

JSC GAZPROM NEFT

3Q 2010 and 9M 2010 Financial Results **November 3rd 2010**

Geydar Mamedov, Goldman Sachs

Good day, dear ladies and gentlemen. My name is Geydar Mamedov. I am here to represent Goldman Sachs Company. We are happy to welcome you at teleconference of Gazprom Neft Company devoted to financial and the operating results for the third quarter and nine months of 2010. Broadcast of the conference as well as the electronic version of this conference, you can find at company website. And I would like to give the floor to a representative of Gazprom Neft. Thank you.

Anna Sidorkina, Head of Investor relation

Good day, ladies and gentlemen. I am Anna Sidorkina from investor relations and let me open this conference call to present you our financial results according to US GAAP for the third quarter and nine months of the year 2010. This presentation is going to be delivered to you by Deputy Chairman of the Management Board and CFO of the Company, Mr Vadim Yakovlev. We also have here Deputy Chairman of the Management Board and Deputy CEO for Exploration and Production, Boris Zilbermint, Deputy CEO for Logistics, Processing and Sales, Mr Anatoly Cherner and after the presentation, we will be happy to answer your questions.

Before switching over to the presentation which you can find on our website, I would like to remind you that this presentation as well as all comments thereon contains forward-looking statements concerning the financial conditions, results of operations and businesses of Gazprom Neft. All statements other than statements of historical facts are or may be deemed to be forwarding-looking statements. Forward-looking statements are statements of future expectations that are based on management's current expectation and assumptions and involve known as well as unknown risks and uncertainties that could cause actual results, performance or events to differ materially from those expressed or implied in these statements. Thank you very much for your attention and now I would like to give the floor to Mr Vadim Yakovlev.

Vadim Yakovlev, Deputy Chairman of the Management Board, First Deputy CEO and CFO

Good day, ladies and gentlemen. Today we are going to present to you financial results of Gazprom Neft Company for the third quarter and nine months of the year 2010. First and foremost, comparing our results with consensus forecast, I see that we manage to surprise you pleasantly. And hopefully you noticed that not only did we manage to cut on the term in which we provide you with

the accounting but also increased our transparency and we provide you with greater volume of information. We take into account all the comments and questions that you addressed us previously.

Let me start with the highlights of the quarter and our main results. We manage to achieve quite considerable growth in terms of production volume and refining throughput. Nine months production year-on-year increased by 6% while refining throughput increased by 13.2% year-on-year which came as a result not only of consolidation our assets that we acquired and consolidated last year like Sibir Energy and Moscow Refinery. It also comes from increased production and refining in the third quarter. This is going to be mentioned in greater details in the course of my presentation.

In the third quarter, we assumed operationship of East Orenburg field and we are getting ready to become a full property owner in the nearest three months. Another important upstream event is that we have sanctioned associated gas utilisation project at South Priobskoye field. We started the construction of gas pipeline and gas is going to be supplied to Yuzhno-Balyksky refinery where this gas is going to be processed by Sibur Company.

We also keep developing our overseas project. For example, we are declared project leader for field development at Venezuela, the Junin-6 field in this year. And our efforts are right now directed at forming a team and structuring the project and all of our overseas projects. Should you have any questions, we will be happy to give you some comments.

And another deal which was not too big but still quite significant for us as a company, we penetrated Kazakh retail market. This retail market is of interest to us by all means since logistically wise delivery from Moscow Refinery to Kazakhstan where we used to be present in wholesale channel more than Balkan. So retail channel is now open for us as well in this country.

Macro environment, few words on that. Macroeconomic environment as compared to the second quarter of this year has not changed considerably. Urals went down by 2% in price and this is on the background of ruble weakening by 1%. Major positive macroeconomic factor was that export duty went down. Export duty in the third quarter was 7.7% lower than that of the second quarter on the year 2010. Year-on-year, we see that oil prices were increasing which couldn't but positively impact on our financial results. As far as EBITDA and net income influence, the constraining factors there were increasing tax burden and increasing tariff of natural monopolies.

A few more words on upstream results. In the third quarter of 2010, we achieved new maximum production of 13.3 million tonnes of oil equivalent and we grew not only year-on-year but also quarter-on-quarter. I would like to point out that this is organic growth as compared to the second field. Our growth leaders are Zapadno-Salymskoye field – this is Salym Petroleum Development field; Priobskoye field; and Vyngapurskoye field. Growth amounted to 12%, 8% and 5% correspondingly year-on-year. And these were the fields that provided for quarter-on-quarter growth as well.

In the third quarter of 2010, we caught up with the saying that we had in geology and exploration due to extreme low temperatures and unfavourable conditions as of today, we are now exceeding our geologic activities programme and exploration and production activities programme. And in terms of investment, we are still within the budget we planned for those measures and activities. And we manage to drill more, spending same amount by means of cutting main time to drill and optimising cost parameters. We were quite active in other side of E&P activities. We carried out 72 hydrofracturings, 12 deepenings and 27 sidetracks.

