

JSC Gazprom Neft

2Q 2011 Financial Results August 3rd 2011

Anna Sidorkina, Head of Investor Relations

Good day ladies and gentlemen, let me open this conference call where you are going to hear US GAAP financial and operating results for second quarter 2011 concerning Gazprom Neft, and let me also introduce to you the participants of today's conference call. Economic comments are going to be delivered by Head of Economics and Corporate Planning Directorate Mr Alexey Yankovich, this side we have Deputy Chairman of the Management Board, Deputy CEO of Exploration and Production Mr Boris Zilbermint, then we will listen to Vladimir Konstantinov. Mr Vladimir Konstantinov is Head of Economics and Investment Department in the Refining and Marketing division. We also have here Yuri Kalner Head of Strategic Planning department and he will join us during the Q&A session for corresponding questions.

Before we start the presentation, the one that you are going to see on our website, I would like to remind you that this presentation contains forward looking statements concerning the financial conditions, result of operation and business of Gazprom Neft and its consolidated subsidiaries. All statements other than statements of historical fact are or maybe deemed to be forward looking statements. Forward-looking statements are statements of future expectations that are based on management's current expectations and assumptions and involve known and unknown risks and uncertainties that could cause actual results, performance to differ materially from those expressed or implied in these statements. Thus the actual results performance can differ materially from those expressed in the presentation. Now I give the floor to your main speaker.

Alexey Yankevich, Head of Economics and Corporate Planning Directorate

Good day colleagues, ladies and gentlemen. Thank you for joining us to listen to US GAAP financial and operating results for the second quarter of 2011. We can sincerely tell you that the financial and operating results have improved substantially. Our revenue increased by 39% year-on-year and our operating profits increased by 58% and our net profit by 74%. We also have increased our main operating results, such as Cenomanian gas production. Year-on-year we have increased our production of hydrocarbons by 7.7%, refining by 19% and sales through premium channels also have increased by almost 45%. To name just a few important events, we started to produce Euro 5 gasoline at the Omsk refinery, and also the legislation has been signed by President for the MET relief for Northern parts of Yamal Nenets region, which increases economic efficiency of the corresponding projects in this region.

As far as the results and the macroeconomic situation, upon the backdrop of which our Company has performed this activity, it has been very positive, the world Brent prices have increased by 11% quarter to quarter and approximately by 50% year-on-year. You can see here that export duty that has a certain time lag to it achieved its maximum in the second quarter, so it caught up with the prices, and thus the duty in the next quarter was a bit higher than it should have been. This duty lag effect is the same that is in charge of the fact that in the second quarter oil and gas companies had results a bit more, let's say, modest than those that we could expect. Following the growth in global prices and demand, domestic prices for petroleum products have increased as well, although both us and other companies have taken our decisions very cautiously since we have special attention from regulatory bodies focused on us. The growth of prices was followed by Rouble appreciation, which happened in the second quarter, and it also happened last year. It actually shrunk the positive effect and our expenditures, both operating expense and Capex thus increased. Besides the higher naphtha and gasoline, our duties have been introduced, this was done to hold the prices and avoid a deficit on the internal market; however, our company hasn't been substantially influenced by the results of this decision because our petroleum products export volumes are relatively small.

Now I would like to give the floor to Mr Zilbermint to speak on the results of our upstream section of operations.

Boris Zilbermint, Deputy CEO of Exploration and Production

Good day colleagues, ladies and gentlemen. As we have already mentioned, results are quite positive, we are quite happy. The volumes of hydrocarbon produced compared to the similar period of last year has gone up around 8%. Key events of the year 2011 is that gas fields operated to full capacity and we expect around 4 billion cubic metres of gas, or 3.2 million of oil equivalent until the end of the year. On Messoyakha project, together with TNK BP we would carry out seismic data acquisition, right now we are carrying out drilling of exploration in appraisal wells, and we are preparing for test production of Messoyakha field. As far as our assets in Orenburg and Novoport are concerned, these are the ones that will be transferred from Gazprom to Gazprom Neft this year. In Orenburg we are in the phase of active development of this field, and we are planning for major drilling tenders, we are going to commence in the fourth quarter this year. As far as Novoport is concerned – you have most probably read the press release, a UK icebreaker has passed by Novoport and now we have it confirmed that the route is there. Right now we are looking at what are the volumes that would be accessible at the peak production, at plateau of production and what would the volumes to be transported along this route. In SeverEnergy we have adopted a long-term strategy, by the subsidiary and it has been presented for Board of Directors' approval. The plan is that first gas and condensate would start coming in the end of this year or beginning of next year.

