

JSC Gazprom Neft

3Q 2012 Financial Results November 8, 2012

Anna Sidorkina, Head of Investor Relations

Good evening ladies and gentlemen! I'd like to welcome you at our conference hall here in Saint Petersburg. My name is Anna Sidorkina, Investor Relations. Today's conference call will present the Company's results in accordance with the IFRS for the nine months of 2012. Allow me to introduce the participants: the financial results will be presented by Alexei Yankevich, Member of the Management Board & CFO; Mikhail Zhechkov will be speaking about the Upstream, he's Head of Economics and Investment Department of Upstream; then Vladimir Konstantinov, Head of Economics and Investment Department of Downstream, and then, for the Q&A, we will be joined by Sergey Vakulenko, Head of Strategic Planning Department, and we also expect the First Deputy General Director, Vadim Yakovlev.

I would like to say that today there is a technical possibility to download the presentation from the Russian version of our website, so again, either watch us online through webcast or you can download the presentation, whichever is more convenient for you.

Before the presentation, and I hope you are seeing it on the website, we would like to remind you once again that the presentation and all the comments thereto and everything that will be said during the conference call will have forward-looking statements that relate to business of Gazprom Neft and its results. So any statements other than statements of historical facts are or may be deemed to be forward-looking statements. So, forward-looking statements are things of future expectations that are based on management's current expectations and assumptions and there are certain risks and uncertainties that could cause the actual results to differ materially from those expressed or implied in the statements during this conference call.

And I am passing the floor to Alexei Yankevich.

Alexei Yankevich, Member of the Management Board, CFO

Good evening ladies and gentlemen! We will be presenting the Gazprom Neft results for the nine months of 2012. The results are good. I hope you are glad about the results too. All key indicators are up: the revenue has grown by 20%, the EBITDA has grown by 10%, the net profit has grown by nearly 9%. The production results have become much better: hydrocarbon production has risen by 5% Y-o-Y and it's the one of the best results in the industry, refining throughput has increased by nearly 6% and the retail throughput per one filling station has risen by 28%. We are continuing with our projects. We are actively carrying out the new projects. We have started test oil production at Messoyakha. We've drilled a first horizontal well on Novoport field and the flow rate is quite great, about 150 tonnes per day. We have started our production in Venezuela, where we've drilled a well which provides 800 barrels a day. We have started the second pilot in the Orenburg region and actually it proved to be a point of growth for the Company. After the start of gasoline and diesel hydrotreaters at Omsk refinery, we are ready to completely switch to Class-5 gasoline and diesel fuel production. Also we have made a serious step in the development of our retail network and we've increased our presence in the bunkering and airplane fuel markets.

Speaking of the results for the third quarter, the third quarter was quite successful, as was for many other oil companies. Compared to the second quarter, we showed stable results in the hydrocarbon production, but we increased the refining throughput volume, increased the revenue, substantially increased the EBITDA and the net profit: the EBITDA grew by 37% and it amounted to a record RUB 96 billion in the third quarter, the net profit grew by 84% and was RUB 56 billion, which is above the expectations.

Speaking of the environment, that was favorable enough after the correction of decreasing oil prices in the second quarter. The prices have recovered in the third quarter and that resulted in so-called duty-lag effect. You can see in that graph very well the export duties in the third quarter were lower despite the price growth, because the customs duties usually lag behind the oil price growth, and that resulted in a positive effect. The most part of this effect was gained by the companies who export a lot of oil. Our company has got a smaller share of the pie. So despite the good growth of financial results, our dynamics is more modest than for our competitors. Nevertheless, the nine months of this year were very successful, showing very good dynamics.

With that I would like to pass the floor to Mikhail Zhechkov, who will speak about the upstream part.

Mihail Zhechkov, Head of Economics and Investment Department of Upstream

Good afternoon ladies and gentlemen! I will show the results for the upstream part for the third quarter. Like Alexey said, we were successful enough in the third quarter. We kept our leading position regarding the growth rate of production in the industry. Our plan is to increase the hydrocarbon production for the current year by 5% Y-o-Y. The superior performance of OPEX/boe was mainly due to increased gas production: Orenburg consolidation and the increased gas production in whole, and also due to the successful realization of the contracting strategy and the effective goal setting within benchmarking project achieving best practice results at key management performance indicators.

Further, jointly with SIBUR we implemented a project at the Vyngapurovskiy gas processing plant in the framework of mutual increase in capacity. We improved our APG utilization rate at the Vyngapurovskaya group of fields from 70% to 79%. This project is the one step of the program to achieve the 95% APG utilization rate. The significant increase of the APG utilization rate is planned in the year 2013 (81%) that fully meets our plans.