Few words on downstream results. Third quarter was record high in refining throughput. It was 10.21 million tonnes and this is our absolute maximum of the company. We grew as compared to the previous year and previous quarter. And this is in all our refineries, especially Moscow Refinery. The reason is that in the second quarter, we actually stopped this refinery for seasonal repairs at Moscow Refinery. We now have registered increase there of plus 44%, so we have 81% of coverage with refining and we have the most profitable result for refining.

As far as netbacks are concerned, they haven't changed considerably quarter-on-quarter and year-on-year. Refining margin is stable and high and amounts to about \$10 a barrel. Correspondingly, in situations like that compared to the previous quarter, we decreased export volumes by 11%, increased refining by 17.6% and improved the sales structure. You can see that sales on domestic market, which are more profitable than export sales, increased by 15%.

We successfully started expansion of our presence in retail product segment like aviation lubricants and bunkering and we continue this trend in this year. You can see considerable growth in all of these areas. In general, premium channel sales plus retail plus small wholesale increased year-on-year by 14% and quarter-on-quarter by 18%.

Financials – if we compare our financials year-on-year, you will see that major sectors are increase in volumes and oil prices growth. As far as quarter-to-quarter comparison is concerned, I would like to point out that price variation was quite stable. Apart from that we manage to achieve growth in our revenues by 5%, EBITDA by 30% and net income by 16%. This comes as a result of organic growth in production and refining in our assets, improvement in our refining structure and the marketing structure in downstream segment. And also, this comes as a result of our actions that we took to cut cost and increase efficiency.

Please find below factual analysis of EBITDA reconciliation in the third quarter as compared to the second quarter. Price factor was not that pronounced in dynamics quarter-to-quarter. The main driving factor was increase in volume to \$153 million and \$40 million additional effect as compared to the previous quarter is due to efficiency in our programmes and our independent companies improving their results also contributed to our success. If you look at nine months and similar period of the previous year and you can find that figures in appendix to this presentation, you will see \$229 million and this is one of the major factors that determine positive dynamics of our financial results.

A few words on our CapEx. I have already pointed out that we cut out the problems we had in realising our geological exploration activities. And third quarter showed peak of CapEx volume as compared to second quarter growth in CapEx amounted to 39% which predominantly refers to upstream which compared to previous year is 32%. I would like to point out specifically that we are planning to spend less than the figure we planned for in the budget. Yet the amount of activities is going to exceed what we planned for which would impact our financial results positively as well.

And now on our cash flows. Operating cash flow of Gazprom Neft in the third quarter of 2010 amounted to almost \$2 billion which is almost two times bigger than our CapEx. Free cash flow in third quarter amounted to \$937 million which allowed us to decrease our debt portfolio by \$811 million and payout dividend of \$139. As of 1 October, we have \$1,175 million in cash and we also have signed in third quarter a credit agreement with bank syndicate: we picked only \$50 million out of \$100.5 million. So as of 1 October, our liquidity which are in place is about \$2 billion.

In the third quarter, not only have we cut on our debt burden, but portfolio became smaller. We also changed the debt structure to the better. Gearing went down to the level of 19%. Net Debt / EBITDA is currently 0.75. Share of short-term debt decreased to 27% and we also reduced average interest rate to 4.5%.

And now just a few words on pride events we have had in each of the segments of our activity. In upstream, one should definitely mention the planned for deal to acquire 51% in SeverEnergy together with Novatek. This deal has been approved of by our Board of Directors and hopefully we will close within the month. Acquisition of SeverEnergia which extends our presence in a very important region, northern part of Yamalo-Nenets region where we already operate Novoport field and other fields and SeverEnergia field is comparable in terms of volumes and quality. So it is a very important thing for us to acquire.

As far as downstream segment is concerned we have already announced a few days ago that we continue modernising our Omsk Refinery. We have launched Isomalk 2 isomerization unit to increase yield of life hydrocarbon. This unit is the biggest isomerization unit in Russia and in Europe and is in top three in the world. It is largest capacity isomerization unit. This own capacity amounts to 800,000 TPA, so it would allow us to produce more high octane component of commercial gasoline and will increase output of high octane gasoline displacing triton gasoline which would increase our revenue by \$100 per tonne.

We mentioned previously new products are lined up G-Energy oils. Right now we can speak about first results. G family sales is brought on this slide and it is in line with our expectations, which proves effectiveness of our advertising campaign that we had for this product and each month we increase not only the sales volumes but also we expand product portfolio. You see that product lines is increasing month and month.

ACT Operator

Thank you. If any participant would like to ask a question, please press *1 on your telephone. If you wish to cancel this request, please press *2.