A few words on our international projects – in Badrah project we finalised our seismic data acquisition. In August or September we are finalising construction of our camp, so our personnel is going to stay right there in the field. We also have carried out a tender to take drilling tenders, Schlumberger won this tender, and we are planning to commence on drilling, so as to have the initial production volumes stipulated in the contract by the year 2013. Equatorial Guinea – we are right

now looking for locations for exploration wells and going to identify them to the end of the year, so we are going to work together with the drilling club that exist in Western Africa, in order to identify the opportunities of going offshore Equatorial Guinea for drilling. A few words on the Venezuela project – we have got approval for drilling appraisal. Together with national oil company PDVSA was approved decision of earlier production in order to accelerate getting production from the field. As far as Cuba is concerned – we just signed our joint venture agreement in Havana, together with Petronas and Cupet the state oil company. Right now Gazprom Neft is a participant to explore Block 4 and 6 in Cuba together with Petronas. First exploration well is to be drilled in the fourth quarter of the current year, or first quarter of the year 2012. Next international project is NIS – we have had hydrocarbon production increase year-on-year by 25%, and in general I would like to say that we have more than doubled production since Gazprom arrived to Serbia and started on this asset. We are planning to keep going and also commence more actively on geologic activity to get even more.

As far as our legacy assets are concerned – mostly we have stabilised production. As far as growing assets, we have Priobskoye field; we have growth there. Right now we have been put into operation Luginetskaya gas compression station after long repair together with Tomskneft. . We have had a very active programme, especially in the Noyabrsk and Muravlenko region to restore and to abandon around 200 the uneconomic and inefficient wells. In order to compensate the loss of production, we increased our geologic activity, and this geologic activity is accompanied by developing of new technologies to be detailed further.

In the next page you can see in dynamics hydrocarbon production grid and you can see that compared to the previous year we have a 7.7% increase, and a 0.2% increase compared to the previous quarter, 1.2% quarter-on-quarter. The main driver among our JV here was most probably Salym Petroleum Development who managed to – after they lagged in the first quarter - catch up and they not only fulfilled their plan for the half year, but keep going at the same rate of production further. A few words about our subsidiaries – our subsidiaries have increased production quarter-on-quarter by about 1%, and year-on-year by 0.1%.

On the next page you can see the modern technologies that we are planning to make use of and develop in the future in order to increase efficiency and increase production volumes in our company. You probably know that at the end of May this year we have signed a strategic agreement with Schlumberger, and right now we have commenced on making use of some new technologies, the ones that haven't yet been used in Russia. We are pioneering these technologies at certain points just in Russia and points globally, and we in particular use it in Badrah in Iraq. We are also looking into working with another important major in high tech market Weatherford, so we are looking into drilling multilateral wells with years of quality in order to decrease drilling costs and increase coverage of fields and thus the flow rate. Here we also have a list of projects where we already use technologies like foam fracking in Priobskoye field, that leads to flow rate increase by 25, 30% as compared to just your ordinary prop frack.

Next two slides I would like to ask Alexey Yankevich to comment on these two slides, because he is going to speak on the economic effect of upstream sector due to tax regime changes.