Then the successful consolidation of the Orenburg assets, as was said by Alexey, allowed us to provide another growth point in this year and for the subsequent time. We managed to begin the project processing and to increase the production in a short time. We made very good moves technically and personnel wise. We increased the production by 8% Q-o-Q. We are actively developing the Orenburg field. The quantity of drilling rigs was tripled. And we are preparing to increase the production in the year 2013. In the framework of the Orenburg production cluster developing was acquired Baleykinskoye field with C1+C2 reserves of 8.2 MMTonnes. Location of this field allows infrastructure sharing with Kapitonovskoye and Tsarichanskoye fields and provides synergy effect and development in this region.

At our previous conference we mentioned a hard-to-recover reserves development program. We are in the process of implementing this program. As was said, the hard-to-recover reserves are 550 MMTonnes. In terms of our legacy fields we increased additionally the production by 1,000 tonnes a day from hard-to-recover reserves in third quarter that provided the 13% growth Q-o-Q. The average flow rate from hard-to-recover reserves amounted to 32.9 tonnes a day. We can say also about the increased technological effectiveness of hydrofracs. In the year 2011, we did not make any multi-stage hydrofracs and did not drill any dual-leg horizontal wells. We drilled the dual-leg horizontal wells in the year 2007, but they were pilots. Now we are going to use that technology on a permanent basis. In the development of hard-to-recover reserves we will rely on our horizontal wells: the number of horizontal wells drilled increased by 72% compared to the last year, the growth of average flow was 46% or 152 tonnes. The efficiency of 4-5 stage hydrofracs in the third quarter was 120 tonnes per day. In the second quarter there were 2-3 stage hydrofracs, so we have improved the technologies, have increased the flow rate, have improved the efficiency. The flow of the dual-leg horizontal wells is 90 tonnes/day but in our plans to increase it further.

As for major projects, as it was mentioned, in terms of Novoport we launched two horizontal wells and now one well is being tested and one well is being drilled. The flow rates are quite good, about 160 tonnes per day. In terms of Messoyakha, we are working on four new wells, one well is being tested and one well is being drilled. Potentially the wells are with a flow rate of 100 tonnes a day. In terms of Orenburg, we have grown by, like I said, 8% Q-o-Q and we've grown by 9% in our SeverEnergiya and there are active drilling works. As for Kuyumba, we have successfully implemented the exploration program. We drilled two wells, we acquired 3D seismic, C1+C2 reserves increased up to 16.5 MMtonnes, we started test production. The flow rate for wells drilled is 80-100 tonnes per day. In Serbia (NIS), the growth was 10% Y-o-Y. In terms of Iraq, Garmian and Shakal production sharing contracts were signed. And in Venezuela we started the "early production" project successfully. We are building railroads and the flow rate is 800 barrels a day, we are drilling four wells. So the works are proceeding as planned.

I've finished, thank you.

Anna Sidorkina, Head of Investor Relations

Now, the presentation about Downstream by Vladimir Konstantinov, Head of Economics and Investment Department of Downstream. Thank you.

Vladimir Konstantinov, Head of Economics and Investment Department of Downstream

Good afternoon, ladies and gentlemen! As for Downstream, we were also very successful in the third quarter. The growth of refining volumes was 5.8% Y-o-Y. Increasing the refining throughput, we are continuing our major investment projects at the all Company's refineries. We've practically completed the construction of diesel hydrotreater at Omsk and in November we expect to launch this unit and improve the qualitative characteristics of diesel fuel production in this refinery. In our Moscow refinery, we are finishing the isomerization and gasoline FCC hydrotreater unit and in the first quarter of the next year we will commission this facility. We are also continuing construction of second line of lubricant plant at Omsk, this refers to construction of lubricant blending complex. Apart from that, we invest in environment protection very actively. We completed construction of closed cycle mechanical treatment facilities at Moscow refinery. By the end of the year we are going to commission our diesel hydrotreater at Omsk. We are also reconstructing a diesel hydrotreater at Moscow refinery that will allow us to increase significantly the production of diesel Class-4 and 5. And one more important event, by the end of the year we plan to launch the hydrotreating and hydro-cracking unit at NIS, which also will allow us to produce Euro-5 gasoline and diesel.

As for sales, it is noteworthy that we have very high growth rate in premium sales, by 20% compared to the last year. This growth is mainly through the growth of average throughput per filling station; the growth has been 28% for Russian network. Apart from that, we are continuing to improve our retail network. In the third quarter we built, rebuilt and bought 32 filling stations and rebranded 26 filling stations. Certainly it increases the efficiency of sales in the retail segment. We are not only increasing the efficiency of sales, we are also expanding our business regarding to aviation, bunkering and lubricants premium channels. We are increasing our presence in international and domestic markets. By the end of the year we are planning to keep the growth rate for premium channels. We are planning to construct, reconstruct and acquire 152 filling stations and rebrand 39 filling stations in Russia and CIS.

