

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis of our financial condition and results of operations for the three months ended 30 June 2008 and 2007 together with our unaudited consolidated interim condensed financial information as of and for the three and six months ended 30 June 2008. The unaudited consolidated interim condensed financial information has been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting*. This consolidated interim condensed financial information should be read together with the audited consolidated financial statements for the year ended 31 December 2007 prepared in accordance with International Financial Reporting Standards (IFRS).

The financial and operating information contained in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" comprises information of OAO NOVATEK and its consolidated subsidiaries (hereinafter jointly referred to as "we" or the "Group").

OVERVIEW

We are Russia's largest independent natural gas producer and the second-largest producer of natural gas in Russia after Gazprom. In terms of proved natural gas reserves, we are the fourth largest holder of natural gas resources in Russia after Gazprom, Rosneft and LUKOIL.

Our exploration, development, production and processing of natural gas, gas condensate, crude oil and related oil products have been conducted primarily within the Russian Federation. We sell our natural gas volumes exclusively in the Russian domestic market. We export our stable gas condensate directly to international markets while liquefied petroleum gas and crude oil are generally delivered to both international (including CIS) and domestic markets. We generally sell our oil products produced from our unstable gas condensate on the domestic market. We began limited commercial trading operations in September 2007 through our wholly-owned Swiss-based trading subsidiary, RUNITEK, by primarily purchasing and reselling refined products on the international markets.

SELECTED DATA

<i>millions of Russian roubles except as stated</i>	Three months ended 30 June:		Change
	2008	2007	%
Financial results			
Total revenues (net of VAT and export duties)	21,352	15,052	41.9%
Operating expenses	(11,822)	(9,010)	31.2%
Profit attributable to NOVATEK shareholders	7,053	4,216	67.3%
EBITDA ⁽¹⁾	10,339	7,109	45.4%
Earnings per share (in Russian roubles)	2.32	1.39	66.9%
Operating results			
Natural gas sales volumes (mmcm)	7,979	7,722	3.3%
Stable gas condensate sales volumes (thousand tons)	383	389	(1.5%)
Liquefied petroleum gas sales volumes (thousand tons)	150	125	20.0%
Crude oil sales volumes (thousand tons)	72	57	26.3%
Oil product sales volumes (thousand tons)	41	13	215.4%
Cash flow results			
Net cash provided by operating activities	7,935	4,494	76.6%
Capital expenditures	9,470	3,003	215.4%

⁽¹⁾ EBITDA represents net income before finance income (expense) and income taxes from the statement of income, and depreciation, depletion and amortization and share-based compensation from the statement of cash flows.

CERTAIN FACTORS AFFECTING OUR RESULTS OF OPERATIONS

Natural gas prices

As an independent natural gas producer, we are not subject to the government's regulation of natural gas prices. Historically, we have sold most of our natural gas at prices higher than the regulated prices set by the government for Gazprom's domestic gas sales, although the prices we can achieve are strongly influenced by the prices regulated by the Federal Tariffs Service (FTS), a governmental agency. In the three months ended 30 June 2008, the weighted average FTS price for the regions where we delivered our natural gas increased by RR 314 per mcm, or 24.6%, to RR 1,593 per mcm compared to RR 1,279 per mcm in the corresponding period in 2007. The terms for delivery of natural gas affect our average realized prices. Natural gas sold "ex-field" is sold primarily to wholesale gas traders, in which case the buyer is responsible for the payment of gas transportation tariffs. Sales to wholesale traders allow us to diversify our gas sales without incurring additional commercial expenses. However, we generally realize higher prices and net margins for natural gas volumes sold directly to the end-customers, as the gas transportation tariff is included in the contract price and no retail margin is lost to wholesale gas traders. During the three months ended 30 June 2008, the average netback margin differential we received on end-customer sales compared to ex-field sales (average end-customer netback less average ex-field price) increased by RR 15 per mcm compared to the period in 2007 as a result of higher average realized prices to end-customers (see "Natural gas sales" below). During the three months ended 30 June 2008, however, the rate of growth in our average natural gas price sold ex-field exceeded the respective rate of growth on our average netback price sold to end-customers by 1.2%.

In November 2006, the FTS approved and published a plan to liberalize the price of natural gas sold on the Russian domestic market by the year 2011. Effective 1 January 2008, the FTS approved a 25% increase in the regulated price of natural gas for the year 2008. As part of that program, we expect further increases in the regulated price for natural gas in 2009 and 2010. The FTS approves the effective increase on an annual basis and reserves the right to modify the percentages published based on market conditions and other factors.

The following table shows our average realized natural gas sales prices (net of VAT) for the three months ended 30 June 2008 and 2007:

<i>Russian roubles per mcm</i>	Three months ended 30 June:		Change %
	2008	2007	
Average natural gas price to end-customers	1,842	1,518	21.3%
Gas transportation expense for sales to end-customers	752	636	18.2%
Average natural gas netback price on end-customer sales	1,090	882	23.6%
Average natural gas price ex-field (wholesale traders)	970	777	24.8%
Average netback margin differential	120	105	14.3%

We also participate in the electronic trading of natural gas at non-regulated prices utilizing the electronic trading facilities of Mezhregiongaz, a subsidiary of Gazprom. Our average natural gas netback prices on electronic trading (e-trading) are shown in the table below:

<i>Russian roubles per mcm</i>	Three months ended 30 June:		Change %
	2008	2007	
Average natural gas price to customers on e-trading sales	1,327	1,057	25.5%
Gas transportation expense on e-trading sales	134	114	17.5%
Average natural gas netback on e-trading sales	1,193	943	26.5%

Crude oil, stable gas condensate, liquefied petroleum gas and oil products prices

Crude oil, stable gas condensate, liquefied petroleum gas (“LPG”) and oil products prices on international markets have historically been volatile depending on, among other things, the balance between supply and demand fundamentals, and the ability and willingness of oil producing countries to sustain production levels to meet increasing global demand and potential disruptions in global crude oil supplies due to war, geopolitical developments, terrorist activities or natural disasters. Crude oil, stable gas condensate, LPG and oil products prices on the domestic market also fluctuate depending on supply and demand fundamentals amongst other factors. Crude oil prices in Russia had historically remained below prices in the international market primarily due to constraints on the ability of many Russian oil companies to transport their crude oil, whereas certain oil products and LPG prices in Russia have more closely followed prices on international markets. Recently, however, the domestic crude oil prices have tracked closely to the international benchmark prices. Crude oil that we sell bound for international markets is transported through the Transneft pipeline system where it is blended with other crude oil of varying qualities to produce an export blend commonly referred to as “Urals blend”, which normally trades at a discount to the international benchmark Brent crude oil.

Our stable gas condensate, LPG (excluding obligatory domestic deliveries at regulated prices), crude oil and oil products prices at both international and domestic markets include transportation expense in accordance with the terms of delivery. Our delivery terms for the sale of crude oil on the domestic market changed effective January 2008 whereby our contract prices cover transportation expense as we are responsible for transportation, and the buyer takes ownership and associated risks at the point of its destination. Correspondingly, revenues and prices for the comparative period of 2007 were adjusted to gross up transportation expenses.