Alexey Yankevich, Head of Economics and Corporate Planning Directorate

Thank you. As I already mentioned the law has just been approved for tax relief in the northern part of YNAO for 10 years. We have two groups of field there, Messoyakha field and SeverEnergy fields. On this slide you have the total production. The total effect from tax relief is going to be in total at around 130 billion Roubles, this is not discounted. This is quite considerable, and I would like to point out specifically that even in view of this tax relief – even without the tax relief, Messoyakha has been quite effective. What I would like to point out specifically that Messoyakha needs oil prices above 100\$ per barrel to recoup investments. However I would like to point out the Kirishi meeting with the Prime Minister that had on agenda the new crude oil export duty exemption, so-called system 60-66, which provides decrease of oil export duty from 65% to 60% and fixing oil products export duty equals to 66% from oil export duty. The effect of this tax decision is going to be positive both in terms of our current economics. We're going to get around \$200 million from that. Not long ago we had a conference call with analysts devoted to this particular topic, but mostly our new projects are going to benefit. This 60-66 tax duty regime as well as tax relief for us Northern Yamal is going to increase net present value of these projects. In this slide you can see in four groups of our fields the effect from introducing this new tax incentive. The cumulative effect is going to be very considerable - around 3,7 bln. dollars; it is around 15% of our capitalisation, which in fact means that company value is going to increase by the same 15%. In the nearest future we are going to arrange a special meeting and analyse it together with analysts to analyse how to account for these effects in other value. I suppose a lot of analysts haven't taken this aspect into account, because some of our projects haven't yet been taken into account in value calculation because they were economically not efficient in the old tax regime.

Now I would like to give the floor to Vladimir Konstantinov to speak on the downstream.

Vladimir Konstantinov, Head of Economics and Investment Department in the Refining and Marketing

Good day ladies and gentlemen. In the second quarter as well as in the first half of the year 2011 we have been solving 2 blocks of tasks. We were aspiring to maximise the advantages that we were getting from the macroeconomic situation that we found in the first half of the year, besides the second half of it was that we were concentrating on our routine activities. As far as macroeconomic and operating activities combined – I would like to point out specifically that we increased downstream volumes up to 19%, as compared to the similar period of the year 2010. This is with taking into account the fact that refining is still more effective than export of crude oil. We keep realising investment projects, in particular we are successful in constructing isomerization units at Moscow and Yaroslavl refineries to improve gasoline quality and go for high-octane gasoline. Besides in order to meet the requirements of technical regulations, we have hydrotreatment units and gasoline hydrotreaters both in Omsk and in Moscow and in Yaroslavl and also in NIS refineries

where we have quite considerable stake. This is of strategic importance. The motor fuel is getting better and better, it is increasing in quality. We try to use the financial results quite efficiently, because when you produce motor fuel actually getting ahead of technical requirements, we save quite considerably on excise; that way increased gasoline of Euro 4 in Moscow refinery. We started to have this gasoline produced in January 2011, and in the second quarter of 2011 we commenced on Euro 5 gasoline production in Omsk refinery. Besides we are getting ready to realise our strategic plans to change refining structure. In June we have tested the gas condensate processing in SeverEnergy in Omsk, because we do take into account that the share of gas condensate in our oil and gas processing might increase in the future.

So much for refining, as far as sales is concerned – well we use the operating advantages that we have here as well, it is just that right by the beginning of the second quarter the structure of our filling stations has changed. We have completed around 70-80% of retail station rebranding, we introduced some new retail stations, we have acquired quite considerable amounts of fuel station networks both in the regions where we traditionally existed, as well as in some new regions. Thus we increased the premium sales by 45% as compared to the first quarter of 2010. We also look into the jobs that are there in the strategic plans. We need to finalise rebranding of all our retail stations and start loyalty programmes in all the regions where Gazprom Neft is present. We have already achieved quite considerable growth, around 30% for retail stations and we also have increased the sales of the related products at our retail sites.

We pay special attention, as to our international projects. We are revamping our Serbia plant. We are in active phase of hydrotreating and hydrocracking unit construction in Panchevo; that is to provide us with the opportunity to have gasoline Euro 5 by the year 2012. We increased premium sales in Serbia and we also are developing and improving on quality level of our Italian asset, Gazprom Neft Lubricants Italia.

