchange between Korea and Indonesia. Through the program, we offer various opportunities for experiences



SangSang Startup Camp Performance Presentation: The Debut



SangSang Fund Hope Food Truck

and exchange through classes related to cultural arts, hobbies, Korean language, and career that they cannot access easily.

In 2019, we began supporting the 'Coffee Lab' which is a vocational school for coffee to aid job creation for the youth. In addition, we are providing emergency relief for natural disasters and epidemics, social infrastructure development for the poverty, volunteering groups, and global scholarship business. As of the end of 2019, we have put accumulated KRW 5 billion to enhance Win-Win Growth with Indonesia.

Smoking Environment Improvement

KT&G endeavors for social responsibility related to the business, and we are promoting a business for improving smoking environment to solve the issues related to indirect smoking. Through the VOC channels of local governments and public institutions, we have embraced the opinions for lack of smoking places, thus have installed about 300 smoking areas nationwide until 2019, and we are also conducting activities for enhancing awareness such as the Smoking Manner Pictogram Campaign.

Through the smoking environment improvement, we expect to create a matured culture where both smokers and nonsmokers respect each other mutually.

Medical Research Support

KT&G continues to the medical research support to enhance the public health. We sponsor research activities for investigating causes of cancer and developing new cures, as well as projects for preventing minors' smoking and solving mental health issues.

4. Creation

KT&G creates a better society through the creation in cultural arts. We run SangSang Madang and SangSang Univ. to build a create and various cultural ecosystem. SangSang Madang provides opportunities to communicate between the local community and new artists in various genres such as performance, movie, and exhibition. SangSang Univ. assists younger generation's growth by operating cultural arts classes and programs.

SangSang Madang

'SangSang Madang', which has been operated as a part of the Mecenat* activity since 2007, is a representative comprehensive cultural arts space of Korea that has about 1.8 million visitors annually. SangSang Madang locations in Hongdae, Nonsan, Chuncheon, and Daechi have become places for communication and exchange between cultural creators and consumers based on each of unique characteristics. In 2020, we will create a new SangSang Madang in Busan to support culture and arts in the local community of Busan.

*Mecenat: Companies' activities contributing to social contribution and national competitiveness by actively supporting culture and arts

SangSang Madang Business Area and Main Programs

Business Areas	Details
Performance	Discovering musicians
Movie	Distributing independent movies
Exhibition	Supporting fine photography
Education	Nurturing talents in culture and arts
Design	Assisting distribution of independent designers' products

SangSang Madang History



Global CSR Activities



Smoking Room Installations

SangSang Univ. History

**Hongdae**

A comprehensive culture & art space in an urban area

**Nonsan**

A culture & arts experience space in nature

**Chuncheon**

A meeting between ART (art center) and STAY (lodging space)

**Daechi**

A multipurpose venue for the public cultural arts

**SangSang Univ.**

SangSang Univ. is an integrated community that helps the youth's imagination to be realized as a social value creation. To support healthy life of the youth who are a basis of culture, we offer opportunities of learning, exchange, and sharing in various areas including culture, arts, life, and career.

In each region, we offer customized assistance by college club, operate main programs under the theme of 'Health life of the youth who are a basis of culture', and recruit a college student executives group, 'SangSang Friends', thereby creating SangSang Univ. that is managed by the youth. In accordance with the 3 design models of SangSang Univ., we operate main programs that connects socially, participate in the society voluntarily, and step up.

SangSang Univ. Design Model and Main Programs

Model Name	Structure	Main Programs
C Model (Connect)	Value creation through multilateral connections	<ul style="list-style-type: none"> SangSang Univ. Fashion Runway Busan Fashion Show
S Model (Step-up)	Recruitment of tournament participants, mentoring assistance by experts	<ul style="list-style-type: none"> SangSang Marketing School University Singing Contest DJ festivals
V Model (Voluntary)	Design and operation directly by participants	<ul style="list-style-type: none"> Rundry Marathon Donation Run



SangSang Madang SangSang Realization Festival



SangSang Univ. Fashion Runway

Advanced Governance to the Global Standard

GOVERNANCE

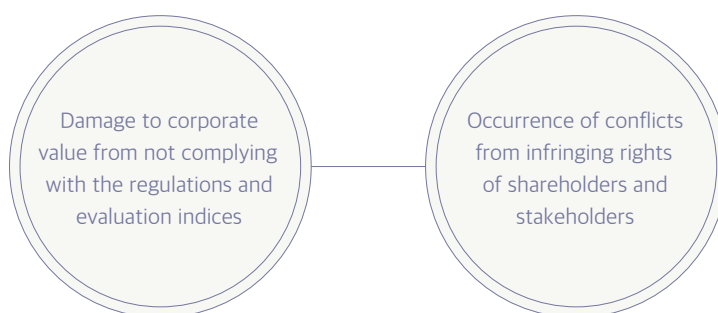




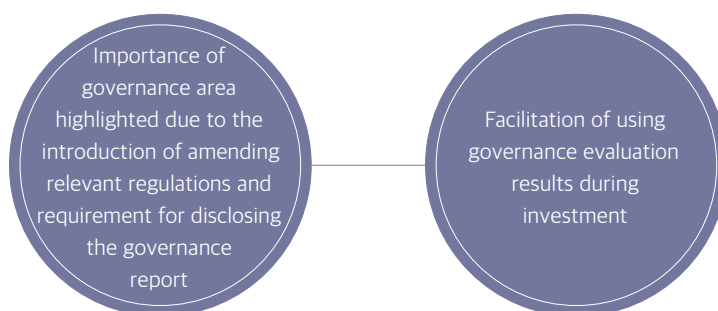
GLOBAL MEGATREND

Establishing a sound governance is an important factor in companies' efficiency and competitiveness. It is essential to secure expertise and independence of the board of directors for maximizing stakeholder values, and based on this, companies need to propose sound alternatives for reasonable decision making of the top management. Moreover, as both domestic and overseas requirements for disclosures related to governance have expanded, we need to enhance managerial transparency by continuously improving governance, thereby protecting stakeholders' rights and interests.

RISKS



OPPORTUNITIES



APPROACH

KT&G established the responsible managerial system centered on the board of directors controlled by outside directors and considers compliance with laws and ethical standards a top priority for all its businesses. We will strengthen schemes to maintain the governance that emphasizes balanced benefits of all shareholders and stakeholders. In addition, we will implement training and other programs for proactively responding to needs for compliance that are changing and becoming complicated.

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PRIORITY AREA

Governance

2019 CASE STUDY

Establishment of the Governance Committee

KT&G revamped and strengthened the function and role of committees under the board of directors in 2019 to realize the responsible management. The Governance Committee established from the decision made by the board on April 30, 2019, oversees the decision making of the entire governance. The committee decides on operational standards and corrective actions for the board of directors and committees, as well as deliberating establishment and amendment of governance-related regulations. Moreover, the committee is given authorities for proposing CEO and outside director candidate deliberation standards, along with the decision making and qualification inspection for executive directors, thereby enhancing transparency in nomination processes for the executives and board.

As of the end of May 2020, the Governance Committee is composed of 3 outside directors and 1 executive director, and the outside director, Youn, Hai-su is the chairman of committee. To secure independence of the committee, the majority of the members shall be constituted by outside directors in accordance with the Article 15 of the Board of Directors Regulation. Through the Governance Committee, we will proactively identify governance-related risks and continue making decisions to prevent any risks.

1. Board of Directors

According to the 'KT&G Charter of Governance' which reflects principles and visions of governance that satisfy global standards, KT&G established a stable governance centered on the board run by outside directors and continue to develop the organization relentlessly up to the global standard. The board is a top decision-making body for company's key agenda such as recommending candidates for CEO and approving business plans. Specific roles of the board are indicated in the articles of association and the board regulation.

*KT&G website, www.ktng.com



Articles of Incorporation



Board of Directors



Corporate Governance

*Data Analysis, Retrieval and Transfer System, dart.fss.or.kr



Corporate Governance Report

2. Board Structure

KT&G operates the board of directors constituting the majority with outside directors so that the board effectively executes the managerial supervisor's role and make independent decisions. According to the Article 25 of the articles of association, 9 executive directors including the CEO can be nominated, and more than half of members should be composed by outside directors.

In 2019, we enhanced fairness and transparency of the director nomination process by establishing the Governance Committee. The Governance Committee participates in the process of establishing deliberation standards for executive and outside directors and performs the qualification assessment for executive directors. For the nomination of the CEO, we added strengthen by the Governance Committee before the 2-step verification process by the CEO Candidates Recommendation Committee and the board of directors. Accordingly, we have secured maximum independence and transparency in the CEO Candidates recommendation process.

Outside directors are recommended based on their independence and expertise, and their experiences in risk management or specified risk management are also considered. Outside director, Lee, Eun-Kyung, who has been an executive director of the finance and operation risk management at Calvin Klein of the PVH Korea since 2012, is in charge of the financial risk examination at KT&G. Outside director, Baek, Jong-Soo is a legal expert who has served as a director of Busan District Public Prosecutor's Office and he manages legal risks in the business activities of KT&G.

As of the end of May 2020, KT&G's board is composed of 7 directors, and 5 are outside directors to exceed legal and regulatory requirements.

Category	Name	Gender	Date of Birth	Full-time	Major Career	Current Position	Term
Executive directors	Baek, Bok-In	Male	Sep. 1965	Yes	Director of Strategy Planning HQ, KT&G Director of Marketing HQ, KT&G	CEO, Management Committee Chairman	Mar. 17, 2018 - Ordinary General Meeting of Shareholders in 2021
	Kim, Heung-Ryul	Male	Mar. 1961	Yes	Director of Management Support HQ, KT&G Head of Key Market Office of Global HQ, KT&G	Chief Vice President	Mar. 17, 2018 - Ordinary General Meeting of Shareholders in 2021
Outside directors	Baek, Jong-Soo	Male	Nov. 1960	No	Lawyer, Dongin Law Group Director, Busan District Prosecutor's Office	Board Chairman, Evolution Committee Member	Mar. 17, 2018 - Ordinary General Meeting of Shareholders in 2021
	Youn, Hai-Su	Male	Feb. 1952	No	President, Seoul University of Foreign Studies Assistant member, Presidential 21st Century Committee	Governance Committee Chairman	Mar. 30, 2019 - Ordinary General Meeting of Shareholders in 2022
	Lee, Eun-Kyung	Female	May 1963	No	Financial/Operational Director, Calvin Klein of PVH Korea Financial Director, Reebok Korea		Mar. 30, 2019 - Ordinary General Meeting of Shareholders in 2022
	Kim, Myung-Chul	Male	Feb. 1956	No	Advisor, Space Entertainment Enterprise (SEE) President, Shinhan Bank America		Apr. 1, 2020 - Ordinary General Meeting of Shareholders in 2023
	Koh, Yun-Sung	Male	Sep. 1973	No	Professor, Business School of Hankuk University of Foreign Studies	Audit Committee Chairman	Apr. 1, 2020 - Ordinary General Meeting of Shareholders in 2023

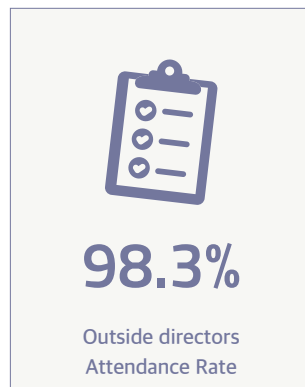
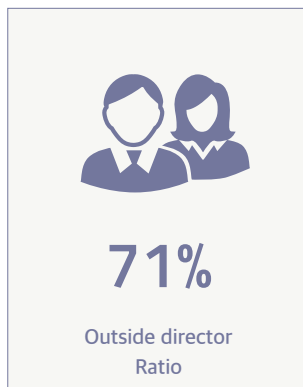
*Outside directors Youn, Hai-Su and Lee, Eun-Kyung were renominated at the 32nd Ordinary General Meeting of Shareholders (Mar. 29, 2019)

**Terms of outside directors Song, Op-Kyo, Lee, JuneQ and Rho, Joon-Hwa have been terminated, and Kim, Myung-Chul and Koh, Yun-Sung were newly nominated at 33rd Ordinary General Meeting of Shareholders. (Mar. 31, 2020)

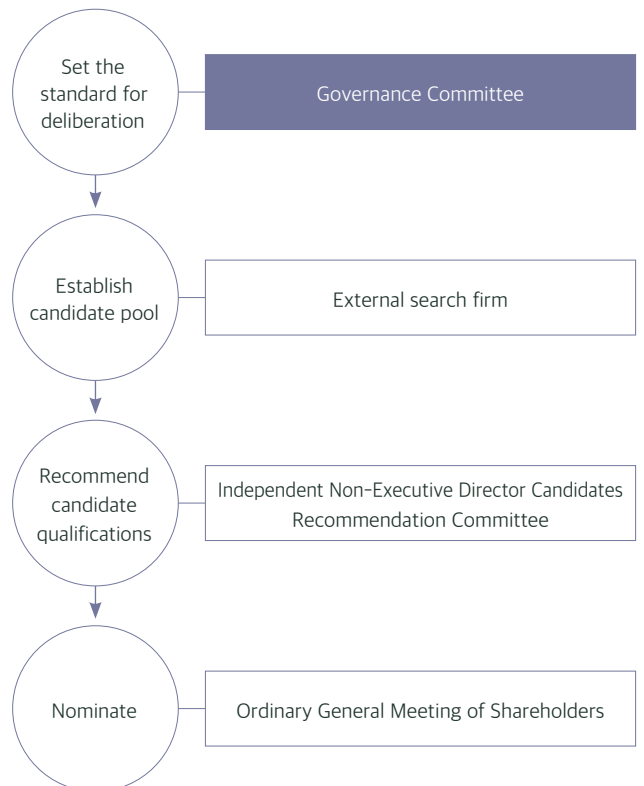
CEO Nomination Process



●: Newly established in 2019



Outside director Nomination Process



■: Newly established in 2019

3. Key Discussion Agenda

In 2019, KT&G board meeting has been held 10 times, and the outside director participation rate is 98.3%. 30 items were discussed at the meeting, and among them, 23 items were decided, and 7 were reported. During the year, governance-related risks were reviewed by the board including the amendment of the Charter of Governance and governance sophistication strategies. Items to be discussed at the meeting are notified to directors beforehand, and we also explain in detail if needed, so that directors are well aware of the contents to discuss them effectively.