In the three months ended 30 June 2008 our stable gas condensate export delivery terms were delivery to the port of destination ex-ship (DES) while in the corresponding period in 2007 delivery terms were delivery to the port of destination ex-ship (DES) or priced at cost and freight (CFR). Our average export stable gas condensate contract price, including export duties, in the three months ended 30 June 2008 was approximately USD 1,063 per ton compared to approximately USD 632 per ton in the corresponding period in 2007.

In the three months ended 30 June 2008, we did not deliver our crude oil to the international markets due to our ability to achieve higher margins on the domestic market.

The following table shows our average realized stable gas condensate and crude oil sales prices (net of VAT and export duties, where applicable) for the three months ended 30 June 2008 and 2007:

<i>Russian roubles (RR) or US dollars (USD) per ton</i>	Three months ended 30 June:		Change
	2008	2007	%
Stable gas condensate			
Net export price, RR per ton	17,098	12,097	41.3%
Net export price, USD per ton	723.6	467.8	54.7%
Domestic price, RR per ton	10,678	8,464	26.2%
Crude oil			
Net export price, RR per ton	-	7,504	n/m
Net export price, USD per ton	-	290.2	n/m
Domestic price, RR per ton	9,076	6,136	47.9%

Our LPG export and CIS delivery terms during the three months ended 30 June 2008 were delivery at frontier (DAF) at the border of the customer’s country. In the three months ended 30 June 2008, our average export LPG contract price, including export duties, was approximately USD 810 per ton compared to USD 492 per ton in the corresponding period in 2007. We are obliged to sell a portion of our LPG volumes at regulated prices while the remaining portion of our sales are sold under commercial terms. In the three months ended 30 June 2008, we sold 13 thousand tons at the average regulated price (excluding transportation expense) of RR 4,500 per ton and 110 thousand tons at a average commercial price of RR 10,918 per ton in the domestic market, compared to 10 thousand tons at RR 3,500 per ton and 84 thousand tons at RR 6,665 per ton, respectively, in the 2007 period.

Domestic sales of oil products associated with our own production were priced free carrier (FCA) at the Surgut railroad station (located in the Khanty-Mansiysk Autonomous Region). In the three months ended 30 June 2008, our foreign trading subsidiary purchased from third parties approximately 36 thousand tons of naphtha and sold 32 thousand tons to the US market at an average contract price USD 1,073 per ton. The delivery terms for these

volumes were delivery to the port of destination ex-ship (DES). There were no applicable export duties on these sales.

The following table shows our average realized liquefied petroleum gas and oil products sales prices (net of VAT and export duties, where applicable) for the three months ended 30 June 2008 and 2007 (excluding trading activities):

<i>Russian roubles (RR) or US dollars (USD) per ton</i>	Three months ended 30 June:		Change %
	2008	2007	
LPG			
Net export price, RR per ton	13,160	9,573	37.5%
Net export price, USD per ton	557.0	370.2	50.5%
CIS price, RR per ton	11,786	8,076	45.9%
Domestic price, RR per ton	10,236	6,317	62.0%
Oil products			
Domestic price, RR per ton	4,126	7,084	(41.8%)

Transportation tariffs

The methodology of calculating transportation tariffs for natural gas produced in the Russian Federation for shipments to consumers located within the customs territory of the Russian Federation and the member states of the Customs Union Agreement (Belarus, Kazakhstan, Kyrgyzstan and Tajikistan) consists of two parts: a rate for the utilization of the trunk pipeline and a transportation rate per mcm per 100 km. The rate for utilization of the trunk pipeline is based on an “input/output” function which is determined by where natural gas enters and exits the trunk pipeline (the maximum “input/output” rate effective from 1 January 2008 is RR 1,351.01 (excluding VAT) per mcm) and includes a constant rate of RR 20.01 (excluding VAT) per mcm for end-customers using Gazprom’s gas distribution systems. The constant rate is deducted from the utilization rate for end-customers using non-Gazprom gas distribution systems. The second component of the transportation rate for natural gas delivered within the customs territory of the Russian Federation and the member states of the Customs Union Agreement was set at RR 6.07 effective from 1 March 2007 and was increased by 19.1% from 1 January 2008 to RR 7.23 per mcm per 100 km (excluding VAT).

The increases in regulated transportation tariffs are passed on to our end-customers pursuant to delivery terms in the majority of our contracts. There is no set timetable for reviews or changes in transportation tariffs set by the FTS, and thus changes in transportation tariffs occur on an irregular basis.

We transport most of our crude oil through the pipeline network owned and operated by Transneft, Russia’s state-owned monopoly crude oil pipeline operator. Our transportation tariffs for the transport of crude oil through Transneft’s pipeline network are also set by the FTS. The overall expense for the transport of crude oil depends on the length of the transport route from the producing field to the ultimate destination.

Our stable gas condensate (to the port of Vitino on the White Sea), LPG and oil products are transported by rail which is owned and operated by Russian Railways, Russia’s state-owned monopoly railway operator. Our transportation tariffs for transport by rail are also set by the FTS and vary depending on product and length of transport route.

We deliver our stable gas condensate to international markets using the loading and storage facilities at the Port of Vitino on the White Sea and tankers for transportation to US, European and South American markets. The costs associated with the transportation of stable gas condensate by tanker are determined by the distance to the final destination, tanker availability, seasonality of deliveries and standard shipping terms.

Transactions with related parties

All natural gas producers and wholesalers operating in Russia transport their natural gas volumes through the Unified Gas Supply System (UGSS), which is owned and operated by OAO Gazprom, a State monopoly and a shareholder of OAO NOVATEK from October 2006. As an independent natural gas producer, we utilize the UGSS to transport natural gas to end-customers at the tariff established by the FTS.

Our tax burden

We have not employed any tax minimization schemes using offshore or domestic tax zones in the Russian Federation.

We are subject to a wide range of taxes imposed at the federal, regional, and local levels, many of which are based on revenue or volumetric measures. In addition to income tax, significant taxes to which we are subject include VAT, unified natural resources production tax (UPT), export duties, property tax, social taxes and contributions.

In practice, Russian tax authorities often have their own interpretation of tax laws that rarely favors taxpayers, who have to resort to court proceedings to defend their position against the tax authorities. Differing interpretations of tax regulations exist both among and within government ministries and organizations at the federal, regional and local levels, creating uncertainties and inconsistent enforcement. Tax declarations, together with related documentation such as customs declarations, are subject to review and investigation by a number of authorities, each of which may impose fines, penalties and interest charges. Generally, taxpayers are subject to an inspection of their activities for a period of three calendar years which immediately precedes the year in which the audit is conducted. Previous audits do not completely exclude subsequent claims relating to the audited period. In addition, in some instances, new tax regulations have been given retroactive effect.