As for our resources, in the third quarter of this year compared to the third quarter of the last year, they have grown significantly thanks to our product facilities and thanks to our active position in the oil market. We increased purchases of oil and as a result we managed despite the repair works at our Moscow plants to increase the oil export. The oil export has grown by more than 30%. Compared to second quarter 2012, the refining has grown by 4.3%, especially at Omsk and YANOS. On the Q-o-Q basis there was not such growth of the oil export because our resources have not grown very significantly.

As for the efficiency of oil delivery to the refineries compared to the efficiency of exports, the traditional picture remains. Only in August 2012 the efficiency was practically equal, but as a whole for the third quarter and for the year the efficiency of refining is much higher than the efficiency of export.

As for separate assets, we increased the refining throughput in Omsk by 5% Q-o-Q. As for Moscow refinery, in 2012 we had repair works, so the refining throughput was smaller by 5%, but because of the increased YANOS refining capacity, we retained our presence in the central region.

We did not only increase the refining throughput, we also increased the quality of our petroleum products. In slide 18, you can see that the production of high-grade fuels increased Y-o-Y. Class-5 gasoline has reached 42% share, taking into account that last year we did not produce Class-5 gasoline at all. As for diesel, one fourth of total diesel output was Class-5 fuel. The share of the high-class products will grow after launching gasoline and diesel hydrotreaters at our refineries. In Yaroslavl, 100% of all diesel and gasoline that is produced is Class-5.

As for our sales in the third quarter, on the one hand, the efficiency of sales is increasing, in particular we have reached a high level of average sales per filling station in the third quarter, which was about 18.5 tonnes a day, which is a very high result and it's quite clear that it improved our economic parameters, especially

given that our network has grown. The number of filling stations was observed both in Russia and in CIS. As for our activities in premium channels, I mean lubricants, aviation and bunkering channels, practically everywhere we increased our share in the Russian market: for jet fuel – up to 19%, for bunkering – up to 19.5% (up 2 p.p.), for lubricants – up to 10.5%. As for the motor fuels sold at filling stations, the growth is even more significant (+3.6%) and our share is 13.6%. In the nine months there was another significant event: our company has become the first in Russia in supplying the fuels and jet fuel to the domestic market and for us this is very important, because on the one hand we recognise that the domestic market for us is very important for our development. On the other hand, we are glad that our activity in modernising our networks and rebranding has been very efficient, as well as building new filling stations and our results even exceeded our expectations.

That is briefly everything, thank you.

Alexey Yankevich, Member of the Management Board, CFO

Ladies and gentlemen, I will continue. Concerning the financial part, as I said already, we had a good revenue growth compared to the last year and the previous quarter, the operation revenue has grown by 10% Y-o-Y. That is because of the improvement of the macroeconomic situation and because of the more efficient management, you can see it in the next slides. The net profit growth Y-o-Y was lagging behind EBITDA and that was because we had an one-off item, realized gain on hedging, for the nine months of 2011 that we didn't have in this year. So given the situation we still feel our net profit should grow by 10%. The growth of net profit was ahead of the operating profit, because of the non-operating activities: there were a foreign exchange gain in the third quarter and a foreign exchange loss in the second quarter.

Traditionally we are conducting a factor analysis and we see the influence of the macroeconomic environment and the management efforts. You can see that this 10% growth of operating income Y-o-Y is explained by half by better macroeconomic conditions and the growth of prices, which were partially compensated by transport tariffs and higher taxes, and the second half is thanks to the efficient management efforts that resulted in increased production volume, in increased refining throughput and sales volume, and also the optimising of product mix, increase of sales in the premium segments, and the reduction of OPEX.

As for the dynamics of the third quarter compared to the previous quarter, here the impact of the environment was more significant. The third quarter was much better than the second one in prices. The duty lag effect was also very beneficial, because export duty was lower – did not grow as fast as the prices. The management contributed too. The growth of volumes and our efficiency improvement program had also the positive effect on dynamics.

Apart from the growth of the operating profit, we can boast of good cash flows. In nine months, \$1.9 billion free cash flow was generated. Net borrowings amounted to RUB 26 billion. The main part of this borrowings was bonds issued in September. A little bit over \$1 billion of dividends was paid and about \$100 million were investments through our joint ventures, as Messoyakha and our projects in Venezuela, in Cuba, and others.