In 2020, we plan to grant the authority related to ESG to the board, and the board plans to discuss in-depth key issues related to ESG.

*Data Analysis, Retrieval and Transfer System, dart.fss.or.kr

Key decided items: 2019 Business Report pp. 319-320

4. Committees under the Board of Directors

KT&G operates committees within the board of directors to enhance execution expertise and operational efficiency. We compose each committee considering expertise of each director to maximize efficiency. In April 2019, the Governance Committee was added to one of the committees for more systematic discussions and decision making in regard to governance. Thus, there are 4 standing committees (Governance Committee, Evolution Committee, Management Committee, and Audit Committee) and 2 non-standing committees (CEO Candidates Recommendation Committee and Independent Non-Executive Director Candidates Recommendation Committee). Governance Committee, Audit Committee, and CEO Candidates Recommendation Committee have their own operational regulations, and structures and functions of each committee are abided by the Article 34 of the articles of association and the Article 15 of the Board of Director Regulation. For efficient cross-check and transparent decision making of the board of directors and top management, Chairmans of all committees except for the Management Committee are assigned with outside directors, thereby operating independent committees under the board of directors.

Functions of Standing Committees

Category	Functions
Governance Committee	Make decisions on overall governance
Evolution Committee	Make decisions on managerial evolution/compensation of employees
Management Committee	Make decisions on general managerial activities and investment below a standardized amount*
Audit Committee	Audit accounting and work

*Decision making on important matters related to key stakeholders such as workers and consumers, post-maintenance and risk management of the investment business, identification of and decision making on social contribution activities costing between KRW 500 million and KRW 1 billion that are not included in the budget approval.

Standing Committee Structure

Category	Name	Governance Committee	Evolution Committee	Management Committee	Audit Committee
Executive directors	Baek, Bok-In			●	
	Kim, Heung-Ryul	○		○	
Outside directors	Baek, Jong-Soo	○	●		○
	Youn, Hai-Su	●	○		
	Lee, Eun-Kyung	○			○
	Kim, Myung-Chul		○		○
	Koh, Yun-Sung		○		●

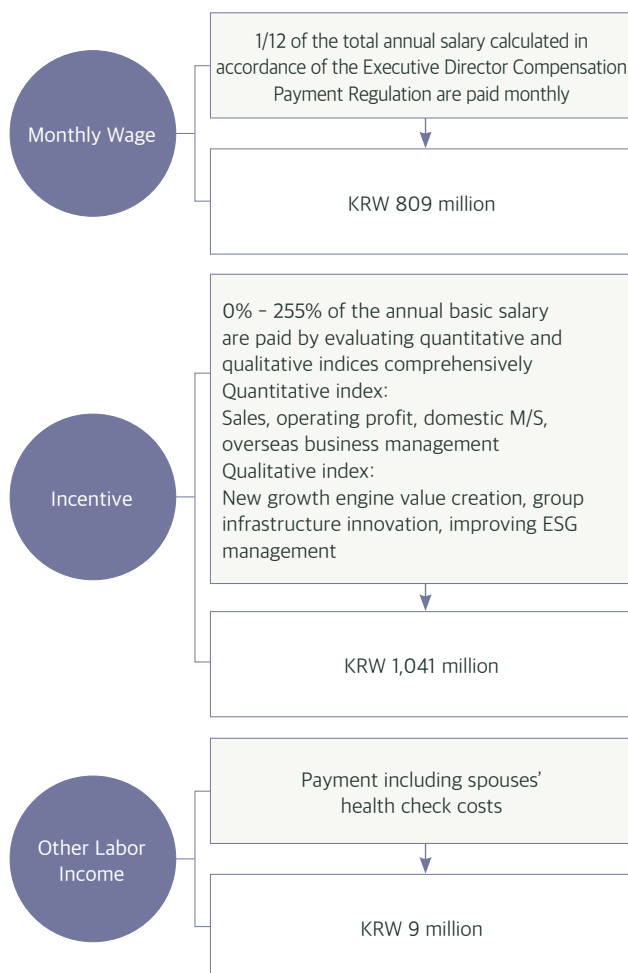
* ●: Committee Chairman / ○: Committee Member

5. Evolution and Compensation

Top Management Evolution and Compensation

KT&G established the Evolution Committee only composed of outside directors and enables compensations for the CEO and managing directors are executed fairly through the management evolution. The Evolution Committee decides on compensation and severance pay of executives, severance pay of general employees, and managerial goals set with CEO candidates. Moreover, the committee deliberates on compensation and severance pay of the CEO and executive directors, and it also has decision-making rights on managerial evolution and compensation of the CEO. In 2019, the Evolution Committee was held twice, and it made decisions on short- to long-term managerial goals and previous year's short- to long-term managerial evolution of the CEO. We currently include ESG-related index in our CEO evaluation index and plan to expand it to more detailed aspects.

Status of 2019 Executive Directors Compensation Regulation and Payment (sum of 2 executive directors)



*KT&G retains the policy for clawbacks and malus of short-term and long-term incentives if any intended or significant mistakes of the executive management and errors in payment are found.

Outside director Evolution and Compensation

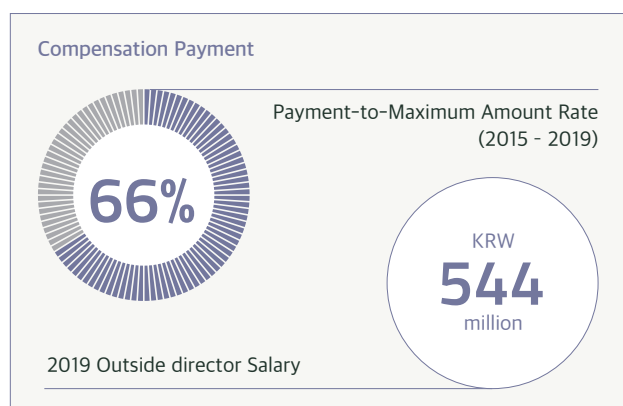
According to the articles of association and the Board of Director Regulation, 'the board may conduct evolution of outside directors and self-assessment of the board activities.' Based on the regulation, the board of directors decides on the 'Board Activity Assessment Plan (draft)' at the end of every year and conducts assessment. In 2019, the assessment was performed in 4 categories. Compensation for directors are paid within the scope of maximum pay amount approved by the General Meeting of Shareholders considering the compensation standards of other companies and competitors in the industry, and specific amount and payment method are decided by the board. Moreover, we provide directors costs related to their activities to encourage their active engagement.

Status of 2019 Outside Director Evolution Items and Compensation Payment

Evolution Items		
Board Performance		Committee Activities
Board Operational Efficiency		Outside director Peer Evaluation

Evolution Results		
Category		Out of 5.0
Performance of the board	Review of active managerial decision making	4.83
	Review of key strategies and examination of accomplishment standard	4.50
	Active engagement in the HR plan	4.50
	Fulfilling a role as an advisor	4.33
	Function of supervising and checking the executive management	4.83
	Efforts for settling a sound governance structure	4.67
Efficiency in the board operation	Appropriateness of board meetings' frequency, size, and method	4.67
	Expertise and utilization of board members	4.33
	Factfulness of data offered to the board members	4.83
	Efficiency of the meeting and discussion cultures	4.67
	Suitability of training and support to the board members	4.67

*The evolution of committee activities were conducted through narrative process, and peer evaluation of outside directors (out of 5.0) is not disclosed in case of impeding objectivity.



6. Board of Directors Independence

KT&G aims for an 'independent board of directors' for it to fulfill its role as overseeing the executive management. Through the Board Regulation, we require 'an outside director to be assigned as the Board Chairman to establish an objective and independent governance system that separates CEO and the Board Chairman. Moreover, each committee (excluding Management Committee) under the board has more than half of its members as outside directors (excluding Management Committee) to oversee and balance between an independent board and the top management. In particular, the Audit Committee and Evolution Committee are only composed of outside directors to realize practical overseeing of the top management.

Outside directors are recommended through the qualification process of the Independent Non-Executive Director Candidates Recommendation Committee among the candidates recommended by an independent external search firm, and they are finally nominated by the General Meeting of Shareholders. When recommending outside directors, we go through the double confirmation process of an external institution and self-verification for the independence standard such as employment status. Moreover, during the process of submitting items for the Ordinary General Meeting of Shareholders, we perform a final check by receiving the 'Outside Directors Qualification Letter' from the candidates directly. Thus, KT&G strives for nominating outside directors who are independent and neutral without any conflict of interest with the company.

7. Expertise of Board of Directors

KT&G's board of directors is composed of directors with expertise and various experiences to enable effective and considerate discussion and decision making. In addition, KT&G operates the Management Coordination Department under the Strategy & Planning Office which is an exclusive organization for the board. The Management Coordination Department conducts training related to outside directors' job execution and offers information relevant to the company and industry, thereby fortifying expertise of the board. In 2019, the department provided training about legal obligations and liabilities, as well as the current issues, to all directors. Henceforth, we plan to diversify specific field of expertise of the directors and strengthen supports of external experts' consultation in order to strengthen the expertise of the board.

Specialized Field of Expertise by Director

Category	Name	Expertise
Executive directors	Baek, Bok-In	Business management, tobacco business
	Kim, Heung-Ryul	Business management, tobacco business
Outside directors	Baek, Jong-Soo	Law
	Youn, Hai-Su	Business management, corporate affairs
	Lee, Eun-Kyung	Global, finance affairs
	Kim, Myung-Chul	Global, finance
	Koh, Yun-Sung	Finance affairs, accounting

Director Expertise Enhancement Activities

Date	Training Host	Participants	Key Training Contents
Jan. 30, 2019	KT&G	Youn, Hai-Su; Song, Op-Kyo; Lee, JuneQ; Lee, Eun-Kyung; Baek, Jong-Soo	Company's pending issues, etc. (Status related to heat-not-burn product, account settlement schedule, etc.)
May 22, 2019	KT&G	Song, Op-Kyo; Youn, Hai-Su; Lee, Eun-Kyung; Baek, Jong-Soo	Corrective actions related to governance
Jun. 13, 2019	KT&G	All directors	Legal obligations and responsibilities of directors
Sep. 18, 2019	KT&G	All directors	Company's pending issues, etc. (mid- to long-term business visions, group process innovation plans, etc.)

8. Audit Committee

KT&G runs the Audit Committee which is an independent auditing organization for business activities. The Audit Committee is held quarterly, and it monitors and assists KT&G to fulfill its responsibility and liability toward stakeholders by auditing lawfulness of directors and top management's job execution and reviewing accuracy of the financial report.

The committee is composed only of outside directors to maintain objectivity in its processes, independent from the board of directors and executive management. As of the end of May 2020, the Audit Committee is composed of 4 outside directors, and Koh, Yun-Sung is a chairman of committee, and Lee, Eun-Kyung, Baek, Jong-Soo, and Kim, Myung-Chul are audit members.

In addition, the Audit Committee is required to include one or more experts in accounting or finance to secure expertise, in accordance with the Charter of Governance and the Audit Committee Operational Regulation.

In 2019, the committee was held 7 times, and it made decisions in regard to the Internal Accounting Management System, internal monitoring means, Audit Report, and audit on items of the Ordinary General Meeting of Shareholders. An audit plan for the Internal Audit Department (Audit Group) had been submitted as a reporting item until 2019, and we are considering setting them as an official meeting agenda in the future. Through this effort, we will strengthen the committee's decision-making function.

9. Protecting Rights of Shareholders

KT&G operates the Shareholder Proposal System and the Cumulative Voting System to protect rights of all shareholders and prevent dismissal of minority shareholders' opinions in the decision-making process.

Shareholders who want to take shareholder proposal may submit a document recommendation for the purpose of the Ordinary General Meeting in paper or online 6 weeks before the Ordinary General Meeting of Shareholders. Shareholders who own 1/100 or more of the total issued shares are given rights for derivative claims in cumulative voting. Shareholders who want the cumulative voting may submit the claim in paper or online 6 weeks before a general meeting of shareholders is held for nominating 2 or more directors (In the case of the Ordinary General Meeting, it is based on the date of the Ordinary General Meeting in the previous year).

In addition to the shareholder proposal and cumulative voting, we guarantee rights of shareholders for demanding Q&As and explanations about items discussed at the General Meeting of Shareholders, in accordance with the Charter of Governance. KT&G strives to reflect opinions of shareholders by providing opportunities to speak after explaining thoroughly about the items, in order to enable fair and efficient deliberation of the meeting agenda. In the future, we plan to introduce the electronic voting system to offer more convenient environment for executing voting rights even for the shareholders who are not able to attend the meeting.