Once again, if you would like to ask a question, please press *1 on your telephone.

Thank you. The first question comes from Maxim Moshkov from UBS. Please go ahead.

Maxim Moshkov – UBS

Hello. Thank you once again for this wonderful presentation and I had a question on SeverEnergiya. As far as I can guess you are planning to close this deal in about one month. Do you have any idea of the price of the deal and what is going to be the development plan for SeverEnergiya?

Are you going for a gas option or oil and condensate option and if it is oil and condensate option then what would be the CapEx for this project for let's say near 7 years? Thank you.

Vadim Yakovlev, Deputy Chairman of the Management Board, First Deputy CEO and CFO

I would like to answer the first part of the question concerning price of the deal, we indeed already have a general idea of how much is going to be and this is according to the board directors of Gazprom preliminary agreements, the minimum price for 51% and I highlight for 51% would amount as RUB 46,279 million which is \$1.5 billion. The final amount however would probably a little bit different and this would depend on value of money on planned date of settlement compared to actual date of settlement plus the Gazprom Neft and Novatek joint venture is going to take up the debt that's currently is on SeverEnergiya. And this debt amounts to \$250 million and it was previously financed by Gazprom. The total for Gazprom Neft and Novatek, this deal would amount to \$1,750 million.

Boris Zilbermintz, Deputy Chairman of the Management Board and Deputy CEO for Exploration and Production

I would like to answer the second part of your question, Maxim, while you can see that the reserves volume is quite considerable there, we have trillion cubic meters of gas and quite considerable volume of oil and condensate as well in this field. Logistically and for structure wise I would say that everything is ready for first launch of gas production that will start by launching gas production. However, subsequently we are planning to produce condensate and oil from this same field.

As far as CapEx is concerned we will have to carry out additional exploration activities since on that field we have a lot of C2 reserves, so hopefully next year, in exactly one year I will be capable

of giving you more or less precise information on CapEx. Right now it is too difficult to comment on CapEx on this field. Thank you.

ACT Operator

We ready to take the question.

Vadim Mitroshin – Otkritye

Good evening. Thank you very much for your presentation and congratulation on fine result. I had a question concerning Lotos Group, Interfax placed information today that Gazprom Neft is so far the only company interested in buying control stock in this Polish company and in these group of companies. Could you comment on that, are you indeed interested in Lotos Group and if yes then what is the strategy for acquiring this group specially in view of the fact that you already have quite a lot of downstream capacity domestically and also some capacity abroad in Serbia?

Anatoly Cherner, Deputy Chairman of the Management Board, Deputy CEO for Logistics, Processing and Sales

Yes, indeed this asset has been place for sale and we are considering it. While Polish market is of interest to us since it's a deficit market. However, this asset is now being considered alongside with other assets that are currently being sold out there. We are now on the stage of analysing the situation and we haven't yet taken any decision and haven't yet actually made any offer.

As far as feedstock for this asset, probable feedstock for this asset is concerned we have export in the amount of 13 million to 15 million per year, so we do have this opportunity to use this our volumes for refining capacity out there.

ACT Operator

OK, thank you. The next question comes from Artem Konchin from Unicredit Securities. Please go ahead.

Artem Konchin – Unicredit Securities

My question has already been answered. Thank you once again.

ACT Operator

Once again, if you would like to ask a question, please press *1 on your telephone. To cancel this request, please press *2.

Thank you. We have a question from Evgenia Dyshlyuk from TKB Capital. Please go ahead.

Evgenia Dyshlyuk – TKB Capital

Yes, thank you. I have a question on the Zapolyarnoye-Purpe pipeline that was very recently approved. This project is approved, do you think it is going to influence your plans for oil production for example Slavneft production in Yamal Peninsula? And just general comments on your oil production plans as connected with Zapolyarnoye-Purpe pipeline approval?

Vadim Yakovlev, Deputy Chairman of the Management Board, First Deputy CEO and CFO

Yes, thank you for this question. In General northern part of Yamalo-Nenets autonomous region is of great major interest of Russian oil industry as of today and Gazprom Neft is not an exception at all. We are quite well presented in this region by our Messoyakh group of fields that currently holds by Slavneft and also through the additional acquisition that we have already discussed today - SeverEnergiya. We are indeed interested in construction of the pipeline you mentioned about, the Purpe - Zapolyarye pipeline.

And as far as the terms of construction and throughput of this pipeline is concerned it is designed in view of and taking account of the stakeholders and subsoil users who have assets in this region. And Gazprom Neft alongside with other holders are very active in discussions thereon.

The construction of this pipeline is that to first of all we have to realise how strategically important project Messoyakha field and SeverEnergiya fields. And besides thanks to this pipeline attractiveness of this whole region is going to be increased, trunk oil pipeline is going to increase attractiveness for all the projects in this facility. And so we definitely are interested in construction of this pipeline and besides this zone is currently I would say understudied. Increasing our resource base through this zone is of interest to our Company as well.