Speaking in more details about the investments, that's the next slide, the investment has grown compared to the last year. The major growth was in refining, 76%, and that is because of the quality improvement program in the Moscow refinery and also the commissioning of MHC/DHT at Panchevo, which was successfully commissioned in the fourth quarter. Also, we have seen a serious growth in Upstream greenfield projects, especially in Orenburg and also in Kurdistan. And there was a growth in marketing and distribution, which is explained by our expansion of our network in Serbia and other countries. We have acquired on behalf of NIS an oil storage facility in Bulgaria. Also we've done a number of efforts in Russia and CIS. There was a growth from quarter to quarter. The greenfields were a major contributor in this case and part of that growth is because of our increasing of investment in Messoyakha field and entry-fee for Kurdistan project.

As for our financial policy and managing the credit portfolio, we are trying to optimise our portfolio to make it longer, on the one hand, and, on the other hand, to optimise the value. We managed to do that in the third quarter. We decreased the share of short-term loans in our portfolio. Apart from that, we reduced average interest rate from 3.37% to 3.35% and that is a good thing. The credit portfolio was extended through the successful placement of the Eurobonds that was one of the best transactions in recent times. There was a 1.5 billion Eurobond issuance with 4.375% coupon rate.

I would like to finish my presentation with that. In summary, I can say that we are happy with the results. This year has been another successful year for the Company and this is proved by the results of the nine months,

and we expect the trend to continue, and we hope that you will be happy about the results and now we are ready to answer your questions.

Questions&Answers

Anton Fedotov – Bank of America Merrill Lynch

Good evening! This is Anton Fedotov, Bank of America Merrill Lynch. Thank you for the presentation. I have three questions. Question number one: your strategy in terms of the Messoyakha field and Slavneft, concerning possible acquisition of TNK-BP by Rosneft. The second question is about the plans for oil shale of JV SPD, and the third one is about your plans for the downstream development in Europe. Thanks.

Sergey Vakulenko, Head of Strategic Planning Department

Good evening! My name is Sergey Vakulenko. The deal between Rosneft and TNK-BP has not been finalised yet. In any case Slavneft proved itself as JV with good results and we are going to continue on this line. We have been cooperating with Rosneft in other joint venture, such as Tomskneft, and that collaboration proved to be very successful. So we do not see any problem in cooperating with neither TNK-BP nor Rosneft.

As per the oil shale at Salym – it is not actually oil shale; it is equivalent of light tight oil what is produced at American fields like Bakken, Barnett, or Eagleford. Our team was at Shell's fields in USA. We are going to drill the pilot wells to prove the geo-mechanical properties of the rock and then we will develop a program for the development of the field. Our geologists tell us that Bazhenov formation in this idea is probably the most promising, when it concerns Salym in western Siberia.

However a third question was about our downstream assets in West Europe, it is an interesting situation, a lot of assets are put forward for sale, but the situation keeps volatile. We keep watching the situation without taking any action so far.

Anton Fedotov – Bank of America Merrill Lynch

I have an additional question about Salym field and about the unconventional oil. The possible tax benefits that would be introduced by the end of the year, how would they impact your policy?

Sergey Vakulenko, Head of Strategic Planning Department

The question contains the answer, we would certainly welcome such tax benefits that stimulate the development of Bazhenov formation. As we understood, our fields are the subjects of tax benefits that are included in proposals which are nearly to be approved by the State Duma. This fact only increases our confidence that this project is commercially viable.

Anna Sidorkina , Head of IR

I would like to ask that you ask only one question please, as there are lots of people wanting to ask questions of our management. Thank you.

I would like to add that we have been joined by the Deputy chairman of the Management Board, the First Deputy CEO Vadim Yakovlev at our questions and answers session. If you have any questions, go ahead.

Maxim Moshkov - UBS

Good evening! The most important question is about the CAPEX' plan for 2012 and 2013. Thanks.

Alexey Yankevich, Member of the Management Board, CFO

As for the investment program for 2012, it was, as you know, about \$5.5 billion and we don't expect it to deviate very much from those plans. We added some projects, we optimized some other projects. And we think that we might invest additionally but the amount will be insignificant, about 50-200 million but not more than that. As for the plans of 2013, the investment program is still being developed, it needs to be discussed and approved by the board, so the number would be not very precise right now.

Alexander Korneev – Prosperity Capital

My question is how much oil did you buy in Russia and at what prices were in second and third quarters? Thank you.