Implementing the Shareholder Rights Protection System

In February 2018, the Industrial Bank of Korea (IBK) suggested to increase the number of outside directors through the Shareholder Proposal System, recommended 2 candidates for outside directors, and filed Cumulative Voting System through the Shareholder Proposal System. In response, KT&G submitted this proposal as a discussion item during the Ordinary General Meeting of Shareholders, but all of the agendas were rejected as a result of voting. In 2019, no items were submitted through the Shareholder Proposal System.

Compliance Management

2019 CASE STUDY

Guideline for Compliance by Job

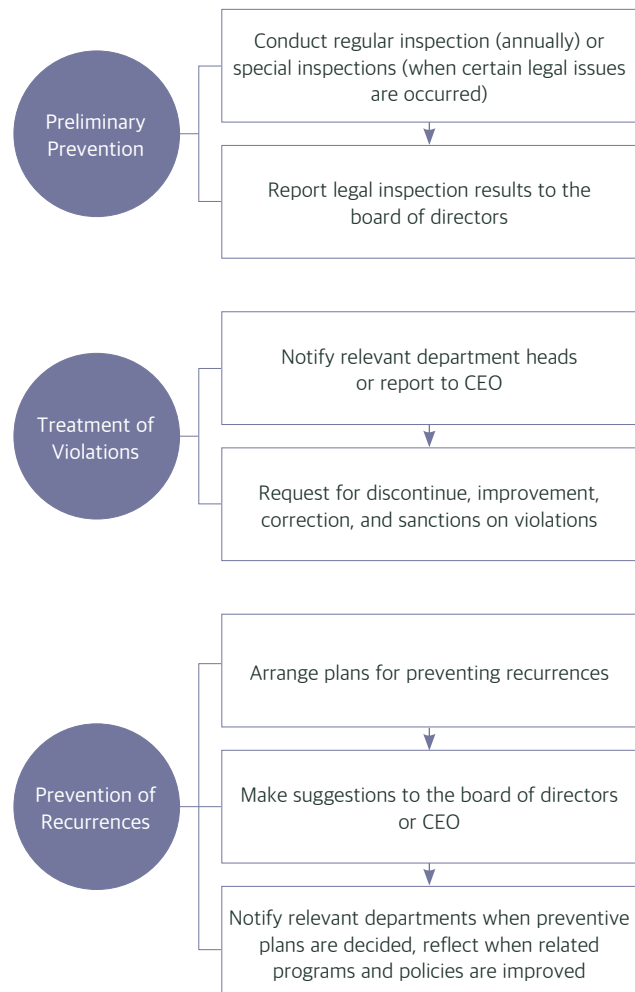
KT&G operates the Employee Voluntary Compliance System as a part of compliance activities. In 2019, we self-checked legal risks that may occur during work process and established the Head Office Compliance Guideline to clearly comply with relevant regulations. In the guideline, we materialized key legal risks in each organization of the head office and indicated any notes about relevant laws, company regulations, and job implementation. Moreover, we provided the compliance checklist to each organization to decide on whether business activities are complied.

1. Compliance Operation System

KT&G established the Compliance Department for the Compliance Management in 2019 and performs compliance activities effectively and efficiently by a compliance manager. The department identifies trends of laws and relevant policies, distributes the Compliance Guideline, and conducts compliance training to employees. Moreover, it regularly examines compliance status of the employees and reports the results to the board of directors.

In addition, we operate the Legal Information System to provide legal information to our employees, and we enhanced accessibility to the system by connecting it to the internal portal. Employees can access the preliminary review service for compliance-related news and legal incidents that may occur during the job tasks.

Compliance Control Process



2. Compliance Activities and Performances

Compliance Check

KT&G performs compliance checks to inspect compliance of employees. In 2019, we focused our compliance check on brand advertising, employment fairness, and subcontracting fairness and reported the results to the board of directors. Starting in 2020, we will expand the scope to the head office, and from 2021, we plan to expand it to the overall company to enhance effectiveness of the compliance check.

Compliance Training Status

Online		
Theme	Target	Date
KT&G compliance assistance	All employees	January
Improving awareness of the disabled people	All employees	May
Preventing sexual harassment	All employees	July
Personal information protection	All employees	September
Preventing workplace harassment	All employees	September
Understanding of the Act on the Promotion of Mutually Beneficial Cooperation between Large Enterprises and SMEs and the Fair Transactions in Subcontracting Act	All employees	December
Offline		
Theme	Target	Date
Ethical Management and preventing sexual harassment	New recruits	January (twice), December (twice)
	Experienced employees	July, November
	New executives	April
	New managers	May
The Tobacco Business Act	New recruits	January (twice)
	Experienced employees	July, November
	New managers	May
The Commercial Act / the Improper Solicitation and Graft Act	New managers	May
The Fair Transactions in Subcontracting Act / the Act on the Promotion of Mutually Beneficial Cooperation between SMEs	Work managers	April (twice)
	NGP business division	December
The Monopoly Regulation and Fair Trade Act	NGP business division	December
Compliance	Work managers	June (twice)

Compliance Training

KT&G plans and operates the compliance training considering job duties and positions to strengthen employees' awareness of compliance. In 2019, we conducted 16 times of on/offline training, and the online training was constituted in 6 themes related to compliance. Moreover, we provided offline training separately for laws that are newly amended or requires concentrated training according to job duties such as the Commercial Act, the Improper Solicitation and Graft Act, and the Monopoly Regulation and Fair Trade Act.

Operation of the Legal Information System

KT&G runs an online portal site, 'Legal Information System' and uses it to efficiently prevent legal risks in the work process. Through this system accessible through the internal portal, employees are able to use job-related services such as legal consultation and contract reviews and legal information including corporate regulations and legal policy trends. In 2019, 6,214 contracts 369 consultations related to business were processed through the Legal Information System.

Composition of KT&G's Legal Information System

• Legal consultation	• Legal information	• Improper Solicitation and Graft Act
• Fair Trade	• Regulation/guideline	• Job manual

Fair Trade and Fair Competition

Based on the 'Operational Guideline for Voluntary Compliance to Fair Trade Program' amended in 2002, KT&G has performed the Compliance Program (CP) continuously. The Compliance Officer nominated by the board of directors is assigned as the CP Manager to oversee the CP operation.

We implement additional supports and management plans to employees and sales representatives in charge of the subcontracting which has high legal risks related to the Monopoly Regulation and Fair Trade Act. Moreover, we offer preventive checklist, as well as professional legal consultations, to employees in subcontracting so that they can voluntarily identify risk factors. In May 2019, we visited the sales field to conduct check of abidance by the Monopoly Regulation and Fair Trade Act and relevant training. In December 2019, we updated and distributed the 'Understanding Sales-related Laws' which includes laws and behavioral guidelines related to sales.

In 2020, we plan to form the Guideline for Voluntary Compliance to Fair Trade into the unfair trade and subcontracting parts and amend the guideline by reflecting recent best practices and policy trends.

3. Risk Management

KT&G operates a committee and exclusive department to identify and prevent potential risks. The Audit Committee, only composed of outside directors, checks the status of company-wide risk management. The Business Management Office, the Compliance Department, and the Internal Control over Financial Reporting Team preliminary diagnose and manage legal and accounting risks. To fortify authority and independence of risk management of each department, we relocated the Audit Group under the Audit Committee, and we are also operating the Controller System to enhance execution ability of the business strategy by managing risks in overall management. The Business Management Office in charge of overseeing the business management directly under the CEO operates the Controller System, and it also analyzes and manages risks that need to be considered when making decisions by standardizing business management tasks. In 2019, we established the controlling standard for spreading the Controller System and conducted managerial checks and audits on domestic subsidiaries and overseas subsidiaries. From 2020, we will expand application of the Controller System to overseas subsidiaries and business divisions and continuously enhance risk capacities of employees by providing relevant training.

Response Plans by Risk Factor

Financial Risks

Key Risks	Factors	Response Plans
Taxation risks	National and local taxes management	<ul style="list-style-type: none"> Analyze tasks and rationalize tax report through taxation review and consultation Conduct preliminary tax review by operating taxation consultation service
Foreign exchange risks	Compliance with the Foreign Exchange Transactions Act	<ul style="list-style-type: none"> Enhance accessibility and usability of foreign exchange menus, Improve the Currency Risks Management System such as supplementing foreign exchange performance analysis Conduct training by external lecturers related to the Foreign Exchange Transactions Act Analyze weekly/monthly foreign exchange performances and the foreign exchange market

Non-financial Risks

Key Risks	Factors	Response Plans
Corruption risks	<ul style="list-style-type: none"> Illegality and corruption between employees and stakeholders Tangible/intangible damages due to employees' illegality and corruption 	<ul style="list-style-type: none"> Anticorruption training and voluntary inspection of ethical awareness on employees, surveys on stakeholders Regular risk monitoring through the E-Audit System, regular check and best practices sharing of incidents
HR risks	<ul style="list-style-type: none"> HR management, employee health management 	<ul style="list-style-type: none"> Manage information about HR, compensation, and welfare through the E-Human Resources Management (E-HRM) Conduct employee health checks (annually)
Legal risks	<ul style="list-style-type: none"> Legal risks related to the domestic/overseas tobacco business and compliance with environmental/ industrial safety Lawsuit filing and loss related to main businesses 	<ul style="list-style-type: none"> Regularly monitor and guide legislation of major laws in business and governmental policy trends Develop the Compliance Guideline categorizing company-wide legal risks
Regulatory risks	<ul style="list-style-type: none"> Implementing the FCTC 	<ul style="list-style-type: none"> Comply with relevant laws to implement the Framework Convention on Tobacco Control (FCTC)

Ethical Management

2019 CASE STUDY

Checking Employees' Ethical Awareness

Preventing unethical behaviors of employees is one of the important goals of the Ethical Management, and it is essential to secure high standard of ethical awareness among each individual employee. In 2019, KT&G measured effectiveness of the Ethical Management system, conducted the ethical awareness check, and reported the results to the board of directors to identify ethical awareness of the employees. We offered employees opportunities to self-evaluate and reconsider their ethical awareness through the checklist composed on items including unethical speech and sexual harassment, corporate confidentiality and information protection, unpublished important information, gifts/bribery and improper treatment, financial transactions, and fair job execution. We will continue to arouse attentions of each employee through the annual ethical awareness checks and enhance the level of the Ethical Management by assessing effectiveness and deriving improvements.

1. Ethical Management System

Ethical Standard and Organization

KT&G enhances ethical awareness of employees, encourages their practices, and sophisticates the Ethical Management System by performing various activities based on the Charter of Ethics and Ethical Regulation as the standard of righteous actions and valuation for all employees. The Compliance Department, as a control tower of the Ethical Management, conducts Ethical Management activities including employees' voluntary check of ethical standard, request for the Ethical Practice Pledge, practice campaign (Think Twice), ethical training, stakeholder survey, and unethical behavior whistleblowing channel operation.

*KT&G website, www.ktng.com

 Ethical Management



Whistleblowing System and Treatment Process for Unethical Behaviors

KT&G operates the Unethical Behavior Whistleblowing System to settle the Transparent/Ethical Management. Internal and outside stakeholders including employees and suppliers may report employees' bribery, corruption, authority abuse, collusion, and complaints through the 'Unethical Behavior Whistleblowing Channel' on the KT&G website regardless of time and place. The whistleblowers' identities are protected in accordance with the 'Unethical Behavior Whistleblower Protection Guideline', and they can receive compensation if the report is found to be true.

In 2019, a total of 159 cases were reported through the 'Unethical Behavior Whistleblowing' channel. We treated all received reports, took corrective actions, and developed preventive methods.

Step 1. Receive reports	Receive reports through the Unethical Behavior Whistleblowing channel
Step 2. Check the truth	Authenticate the case and decide on whether to investigate or not (Compliance Support Dept.)
Step 3. Investigate in detail	Investigate truth (Audit Group)
Step 4. Treat	Take corrective actions in accordance with the investigation result

Status of Unethical Whistleblowing Channel Receipt in 2019

Category	No. of Cases (EA)
Consumer complaints	95
Unethical behaviors	4
Others	60
Total	159

Spreading Ethical Management

KT&G strives to spread the culture of Ethical Management as well as preventing unethical actions in the business activities. These efforts are not limited to the domestic operation or head office, but it is applied to all worksites, subsidiaries, and suppliers throughout the world. KT&G makes an effort to comply with the labor principles including laws and schemes, safety and health recommended by the ILO, and worktime in every country and region for fair and transparent trade. In addition, KT&G has prepared various systematic means including the Supplier Code of Conduct and comprehensive supplier evaluation to encourage all suppliers to fulfill their social responsibility based on the Ethical Management. Henceforth, we plan to develop the Ethical Management system, training, and programs and establish the company-wide management system to apply them in global worksites as well. Moreover, we will continuously strengthen the Ethical Management System by amending the Charter of Ethics and the Ethics Regulation by applying legislation and new issues.

Sophisticating the Ethical Management

Since the establishing of an exclusive organization and system related to the Ethical Management in 2003, KT&G has been sophisticating the Ethical Management System so that all employees can use it as a basis for righteous valuation and action.