OPERATIONAL HIGHLIGHTS

Hydrocarbon sales volumes

In the three months ended 30 June 2008, our natural gas sales volumes increased primarily due to an increase in both production by 152 mmcm and purchases from third parties by 216 mmcm. Our liquids sales volumes (crude oil, stable gas condensate, LPG and oil products) increased primarily due to an increase in liquids production and purchases.

Natural gas sales volumes

<i>millions of cubic meters</i>	Three months ended 30 June:		Change %
	2008	2007	
Production from:			
Yurkharovskoye field	2,526	2,383	6.0%
East-Tarkosalinskoye field	3,781	3,780	0.0%
Khancheyevskoye field	1,064	1,056	0.8%
Other fields	7	7	0.0%
Total natural gas production	7,378	7,226	2.1%
Purchases from:			
Gazprom	483	474	1.9%
Other	318	111	186.5%
Total natural gas purchases	801	585	36.9%
Total production and purchases	8,179	7,811	4.7%
Purovsky Plant and own usage	(5)	(7)	(28.6%)
Decrease (increase) in pipeline and underground gas storage facilities	(195)	(82)	137.8%
Total natural gas sales volumes	7,979	7,722	3.3%
<i>Sold to end-customers</i>	<i>3,430</i>	<i>3,266</i>	<i>5.0%</i>
<i>E-trading sales</i>	<i>23</i>	<i>265</i>	<i>(91.3%)</i>
Subtotal sales treated as sold to end-customers	3,453	3,531	(2.2%)
Sold ex-field	4,526	4,191	8.0%

In the three months ended 30 June 2008, our total consolidated natural gas production increased by 152 mmcm, or 2.1%, compared to the corresponding period in 2007. The increase was mainly due to organic growth in natural gas production at our Yurkharovskoye field.

In the three months ended 30 June 2008, our natural gas purchases increased by 216 mmcm, or 36.9%, compared to the corresponding period in 2007, primarily due to an increase in purchases from 'other' suppliers. In the 2008 period, we purchased additional volumes of natural gas to meet additional demand and maximize our end-customer sales.

At 30 June 2008, our natural gas volumes stored in Gazprom's underground gas storage facilities totaled 210 mmcm, representing an increase of 209 mmcm during the period. The remaining change related to decreases in gas volumes in pipeline. We expect our volumes of natural gas injected into underground gas storage facilities to continue to fluctuate period-to-period depending on market conditions, storage capacity constraints and our development plans to either sustain and/or grow production during periods of seasonality.

Liquids sales volumes

<i>thousands of tons</i>	Three months ended 30 June:		Change %
	2008	2007	
Production from:			
Yurkharovskoye field	188	172	9.3%
East-Tarkosalinskoye field	220	204	7.8%
Khancheyevskoye field	164	175	(6.3%)
Other fields	25	24	4.2%
Total liquids production	597	575	3.8%
Purchases from:			
Other	38	-	n/m
Total liquids purchases	38	-	n/m
Total production and purchases	635	575	10.4%
Losses ⁽¹⁾	(5)	(5)	0.0%
Decreases (increases) in liquids inventory balances	16	14	14.3%
Total liquids sales volumes	646	584	10.6%
<i>Stable gas condensate export</i>	<i>380</i>	<i>386</i>	<i>(1.6%)</i>
<i>Stable gas condensate domestic</i>	<i>3</i>	<i>3</i>	<i>n/m</i>
Subtotal stable gas condensate	383	389	(1.5%)
<i>LPG export</i>	<i>13</i>	<i>20</i>	<i>(35.0%)</i>
<i>LPG CIS</i>	<i>14</i>	<i>11</i>	<i>27.3%</i>
<i>LPG domestic</i>	<i>123</i>	<i>94</i>	<i>30.9%</i>
Subtotal LPG	150	125	20.0%
<i>Crude oil export</i>	<i>-</i>	<i>32</i>	<i>n/m</i>
<i>Crude oil domestic</i>	<i>72</i>	<i>25</i>	<i>188.0%</i>
Subtotal crude oil	72	57	26.3%
<i>Oil products export</i>	<i>33</i>	<i>-</i>	<i>n/m</i>
<i>Oil products domestic</i>	<i>8</i>	<i>13</i>	<i>(38.5%)</i>
Subtotal oil products	41	13	215.4%

⁽¹⁾ Losses associated with processing at the Purovsky Plant and Surgutsky refinery as well as during rail road, trunk and tanker transportation.

In the three months ended 30 June 2008, our gas condensate and crude oil production increased by 22 thousand tons, or 3.8%, to 597 thousand tons compared to 575 thousand tons in the 2007 period. The higher gas condensate yields from the East-Tarkosalinskoye field were due to changes in the technical parameters of the gas separation process which result in a higher output of gas condensate from gas mix. The increase at our Yurkharovskoye field was due mainly to organic production growth at the field. We also put into operation new wells at our East-Tarkosalinskoye field in the second half of 2007 which increased our crude oil production in the 2008 period.

At 30 June 2008, we had 149 thousand tons of stable gas condensate in transit and recognized as inventory until such time as it is delivered to the port of destination compared to 176 thousand tons as of 30 June 2007. Our stable gas condensate in transit and recognized as inventory was reduced by 23 thousand tons as at 30 June 2008 as compared to the inventory balance as at 31 March 2008, while in the corresponding period of 2007 the inventory balance reduced by 14 thousand tons. The remaining change in liquids inventory balances related to changes in other liquid products.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED 30 JUNE 2008 COMPARED TO THE THREE MONTHS ENDED 30 JUNE 2007

The following table and discussion is a summary of our consolidated results of operations for the three months ended 30 June 2008 and 2007. Each line item is also shown as a percentage of our total revenues.

<i>millions of Russian roubles</i>	Three months ended 30 June:			
	2008	% of total revenues	2007	% of total revenues
Total revenues (net of VAT and export duties)	21,352	100.0%	15,052	100.0%
<i>including:</i>				
natural gas sales	10,740	50.3%	8,494	56.4%
liquids sales	9,672	45.3%	6,056	40.2%
Other income (loss)	(195)	(0.9%)	9	0.1%
Total revenues and other income	21,157	99.1%	15,061	100.1%
Operating expenses	(11,822)	(55.4%)	(9,010)	(59.9%)
Profit from operations	9,335	43.7%	6,051	40.2%
Finance income (expense)	22	0.1%	42	0.3%
Share of income (loss) of associated companies	(45)	(0.2%)	-	n/m
Profit before income tax and minority interest	9,312	43.6%	6,093	40.5%
Total income tax expense	(2,256)	(10.6%)	(1,883)	(12.5%)
Profit for the period	7,056	33.0%	4,210	28.0%
Minority interest	(3)	0.0%	6	0.0%
Profit attributable to NOVATEK shareholders	7,053	33.0%	4,216	28.0%