As far as more detailed information on refining is concerned, I would like to point out the following – in the second half of 2011 as compared to the similar period of 2010, the throughput has increased by 19%, and this is mainly due to Omsk and Moscow refineries. 0.5 million tonnes in Omsk in particular of increment, this is actually something that increased efficiency in providing for the domestic market, and also we have Moscow refinery growing. This is half due to market factors and half due to the revamp cycle that was carried out in 2010. NIS refining stayed as you can see almost the same taking into account their technical abilities from the one hand and the effectiveness of refining from the other. As far as quality of motor fuel is concerned, please have a look at the right side of the slide and you will see that as compared to the year 2010, we have decreased the volume of gasoline and diesel quality lower than Class 3 for gasoline. In 2011 we just were not producing gasoline Class 2 due to Technical regulations demand.. We significantly increased production of Class 3 gasoline – to 70% and also around 11% of Class 4 and 5 gasoline. As far as diesel fuel is concerned there was a little bit different here. According to technology regulations, the second quality is in for 5th September, and yet we thought that we would get excise advantages by producing petroleum products of higher quality and therefore in the second quarter we decreased the volumes of diesel fuel from 82 to 70%, and thus it allowed us to increase the volumes of fuels Class

4 and 5 by 30%. We now produce more jet fuel by 21% year-on-year, and this is also an important factor. As you probably remember that at the end of last year we had quite considerable issues in the market, in providing consumers with gasoline, diesel and jet fuel.

As far as channel structure is concerned both for crude and petroleum products please check slide 17. You see here that we have increased quite considerably the second quarter of the year 2011 compared to the year 2010 production and supplies to domestic market – domestic product sales are up more than 22%. We also have increased supply for CIS market. Our next neighbours, the efficiency of working with them is almost equal the one of the domestic market. We have +17% of export and this is due to our refining volumes. You can see how it tells on the fuel oil production and you can see that any increase is accompanied by making products or having an output of products that we have to export rather than use domestically. As far as crude export is concerned, it is -24%, and this is due to what we see in the right hand part of the slide. It is quite obvious here that crude export netback in the first quarter has come closer to the blue line, the refining netback, which basically means that the spread between refining and crude export netback has come down, and yet refining netbacks are higher. Alexey Yankevich has already mentioned the reasons – this is most probably due to export duties and the effect of lag in crude oil export duty and stabilising oil price environment is another factor. The price of oil is not now increasing quite actively, and right now the lag does not really tell that much on the correlation between effectiveness of export and domestic sales.

Petroleum products have increased in price in domestic market. We have effectively overcome the stabilisation and the price non-increasing effect that existed from February to April. The difference between refining and export is growing even further. In certain parts of the second quarter it amounted from \$80 to \$150 per tonne. Obviously under such circumstances we increased refining volumes.

Now a few words about the premium channels. I have already mentioned that this is one of the major areas of our activity, strategic activity and operating activity. We changed our retail sides both in terms of more fuel sold as well as aviation and bunkering, this is also changing. This allowed us to achieve double-digit growth in sales, as you can see in the right hand part of the slide. This increased our market share. Thus our retail market share in jet fuel has amounted to 18% and bunker into 17%. I would like to point out specifically that not only did we look at quality; we also looked at the opportunities to sell. This has to do with lubricants as well as jet fuel. Now with geographical span it has increased. We're entering new markets both domestically and overseas. We are going for new markets, new ports for bunkering, and again this has to do with both domestic and the overseas ports. You can see those on the slide.

In general, both in downstream and upstream, I mean just like in upstream, we suppose that downstream has performed quite well. Thank you.

Alexey Yankevich, Head of Economics and Corporate Planning Directorate

Now let's get back to financials. As I have already mentioned these are quite strong results. We can see that revenues grew by 39% year-on-year, EBITDA increased by 57.7% year-on-year and this is not only due to strong revenues, but also due to an increase in refining. We also optimised our sales structure and product mix and we also had in place other measures to increase efficiency. Net income has increased quite considerably as well by 74%, that is more than operating income growth. The result was influenced by the fact that some of our service companies have been sold at the figures higher than book value and it also told positively on us.