History of Sophistication of the Ethical Management

Introduction (2003~2004)	<ul style="list-style-type: none"> Amended the Charter of Ethics Established the Ethical Management infrastructure such as organizations and system
Settlement (2005~2009)	<ul style="list-style-type: none"> Audited the work process Improved the Ethical Management infrastructure such as organizations, regulations, and system
Development (2010~2015)	<ul style="list-style-type: none"> Proactively managed business risks Continuously developed the Ethical Management Practice Program and expanded it to the group
Internalization (2016~2018)	<ul style="list-style-type: none"> Established the Ethical Management Audit Group system Strengthened independence and expertise of the Ethical Management organization
Sophistication (2018~2019)	<ul style="list-style-type: none"> Transferred Ethical Management-related work to the Ministry of Justice Established the Compliance/Ethical Management system
Stabilization (2019~)	<ul style="list-style-type: none"> Established the 'Compliance Department' exclusive for Compliance/Ethical Management-related tasks Established the Ethical Management infrastructure through amendment and enactment of relevant regulations

2. Ethical Management Practice Program

Ethics Pledge

All of KT&G's employees acknowledges the Ethical Regulation and promises to actively engage in the Ethical Management pursued by the company by signing the 'Ethical Management Pledge' annually.

Activities for Preventing Sexual Harassment

KT&G performs activities for preventing sexual harassment to improve awareness and customs of sexual harassment and create beautiful and health workplace culture. We regulated obligation for prohibiting and preventing sexual harassment in the rule of employment and set the 'Sexual Harassment Prevention Plan' based on analyses of relevant laws, best practices, and internal system. Moreover, we annually conduct online training to enhance employees' awareness of ethics.

Think Twice Campaign

KT&G regularly conducts the 'Think Twice' campaign that encourages employees' ethical practices. Through the intranet, we share campaigns with themes of not giving and receiving gifts for holidays, preventing year-start and year-end drinking accidents, and prohibiting workplace harassment, in order to preliminarily prevent relevant accidents and incidents.

Ethical Management Training

KT&G performs training on the Ethical Management toward new recruits, executives, and managers to settle the Ethical Management and legal compliance. In 2019, we provided all employees preventive training for workplace harassment to highlight the importance of the issue. Offline training was provided to those who need focused training on work-related laws by job duty and position, and a total of 324* employees participated in 2019.

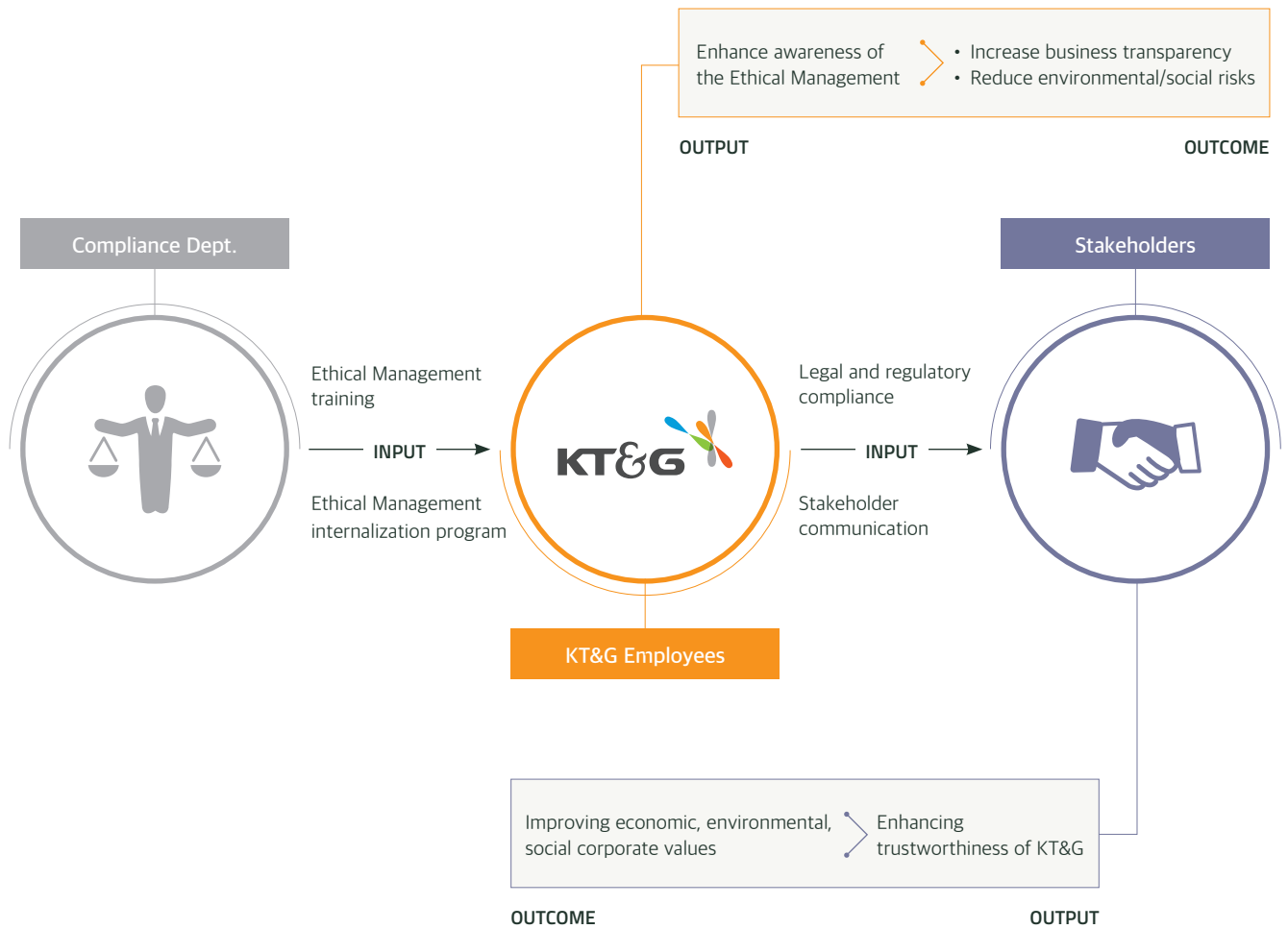
*No. of training participants is based on cumulative calculation

Spreading the Ethical Management to Stakeholders

KT&G attaches the 'Specialized Terms for Ethical Practices' in the agreement signed with suppliers. Thus, we urge them to practice ethical behaviors and strive to settle the ethical corporate culture in the overall industry. Moreover, we conduct surveys to external stakeholders and monitor transaction satisfaction and our employees' unethical behaviors. Through the survey result, we are not only checking the status but also discovering correcting directions.

3. Measuring Effectiveness of the Ethical Management

KT&G conducts employees' self-check of ethical awareness annually to measure effectiveness of the Ethical Management practices and diagnosis programs. We derive problems, correction methods, and results of corrections by collecting and analyzing the self-check results, and if needed, we consult with relevant departments to solve the issues. Henceforward, we will sophisticate the Effectiveness Measurement System for the Ethical Management to evaluate the effect of the Effectiveness system and programs more objectively.



New Market Creation through Innovation

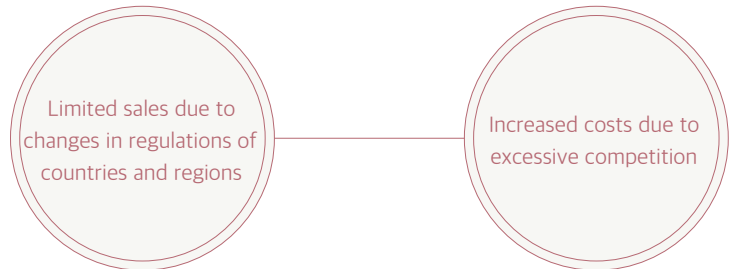
INNOVATION



GLOBAL MEGATREND

Cigarettes are a key preferred product that shows various needs according to individual's taste and habits. Expectations of domestic and overseas customers are changing fast, and characteristics of cigarettes favored by customers vary in each market. Therefore, it is required to launch innovative products that can satisfy customer expectations based on differentiated R&D capacities and constant investment.

RISKS



OPPORTUNITIES



APPROACH

KT&G is growing into a global tobacco manufacturer by developing innovative technologies and identifying new ideas. In particular to respond to the next generation tobacco market actively, we are striving to conduct R&D in various areas such as materials, product planning, and manufacturing. KT&G will develop into the 'Global Top 4 Tobacco Company' by launching various products tailored for consumer preferences.

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PRIORITY AREA

Next Generation Product

2019 CASE STUDY

Global Collaboration



KT&G has been recognized for technology and innovativeness of lil product line which is the next generation product (NGP), based on the excellent performance in the domestic market. In 2019, we expanded the target market for lil products to overseas and concentrated our capacity in the overseas market to enhance overseas consumers' awareness of KT&G's products. As a result, in November 2019, we processed the Head of Agreement (HOA) with a global company, Philip Morris International (PMI) for overseas distribution, and in January 2020, we signed the contract. Through the contract, PMI is now capable of selling 3 types of heat-not-burn products (HNB): lil Hybrid, lil Plus, and lil Mini and a liquid vape type, lil Vapor to all countries internationally except for Korea. KT&G intends to accelerate exploring overseas markets by utilizing marketing resources and knowhows of PMI, thereby fostering lil as a global brand.

1. NGP Portfolio

Since the initial launch of lil products in November 2017, KT&G has swiftly expanded stick products and launched lil Plus, lil Mini, lil Hybrid, and lil Vapor by reflecting various needs of consumers. In February 2020, we launched the lil Hybrid 2nd Version that improved consumer convenience, and we are leading the heat-not-burn product market.

lil Plus



This is a battery-combined all-in-one device with internal heating of sticks at about 320°C. Due to the heat-not-burn technology, it does not generate smoke smell. This enables continuous smoking without wait time, and its

heated cleaning function makes cleaning and maintenance easier. Stick can be inserted and removed easily, and the dual heating function realizes balanced taste.

lil Hybrid



This is a battery-combined all-in-one device with external heating of sticks and liquid cartridge simultaneously, and it is a distinctive platform of KT&G. It provides abundant smoke and relieved inconvenience of cleaning and

maintenance with unique stick structure. It does not generate smoke smell and offers soft feeling and taste.

lil Mini



This has same format and function as lil Plus; however, it is a miniaturized version that enables smoking of 10 cigarettes with single full charge.

lil Vapor



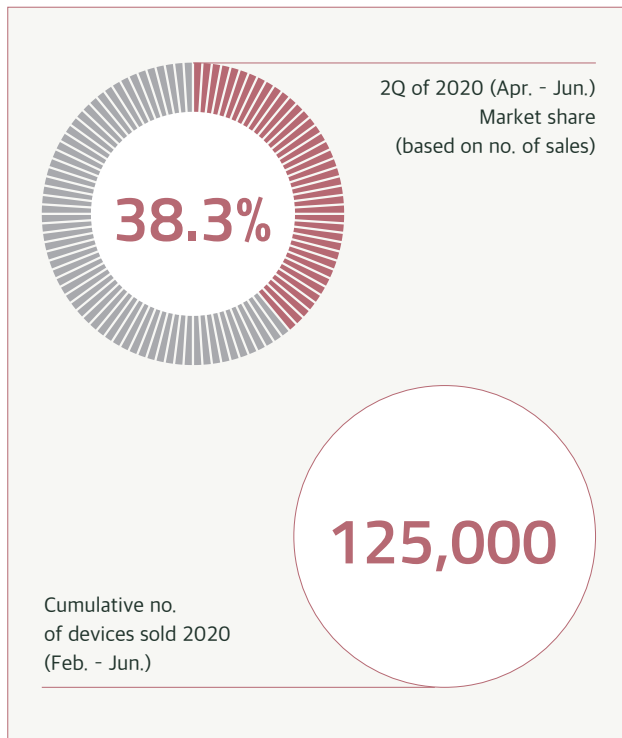
This is a CSV, vaping product that is used by combining liquid cartridge, 'SiiD'. It is applied with the 'Puff Signal' method that vibrates when used 1 cigarette worth of smoke to improve drawbacks of the existing vapors. It is

operated when the slide is pulled down, and it provides affluent feeling from the first puff.

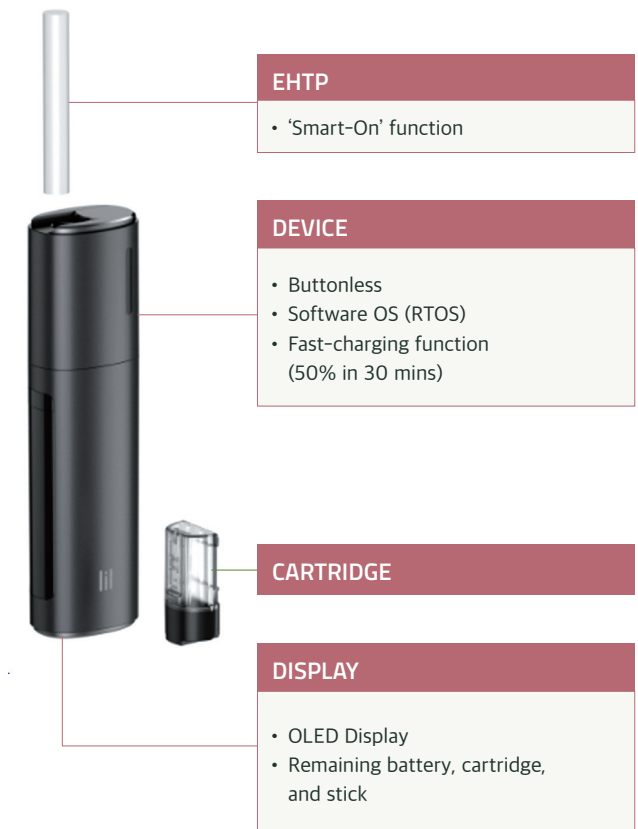
2. Launch of lil Hybrid 2.0

In February 2020, KT&G launched the 'lil Hybrid 2.0' which maximized user convenience by applying high-end technology into the existing lil Hybrid. 'lil Hybrid 2.0' is the first heat-not-burn product to remove all buttons, and it has a 'Smart-On' function that starts preheating automatically when a stick is inserted. In particular, we installed the OLED Display as the first among global electronic cigarette developer to enable checking of remaining battery, cartridge, and puffs in real time. Moreover, the Real-Time Operating System (RTOS) is applied to the software OS to secure stability and strengthen user's safety functions such as overheating prevention.