Geydar Mamedov – Goldman Sachs

Yes, I have a question on the assets that currently are on Gazprom balance and are to be transferred to Gazprom Neft - Novoport field and Orenburg field. What is the status of this process? Thank you.

Boris Zilbemints, Deputy Chairman of the Management Board and Deputy CEO for Exploration and Production

These questions do come regularly, don't they? And hopefully I hear them rarely in end of this year, beginning of next year when the licenses will finally be fully transferred on our balance. As far as Orenburg fields are concerned, Gazprom Neft at Orenburg already operates this field since April this year and business plan already is compiled by our managing companies. As far as formalities are concerned hopefully we will end up with all those formalities by the end of this year.

As far as Novoport field is concerned we are now planning for our test production from this field and hopefully we will finalise license transfer by the end of this year, maximum beginning of next year.

ACT Operator

Thank you. We have a follow up question from Konstantin Cherepanov. Please go ahead.

Konstantin Cherepanov – UBS

Thank you very much for this presentation and indeed you increased transparency and thank you for MD&A. From what we see in MD&A we see that some of the costs have actually been restated, so in particular transportation costs and some other costs I can see in the second quarter were restated. Could you please comment on that, is this restatement really occur and if yes then why?

I also have a question on operating cost. If you remember in the second quarter in the course of similar conference call analysts were somewhat concerned about increase in your lifting cost. If we look at the third quarter results we see that lifting costs went down a little bit and last quarter you explained it by the fact that you had more hydraulic fracturing operations and in general more E&P activities. In this year commenting on operating costs increase would you say that this is again due to some additional operations or should we take it as base for our further forecast and take this lifting cost as the lifting cost you just live with?

Andrey Shvetsov, Head of Consolidation and International Reporting Department

I would like to comment on the financial result and financial accounting in the nine months, we indeed did restatements of our costs. And now the cost that were previously assigned to acquisition of oil and petroleum products are now seen as transportation costs. And this is due to the fact that we want to make our accounting better in terms of analysability so that you can analyse it easier and compare facts easier. This is what we did.

In terms of operating expenses we did a re-class of OpEx and you can see this request on one of the slide in the presentation. We did re-class of operating cost for third parties from Messoyakha assets. And should you have any questions containing interpretation of this re-class and OpEx please feel free to address investor relations with this question.

Vadim Yakovlev, Deputy Chairman of the Management Board, First Deputy CEO and CFO

I would like to answer the second part of your question. As far as dynamics of OpEx is concerned, it is very difficult to compare it quarter-on-quarter. As you probably remember first quarter results were quite uncharacteristic and second quarter we had to catch up in terms of volume of our activity and key activities. And third quarter in this respect is I would say we didn't have any unusual factors or unusual events, so it can by all means used as a basis for your forecast.

However in order to follow the dynamics I would rather recommend you to use year-on-year data. If we compare nine months of the previous year and nine months of this year we will see that hydraulic extraction expenses are up only 0.3% which is pretty good if you compare it to the industry in general if you understand. And as far as rate of growth of lifting cost is concerned, we will do our best to keep it below industry average.

Maxim Moshkov – UBS Securities

There was an additional question concerning Yamal project and this project is indeed is the one that would contribute a lot to long-term growth. I have a question concerning attracting finance and funding this project. Are you planning to use exclusively your own capital and also some debt capital or are there any other sources of funding you are planning for this project? Thank you.

Vadim Yakovlev, Deputy Chairman of the Management Board, First Deputy CEO and CFO

Maxim, I would like to answer your question and point out, restate once again that we have quite enough liquidity on our hands, \$2 billion, which would suffice to finance SeverEnergiya acquisition probably but it will take a little bit from the already existent as syndicated loan that we now haven't yet used to full extent. We would like to point out specifically that our debt burden in the company is not too high. Our net debt to EBITDA is 0.75 while our goal is not to exceed 1.5 net debt to EBITDA which allows us to potentially attract new debt should we deem it necessary.

Debt financing is going to be the main source of financing for our project. And we are planning to take long term debts, for example the syndicated loan I referred to previously is for five years. And the affiliation in the market allows us to take more long-term loans and this is what we are planning to do in the future. As far as SeverEnergiya is concerned we are also right now considering the opportunity of using project financing.

Anna Sidorkina, Head of investor relation

Ladies and gentlemen. Thank you very much for the interest in our Company and let me also on your behalf thank our management for detailed answers to all your questions. However, should you have any additional questions, please feel free to ask investor relations department and see you next year at our annual conference call.

ACT Operator

Thank you. This concludes the conference call. Thank you for participating. You may now all disconnect.