Company: **NOVATEK**

Conference Title: **Q3 2011 Financial Results**

Presenter: **Mark Gyetvay**

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Operator: Good day and welcome to the NOVATEK Q3 2011 Financial Results Conference Call. Today's conference is being recorded. At this time I would like to turn the conference over to Oleg Maximov, Senior Analyst of Troika Dialog. Please go ahead.

Oleg Maximov: Good afternoon and welcome. I am Oleg Maximov from Troika Dialog and this is NOVATEK's Third Quarter 2011 IFRS Results Conference Call. With us today is Mark Gyetvay, NOVATEK's Chief Financial Officer and member of the Board of Directors. Mark, please start with your presentation. Thank you.

Mark Gyetvay: Thank you Oleg. Ladies gentlemen, shareholders and colleagues, good evening and welcome to our Third Quarter 2011 Earnings Conference Call. I would like to thank everyone for joining us this evening and again extend our sincere gratitude to Troika Dialog for organising and hosting our earnings conference call.

Before we begin with the specific conference call details I would like to refer you to our disclaimer statement as is our normal practice. During this conference call we may make reference to forward-looking statements by using words such as 'plans', 'objectives', 'goals', 'strategies' and other similar words which are other than statements of historical facts. Actual results may differ materially from those implied by such forward-looking statements due to know and unknown risks and uncertainties and reflect our views as of the date of this presentation. We undertake no obligation to revise or publicly release the results of any revisions to these forward-looking statements in light of new information or future events. Please refer to our regulatory filings including our annual review for the year ended 31st December 2010 as well as any of our earnings press releases for more descriptions of the risks that may influence our results.

We continue to witness the macro environment overshadowing another quarter of solid financial and operational results for the company. Of particular note was a negative non-cash impact of our earnings and earnings per share due to the 13.5% quarter on quarter depreciation of the Russian rouble relative to the US dollar as applied to our present US dollar influenced debt portfolio. Ironically this negativity centres on the continuing debt crisis plaguing the Eurozone rather than the macro situation here in Russia, but nonetheless the volatility in the currency markets as well as the equity capital markets tend to be negatively biased towards emerging markets despite a rather benign period of economic and finance news out the area save the unexpected resignation of Minister of Finance Mr. Kudrin and some encouraging concrete progress for Russia's accession to WTO. The final vote for WTO is expected to occur on 16th and 17th December and all hurdles to Russia's long and arduous road towards WTO accession have been resolved and agreed. Russia has been the largest economy excluded from the WTO and this session ushers in a new era for potential economic growth in the country.

We also received some clarity on the political situation here in Russia with Mr. Putin's decision to run for the 2012 presidency scheduled for March although there were some mixed signals from the capital markets and liberal minded political commentators. This should signal another orderly political transition within the country and I believe the policies formulated in the next administration will continue to support economic growth in the country and remain investor friendly.

From an operational perspective NOVATEK has had a very strong third quarter characterised by little or no impact on our core natural gas production from the traditional seasonal or trough period. Moreover we demonstrated to our sceptics and more importantly to the global oil and gas industry that the northern sea route is navigable during the period commencing from October to November and after taking into consideration this crucial fact our ability to move liquid hydrocarbons utilising this important sea route bodes well for our future Yamal LNG project as well as allowing us to diversify and arbitrage our commercial customer base between the United States, European and Asian Pacific markets. During this navigable period we made further inroads in the Asian Pacific markets by delivering stable gas condensate cargoes to new customers located in Thailand combined with delivering hydrocarbons to our additional commercial accounts located in China and South Korea. All told we dispatched nine takers carrying approximately 600,000 tonnes of stable gas condensate during the navigable season via the Northern Sea route representing a nine fold increase over those volumes transported in 2010 when we made our inaugural voyage utilising this important logistical route.

Within Russia we managed to make further increases in our domestic market share by executing a new long term contract to purchase and resell natural gas to Sibur including marketing approximately 2 billion cubic metres of our own equity natural gas to their facilities in new regions, the signing of a new gas contract with OGK-3 for delivery of natural gas to two of their three power plants although we have been delivering some volume of natural gas to this customer as well as anticipating the closing of a transaction to purchase Gazprom's regional trader by year end which will provide us with the opportunity to supply the majority of natural gas deliveries to the Chelyabinsk region. All three commercial events are expected to commence in 2012.