Total revenues and other income

The following table sets forth our sales (net of VAT and export duties where applicable) and other income (loss) for the three months ended 30 June 2008 and 2007:

<i>millions of Russian roubles</i>	Three months ended 30 June:		Change %
	2008	2007	
Natural gas sales	10,740	8,494	26.4%
<i>End-customer</i>	6,319	4,956	27.5%
<i>E-trading</i>	30	281	(89.3%)
<i>Ex-field</i>	4,391	3,257	34.8%
Stable gas condensate sales	6,525	4,692	39.1%
<i>Export</i>	6,497	4,668	39.2%
<i>Domestic</i>	28	24	16.7%
Liquefied petroleum gas sales	1,601	877	82.6%
<i>Export</i>	174	194	(10.3%)
<i>CIS</i>	163	88	85.2%
<i>Domestic</i>	1,264	595	112.4%
Crude oil sales	655	395	65.8%
<i>Export</i>	-	241	n/m
<i>Domestic</i>	655	154	325.3%
Oil products sales	890	92	867.4%
<i>Export</i>	819	-	n/m
<i>Domestic</i>	71	92	(22.8%)
Total oil and gas sales	20,411	14,550	40.3%
Sales of polymer and insulation tape	580	411	41.1%
Other revenues	361	91	296.7%
Total revenues	21,352	15,052	41.9%
Other income (loss)	(195)	9	n/m
Total revenues and other income	21,157	15,061	40.5%

Natural gas sales

In the three months ended 30 June 2008, our revenues from sales of natural gas increased by RR 2,246 million, or 26.4%, compared to the corresponding period in 2007. The increase in natural gas revenues was primarily attributable to an overall increase in prices and to a lesser extent an increase in volumes sold. Revenues from the sale of natural gas accounted for 50.3% and 56.4% of our total revenues in the three months ended 30 June 2008 and 2007, respectively. The change in natural gas sales as a percentage of total revenues was primarily due to an increase in both our average prices for liquids and volumes sold.

In the three months ended 30 June 2008, our average realized natural gas price per mcm increased by RR 246 per mcm, or 22.4%, to RR 1,346 per mcm from RR 1,100 per mcm in the corresponding period in 2007. Our proportion of natural gas sold to end-customers, including e-trading sales, on a volume basis, decreased from 45.7% in the three months ended 30 June 2007 to 43.3% in the 2008 period mainly due to a decrease in volumes sold on the electronic exchange as well as an increase in volumes sold ex-field. The average realized prices of our natural gas sold directly to end-customers, at the electronic trading system and natural gas sold ex-field were higher by 21.3%, 25.5% and 24.8%, respectively, in the three months ended 30 June 2008 compared to the corresponding period in 2007. Our sales of natural gas to end-customers were primarily to energy utilities and large industrial companies in both periods.

In the three months ended 30 June 2008, our e-trading natural gas sales decreased by RR 251 million, or 89.3%, primarily due to a reduction in volumes sold on the electronic trading exchange by 242 mmcm, or 91.3%, from 265 mmcm in the 2007 period which was partially offset by an increase in the average sales prices we received for these volumes sold. Our e-trading natural gas sales were primarily to energy utility companies in both periods.

Stable gas condensate sales

In the three months ended 30 June 2008, our revenues from sales of stable gas condensate increased by RR 1,833 million, or 39.1%, compared to the corresponding period in 2007 due to an overall increase in export contract prices.

In the three months ended 30 June 2008, we exported 380 thousand tons of stable gas condensate, or 99.2% of our sales volumes, to the United States, while in the corresponding period in 2007 our export sales volumes were higher by 6 thousand tons with delivery to markets both in the United States and Europe. We delivered all of our stable gas condensate to the international markets using the loading and storage facilities at the Port of Vitino on the White Sea and via leased tankers.

In the three months ended 30 June 2008, our average realized price, excluding export duties, and translated into US dollars, for stable gas condensate sold on the export market increased by USD 255.8 per ton, or 54.7%, to USD 723.6 per ton (DES) from USD 467.8 per ton (DES and CFR) in the corresponding period in 2007. The increase in the average realized export price was the result of a 68.2% increase in our average export contract price that was partially offset by an increase in our average export duty per ton by 107.2%. The increase in our average realized contract prices was due to the overall increase in prices on international markets in the 2008 period.

Liquefied petroleum gas sales

In the three months ended 30 June 2008, our revenues from the sales of LPG increased by RR 724 million, or 82.6%, compared to the corresponding period in 2007, primarily due to an increase in domestic prices and volumes.

In the three months ended 30 June 2008, we increased our sales volumes of LPG by 25 thousand tons, or 20.0%, to 150 thousand tons mainly due to an increase in LPG throughput at our Purovsky Plant, of which 82.0% of LPG volumes was sold domestically for an average price of RR 10,236 per ton (FCA excluding VAT). This represents an increase of RR 3,919 per ton, or 62.0%, compared to the corresponding period in 2007. The remaining volumes of LPG were sold as follows: 8.7% was sold to the export market for an average price of USD 557.0 per ton (DAF excluding export duties) representing an increase of USD 186.8 per ton, or 50.5%, compared to the three months ended 30 June 2007; and 9.3% was sold in the CIS for an average price of RR 11,786 per ton (DAF) representing an increase of RR 3,710 per ton, or 45.9%, compared to the three months ended 30 June 2007. The increase in our average realized export prices (excluding export duties) was primarily due to an increase in our average contract prices by 64.6% combined with a 101.3% increase in our average export duty per ton in the 2008 period.

Crude oil sales

In the three months ended 30 June 2008, our revenues from the sales of crude oil increased by RR 260 million, or 65.8%, compared to the corresponding period in 2007, due to an increase in both prices and volumes sold. The increase in crude oil volumes available for sale by 15 thousand tons, or 26.3%, from 57 thousand tons in the three months ended 30 June 2007 to 72 thousand tons in the 2008 period was mainly attributable to an increase in crude oil production at our East-Tarkosalinskoye field.

Our average realized crude oil domestic sales price (excluding VAT) increased by RR 2,940 per ton, or 47.9%, to RR 9,076 per ton in the three months ended 30 June 2008, compared to RR 6,136 per ton in the 2007 period. The increase in our average realized contract prices was due to the overall increase in prices on international and domestic markets in the 2008 period.

Oil products sales

In the three months ended 30 June 2008, our revenue from the sales of oil products increased by RR 798 million, or 8.7 times, compared to the corresponding period in 2007, due to the commencement of oil products trading activities on the international markets by our foreign trading subsidiary.

In the three months ended 30 June 2008, we purchased 36 thousand tons of oil products and resold 32 thousand tons to customers in the United States for an average contract price of USD 1,073 per ton (DES). At 30 June 2008, 14 thousand tons were recorded as "goods in transit" in inventories until such time as they are delivered to the port of destination compared to 11 thousand tons at 31 March 2008.

Our domestic oil products sales decreased by RR 21 million, or 22.8%, to RR 71 million in the three months ended 30 June 2008 from RR 92 million in the 2007 period due to a decrease in volumes sold.