Performance from the Launch in 2020



Differentiated Function of lil Hybrid 2.0



3. NGP Performance and Plans

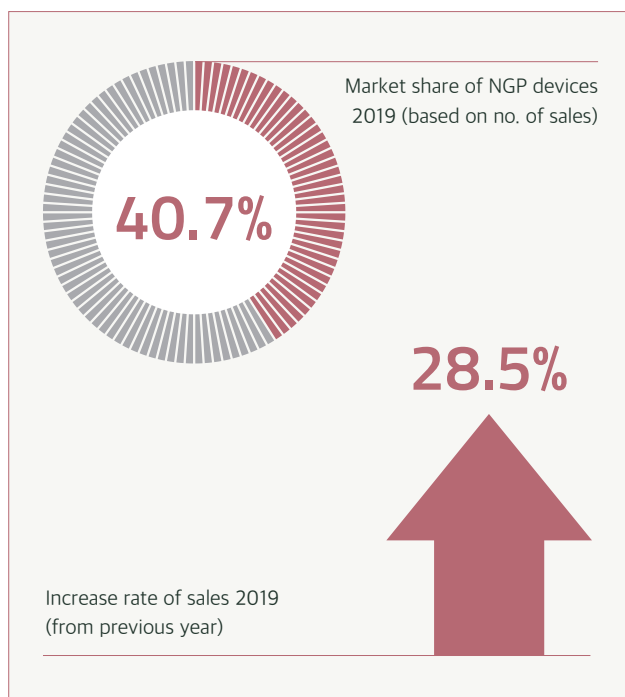
Market demands for NGPs, HNB/CSV products are continuously increasing, and as of 2019, it grew by about 6% from the previous year. As customers' preferences to NGP products are expanding, the next generation product market is expected to grow constantly. KT&G is creating outcomes in the NGP market by swiftly developing high-quality products based on the differentiated strategy, despite its late start in the NGP sector.

KT&G is planning to penetrate the global market based on the performance and technologies in the domestic NGP market. Through the global collaboration with PMI, we will launch lil products in the global market in 2020 and secure leadership in the global NGP market.

NGP Sales Performance in 2019

NGP Sales Performance in 2019		2019
Sales* (KRW 100M)		2,523
No. of products sold	Devices (10,000 EA)	105.4
	Sticks (100M EA)	24.6

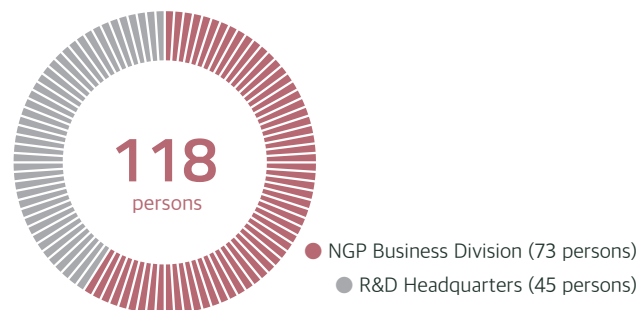
*Excluding indirect taxes passed on to consumers (i.e. tobacco excise, local education tax, charges for waste, charges for national health promotion, Individual consumption tax)



4. Strengthening NGP Development Infrastructure

KT&G began developing NGPs by establishing the Product Innovation Office under the Marketing Headquarters in July 2016. In 2019, we expanded the Product Innovation Office to the NGP Business Division and established the sub-organization, NGP Development Department. Moreover, we extended teams under the NGP Development Office to strengthen new development functions of NGPs. In addition, in the R&D Headquarters, we expanded stick development departments by platform, thereby fortifying functions of safety analysis and compliance. Through these continuous improvements in organization and HR infrastructure, the collaboration between the NGP Business Division and R&D Headquarters is creating synergy in developing innovative products and establishing leading position in the NGP market.

Status of NGP Development HR



Functions of NGP Development Organization



5. Securing Patents through NGP Research Innovation

KT&G is achieving continuous performances in research innovation based on the NGP development infrastructure, and the number of NGP patent applications are increasing accordingly. In 2019, number of overseas patent applications increased by 5 times from the previous year, thereby exceeding the number of domestic patent applications.

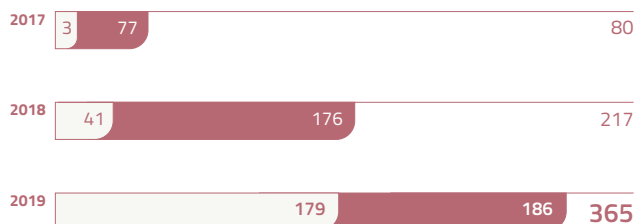
Key Patent-applied Technologies Related to lil Hybrid

Patented Technologies Details	
Stick identification technology	The device is operated only when an exclusive stick, MIIX is inserted.
Smart on/off technology	The device is operated automatically when a stick is inserted without any additional process.
Liquid preheat technology	The device is preheated when a stick is inserted to increase smoke amount of the first puff
Air pressure pattern-based puff detection technology	The device detects whether the smoker has inhaled or not, regardless of surrounding air pressure.
Stick cap technology for optimized smoke amount	The inverted Y-shaped tube stick technology generated optimized smoke about while preventing leakage of tobacco substances.
Aerosol cooling stick technology	The technology cools aerosol efficiently by optimizing volume of perforated paper pipe and rate of air input.

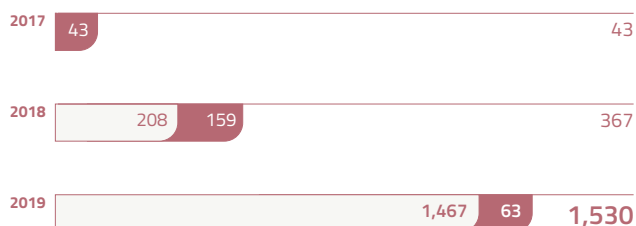
NGP IP* Applications 2017 - 2019

● Domestic ● Overseas (unit: EA)

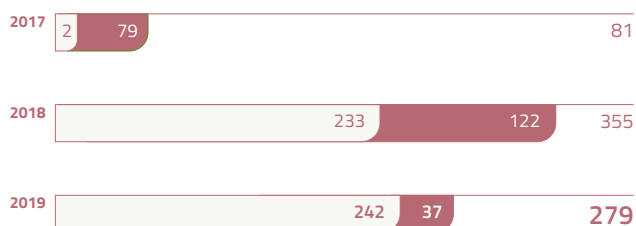
Patent



Trademark



Design



*IP: Intellectual Property

Research & Development

2019 CASE STUDY

Promoting Research on Product Smell Reduction

KT&G established the 'Smell Care Center' in the Product Research Center and assigned experts with knowhows in product and technological development to conduct research on reducing smell of the combustible tobacco products. As the market for NGPs including lil and lil Hybrid has expanded, consumers' need for smell reduction is increasing. To respond to the consumers' request, KT&G developed the 'ESSE Change Himalaya' through the collaboration of all research institutes including the Smell Care Center. From its launch in April 2019, 'ESSE Change Himalaya' recorded 16 million packs within 6 months, and this is 4 months shorter than the average time of 1 year and 6 months to sell 10 million packs of general new products. Followingly, 'Raison Hyvaa Renewal' which is applied with birch-made filter and finger-zone technology and 'Raison French Cleo' applied with the triple care system of smell reduction in mouth, hand, and clothes were launched, thereby leading the growth of KT&G in 2019. Moreover, through the innovative technological development such as patent applications and an official analytic institution's assurance in regard to smell reduction technology, we are launching 'The One Sky' and 'ESSE Change Frozen' in 2020 to create sustainable performance.

1. R&D Capacity Building

KT&G is growing through relentless innovation to respond to the changes in social environment and satisfy consumers' expectations. Based on the organization with expertise and system, we are building a foundation to become an internationally recognized company by developing smell reduction technology.

R&D Organization

The R&D Headquarters is developing core technologies related to combustible tobacco products and NGP products. Therefore, we established expertise sectors in each task area systematically. KT&G's R&D organization is composed of 3 research centers (Product Research Center, Future Technology Research Center, and Analytic Research Center) and the R&D Planning Office.

Research Institutes	Research Areas
Product Research Center	<ul style="list-style-type: none"> Develop and improve the existing products tailored for domestic/overseas customers Develop smell reduction technologies (Smell Care Center)
Future Technology Research Center	<ul style="list-style-type: none"> Research technologies for tobacco materials, ingredients, and flavors
Analysis Research Center	<ul style="list-style-type: none"> Study component analysis and develop technologies for new analysis techniques Operate KOLAS and conduct joint international research
R&D Planning Office	<ul style="list-style-type: none"> Establish mid- to long-term R&D strategies/goals and manage projects Manage/operate R&D IPs

2. R&D Activities

KT&G researchers develop differentiated products by combining numerous ideas and technologies to respond to various needs of customers.

Key R&D Activities

Category	Details
Strengthening product development	<ul style="list-style-type: none"> Propose technologies that materializes product brand concepts by analyzing trends of domestic/overseas technologies Enhance competitiveness of products by manufacturing prototypes and verifying quality Maximize performance by establishing intimate collaborative system between internal organizations and external research centers
Establishing international standards	<ul style="list-style-type: none"> Establish new analytic methods and international standards as an institution of the Board of Cooperation Centre for Scientific Research Relative to Tobacco (CORESTA)
Joint research	<ul style="list-style-type: none"> Conduct joint international research with research institutes under the China National Tobacco Corporation (CNTC) and the Asia Tobacco Component Analysis Joint Research Association
Support exporting business	<ul style="list-style-type: none"> Support exporting business by enhancing product credibility after accepted as an international certified testing institution

Cigarette Product Research

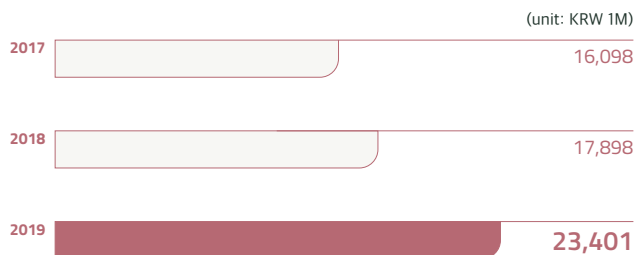
Smell reduction of cigarettes has been a long-term need of consumers. To satisfy this consumer need, KT&G developed the 'Triple Care System' technology. Moreover, we have launched products by applying the differentiated filter (i.e. HEPA filter) and leaf tobacco (i.e. bud pipe).

For the overseas cigarettes, we are developing localized products based on the results of consumer research in each market. In particular, we have retained technological competitiveness including Kretek tobacco in Indonesia and Virginia Blending Type in China, and we are enhancing our technological competence constantly.

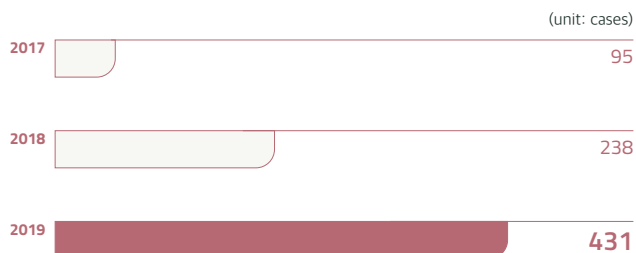
Self-development of Fat-soluble Liquid Capsule Technology

In the past, the fat-soluble liquid capsule technology has been owned by only a few pharmaceutical manufacturers in Japan and Europe; however, KT&G applied both domestic and overseas patents for the technology by self-developing through the efforts by its Chief Researcher. The researcher was recognized by receiving the Prime Minister's Award at the 'Invention Day' hosted by the Korea Invention Promotion Association. Through the development of the technology, we were able to localize cigarette capsules that were used to be relied upon imports from Japan, thereby expecting effects worth KRW tens of billions annually. We believe that this technology can also be applied to various industries including pharmaceuticals and food products.