Our wholly owned subsidiary NOVATEK Chelyabinsk will purchase natural gas directly from Sibur under a long term sales and purchase contract. The initial volumes are projected to be approximately 3.5 billion cubic metres in 2012, an increase in the 4 billion cubic metres per annum until 2016. More broadly we review the Chelyabinsk market as a very attractive and growing industrial market for NOVATEK to pursue as this region presently consumers' approximately 16.5 billion cubic metres of natural gas annually. The size, potential and stability of consumption support our decision to further penetrate this key consuming industrial region through the acquisition of the regional trader.

As part of our commercial strategy we will continue to grow our market share vis-à-vis our competitors and as such it is important that we target attractive markets to achieve our goals and objectives. In addition we plan to expand our commercial reach into new areas as well as different customer segments as a means to stabilise the production profile throughout the year and we believe that our ability to deliver gas directly to Sibur petrochemical complexes is one example towards achieving the production stability.

During the quarter we achieved very positive exploration results as we discovered five new gas condensate deposits: two discoveries at the Olimpiysky licence area; two discoveries at the South Tambeyskoye field; and a discovery at the Sever-Russkoye licence area. All told we drilled approximately 15,000 metres of exploration drilling in the period.

For our development activities we remained active by drilling and completing wells at three primary development sites: five gas condensate wells at the Yurkharovskoye field, two oil wells and four reconstructed gas wells at the East Tarkosalinskoye Field and one gas well at the [Samburgskoye] field which is part of the SeverEnergia assets.

During my second quarter conference call I mentioned that the strong demand during the seasonally adjusted trough period led us to reconsider our production target for the year, thus we raised our full year production guidance from 48.9 billion cubic metres to the higher range between 50 and 51 bcm subject to normal weather and market conditions. Due to our strong production figures year to date we are raising our full year production guidance a second time this year between the range of 51 and 52 bcm to reflect stronger than expected demand during the third quarter as well as our ability to inject approximately 1 billion cubic metres of natural gas in the underground storage facility. We believe that this new range is more indicative of our expected full year production results based on production to date.

While on the subject of natural gas production I would like to provide our investors and analysts with some preliminary guidance on our production growth for 2012. Based on next year's development programme we conservatively anticipate production growth of natural gas in a range of 6-7% for the upcoming year which is largely on top of a significant percentage increase year on year in 2011. During 2012 production growth will again be loaded back and with further development activities at the Yurkharovskoye field where we intend to complete stage 4 of the field's phase 2 development activities. We will effectively increase the Yurkharovskoye field productive capacity by another 4 bcm next year to approximately 37 billion cubic metres thus bringing NOVATEK's overall productive capacity to roughly 57 bcm. This expected growth will not happen until the latter part of 2012 effectively negating this full impact until 2013 and beyond.

As a result of these work activities our overall infrastructure capacity will increase to approximately 67 billion cubic metres which supports future production growth in our business. Another important factor is the commission of the first natural gas production at SeverEnergia which is now expected to occur towards the end of February and accordingly we will benefit via a 25.5% indirect equity stake in the joint venture.

In the third quarter it was reported at an event in Sochi that Gazprom will be the purchaser of 100% of the gas production and we, NOVATEK, will be the buyer of all liquids in the field. Our nature gas production included equity purchases for the nine months of 2011 totalled 38.6 billion cubic metres representing an increase of 12.1 bcm or 45.5% over the corresponding reporting period of which 51% represented organic growth at the Yurkharovskoye field, 16% represented resumption of dry gas at our existing core asset portfolio and 33% represented contributions from our equity share of production from Sibneftegaz. We continued our strong production trend during the month of October by producing approximately 4.9 billion cubic metres which represents an increase of 52% year on year and 7.3% quarter on quarter. It is also important to note that resumption of dry natural gas production at our East Tarkosalinskoye field relative to prior periods which represented a 97% and 51% increase year on year and quarter on quarter respectively. During the quarter we increased our natural gas production year on year and quarter on quarter by 4.9 billion cubic metres and 1.3 billion cubic metres respectively although we reported no purchase gas in the third quarter 2010.