Alexey Yankevich, Member of the Management Board, CFO

I will answer this question – all that information has been published and you can see in the MD&A (Crude Oil Purchases, p.6) that in the third quarter we purchased about 2 MMtonnes in Russia and about 1.2 MMtonnes abroad. As for the prices, I can't say precise data right now but there were market prices and you can see them in Argus, and of course they are formed on the basis of export parity prices, so you can calculate them.

Alexander Korneev – Prosperity Capital

The volumes are agreed together with Slavneft and Tomskneft, not disclosed in MD&A and so I will wonder at the value of that oil.

Anna Sidorkina , Head of IR

Alexander, we will provide you a breakdown of those purchases both in Russia and abroad.

Pavel Sorokin – Morgan Stanley

Good evening, thank you for the comprehensive presentation! One small question. Lahta – Center is one of the important project in your CAPEX' plan, so it will be great to get the following information: the capital expenses on that contract, when do you plan to start the construction and how long, do you think, it will take to build it? Thank you.

Alexey Yankevich, Member of the Management Board, CFO

The overall value of the project, amount of the project will be \$1.5 billion and we are planning to start construction by the end of this year, early next year and we are planning to complete construction by 2018.

Stanislav Kondratyev – URALSIB Capital

Thank you for the very good presentation and I am going to ask a question also about Lahta – Center. As I understood correctly, the significant part of the building will be leased out as commercial property. Do you expect that the rent that you will get for leasing out the centre will cover the operating expenses for maintaining the centre or even recover the construction costs? Thank you.

Alexey Yankevich, Member of the Management Board, CFO

We see this project as a completely commercial project. We are looking right now for the partners in this project because we will be certainly leasing part of the premises that will not be occupied by our offices. Right now we quoted the numbers on that project already but we are not going to pay the whole cost of the project ourselves. We think that part of the price will be paid by our partners who would use the premises or lease them out, and certainly I would expect that the projects will not only cover our operating costs but also bring us profit and that will meet our criteria of profitability.

Andrey Gromadin – Sberbank

Good evening! My congratulations with good results! I had four questions actually, may I ask at least two of them. My first question is about EBITDA of affiliated companies: in third quarter EBITDA was at least 70 million, and my question is whether that is because of some one-off items. And the second question: when you are going to receive Novoport from Gazprom? Thank you.

Alexey Yankevich, Member of the Management Board, CFO

As for EBITDA, in the third quarter there were no one-time items that would affect the revenues. A reversal of RUB 1.2 bln reserve did not influence significantly on the profit.

In terms of Novoport field, we are planning to get it by the end of the year.

Ivan Khromushin – Gazprombank

Good evening! My name is Ivan Khromushin, Gazprombank. Could you provide a breakdown of EBITDA by main JV?

Anna Sidorkina , Head of IR

We will send you the breakdown as usual.

Ivan Khromushin – Gazprombank

Would you be able to publish the data in the future, please?

Andrey Shvetsov, Head of Financial reporting and Methodology Department

Unfortunately we have some limitations concerning the information about separate joint ventures because that information has not yet been audited. We will send you this information separately.

Ekaterina Rodina – VTB Capital

Thank you very much for the presentation and for the good results. May you specify: the 5.5 billion CAPEX, does that include the joint ventures?

Alexey Yankevich, Member of the Management Board, CFO

That does not cover the joint ventures, with the exception of their needs that are not covered by their own cash flows so we loan them money and that is included into the CAPEX number.

Ekaterina Rodina – VTB Capital

My other question is about the Upstream CAPEX per bbl. This figure has grown significantly Q-o-Q by nearly 30% (from 10.5 up to 13.5 \$/bbl according to my calculations). What can explain that?

Alexey Yankevich, Member of the Management Board, CFO

I have already shown in the presentation the key factors of the CAPEX growth Q-o-Q. Firstly, we entered into the project in Kurdistan, you know the amount from our press-release, and, secondly, we have also invested into the Bulgarian storage facility – this amount was not very significant.

And you know that the investment in the filling station is usually done in the second half of the year, it also influenced.

Ekaterina Rodina – VTB Capital

What I meant was the Upstream part, CAPEX per bbl, I did not mean the Downstream part. I think that the filling stations and the Bulgarian storage facility are part of Refining&Marketing CAPEX.

Alexey Yankevich, Member of the Management Board, CFO

Katya, you said it correctly that you took only Upstream but you took both brownfields and greenfields CAPEX. As for new projects, the production lags the investments. The one-off item Kurdistan is one of such greenfield project.

Anna Sidorkina , Head of IR

Ladies and gentlemen we have exhausted our questions. Thank you for your interest in our conference-call and if you still have some questions please send them to us. We will be happy to discuss the nine months results. We express our great gratitude to our management for participating in this conference-call and for answering the questions in details. Thank you.