Amount of R&D Investment



No. of Patent Applications



Status of Intellectual Properties 2019

Category	Details	EA
Trademark	ESSE, etc.	3,436
Design	Cigarette pack paper, etc.	438
Patent	Lighting bar for cigarette showcase, etc.	200
Utility model	Stationary cigarette pack for mobile devices, etc.	11
Total		4,085

R&D Performance

2017		
R&D Performance		63 cases
Key research tasks	<ul style="list-style-type: none">• Develop differentiated ingredients and leaf materials• Develop products for expanding the overseas market	
Expectations	<ul style="list-style-type: none">• Satisfy needs of domestic/overseas consumers and strengthened product competitiveness• Create new markets	
2018		
R&D Performance		54 cases
Key research tasks	<ul style="list-style-type: none">• Develop differentiated ingredients/materials for responding to the conventional market• Develop and diversify globally customized products	
Expectations	<ul style="list-style-type: none">• Maintain competitive advantages in the conventional cigarette market• Strengthen product competitiveness in the new global market	
2019		
R&D Performance		48 cases
Key research tasks	<ul style="list-style-type: none">• Develop new products• Develop products to respond to diversification in the global market trend	
Expectations	<ul style="list-style-type: none">• Secure market superior technologies and products• Secure growth engines in the global market	

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FINANCIAL STATEMENT

Consolidated Balance Sheet

(unit: KRW 1M)

Category	2017	2018	2019
Assets			
Current assets	6,585,704	6,413,375	6,417,192
Cash and cash equivalents	715,117	932,969	891,306
Other current financial assets	2,081,586	584,580	397,949
Financial assets at fair value through profit or loss	0	1,139,705	1,239,263
Trade and other receivables	1,124,280	975,921	1,023,386
Derivative financial instruments	0	1,239	2,277
Inventories	2,317,773	2,461,290	2,447,214
Refund assets	0	2,356	3,027
Accrued tobacco excise and other taxes	261,459	232,237	291,482
Short-term advance payments	59,175	54,208	83,696
Prepaid expenses	26,316	24,623	33,345
Assets classified as held for sale	0	4,247	4,247
Non-current assets	3,395,656	3,741,727	4,294,906
Other non-current financial assets	6,351	8,566	4,480
Long-term deposits	510,223	615,528	751,437
Fair value through profit or loss	0	210,655	251,895
Long-term trade and other receivables	63,687	62,903	77,062
Fair value through other comprehensive income or loss	0	249,575	257,640
Available-for-sale financial assets	471,763	0	0
investment in associates and joint ventures	51,031	83,989	49,393
Property, plant, and equipment	1,775,342	1,818,788	1,753,358
Intangible assets	84,748	71,954	89,694
Investment property	317,784	495,049	885,325
Right to use asset	0	0	45,484
Long-term refund assets	0	224	0
Long-term advance payments	69,774	71,394	72,519
Long-term prepaid expenses	5,548	7,873	7,465
Deferred income tax assets	39,405	45,230	49,153
Total assets	9,981,360	10,155,102	10,712,098
Liabilities			
Current liabilities	1,816,392	1,640,708	1,600,094
Short-term borrowings	174,657	129,924	27,066
Current long-term debt	3,702	5,000	5,285
Trade and other payables	528,754	560,507	656,583
Current lease liabilities	0	0	18,909
Derivative liabilities	0	461	0

(unit: KRW 1M)

Category	2017	2018	2019
Advance receipts	10,600	171,501	77,029
Current provision	7,131	15,101	26,667
Income tax payable	175,150	200,797	212,538
Tobacco excise and other taxes payable	916,398	557,418	576,018
Non-current liabilities	335,208	381,313	406,070
Long-term debt	100,589	93,475	90,954
Long-term trade and other payable	34,436	53,240	59,638
Non-current lease liabilities	0	0	24,397
Long-term advance receipts	7,050	5,580	4,155
Net defined benefit liability	75,783	96,215	91,083
Long-term refund liabilities and payables	9,202	3,845	3,090
Deferred income tax liabilities	108,149	125,559	129,918
Non-controlling interest liabilities	0	3,400	2,836
Total liabilities	2,151,600	2,022,021	2,006,164
Equity			
Capital and reserves attributable to owners	7,772,054	8,079,280	8,650,565
Share capital	954,959	954,959	954,959
Other capital surplus	-29,720	-29,720	-29,556
Treasury stocks	-328,157	-328,157	-318,789
Gain on sale of treasury stocks	513,776	513,776	528,894
Reserve	4,927,332	5,355,628	5,671,480
Retained earnings	1,733,863	1,612,794	1,843,577
Non-controlling interests	57,707	53,800	55,369
Total equity	7,829,760	8,133,080	8,705,934
Total liabilities and equity	9,981,360	10,155,102	10,712,098

Consolidated Comprehensive Income Statement

(unit: KRW 1M)

Category	2017	2018	2019
Sales	4,667,193	4,471,516	4,963,202
Cost of goods sold	1,908,887	1,836,031	2,088,576
Gross profit	2,758,306	2,635,484	2,874,626
Selling and administrative expenses	1,332,192	1,380,378	1,492,608
Operating profit	1,426,114	1,255,107	1,382,018
Other incomes	98,281	110,050	105,871
Other losses	226,018	140,370	109,668
Finance incomes	68,635	91,585	96,705
Finance costs	27,107	6,957	13,796
Share of net profit of investment accounted for using the equity method	5,717	9,255	1,541
Profit before income tax	1,345,622	1,318,670	1,462,671
Income tax expense	181,414	420,011	424,000
Net income	1,164,208	898,659	1,038,670
Other comprehensive income	47,428	-44,724	19,464
Items that will not be reclassified to profit or loss	27,593	-52,498	-3,602
Remeasurements of net defined benefit liability	27,593	-24,807	-10,425
Gain or loss on valuation of fair value through other comprehensive income or loss	0	-27,707	6,923
Changes in assets accounted for using equity method	0	17	-100
Items that are or may be reclassified subsequently to profit or loss	19,835	7,774	23,066
Exchange differences on translation of foreign operations	-6,837	7,774	23,066
Gain or loss on valuation of available-for-sale financial assets	26,672	0	0
Total comprehensive income	1,211,637	853,935	1,058,134
Attributable net income			
Net income attributable to owners	1,163,750	901,650	1,036,475
Net income attributable to non-controlling interests	458	-2,991	2,195
Attributable comprehensive income			
Total comprehensive income attributable to owners	1,207,694	857,858	1,056,366
Total comprehensive income attributable to non-controlling interests	3,942	-3,923	1,768
Earnings per share			
Basic earnings per share	9,217	7,141	8,208
Diluted earnings per share	9,271	7,141	8,208

Statement of Changes in Equity

(unit: KRW 1M)

Category	Equity								
	Equity attributable to owners							Non-controlling interests	Total equity
	Share capital	Other capital surplus	Treasury stocks	Gain on sale of treasury stocks	Reserve	Retained earnings	Total equity attributable to owners		
Balance at January 1, 2017	954,959	-3,429	-328,157	513,776	4,296,523	1,611,532	7,045,205	72,554	7,117,758
Change in accounting policy	0	0	0	0	0	0	0	0	0
Net income	0	0	0	0	0	1,163,750	1,163,750	458	1,164,208
Other comprehensive income	0	0	0	0	16,894	27,050	43,944	3,484	47,428
Dividends	0	0	0	0	0	454,554	454,554	0	454,554
Increase (decrease) from transaction of treasury stocks	0	0	0	0	0	0	0	0	0
Increase (decrease) from disposal of retained earnings	0	0	0	0	613,915	-613,915	0	0	0
Increase (decrease) from changes in interests attributable to owners/ changes in non-controlling interests	0	-26,291	0	0	0	0	-26,291	-18,789	-45,080
Balance at December 31, 2017	954,959	-29,720	-328,157	513,776	4,927,332	1,733,863	7,772,054	57,707	7,829,760
Balance at January 1, 2018	954,959	-29,720	-328,157	513,776	4,927,332	1,733,863	7,772,054	57,707	7,829,760
Change in accounting policy	0	0	0	0	-36,766	-8,805	-45,571	0	-45,571
Net income	0	0	0	0	0	901,650	901,650	-2,991	898,659
Other comprehensive income	0	0	0	0	-19,766	-24,027	-43,793	-931	-44,724
Dividends	0	0	0	0	0	505,061	505,061	0	505,061
Increase (decrease) from transaction of treasury stocks	0	0	0	0	0	0	0	0	0
Increase (decrease) from disposal of retained earnings	0	0	0	0	485,036	-485,036	0	0	0
Increase (decrease) from changes in interests attributable to owners/ changes in non-controlling interests	0	0	0	0	-208	208	0	16	16
Balance at December 31, 2018	954,959	-29,720	-328,157	513,776	5,355,628	1,612,794	8,079,280	53,800	8,133,080
Balance at January 1, 2019	954,959	-29,720	-328,157	513,776	5,355,628	1,612,794	8,079,280	53,800	8,133,080
Change in accounting policy	0	0	0	0	0	-4,670	-4,670	0	-4,670
Net income	0	0	0	0	0	1,036,475	1,036,475	2,195	1,038,670
Other comprehensive income	0	0	0	0	29,886	-9,995	19,891	-428	19,464
Dividends	0	0	0	0	0	505,061	505,061	0	505,061
Increase (decrease) from transaction of treasury stocks	0	0	9,368	15,118	0	0	24,486	0	24,486
Increase (decrease) from disposal of retained earnings	0	0	0	0	285,966	-285,966	0	0	0
Increase (decrease) from changes in interests attributable to owners/ changes in non-controlling interests	0	164	0	0	0	0	164	-199	-36
Balance at December 31, 2019	954,959	-29,556	-318,789	528,894	5,671,480	1,843,577	8,650,565	55,369	8,705,934

Consolidated Cash Flow Statement

(unit: KRW 1M)

Category	2017	2018	2019
Cash flow from operating activities	1,143,112	821,654	1,042,489
Cash generated from operations	1,538,070	1,161,901	1,464,083
Income tax paid	-394,958	-340,247	-421,593
Cash flows from investing activities	-683,019	-46,256	-459,191
Interest received	48,763	15,800	19,146
Dividends received	24,677	21,665	24,693
Proceeds from sale of other finance assets	0	0	534,003
Reduced fair value through long-term profit or loss	0	43,058	15,892
Reduced fair value through short-term profit or loss	0	813,268	0
Reduced fair value through other comprehensive income	0	1,153	0
Proceeds from sale of tangible assets	4,324	27,335	3,738
Proceeds from sale of intangible assets	1,441	833	1,100
Proceeds from investments accounted for using the equity method	7,319	5,025	34,151
Collection of loans	13,972	14,740	12,321
Withdrawal of lease deposits	8,505	3,710	1,212
Acquirement of government funding	0	63	0
Changes in consolidated scope	482	0	0
Retrieval of finance lease receivables	0	0	75
Proceeds from held-for-sale assets	19,303	0	0
Proceeds of available-for-sale financial assets	22,835	0	0
Acquisition of tangible assets	-318,334	-353,313	-222,248
Acquisition of intangible assets	-6,390	-6,292	-34,948
Acquisition of investment properties	0	-40,557	-256,285
Acquisition of investments accounted for using the equity method	-1,000	-30,500	0
Increase in loans	-9,880	-5,935	-19,004
Increase in lease deposits	-11,578	-6,679	-3,133
Increase in long-term deposits	-72,040	-72,399	-114,412
Increase in fair value through short-term profit or loss	0	0	-57,593
Increase in fair value through long-term profit or loss	0	-93,500	-54,677
Increase in fair value through other comprehensive income	0	-1,350	0
Acquisition of other finance assets	-270,919	-382,381	-343,223
Acquisition of available-for-sale financial assets	-98,453	0	0
Acquisition of subsidiary	-46,046	0	0
Cash flows from financing activities	-438,585	-549,376	-632,146
Payment of lease liabilities	0	0	-18,604
Dividends paid	-454,554	-505,061	-505,061
Proceeds from borrowings	629,452	641,712	202,160
Transactions with non-controlling shares	0	3,430	0
Interest paid	-29,406	-2,464	-3,581
Debt paid	-584,557	-686,994	-307,061
Increase in rent deposit	1,155	0	0
Decrease in rent deposit	-652	0	0
Proceeds from issues of shares	-23	0	0
Effect of exchange rate fluctuation on cash held	3,185	-8,170	7,184
Net increase in cash and cash equivalents	24,694	217,852	-41,663
Cash and cash equivalents at January 1	690,423	715,117	932,969
Cash and cash equivalents at December 31	715,117	932,969	891,306

SUSTAINABILITY MANAGEMENT PERFORMANCE DATA

ENVIRONMENT. Environmental Responsibility for the Future

Climate Change Response

GHG emissions are managed by categorizing into direct and indirect emissions from 5 plants (Shintanjin, Youngju, Gwangju, Gimcheon, and Cheonan) and about 100 sales branches nationwide. In 2018, both GHG emission intensity and energy consumption intensity were increased due to the expansion and installation of facilities (air conditioner and water/power facilities) for producing heat-not-burn products.

Category		Unit	2017	2018	2019
GHG emissions	Direct emission (Scope 1)	tCO ₂ eq	31,187	32,980	33,509
	Indirect emission (Scope 2)	tCO ₂ eq	67,941	70,796	71,050
	Total	tCO ₂ eq	99,128	103,776	104,559
	Intensity of GHG emissions	tCO ₂ eq/KRW 100M	3.30	3.95	3.55
Energy consumption	Fuel (LNG)	TJ	540	580	591
	Electricity	TJ	1,363	1,422	1,428
	Steam	TJ	-	13	1
	Total	TJ	1,903	2,015	2,020
	Intensity of energy consumption	TJ/KRW 100M	0.06	0.08	0.07
Environmental investment*	Environmental investment plan	KRW 1M	-	-	569.5
	Environmental investment amount	KRW 1M	-	-	561.3
	Execution-to-plan rate	%	-	-	98.6

*Introduction of facilities for energy efficiency and eco-friendliness

Water Management

The data of water consumption is collected based on each water bill of Shintanjin Plant, Youngju Plant, Gwangju Plant, Gimcheon Plant, and Cheonan Plant. We comply with the principle to discharge wastewater below the standard of influencing nearby ecosystem and perform activities to reduce water discharge amount. In 2018, water consumption intensity was increased due to the expansion and installation of facilities (air conditioner and water/power facilities) for producing heat-not-burn products.