In the current reporting period we have scheduled maintenance and repair work at the Yurkharovskoye field so the primary growth in our gas production quarter on quarter was driven largely by the resumption of dry gas at the East Tarkosalinskoye and Khancheyskoye fields. For liquids we increased our production during the reporting period by 428,000 tonnes or by 16.3%. This growth was achieved through continued wet gas production increases at the Yurkharovskoye field which as at reporting date accounted for approximately 66% of our liquid production. We continue to see relative declines in liquid output from both the East Tarkosalinskoye and Khancheyskoye fields which correspond to the declining concentration levels of unstable gas condensate at our mature fields. We anticipate compensating for these natural declining levels of liquid concentration by bringing on stream other wet gas fields such as the field of SeverEnergia.

On my last conference call I reported that there were recent reports indicating that the Arctic ice melt is decreasing at a record rate and may surpass the previous low period set in September 2007. This was a case which essentially meant that the navigational period was extended by another month to November thereby increasing the number of potential voyages utilising the Northern Sea Route from July to November. As expected we took full advantage of this extended navigable period to collect important shipping data, test tanker sizes and as already mentioned demonstrate the viability of this important shipping route for future deliveries of stable gas condensate and liquefied natural gas.

As you know already NOVATEK and Total concluded our sales and purchase agreement in October paving the way for Total to purchase a 20% equity stake in Yamal LNG. We reported this signing as a post balance sheet even and will provide more details of the deal structure in our upcoming strategy presentation. We are also very active in discussions with other potential partners as of this conference call but it is still premature at this point to discuss the timing and closure of our negotiations. We are optimistic that we will make progress in these discussions and hopefully have more to report in the near term. We fully anticipate that Yamal LNG will be a major player in the LNG market when this transformational project comes on stream and these sentiments were recently echoed by energy minister Sergei Shmatko in Doha at the gas exporting conference forum.

In other developments we concluded the purchase of the four new licence areas in the Yamal Gdansk peninsula and we are optimistic that further exploration and development activities over the mid to long term will yield significant production opportunities. Two of the four licence areas already have proven reserves under the Russian reserve classification C1+C2 of 6.8 billion barrels of oil equivalent as well as having huge upside exploration potential in the D1, D2 resources of 13.3 billion barrels of oil equivalent. Our goal is to devise an exploration and development programme for these new licence areas over the next 3-5 years and based on these activities open up a whole new area of development for the company. We also remain diligent in assessing new licence areas and potential acquisition opportunities to complement our existing asset base in the prolific Yamal-Nenets region.

We increased our natural gas sales volumes by 51% during the reporting period whereby 4.1 billion cubic metres as compared to the prior year period. Seasonally adjusted on a quarter on quarter sales volume increased from 11.8 bcm to 12.3 bcm or by 3.7% reflecting continued strong sales throughout the period. Although we expect adjustments in our volumes sold to reflect the seasonal nature of gas consumption in the domestic market, we nonetheless achieved very strong and consistent performance in the nine months ending 30th September versus the prior comparable period by increasing our sales volumes by 45.7% or by approximately 12 billion cubic metres. Within our sales mix for natural gas, end customers represented 54% versus 67% year on year for the nine months ended 30th September with volumes sold to the power generation sector accounting for approximately 41% of the total sales volumes or 76% of our end customer category. During the respective quarter our sales mix was 57% end customers and 43% wholesale traders. The year on year reduction in our end customer sales was largely attributable to the initiation of a high net back margin wholesale contract with Itera effective 1st January.

Our volumes of natural gas sold to end customers increased by 14.6% as compared to the third quarter 2010 and represented 57% of our total sales volumes versus 75% year on year. During the reporting period we demonstrated strong organic production growth from our Yurkharovskoye field of 27% and resumed production levels at the East Tarkosalinskoye field. In the prior reporting period we curtailed gas production at both the East Tarkosalinskoye and Khancheyskoye fields to maximise wet gas production at the Yurkharovskoye field with the completion and launch of the second and third stages of Phase 2 development activities on the filed. We resumed dry gas production held in reserve to meet increased market demand and we also benefited as I mentioned previously from the positive contribution from our share of equity production from Sibneftegaz. During the third quarter 2011 we injected approximately 991 million cubic metres of natural gas into the underground storage facility and ended the reported period with an inventory balance of approximately 1.2 billion cubic metres to be withdrawn during the peak consumption periods.