In the three months ended 30 June 2008, our domestic oil products sales volumes related to our own production decreased from 13 thousand tons to 6 thousand tons due to the migration of processing of our unstable gas condensate from the Surgutsky refinery to the Purovsky Plant. The price we received for our oil product sales also decreased by RR 2,958 per ton, or 41.8%, from RR 7,084 per ton to RR 4,126 per ton as the output we received from the refining process resulted in lower value products as compared to the corresponding 2007 period.

In the three months ended 30 June 2008, our domestic oil products sales volumes sold via our domestic trading operations were two thousand tons compared to nil in the corresponding period in 2007. The price we received from our trading activities in the 2008 period was RR 20,142 per ton.

Sales of polymer and insulation tape

Our revenues from the sales of polymer and insulation tape increased by RR 169 million, or 41.1%, to RR 580 million in the three months ended 30 June 2008, compared to RR 411 million in the 2007 period mainly due to an increase in BOPP film wrap production.

Revenues from our sales of BOPP film wrap increased by RR 212 million, or 145.2%, from RR 146 million in the three months ended 30 June 2007 to RR 358 million in the 2008 period due to a more efficient utilization of the facilities which increased the volumes available for sale. The proportion of BOPP film wrap sales to total sales of polymer and insulation tape increased by 26.2% to 61.7% in the three months ended 30 June 2008 compared to 35.5% in the 2007 period.

Our revenues from pipe insulation product sales increased by RR 3 million, or 2.0%, from RR 152 million in the three months ended 30 June 2007 to RR 155 million in the 2008 period mainly due to an increase in prices. Revenues from polymer pipes sales decreased by RR 29 million, or 30.5%, from RR 95 million in the three months ended 30 June 2007 to RR 66 million in the 2008 period primarily due to a decrease in volumes sold. The remaining RR 1 million and RR 18 million in the three months ended 30 June 2008 and 2007 related to sales of other polymer products.

Other revenues

Other revenues include geological and geophysical research services, rent, polymer tolling, transportation, handling, storage and other services. In the three months ended 30 June 2008, other revenues increased by RR 270 million, or 296.7%, to RR 361 million from RR 91 million in the corresponding period in 2007. The increase in other revenues was primarily due to commencement of selling geological and geophysical research to our associates in the fourth quarter 2007, which accounted for RR 248 million in the three months ended 30 June 2008, compared to nil in the corresponding period in 2007.

In the three months ended 30 June 2008, revenues from transportation, handling and storage services increased by RR 17 million whereas the remaining increase of RR 5 million was composed of various immaterial items.

Other income (loss)

In the three months ended 30 June 2008, we realized other net loss of RR 195 million, while in the corresponding period of 2007 we realized a net income of RR 9 million.

In June 2008, we disposed our long-term finance lease with OAO "Gazprom" for a cash consideration of RR 360 million and, as a result, recognized a net loss of RR 212 million. The subject of the finance lease was certain oil and gas assets located at the West-Tarkosalinskoye field, which license belongs to Gazprom. The usage of the disposed items was no longer considered economically viable to maintain on our balance sheet.

Operating expenses

In the three months ended 30 June 2008, our total operating expenses increased by RR 2,812 million, or 31.2%, to RR 11,822 million as compared to RR 9,010 million in the corresponding period in 2007. The increase was largely due to purchases of natural gas and liquid hydrocarbons, as well as increases in transportation costs, materials, services and other, and general and administrative expenses. Total operating expenses decreased as a percentage of total revenues to 55.4% in the three months ended 30 June 2008 compared to 59.9% in the corresponding period in 2007, as shown in the table below.

<i>millions of Russian roubles</i>	Three months ended 30 June:			
	2008	% of total revenues	2007	% of total revenues
Transportation expenses	4,229	19.8%	3,528	23.4%
Taxes other than income tax	1,792	8.4%	1,615	10.8%
Non-controllable expenses	6,021	28.2%	5,143	34.2%
Materials, services and other	1,743	8.2%	1,141	7.6%
Purchases of natural gas and liquid hydrocarbons	1,632	7.6%	423	2.8%
General and administrative expenses	1,516	7.1%	1,109	7.4%
Depreciation, depletion and amortization	984	4.6%	992	6.6%
Exploration expenses	185	0.9%	207	1.4%
Net impairment expense	10	n/m	16	n/m
Change in natural gas, liquid hydrocarbons, and polymer products and work-in-progress	(269)	n/m	(21)	n/m
Total operating expenses	11,822	55.4%	9,010	59.9%

Non-controllable expenses

A significant proportion of our operating expenses are characterized as non-controllable expenses since we are unable to influence the increase in regulated tariffs for transportation of our hydrocarbons or the rates imposed by federal, regional or local tax authorities. In the three months ended 30 June 2008, non-controllable expenses of transportation and taxes other than income tax increased by RR 878 million, or 17.1%, to RR 6,021 million from RR 5,143 million in the corresponding period in 2007. The change was primarily due to an increase in the transportation tariff for natural gas and a combined increase in the transportation tariffs and volumes sold for liquids. Taxes other than income tax increased primarily due to higher mineral production taxes for crude oil. As a percentage of total revenues our non-controllable expenses decreased by 6.0% to 28.2% in the three months ended 30 June 2008 compared to 34.2% in the corresponding period in 2007.

Transportation expenses

In the three months ended 30 June 2008, our total transportation expenses increased by RR 701 million, or 19.9%, compared to the corresponding period in 2007.

<i>millions of Russian roubles</i>	Three months ended 30 June:		Change %
	2008	2007	
Natural gas transportation to customers	2,581	2,106	22.6%
Stable gas condensate, liquefied petroleum gas and oil products transportation by rail	1,004	839	19.7%
Stable gas condensate transported by tankers	523	519	0.8%
Unstable gas condensate transportation from the fields to the processing facilities through third party pipelines	48	30	60.0%
Oil products transported by tankers	34	-	n/m
Crude oil transportation to customers	31	33	(6.1%)
Other transportation costs	8	1	n/m
Total transportation expenses	4,229	3,528	19.9%

In the three months ended 30 June 2008, our transportation expenses for natural gas increased by RR 475 million, or 22.6% to RR 2,581 million from RR 2,106 million in the corresponding period in 2007. The increase was mainly due to higher transportation tariffs effective from 1 January 2008 (see "Transportation tariffs" above). We are not able to influence the transportation route of natural gas sold to end-customers and

therefore we have no control over our average delivery distance. Our average transportation distance for natural gas sold to end-customers fluctuates period-to-period.

In the three months ended 30 June 2008, our total expenses for transportation by rail increased by RR 165 million, or 19.7%, due to a slight increase in volumes sold and higher railroad transportation tariffs. In the three months ended 30 June 2007, our combined volumes of stable gas condensate, LPG and oil products sold and transported via rail increased by 14 thousand tons, or 2.7%, to 541 thousand tons from 527 thousand tons in the 2007 period.