Category		Unit	2017	2018	2019
Water consumption	Water supply	Tons	365,873	376,274	386,593
	Ground water	Tons	98,700	93,646	102,594
	Total	Tons	464,573	469,920	489,187
	Intensity of water consumption	Tons/KRW 100M	15.49	17.90	16.62

Pollutant Emissions Management

The scope of waste emissions data is Shintanjin Plant, Youngju Plant, Gwangju Plant, Gimcheon Plant, and Cheonan Plant, and that of air pollutants and water pollutants is Shintanjin Plant only. In 2018, wastes emissions intensity was increased due to the expansion and installation of facilities (air conditioner and water/power facilities) for producing heat-not-burn products.

Category		Unit	2017	2018	2019
Waste emissions and recycling	Emission amount	kg	3,232,144	3,892,771	4,195,743
	Recycled amount	kg	688,006	967,600	1,283,506
	Intensity of waste emissions (excluding recycled amount)	kg/KRW 100M	84.80	111.45	98.97
Air pollutant emissions*	NOx	ppm	Not collected	Not collected	53.5
	SOx	ppm	Not collected	Not collected	Not found
	Dust	mg/Sm3	Not collected	Not collected	3.1
	VOCs	ppm	Not collected	Not collected	Not found
Water pollutant emissions*	COD	mg/L	Not collected	Not collected	13.2
	BOD	mg/L	Not collected	Not collected	7
	SS	mg/L	Not collected	Not collected	10.1

*Only applied to Shintanjin Plant

Category		2019	2020
Environmental Management training on employees	Purpose	Risk prevention training for creating a stable plant operation environment	
	Contents	<ul style="list-style-type: none"> • New or amended laws related to environment • Procedure for categorizing and treating wastes • Plans for effect response to environmental regulations 	<ul style="list-style-type: none"> • Plans for response to air pollutants by plant • Change waste management indices • Overall tasks related to environment
	Targets	Environmental managers and production managers at plants	Materials managers, compliance managers, and plant environmental managers

SOCIAL. A Better Society through Embracement

Customer Satisfaction

KT&G is strengthening the standard of customer information protection by complying with relevant laws and guidelines and acquiring domestic/overseas security certifications. As a result, there was not any breaches of customer information in 2019. We operate various channels to receive VOCs and resolve inquiries.

Category		Unit	2019
Customer information protection	No. of customer information breach	EA	0
VOC receipts by channel	Phone consultation	EA	262,760
	ARS	EA	19,372
	1 on 1 consultation	EA	19,996
	Total	EA	302,128
VOC receipts by type	Inquiries for product purchase and locations	EA	29,916
	Use of discount coupons and homepage	EA	11,349
	A/S-related inquiries	EA	237,383
	Combustible tobacco product	EA	118
	Others (phone number, general inquiries)	EA	23,362
	Total	EA	302,128

Better Work Place

As of 2019, KT&G is in contract with 4,623 employees (4,374 permanent employees and 249 temporary employees). To contribute to the job creation, we recruited 313 new employees in 2019 which is 2.4 times increase from the previous year. When signing an employment contract, we indicate that KT&G does not discriminate in labor conditions against nationality, gender, and religion, and we also strive to enhance diversity of employees. Moreover, we conduct collective bargaining with the labor union with 90% membership from employees, as well as holding the labor-management agreements. KT&G also operates systematic programs for capacity building based on autonomy to enable growth of the company and employees who are the basis for KT&G's competitiveness. Moreover, we established the organizational culture of mutual respect and provide compensation based on fair evolutions to respect employees.

Category		Unit	2017	2018	2019
Number of employees (including temporary employees)		persons	4,295	4,432	4,623
Minority employment	Employment of disabled persons	persons	136	137	125
Recruitment and turnover	New recruits	persons	100	128	313
	Turnover (retirement)	persons	127	164	144
Maternity and childcare leaves	Paternity leave	persons	97	69	73
	Maternity leave	persons	16	15	17
	Rate of return after maternity/paternity leave	%	100	100	100
	Childcare leave (male)	persons	34	30	47
	Childcare leave (female)	persons	22	25	50
	Rate of return after childcare leave (male)	%	100	100	100
	Rate of return after childcare leave (female)	%	100	100	100
	Turnover rate within 12 months of return (male)	%	2	2	6
	Turnover rate within 12 months of return (female)	%	3	-	-
Labor union	No. of qualified employees	persons	3,981	4,000	4,023
	No. of members	persons	3,577	3,515	3,604
	Membership rate	%	89.9	87.9	89.6
Employee training	Cumulative no. of training participants	persons	22,138	25,375	32,454
	Annual average training costs per person	KRW 1,000	1,070	1,050	1,387
	Annual average training hours per person	hours	117	115	124
Performance appraisal	Target employees	persons	3,699	3,707	3,796
	Rate of appraised employees	%	95.3	97.5	97
Human rights protection	No. of sexual harassment training	times	1	2	1
	No. of sexual harassment trainees	persons	3,933	3,945	3,950

KT&G identifies needs by employee lifecycle and operates various welfare system to support them. We established the assistance system for living stability, medical expense, childbirth, and childcare to enable employees to accomplish work-life balance, and we also operate various programs including leisure activities and education to offer opportunities for self-development and recharge.

Category	Details
Living stability assistance	<ul style="list-style-type: none"> • Offer housing for non-resident workers • Loan through the internal Labor Welfare Fund • Offer childcare expenses, elementary/middle school admission congratulatory money, and middle/high school and university scholarship • Special education costs for the disabled • Provide congratulatory and condolence money, accident relief money • Operate the Employee Share Ownership System
Medical expense assistance	<ul style="list-style-type: none"> • Health check: Conduct health check on an employee and spouse or one of parents annually • Medical expenses: Medical expense aid for illness of employee, spouse, and children
Leisure activities assistance	<ul style="list-style-type: none"> • Welfare card: Use in accordance with employees' various needs including fitness club, restaurant, theaters, or educational academy • Leisure facility: Use in condominiums and lodging nationwide such as Jeju Island and Gangwon Province, throughout the year • Cultural activities: Support sports game tickets and performances in SangSang Art Hall and SangSang Madang • Provide summer vacation pay
Education and other work activities assistance	<ul style="list-style-type: none"> • Support self-development of employees through various training system • Provide legalized insurances such as the 4 basic insurances • Refresh vacation system: Implement 3-week refresh vacation every 5 years (vacation pay provided) • Support internal clubs and athletic competitions • Workplace childcare facility: Located in Daejeon Head Office and Shintanjin Plant • Overseas learning for retirement • Financial assistance for capacity building
Pregnancy and childcare assistance and leave system	<ul style="list-style-type: none"> • Children schooling costs: Provide childcare financial aid until 6 years of age, provide middle/high school and university scholarship • Maternity/paternity leave: Provide leave from pregnancy to childbirth for healthy childbirth, provide KRW 1 million monthly • Childcare leave: Maximum of 2 years for stable childcare provide KRW 1 million for the 1st year, KRW 2 million for the 2nd year • In-company venture leave • Job transfer support leave: Offering opportunities to transition career for long-term employees, etc.

Worksite Safety & Health

KT&G practices the Safety Management based on the Safety/Health Management policies. The Safety & Health Office conducts industrial safety and health training to all employees, and we constantly monitor risks related to human rights in all domestic/overseas worksites.

Category		Unit	2017	2018	2019
Safety incidents	Industrial accident rate	%	0.021	0.042	0.062
	Operation hold rate	%	0.101	0.206	0.299
	Total working hours	hours	9,806,070	9,454,656	9,828,048
	Lost time days	days	272	130	390
	Lost time day rate	%	0.028	0.014	0.040

*Including laborers and temporary employees

Supply Chain Partnership

The core material of KT&G's production is tobacco leaf. We purchase tobacco leaves produced nationwide, process them to separate leaves and stems, complete production and processing of tobacco leaf materials and supplements, and produce them into cigarettes. In addition to tobacco leaves, we source non-tobacco materials (NTM) such as filters and packaging from domestic and overseas suppliers.

We set fair trade with suppliers as the principle and execute various programs for their growth and development in order to contribute to creation of health industrial ecosystem and enhance sustainability of the supply chain. To relieve financial burden of suppliers right before national holidays, we proceed with the payment earlier. Moreover, we implement the 'Haearin Project' to assist tobacco farms' extra income generation.

Category			Unit	2017	2018	2019
Materials purchase and use	Amount of materials purchase (tobacco leaf, RTL, supplements)*		KRW 1M	312,329	282,812	288,833
	Amount of materials used		Tons	43,361	37,405	38,095
Tobacco leaf supplier status	Suppliers	Domestic farmers	persons	3,365	3,144	2,880
		Overseas	EA	16	17	19
	Purchase amount	Domestic*	KRW 100M	951	947	1,175
		Overseas	KRW 100M	2,172	1,881	1,713
NTM supplier status	Suppliers	Domestic	EA	69	71	69
		Overseas	EA	9	9	12
	Purchase amount	Domestic	KRW 100M	3,364	4,258	4,122
		Overseas	KRW 100M	237	293	440
Supplier assistance	Amount of early payment		KRW 1M	46,666	30,474	45,885
Haearin Project	No. of supplying farmers		persons	23	21	20
	Amount of dried red pepper purchased		kg	9,409	11,691	10,488
	Purchase amount of dried red pepper		KRW 100M	1.87	3.23	1.58

*Including purchase amount from Tae-A Industrial (RTL manufacturer)

Social Contribution

KT&G conducts social contribution activities based on the value system of 'Hope', 'Creation', and 'Shared Growth' to fulfill social responsibility as a corporate citizen. We implement all business to operate organically from supporting the vulnerable social group to creating shared values through social issue resolution.

Category		Unit	2017	2018	2019
Social contribution investment	Social responsibility activities (Youth startup, SangSang Fund, business-related CSR, donation, etc.)	KRW 100M	174	285	507
	Cultural arts activities (SangSang Madang, SangSang Univ., etc.)	KRW 100M	813	227	343
	Amount of Scholarship Foundation/ Welfare Fund Social Contribution Investment	KRW 100M	152	157	160
	Total	KRW 100M	1,139	669	1,010
	Investment-to-sales ratio	%	3.8	2.5	3.4

GOVERNANCE. Advanced Governance to the Global Standard

Governance

As of end of May 2020, KT&G's board of directors is composed of 5 outside directors (71%) out of total 7 directors. This not only satisfies with the recommended standard of the governance structure (more than half of the board shall be outside directors), but also exceeds the average of domestic companies (51.3%, announced by the Fair Trade Commission regarding the status of large enterprises' governance in December 2019). Moreover, we stipulated that CEO and chairman of board shall be separated to create a condition that all directors can propose their opinions freely. In 2019, the board meeting was conducted 10 times, and the attendance rate of outside directors recorded 98.3% which is an increase by 1.2%p from the previous year.

Since 2011, KT&G has maintained outstanding grade in the Governance Sector of the ESG Evaluation by the KCGS for 8 consecutive years.

Category		Unit	2017	2018	2019
Board operation	No. of board meetings held	times	13	17	10
	Outside director attendance rate	%	92.2	97.1	98.3
Director compensation (Incl. directors and audit members)	Amount of compensation payment	KRW 1M	2,333	4,099	2,403
KCGS ESG evaluation rating	Governance sector	Rating	A+	A+	To be announced in October 2020

Ethical Management

In July 2019, KT&G established the 'Compliance Department' under the Business Policy Office of the Sustainability Management Headquarters to implement systematic and consistent tasks of the Compliance/Ethical Management. In 2019, we conducted the ethical awareness evaluation as a part of the compliance check to identify status of employees' ethical awareness and reported the results to the board of directors. Moreover, we are endeavoring to eliminate unethical behaviors of our employees by requesting the Ethical Practice Pledge and conducting stakeholder surveys. In addition, we take disciplinary actions such as dismissal, suspension, salary cut, and warning for any reported or exposed improper actions of employees.

- Request for employees' Ethical Practice Pledge (January)
- External stakeholder survey for checking employees' compliance with the Ethical Regulation (February)
- Think-Twice Campaign (5 times)
- Training on the Ethical Management and sexual harassment prevention to new recruits, experience employees, new executives, and managers (8 times)

Category		Unit	2017	2018	2019
Status of disciplinary actions	dismissal	cases	4	1	0
	suspension	cases	5	5	9
	salary cut	cases	1	4	7
	warning	cases	5	5	9
	Total	cases	15	17	25

INNOVATION. New Market Creation through Innovation

Research & Development

KT&G strives to develop core/base technologies for NGPs and new products customized for global customers to enhance product competitiveness. In 2019, the amount of R&D investment increased by 30.7% from the previous year.