Our average realised prices for end customer sales during the third quarter increased by 14.2% in comparison to year on year and were consistent with those prices realised quarter on quarter. The prices we realised for natural gas were consistent with the expectation vis-à-vis the general tariff increase effected 1st January and the relative geographical mix of our primary customer base. For ex-field or wholesale gas traders our average realised price increased year on year by approximately 155 rubles per thousand cubic metres or by 13.5% and was consistent with the prices we received for this category of sales quarter on quarter. Our combined average realised price increased year on year by 16.8% thus improving our average net backs for natural gas sold to end customers by approximately 215 rubles per thousand cubic metres or 18.1% which was slightly lower than the average net back received quarter on quarter by 1.1%. We achieved a higher margin differential between end customers and ex-field netbacks in the third quarter as compared to the prior period which continues the pricing dynamic trends achieved prior to the economic crisis.

During the period our overall transport costs per thousand cubic metres was reduced because the average distance to transport our natural gas to end customers was lower year on year and quarter on quarter by 13% and 7% respectively averaging approximately 1,775 km in the current reporting period which was slightly offset by the 9.3% increase in the transport tariff approved by the Federal Tariff Service effective 1st January. The geographical markets representing at least 10% of our sales volumes were the Moscow, Orenburg, Chelyabinsk and Perm regions which was consistent with both reporting periods.

Meanwhile for liquids we sold 933,000 tonnes of liquids which represented a 9.2% decrease over our comparable quarter on quarter sales but was roughly 487,000 tonnes higher than the prior period, a year on year increase of approximately 20%. Within our liquids sales mix stable gas condensate increased by 28% year on year but decreased by 13% quarter on quarter which was slightly offset by our increase in crude oil volumes sold. Essentially the quarter on quarter decrease in volumes sold relate to a timing of revenue recognition difference with the corresponding increase in goods in transit during the reporting period.

The Yurkharovskoye field continues to yield organic growth in both natural gas and liquids productions. With the increase in natural gas volumes produced we also correspondingly increased our unstable gas production by approximately 532,000 tonnes of by 36%. We continued to experience declining liquids from our older, more mature fields which is consistent with our original experience at these fields. What is important to note is that the resumption of natural gas from these field are basically dry gas from the Cenomanian layers and they will not yield liquid production like the deeper wet Valenginian formation.

Specifically we had strong year on year growth in our export sales of stable gas condensate which was slightly offset by the reduction in volumes sold for LPG. During the period our volumes of stable gas condensate in transit and storage were approximately 325,000 tonnes which were higher by 51,000 tonnes quarter on quarter and by 119,000 tonnes year on year. Our overall liquid hydrocarbon volumes and inventory aggregated 422,000 tonnes at period end versus 296,000 tonnes year on year and 371,000 tonnes quarter on quarter. The most notable difference in our liquid sales year on year was the significant increase in commodity prices between the respective periods, particularly the price for Brent in euros blend which positively affected our overall liquid netbacks. Our average export netbacks on a US dollar basis for stable gas condensate and LPG volumes sold during the period increased by approximately 46% and 29% respectively despite increases in both export duties and average transportation expenses. In comparison to the second quarter 2011 our average exports netback for stable gas condensate decreased by 21% largely due to an increase in the export duties and a reduction in our average sales contract price.

I had previously mentioned on prior earnings conference calls that it would be very difficult for analysts and investors to precisely calculate our export liquid sales for a number of reasons such as timing and destination of cargoes, but equally important the benchmark pricing used at the base of our contractual arrangements which also must take into consideration any premium or discounts based on present market conditions in demand. Generally speaking I believe most analysts are using the [Brent prices or Urals blend] as their pricing estimates but we often use a formula pricing that takes a 50-50 ratio between WTI and Brent as well as pricing based on naphtha Japan and Dubai, so it is not too surprising to receive and read post earnings releases comments that if liquid prices were weaker than expected when the basis of estimation was probably skewed to the higher Brent pricing during the period. We consider a whole range of market based factors to sell our stable gas condensate to diverse regional markets and industrial segments and we believe the pricing formula used during the period was consistent with our market assessment and traders' expectations.