Here we have an effect of our duty lag, its day-on-day structure, and if it were more even than EBITDA it would have grown quarter-on-quarter. Net income has actually gone down, but here we have effect of our activity. We valued our non-realised hedging contracts and the general result in the first half year was positive, but since we had quite positive results in the first half of the year, we adjusted to the negative side in the second quarter; otherwise the dynamic would have looked more like operating profit.

In this slide you can see factor analysis of operating profit. We are comparing our results against the previous year, and here you can see that macroeconomic environment was quite positive. It is 1.4 billion plus to EBITDA, but management also introduced its contribution in the form of a production increase in refining, optimising of sales, and cost optimisation as well. Another positive contribution was made due to our joint ventures. As far as changes in expenditures is concerned – they have increased year-on-year and there are a lot of factors that contributed. Here you can see Rouble appreciation and also the fact that we have increased our geologic activity, and also we have here macroeconomic aspects. Cenomanian gas production has had its contribution, tariffs of natural monopolies have had their contribution, as well a salaries and taxation and increase in price for oil services. The positive effect was introduced by our cost optimisation programme, but generally speaking year-on-year we have increased expenditures.

As far as cash flows are concerned – unlike the first quarter we have improved just like promised. We have earned around 1 billion of free cash flow, after deduction of our regular Capex. This free cash flow has been used to acquire, we have increased our share in Sibir Energy and we bought out 5% of NIS. We have also paid dividends, the remaining of 2009. Credit portfolio was only increased by 168 mln Dollars, so cash at the second quarter of 2011 is almost equal to cash at the beginning of the year.

Growth and improvement in investments is the topic of the next slide – it improved both compared with the previous year as well as the previous quarter. The growth quarter-on-quarter is explained by seasonality, especially in as much as production and sales is concerned. As far as refining is concerned – the growth is related to active phase of revamping in our refineries, this being construction of diesel fuel hydrotreatment at Omsk refinery, isomerization unit at Moscow refinery and active phase to construct hydrocracking unit in Pancevo. These same factors had their share in increase of investments in refining as compared to the previous year. As far as Capex in upstream

is concerned and production in particular – we have increased our activity in geologic measures taken and in drilling, and this is due to the fact that our macroeconomic conditions have gotten better, and so it allowed us to realise some additional activity. Besides we have a programme to broaden and revamp our retail network and therefore we invest heavily into it.

Despite the fact that we realise our investment programme quite actively, we are thinking of improving our financial stability and in the second quarter we managed to improve our debt to EBITDA and its minimum for the last few years - 0.8. We also decreased the share of short-term debt by 10.3 p.p. q-o-q, and the share of short-term debt actually decreased also year-on-year by 26,5 p.p.as you can see on the diagram. While the average rate also decreased year-on-year by 1% which is quite considerable as well.

Bringing conclusions I would like to point out that Gazprom Neft is happy with the results of the first half year. We have improved our financial results and operating results. We are within the plan for our major projects and the decision on northern part of Yamal and Nenets region has already been taken. As far as system 60-66 concerning the duties is a positive thing as well, because it means that government listens to us and we do hope that the tax burden would be more favourable and including the new projects, it would be in favour of the new projects. Now we are ready to answer your questions.

Q&A

Vadim Mitroshin – Otkritie Capital

Good day I have two questions. My first question concerns tax regulation. You mentioned that tax regulation 60-66 is being introduced. However we heard rumours of a modification to the system, this being 55-86. Which of those 60-66 or 55-86 do you find most probable to be realised? Thank you.

Alexey Yankevich, Head of Economics and Corporate Planning Directorate

In fact both the 60-66 and 55-86 systems actually can be actively used. Up to \$90 per barrel of oil prices the system would be 60-66. Above \$90 per barrel it would be 55-86, and it would be to our benefit in any case. As far as probability is concerned – system 60-66 we find highly more probable, and besides according to the public information and the meeting with the Prime Minister, this is exactly the order that he has given to the government to development, such a system for 60-66. Besides it is a certain industry consensus that 55-86 is more restrictive and less beneficial for refining system and carries higher risks in terms of the domestic market.