Category		Unit	2017	2018	2019
Status of R&D	R&D investment costs	KRW 1,000	16,097,835	17,898,338	23,401,005
	R&D outcomes	EA	63	54	48
	Patents (holding)	EA	156	222	200

GRI STANDARDS INDEX

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GRI 206: Anti-competitive Behavior 2016	206-1		Legal actions for anti-competitive behavior, anti-trust, and monopoly practices	102

ENVIRONMENTAL PERFORMANCE (GRI 300)				
Topic	No.	Main Topic	Title	page
GRI 301: Materials 2016	301-1		Materials used by weight or volume	98
	301-3		Reclaimed products and their packaging materials	40
GRI 302: Energy 2016	302-1		Energy consumption within the organization	37, 94
			Energy intensity	37, 94
	302-4		Reduction of energy consumption	36~37
Main Topic: Reducing environmental impacts of worksites				
GRI 103: Management Approach	103-1		Explanation of the material topic and its Boundary	32~33
	103-2		The management approach and its components	39~41
	103-3		Evaluation of the management approach	35
GRI 303: Water 2016	303-1	●	Water withdrawal by source	94
Main Topic: Reducing GHG emissions				
GRI 103: Management Approach	103-1		Explanation of the material topic and its Boundary	32~33
	103-2		The management approach and its components	36~38
	103-3		Evaluation of the management approach	35

ENVIRONMENTAL PERFORMANCE (GRI 300)				
Topic	No.	Main Topic	Title	page
GRI 305: Emissions 2016	305-1	●	Direct (Scope 1) GHG emissions	94
	305-2	●	Energy indirect (Scope 2) GHG emissions	94
	305-4	●	GHG emissions intensity	37, 94
	305-5	●	Reduction of GHG emissions	36~37
	305-7		Nitrogen oxides (NOX), sulfur oxides (SOX), and other significant air emissions	95
GRI 306: Effluents and Waste 2016	306-2		Waste by type and disposal method	41, 95
GRI 307: Environmental Compliance 2016	307-1		Non-compliance with environmental laws and regulations	102
GRI 308: Supplier Environmental Assessment 2016	308-1		New suppliers that were screened using environmental criteria	48

SOCIAL PERFORMANCE (GRI 400)				
Topic	No.	Main Topic	Title	page
GRI 401: Employment 2016	401-1		New employee hires and employee turnover	96
	401-2		Benefits provided to full-time employees that are not provided to temporary or part-time employees	54, 57, 97
	401-3		Parental leave	96
GRI 403: Occupational Health and Safety 2016	403-2		Types of injury and rates of injury, occupational diseases, lost days, and absenteeism, and number of work-related fatalities	56, 97
	403-3		Workers with high incidence or high risk of diseases related to their occupation	56
GRI 404: Training and Education 2016	404-1		Average hours of training per year per employee	55, 96
	404-2		Programs for upgrading employee skills and transition assistance programs	54~55
	404-3		Percentage of employees receiving regular performance and career development reviews	96
GRI 405: Diversity and Equal Opportunity 2016	405-1		Diversity of governance bodies and employees	68~69, 96
	405-2		Ratio of basic salary and remuneration of women to men	54
GRI 406: Non-discrimination 2016	406-1		Incidents of discrimination and corrective actions taken	77~78
Main Topic: Respecting human rights				
GRI 103: Management Approach	103-1		Explanation of the material topic and its Boundary	32~33
	103-2		The management approach and its components	48, 53
	103-3		Evaluation of the management approach	43, 53
GRI 412: Human Rights Assessment 2016	412-1	●	Operations that have been subject to human rights reviews or impact assessments	48
	412-2	●	Employee training on human rights policies or procedures	53, 75
GRI 414: Supplier Social Assessment 2016	414-1	●	New suppliers that were screened using social criteria	48
Main Topic: Strengthening consumer protection and product responsibility				
GRI 103: Management Approach	103-1		Explanation of the material topic and its Boundary	32~33
	103-2		The management approach and its components	44~45
	103-3		Evaluation of the management approach	43
GRI 416: Customer Health and Safety 2016	416-1	●	Assessment of the health and safety impacts of product and service categories	44~45
	416-2	●	Incidents of non-compliance concerning the health and safety impacts of products and services	102
Main Topic: Responsible marketing				
GRI 103: Management Approach	103-1		Explanation of the material topic and its Boundary	32~33
	103-2		The management approach and its components	46~47
	103-3		Evaluation of the management approach	43
GRI 417: Marketing and Labeling 2016	417-1	●	Requirements for product and service information and labeling	46~47
		●	Incidents of non-compliance concerning product and service information and labeling	102
	417-3	●	Incidents of non-compliance concerning marketing communications	102
GRI 418: Customer Privacy 2016	418-1		Substantiated complaints concerning breaches of customer privacy and losses of customer data	102
GRI 419: Socioeconomic Compliance 2016	419-1		Non-compliance with laws and regulations in the social and economic area	102

1. Among the main topics, 'Transparency in forming and operating the board of directors' and 'Product innovation' are not subject to GRI Standard Topic Specific

2. Out of the current status of sanctions disclosed on page 357 of KT&G business reports in 2019, no cases have been sanctioned for 'Legal actions for anti-competitive behavior, anti-trust, and monopoly practices(206-1)', 'Non-compliance with environmental laws and regulations(307-1)', 'Incidents of non-compliance concerning the health and safety impacts of products and services(416-2)', 'Incidents of non-compliance concerning product and service information and labeling(417-2)', 'Incidents of non-compliance concerning marketing communications(417-3)', 'Substantiated complaints concerning breaches of customer privacy and losses of customer data(418-1)', 'Non-compliance with laws and regulations in the social and economic area(419-1)' during the 2019 period.

SASB INDEX

FOOD & BEVERAGE SECTOR - TOBACCO

Sustainability Disclosure Topics & Accounting Metrics

Code	Topic	Accounting metric	Category	Unit of measure	page
FB-TB-260a.1	Public Health	(1) Gross revenue and (2) revenue net of excise taxes from (a) non-tobacco nicotine products and (b) heated tobacco products	Quantitative	KRW	84
FB-TB-260a.2		Discussion of the process to assess risks and opportunities associated with “tobacco harm reduction” products	Discussion and Analysis	n/a	45, 80~85
FB-TB-270a.1	Marketing Practices	Total amount of monetary losses as a result of legal proceedings associated with marketing, labeling, and/or advertising practices	Quantitative	KRW	47
FB-TB-270a.2		Description of the company’s marketing policy and relevant positions on Articles 11 and 13 of the World Health Organization Framework Convention on Tobacco Control (WHO FCTC)	Discussion and Analysis	n/a	46

Activity Metrics

Code	Activity metric	Category	Unit of measure	page
FB-TB-000.A	Combustible tobacco product sales volume: (1) cigarette, (2) cigar, and (3) other smoked tobacco products	Quantitative	Number, Metric tons (t)	2019 KT&G Business Report (pp.41~42)
FB-TB-000.B	Non-combustible product sales volume: (1) traditional smokeless tobacco, (2) non-tobacco nicotine products, (3) heated tobacco products, and (4) nicotine replacement therapy products	Quantitative	Number	84

THIRD PARTY'S ASSURANCE STATEMENT

To the Readers of 2019 KT&G Report:

Foreword

Korea Management Registrar Inc. (hereinafter "KMR") has been requested by of KT&G Corporation to verify the contents of its 2019 KT&G Corporation Report (Hereby referred to as "the Report"). KT&G is responsible for the collection and presentation of information included in the Report. KMR's responsibility is to carry out assurance engagement on specific data and information in the assurance scope stipulated below.

Verification Methodology

KT&G describes its efforts and achievements of the corporate social responsibility activities in the Report. KMR conducted based on SRV1000 from KMR Global Sustainability Committee and SRV1000 from KMR Global Sustainability Committee as assurance standards. The assurer's assurance team (hereinafter "the assurance team") evaluated the adherence to Principles of Materiality, Understandability, Reliability and the reliability of specified sustainability performance information. In addition, the assurance team checked whether the Report satisfied the 'Core Option' requirements of GRI Standards Guidelines.

The team checked whether the Report has been prepared in accordance with the 'Core Option' of GRI Standards which covers the followings.

- GRI Standards Reporting Principles
- Universal Standards
- Topic Specific Standards
 - Management approach of Topic Specific Standards
 - Economic performance : 201-1
 - Market Presence : 202-2
 - Indirect Economic Impacts : 203-2
 - Procurement Practices : 204-1
 - Anti-Corruption : 205-3
 - Energy : 302-1, 302-4
 - Water : 303-1
 - Emissions : 305-1, 305-2, 305-5
 - Effluents and Waste : 306-2
 - Employment : 401-1, 401-2, 401-3
 - Occupational Health and Safety : 403-6
 - Training and Education : 404-1, 404-2
 - Diversity and Equal Opportunity : 405-1, 405-2
 - Human Rights Assessment : 412-1
 - Local Communities : 413-1
 - Customer Health and Safety : 416-1
 - Marketing and Labeling : 417-1
 - Customer Privacy : 418-1

This Report excludes data and information of joint corporate, contractor etc. which is outside of the organization, i.e. KT&G, among report boundaries.

Our approach

In order to verify the contents of the Report within an agreed scope of assurance in accordance with the assurance standard, the team has carried out an assurance engagement as follows:

- Reviewed overall report
- Reviewed materiality test process and methodology
- Reviewed sustainability management strategies and targets
- Reviewed stakeholder engagement activities
- Interviewed people in charge of preparing the Report

Our conclusion

Based on the results we have obtained from material reviews and interviews, we had several discussions with KT&G on the revision of the Report. We reviewed the Report's final version in order to confirm that our recommendations for improvement and our revisions have been reflected. When reviewing the results of the assurance, the assurance team could not find any inappropriate contents in the Report to the compliance with the principles stipulated below. Nothing has come to our attention that causes us to believe that the data included in the verification scope are not presented appropriately.

■ Materiality

- The Report includes all important reporting boundaries under KT&G operation and presents specific and long-term CSR strategy and targets. KT&G is determining the materiality of issues found out through stakeholder communication channels through its own materiality evaluation process, and the assurance team could not find any critical issues nor any critical stakeholder group left out in this process.

■ Understandability

- Being prepared in sustainability context, the Report specifies the targets on sustainability issues which are identified through the materiality evaluation process, and presents the backgrounds of selection of the critical issues and the management approach. And the Report explains the performance indicators in more detail and comparable way.

■ Reliability

- The assurance team identified errors in some data and information, and KT&G completed the modification before finishing the final version of the Report. We judge the data and information in the Report to be correct and reliable, and the assurance team could not find any evidence that KT&G counter measures to critical stakeholder issues were inappropriately recorded in the Report.

We could not find any evidence the Report was not prepared in accordance with the 'Core Option' of GRI standards.

Recommendation for improvement

We hope the Report is actively used as a communication tool for stakeholders and we recommend the following for improvements.

- KT&G properly placed qualitative content and images and reported key sustainability achievements based on data, enhancing understandability and readability. We recommend that the company continue to cover both positive and negative issues as it disclosed marketing lawsuits with transparency in order to deliver a balanced, reliable report.

Our independence

With the exception of providing third party assurance services, KMR is not involved in any other KT&G's business operations that are aimed at making profit in order to avoid any conflicts of interest and to maintain independence.

Aug. 6th, 2020
CEO, Eunju Hwang



E. J. Hwang

ASSOCIATIONS & MEMBERSHIPS

Membered Associations	Purpose of Establishment
Korea International Trade Association (KITA)	KITA is a trade promotion institution that suggests relaxing regulations and issues in the field of trade to the government and assists collaborative activities of the private trade and commerce and establishment of trade infrastructure.
Korea Mecenat Association (KMA)	KMA is an institution that supports mutual development of the economy and culture by playing a role as a bridge between companies that assist culture & arts and cultural groups that performs creative activities continuously.
Korea Tobacco Association (KTA)	KTA is a private organization that has the 4 major tobacco companies of Korea as members. It pursues the society's fair and objective understanding of the tobacco industry by through the data collection and distribution of information about tobacco and contributes to sound development of the Korean tobacco industry and the public economy by promoting collaboration within the industry based on the fair infrastructure and responding to social environment in regard to tobacco products.
Korea Fair Competition Federation (KFCF)	KFCF implements its role as a bridge between the government and industry by enhancing private companies' understanding of the Fair Trade Scheme, creating an environment for voluntary fair competition, and proposing to the government regarding the Fair Trade Policy.
Korea Trade-Investment Promotion Agency (KOTRA)	KOTRA is a governmental investment institution established for contributing to the national economic growth by assisting promotion of trades, investment among domestic/overseas companies, and collaboration of industrial technologies.
Korea Industrial Safety Association (KISA)	KISA is a non-profit organization for the integrated safety & health consulting aimed to create an accident-free industrial society, and it efficiently executes various tasks for preventing industrial accidents.
Korea Environmental Preservation Association (KEPA)	KEPA is a public organization under the Ministry of Environment that executes investigation/research, R&D, training/promotion, and ecological restoration on environmental preservation in order to contribute to enhance the public life by maintaining pleasant environment.

REPORT FOOTPRINTS

KT&G REPORT

KT&G published its first Sustainability Report in 2007. Since 2017, KT&G has annually published the KT&G Report that integrates an annual report that summarizes sales and financial performances and the sustainability report that includes governance, social, and environmental information. KT&G Report is developed in accordance with the GRI Standard and offered in both Korean and English.





This report was printed in soy ink.