Our expense for stable gas condensate transported by rail to export markets increased by RR 79 million, or 14.5%, from RR 544 million to RR 623 million, or from RR 1,409 per ton in the three months ended 30 June 2007 to RR 1,639 per ton in the 2008 period. The increase in the transportation rate per ton was primarily due to a tariff increase of approximately 14.9% from 1 January 2008 and 1.2% from 1 April 2008.

In the three months ended 30 June 2008, our expense for LPG transported by rail amounted to RR 378 million, of which RR 71 million was related to export sales, RR 40 million to CIS sales, and RR 267 million to domestic sales, or RR 5,383 per ton, RR 2,891 per ton, and RR 2,165 per ton, respectively. In the three months ended 30 June 2007, transportation expenses for LPG amounted to RR 287 million, of which RR 100 million was related to export sales, RR 26 million to CIS sales, and RR 161 million to domestic sales, or RR 4,935 per ton, RR 2,344 per ton and RR 1,711 per ton, respectively. In the three months ended 30 June 2008, our LPG rail transportation expense was primarily affected by an increase in both transportation tariffs and volumes sold.

The remaining RR 3 million of the transportation expenses by rail in the three months ended 30 June 2008 and RR 8 million in the corresponding period in 2007 were related to the transportation of oil products and other railroad services not allocated between products.

Total transportation expense for delivery of stable gas condensate by tanker to international markets increased marginally by RR 4 million, or 0.8%, from RR 519 million in the three months ended 30 June 2007 to RR 523 million in the 2008 period. The change was primarily due to higher average freight rates as a result of increasing the average delivery distance to international markets that was partially offset by a 1.6% decrease in stable gas condensate volumes sold. In the three months ended 30 June 2008, we delivered 100.0% of our stable gas condensate export volumes to the US market compared to 85.7% in the corresponding period in 2007.

Taxes other than income tax

<i>millions of Russian roubles</i>	Three months ended 30 June:		Change
	2008	2007	%
Unified natural resources production tax (UPT)	1,631	1,421	14.8%
Property tax	142	152	(6.6%)
Other taxes	19	42	(54.8%)
Total taxes other than income tax	1,792	1,615	11.0%

In the three months ended 30 June 2008, taxes other than income tax increased by RR 177 million, or 11.0%, of which RR 210 million was due to UPT increase, that was partially offset by decreases of RR 10 million and RR 23 million in property tax and other taxes, respectively.

The increase in our UPT by RR 210 million, or 14.8%, was primarily due to an increase in mineral production taxes for crude oil and gas condensate, which accounted for RR 123 million and RR 60 million, respectively. In the three months ended 30 June 2008, our crude oil production tax rate increased by 73.1% and our volumes of crude oil produced increased by 10.7%.

In the three months ended 30 June 2008, our property tax expense decreased by RR 10 million, or 6.6%, to RR 142 million compared to RR 152 million in the corresponding period in 2007 primarily due to disposal of assets in one of our production subsidiaries.

Materials, services and other

In the three months ended 30 June 2008, our materials, services and other expenses increased by RR 602 million, or 52.8%, to RR 1,743 million compared to RR 1,141 million in the corresponding period in 2007. The main components of this expense were employee compensation and materials and supplies, which comprised 34.9% and 25.2%, respectively, of total materials, services and other expenses in the 2008 period.

<i>millions of Russian roubles</i>	Three months ended 30 June:		Change %
	2008	2007	
Employee compensation	608	422	44.1%
Materials and supplies	439	383	14.6%
Repair and maintenance	83	94	(11.7%)
Electricity and fuel	71	52	36.5%
Tolling and processing fees	65	52	25.0%
Fire safety and security expense	41	65	(36.9%)
Other	125	73	71.2%
Subtotal materials, services and other	1,432	1,141	25.5%
Operator services expense	311	-	n/m
Total materials, services and other	1,743	1,141	52.8%

Employee compensation increased by RR 186 million, or 44.1%, to RR 608 million compared to RR 422 million in the corresponding period in 2007. The change was primarily due to an increase in average wages and bonuses paid at our production entities which resulted in an additional RR 160 million in employee compensation paid in the 2008 period. The remaining increase in employee compensation of RR 26 million was due to additional staffing at our subsidiaries, mainly Yurkharovskoye field and the Purovsky processing plant, due to growth in our activities.

Materials and supplies expense increased by RR 56 million, or 14.6%, mainly due to higher production of polymers and insulation tape products and the associated increase in purchases of raw materials.

Repair and maintenance expenses decreased by RR 11 million, or 11.7%, from RR 94 million in the three months ended 30 June 2007 to RR 83 million in the 2008 period due to the disposal of certain assets in our subsidiaries.

In the three months ended 30 June 2008, we incurred an increase in our average electricity tariff mainly at our production entities which increased our electricity and fuel expenses by RR 19 million, or 36.5%.

Tolling and processing fees increased by RR 13 million, or 25.0%, primarily due to an increase in third parties processing tariffs related to de-ethanization of unstable gas condensate produced at the Yurkharovskoye field.

Fire safety and security expenses decreased by RR 24 million, or 36.9%, to RR 41 million from RR 65 million in the three months ended 30 June 2007 primarily due to a reduction in fire safety services provided by third parties at our production entities. During the fourth quarter 2007, the Group organized its own fire safety departments to meet the Group's overall fire and safety requirements at its production and processing facilities.

Other expenses include rent expenses, transport of raw materials, telecommunication services, and miscellaneous operating expenses. In the three months ended 30 June 2008, other expenses increased by RR 52 million, or 71.2%, of which RR 24 million related to transportation expenses related to raw materials.

Operator services expense represents geological and geophysical research provided by the Group to our associated companies. In the three months ended 30 June 2008, we provided services totaling RR 311 million to the Severo Russkiy, Anomalniy, Zapadno-Tazovskiy and Sredniy Chaselskiy fields. Corresponding revenues received from our associates are shown as other revenues in the consolidated statement of income.

In the three months ended 30 June 2008, our materials, services and other expenses, excluding operator services expenses, increased by RR 291 million, or 25.5%, to RR 1,432 million as compared to RR 1,141 million in the corresponding period in 2007.

Purchases of natural gas and liquid hydrocarbons

Purchases of natural gas and liquid hydrocarbons increased by RR 1,209 million, or 285.8%, to RR 1,632 million from RR 423 million in the corresponding period in 2007 primarily due to purchases of oil products, namely naphtha, on the international markets for resale, which amounted to RR 900 million in the 2008 period. Purchases of natural gas increased by RR 286 million, or 67.8%, from RR 422 million in the three months ended 30 June 2007 to RR 708 million in 2008 period, due to increases in both volumes purchased from third parties and prices.