Vadim Mitroshin – Otkritie Capital

My second and last question is about hedging. You mentioned that you had some hedging effect in the second quarter of the year 2011. This I suppose is the figure 106 million of exchange loss. If

Rouble stays the same – what do you expect in terms of hedging effect? Can you effectively forecast the hedging effect? Is it going to be zero or is it going to be something other than zero?

Alexey Yankevich, Head of Economics and Corporate Planning Directorate

Hedging effect is something that has already been taken into account to our accounting date and closing the accounts as of 30th June. The effect has already been mentioned, the hedging effect is positive in the second quarter, and it reversed as compared to the first quarter of the same year. As far as the future is concerned, well I suppose the fact is there is going to be zero rather than anything else.

Vadim Mitroshin – Otkritie Capital

Thank you.

Andrey Gromagin – JP Morgan

My first question is about operating cash flow. We do see positive results in net income and EBITDA. However we also see that operating cash flow could have been better, and this I suppose is something that could be effectively explained by change in working capital that according to my calculations adjusted to dividends payable amounts to around \$1.5 billion. What is your explanation for these changes in accounts receivable and inventory and what is your forecast for operating cash flow in the future. Thank you.

Alexey Yankevich, Head of Economics and Corporate Planning Directorate

You are right, indeed working capital did increase and indeed the amount was more than \$1 billion. Here I would like to cite several factors. This is first and foremost due to the increase in prices, both globally and domestically. The price did increase in the second part late into the half of the year, as compared to the beginning half of the year. Besides I already mentioned that our refining volumes have increased and this is due to the fact that margins were quite high. Obviously if you increase refining volumes you can't decrease inventory that increases as well. Besides refining and getting petroleum products is a cycle, so you have to take this into account in terms of the way it tells on inventory and accounts receivable. I would also mention sales through the premium channel. Here again if you sell through premium channel you most probably sell for credit, so it also adds to account receivable, but the main affect here is price and refining volumes.

As far as our forecast is concerned – we are not seeing that our working capital is going to increase onwards. It is however dependent on the prices, if prices are not increasing then working capital is not increasing. As far as inventory is concerned – most probably we are going to decrease it. However right now we are expecting the usual seasonal deficit in diesel, so at some point of time the inventories will stay high, but then we hope to decrease inventory.

Andrey Gromagin – JP Morgan

Thank you for this detailed answer. I would like to ask another question about excise that increased by \$180 million as I can see and more than 50% is due to NIS. My question is effectively – do you have any forecasting mechanism, how do you forecast those taxes and this amount for NIS specifically.

Alexey Yankevich, Head of Economics and Corporate Planning Directorate

I would say NIS is not the main factor that affected on excise growth. I suppose that is the above mentioned increase in refinery volumes, is rather the one that has an impact. When domestic demand goes up sales go up. It is quite obvious that excise then will go up as well. As far as excise for NIS, well indeed it has increased, but it is going to be passed onto the end consumers and it is not going to tell in our financial results.

Andrey Gromagin – JP Morgan

Thank you.

Alexander Burgansky – Otkritie Capital

If I may have a question to Mr Boris Zilbermint. I was wondering about organic rate of decline in Western Siberia assets. Can you comment on that? Also could you please comment on the peak of production on the Priobskoye sales? Probably you would give us the figures. Also what are the technologies that you are considering in order to increase this peak production figure or prolong the period in which the production will stay in its peak? Thank you.

Boris Zilbermint, Deputy CEO of Exploration and Production

As far as rate of decline is concerned – I suppose that you know that most of our assets are in the third production stage, and this is the stage after which we are getting into the fourth stage which sees stabilisation. This is something that we see in most of our main production fields such as Noyabrsk and Muravlenko, the ones that are situated in that region I mean.

As far as our 100% assets are concerned – we are planning to stabilise production on them mainly on behalf of Priobskoye field., Peak production at this field will be of 10 million tonnes and we intend to keep this at plateau of the same value for about three years.

Anna Sidorkina, Head of Investor Relations

Ladies and gentlemen, unfortunately we don't have any more questions. Thank you for your attention and if you have any further questions please feel free to address Investor Relations with those. Thank you to Otkritie Capital for organising this conference call and thank you for being with us today.