General and administrative expenses

In the three months ended 30 June 2008, our general and administrative expenses increased by RR 407 million, or 36.7%, to RR 1,516 million compared to RR 1,109 million in the corresponding period in 2007. The main components of these expenses were employee compensation, maintenance of social infrastructure and charitable contributions, legal, audit, and consulting services which, on aggregate comprised 80.3% and 79.2% of total general and administrative expenses in the three months ended 30 June 2008 and 2007, respectively.

<i>millions of Russian roubles</i>	Three months ended 30 June:		Change %
	2008	2007	
Employee compensation	995	576	72.7%
Maintenance of social infrastructure and charitable contributions	136	140	(2.9%)
Legal, audit, and consulting services	87	162	(46.3%)
Business trip expenses	71	45	57.8%
Rent expense	39	39	0.0%
Fire safety and security expense	34	32	6.6%
Insurance expense	26	29	(10.3%)
Other	128	86	48.8%
Total general and administrative expenses	1,516	1,109	36.7%

Employee compensation increased by RR 419 million, or 72.7%, to RR 995 million compared to RR 576 million in the corresponding period in 2007, primarily due to higher bonuses resulted in employee compensation increase of RR 255 million, or 60.9%. The remaining RR 164 million related to increase in staff wages.

In the three months ended 30 June 2008, our maintenance of social infrastructure and charitable contributions decreased marginally by RR 4 million, or 2.9%, to RR 136 million compared to RR 140 million in corresponding period in 2007, and were primarily related to our continued support for charities and social programs in the regions where we operate.

Legal, audit and consulting services expenses decreased by RR 75 million, or 46.3%, to RR 87 million compared to RR 162 million in the corresponding period in 2007. The decrease was largely due to a reduction in consulting services provided to the Group for various management efficiency programs and information technology system reviews that were provided for in the 2007 period.

Our rent expenses remained unchanged and amounted to RR 39 million in the three months ended 30 June 2008 and 2007, respectively, and were primarily attributable to rent of office space in Moscow.

Insurance expense decreased by RR 3 million, or 10.3%, to RR 26 million compared to RR 29 million in the three months ended 30 June 2007. The decrease was primarily due to lower Group insurance rates resulted from a reduction in claims for accidents.

Depreciation, depletion and amortization

In the three months ended 30 June 2008, our depreciation, depletion and amortization (“DDA”) expense decreased by RR 8 million, or 0.8%, compared to the corresponding period in 2007 due to reduction in straight-line depreciation. In the 2008 period, our DDA per barrel of oil equivalent (boe) was RR 16.4 compared to DDA per boe of RR 16.8 in the corresponding period in 2007. The change in our DDA per boe was largely due to an increase in our proved developed reserves estimates as of 31 December 2007.

Change in natural gas, liquid hydrocarbons, and polymer products and work-in-progress

We reduced our operating expenses by recording a credit to our change in inventory of RR 269 million in the three months ended 30 June 2008 as compared to the RR 21 million in the corresponding period in 2007. The credit represents an adjustment to our operating expenses for “goods in transit” and volumes held in storage at the end of the period (see “Operational highlights” above).

In the three months ended 30 June 2008, our inventory balance of oil products purchased on international markets and not sold increased by three thousand tons. In addition, in the three months ended 30 June 2008, we injected 209 mmcm of natural gas into the underground gas storage facilities as compared to 140 mmcm in the corresponding period in 2007.

In addition, we recorded a change in inventory relating to work-in-progress for operator services provided to our associates in the amount of RR 136 million for the three months ended 30 June 2008.

Profit from operations

As a result of the factors discussed above, our profit from operations increased by RR 3,284 million, or 54.3%, to RR 9,335 million in the three months ended 30 June 2008 compared to RR 6,051 million in the corresponding period in 2007. In the three months ended 30 June 2008, our profit from operations as a percentage of total revenues increased to 43.7 % as compared to 40.2% in the corresponding period in 2007.

Finance income (expense)

In the three months ended 30 June 2008, we recorded a net finance income of RR 22 million compared to RR 42 million in the 2007 period. The decrease was mainly due to hard currency conversion costs incurred in the 2008 period.

In the three months ended 30 June 2008, interest expense decreased by RR 13 million, or 20.3%, due to a reduction in our weighted average debt balances. Interest income decreased by RR 17 million, or 17.2%, primarily due to a decrease in interest income on funds held on account as bank deposits, that was partially offset by an increase in interest income on loans issued to our associates. During the period, we recorded a net foreign exchange loss of RR 9 million compared to a net gain of RR 7 million in the corresponding period in 2007.

Share of income (loss) of associated companies

In the three months ended 30 June 2008, we recognized share in loss of associated companies of RR 45 million. Loss recognized by our associated companies was due to expensing of geological and geophysical research incurred in the 2008 period under the successful efforts accounting policy.

Income tax expense

Our overall consolidated effective income tax rates (total income tax expense calculated as a percentage of our reported IFRS profit before income tax) were 24.1% and 30.9% for the three months ended 30 June 2008 and 2007, respectively. Our effective income tax rate, after excluding the effect of foreign subsidiaries, was 24.1% and 32.2% in the 2008 and 2007 periods, respectively. Russian statutory income tax rate for both periods was 24%. The difference between our effective and statutory income tax rates is primarily due to certain non-deductible expenses.

Profit attributable to shareholders and earnings per share

As a result of the factors discussed above, profit for the period increased by 2,846 million, or 67.6%, to RR 7,056 million in the three months ended 30 June 2008 from RR 4,210 million in the corresponding period in 2007. The profit attributable to NOVATEK shareholders increased by RR 2,837 million, or 67.3%, to RR 7,053 million in the three months ended 30 June 2008 from RR 4,216 million in the corresponding period in 2007.

We increased our weighted average basic and diluted earnings per share by RR 0.93 per share, or 66.9%, from RR 1.39 per share in the three months ended 30 June 2007 to RR 2.32 per share in the 2008 period based on the profits attributable to NOVATEK’s shareholders.

LIQUIDITY AND CAPITAL RESOURCES

The following table shows our net cash flows from operating, investing and financing activities for the three months ended 30 June 2008 and 2007:

<i>millions of Russian roubles</i>	Three months ended 30 June:		Change %
	2008	2007	
Net cash provided by operating activities	7,935	4,494	76.6%
Net cash used in investing activities	(9,497)	(2,813)	237.6%
Net cash provided (used) in financing activities	294	(2,817)	n/m

<i>Liquidity ratios</i>	30 June 2008	31 December 2007	Change %
Current ratio	1.49	1.41	5.7%
Total debt to equity	0.09	0.08	12.5%
Long-term debt to long term debt and equity	0.046	0.001	n/m
Net debt to total capitalization ⁽¹⁾	0.03	0.03	0.0%

⁽¹⁾ Net debt represents total debt less cash and cash equivalents. Total capitalization represents total debt, total equity and deferred income tax liability.

Net cash provided by operating activities

In the three months ended 30 June 2008, our net cash provided by operating activities increased by RR 3,441 million, or 76.6%, to RR 7,935 million compared to RR 4,494 million in the corresponding period in 2007. The change was mainly attributable to higher operating income from our oil and gas sales as a result of strong average realized prices for our natural gas and liquids volumes that were partially offset by an increase in income tax paid.

Net cash used in investing activities

Net cash used in investing activities increased by RR 6,684 million, or 237.6%, to RR 9,497 million in the three months ended 30 June 2008 compared to RR 2,813 million in the corresponding period in 2007. The change in the 2008 period was primarily due to an increase in capital expenditures related to further development of our three core fields and the construction activities associated with the second phase expansion of the Purovsky Processing plant.

Net cash used in financing activities

In the three months ended 30 June 2008, net cash provided by financing activities amounted to RR 294 million compared to net cash used in financing activities amounted to RR 2,817 million in the corresponding period in 2007. A significant amount of net cash used in financing activities in the three months ended 30 June 2007 related to repayments of borrowings and the payment of dividends. Net cash provided by financing activities in the 2008 period represents an excess of our proceeds from borrowings over debt repayments and dividends paid.

Working capital

Our net working capital position (current assets less current liabilities) at 30 June 2008 was RR 6,111 million compared to RR 4,963 million at 31 December 2007. The strengthening of our working capital position was the result of strong operating activities and financial results. The change by RR 1,148 million was mainly due to an increase in cash and cash equivalents and trade and other receivables and a decrease in short-term debt that was partially offset by an increase in accounts payable and a decrease in prepayments and other current assets at 30 June 2008.

Capital expenditures

Total capital expenditures on property, plant and equipment for the three months ended 30 June 2008 and 2007 are as follows:

<i>millions of Russian roubles</i>	Three months ended 30 June:		Change %
	2008	2007	
Exploration and production	8,793	2,862	207.2%
Other	677	141	380.1%
Total	9,470	3,003	215.4%

Exploration and production expenditures represent our investments in exploring for and developing our oil and gas properties. During both reporting periods, the majority of our capital expenditures related to ongoing development and exploration activities at our three core fields. In the three months ended 30 June 2008, we spent RR 364 million, RR 784 million, RR 4,246 million and RR 985 million for field development at the Khancheyskoye, East-Tarkosalinskoye, Yurkharovskoye and Sterkhovoye fields, respectively, and RR 2,163 million on construction of the second phase at the Purovsky Processing Plant.

Debt obligations

At 30 June 2008, the Group had a short-term USD denominated loans from BNP PARIBAS Bank in the amount of RR 2,346 million (USD 100 million) repayable in September 2008. In the three months ended 30 June 2008, the Group repaid loans from CALYON S.A. and CALYON RUSBANK Corporate and Investment Bank in total amount of RR 2,367 million (USD 100 million) according to the scheduled maturities.

In the three months ended 30 June 2008, the Group obtained a USD 800 million unsecured syndicated term loan facility for general corporate purposes. At 30 June 2008, RR 4,423 million (USD 189 million), net of transaction costs incurred, was withdrawn under this facility agreement.

At 30 June 2008, the Group had unused short-term credit facilities in the aggregate amount of RR 7,588 million (USD 323 million) on either fixed or variable interest rates subject to the specific type of credit facility. In addition, the Group has available funds up to the maximum amount of RR 2,346 million (USD 100 million) under a two year credit line facility with UniCredit Bank with interest rates negotiated on each withdrawal dates. At 30 June 2008 no funds were withdrawn under this facility.

QUALITATIVE AND QUANTITATIVE DISCLOSURES AND MARKET RISKS

We are exposed to market risk from changes in commodity prices, foreign currency exchange rates, and interest rates. We are exposed to commodity price risk as our prices for crude oil and stable gas condensate destined for export sales are linked to international crude oil prices. We are exposed to foreign exchange risk to the extent that a portion of our sales revenues, costs, receivables, loans and debt are denominated in currencies other than Russian roubles. We are subject to market risk from changes in interest rates that may affect the cost of our financing. From time to time we may use derivative instruments, such as commodity forward contracts, commodity price swaps, commodity options, foreign exchange forward contracts, foreign currency options, interest rate swaps and forward rate agreements, to manage these market risks, and we may hold or issue derivative or other financial instruments for trading purposes.

Foreign currency risk

Our principal exchange rate risk involves changes in the value of the Russian rouble relative to the US dollar and Euro. As of 30 June 2008, RR 4,445 million, or 54.5%, of our long-term debt was denominated in US dollars (out of RR 8,160 million of our total borrowings at that date). Changes in the value of the Russian rouble relative to the US dollar will impact our foreign currency-denominated costs and expenses and our debt service obligations for foreign currency-denominated borrowings in Russian rouble terms as well as receivables at our foreign subsidiaries. We believe that the risks associated with our foreign currency exposure are partially mitigated by the fact that a portion of our total revenues, approximately 35.1% in the three months ended 30 June 2008, is denominated in US dollars. As of 30 June 2008, the Russian rouble had appreciated by approximately 4% against the US dollar since 1 January 2008.

A hypothetical and instantaneous 10% strengthening in the Russian rouble in relation to the US dollar as of 30 June 2008 would have resulted in an estimated foreign exchange gain of approximately RR 679 million on foreign currency denominated borrowings held at that date.

Commodity risk

Substantially all of our crude oil, stable gas condensate and LPG export sales are sold under spot contracts. Our export prices are linked to international crude oil prices. External factors such as geopolitical developments, natural disasters and the actions of the Organization of Petroleum Exporting Countries affect crude oil prices and thus our export prices.

The weather is another factor affecting demand for and, therefore, the price of natural gas. Changes in weather conditions from year to year can influence demand for natural gas and to some extent gas condensate and oil products.

From time to time we may employ derivative instruments to mitigate the price risk of our sales activities. In our consolidated interim condensed financial information all derivative instruments are recorded at their fair values. Unrealized gains or losses on derivative instruments are recognized within other income (loss), unless the underlying arrangement qualifies as a hedge.

Pipeline access

We transport substantially all of our natural gas through the Gazprom owned UGSS. Gazprom is responsible for gathering, transporting, dispatching and delivering substantially all natural gas supplies in Russia. Under existing legislation, Gazprom must provide access to the UGSS to all independent suppliers on a non-discriminatory basis provided there is capacity not being used by Gazprom. In practice, however, Gazprom exercises considerable discretion over access to the UGSS because it is the sole owner of information relating to capacity. There can be no assurance that Gazprom will continue to provide us with access to the UGSS, however, we have not been denied access in prior periods.

Ability to reinvest

Our business requires significant ongoing capital expenditures in order to grow our production. An extended period of low natural gas prices or high transportation tariffs would limit our ability to maintain an adequate level of capital expenditures, which in turn could limit our ability to increase or maintain current levels of production and deliveries of natural gas, gas condensate, crude oil and other associated products, adversely affecting our results.

Off balance sheet activities

As of 30 June 2008, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are typically established for the purpose of facilitating off-balance sheet arrangements.