For stable gas condensate we sold 657,000 tonnes realising and average netback per tonne of $357 in the third quarter as compared to $303 per tonne in the third quarter 2010 and $450 per tonne in the second quarter 2011. The difference per tonne year on year was largely attributable to the overall increase in our contractual price which exceeded the increases in export duties and transport expenses. Conversely the main factor contributing to the lower average netback price was a reduction in our average contractual price by roughly $51 per tonne or by 9%.

Our LPG export volumes increased by 10,000 tonnes year on year to approximately 112,000 tonnes and at the same time we managed to increase our average realised netback by approximately $26 per tonne largely attributable to an increase on our contractual price which was offset by increases in export duties and transport expenses. Our volumes of LPG exports were relatively consistent quarter on quarter but the average netback decreased by 11% largely due to a 73% increase in export duties which effectively negated the increase on our contractual price.

During the third period we dispatched 11 tankers carrying approximately 718,000 tonnes from the Vitino sea terminal of which two tankers or approximately 17% of the volumes dispatched were destined to the European markets; three tankers or approximately 25% of the volumes were dispatched to the United States; and the remaining six tankers or approximately 58% of volumes were destined to the Asian pacific region. Our Purovsky Processing Plant operated at 74% of its rated capacity with total plant output reaching 921,000 tonnes comprised of 709,000 tonnes of stable gas condensate, 209,000 tonnes of LPG and 3,000 tonnes of methanol products. On a total barrel of oil equivalent basis we increased our production to 95.2 million barrels of oil equivalent in the third quarter versus 62.2 million in the prior reporting period.

During the first and second quarters 2011 we produced 95.6 million and 87.2 million boe respectively which essentially indicates that we have relatively stable production during the past year despite our seasonally adjusted production plans.

We increased our capital expenditures year on year by approximately 5% to 7.5 billion rubles but decreased the amount spent on capital projects marginally quarter on quarter. During the third quarter the Yurkharovskoye field accounted for approximately 37% or 2.7 billion rubles of our invested capital which is higher by 6% and 5% relative to the capital spent on the field year on year and quarter on quarter respectively. As I mentioned earlier we are planning to expand the productive capacity of the Yurkharovskoye field during the latter part of 2012 but nonetheless we are slowly approaching a point whereby the Yurkharovskoye field will begin its capital programme and the overall reduction in capital spend of the past 12 months reflects that fact.

Since we are presently working on our business plans for the upcoming year I will not provide any guidance on our expected capital expenditures for 2012 but I will update everyone on our capital programme for the upcoming year on our strategy day presentation.

During the reporting period natural gas represented approximately 64% of our total revenues as compared to 56% level achieved year on year and was also higher than the percentage of revenues achieved in the second quarter of 60%. We maintained our revenue split of 63%-37% between natural gas and liquids which is relatively consistent with our revenue guidance of 60%-40% but the present revenue mix was skewed toward natural gas because of the timing of the revenue recognition with our stable gas condensate in transit.

We maintained strong cost control over operating costs during the third quarter relative to the size of our business and continued growth of our revenues and as a result there are no real surprises on the cost side during the reporting period. Our total operating expenses increased year on year in absolute terms from 17.6 billion rubles to 22.9 billion but decreased as a percentage of total revenues from 60% to 57%. Operating expenses in the second quarter 2011 amounted to approximately 22.4 billion rubles and was lower as a percentage base due to an increase in our non-controllable expenses reflecting higher production and transport costs.

As expected the most significant changes in our operating expenses for the comparable periods was the relative increases in our transportation expenses which is explainable by the overall growth in our end customer sales combined with our annual tariff increases as well as taxes other that income which increased year on year largely due to the volumetric nature of expense items and a 61% increase in the mineral extraction tax for natural gas effective 1st January.

We continue to effectively manage and control our general & administrative expenses as a normal course of business; however we continue to fluctuate period on period in the controllable expense category due primarily to semi-annual and annual payments, charitable contributions, consultant services and business travel expenses among other line items. The main increase in our G&A expenses year on year was the increase in charitable contributions and social programmes in the Yamal Peninsula which was directly related to our ongoing activities in the Yamal LNG project. In comparison to the second quarter 2011 we managed to reduce our controllable expenditures by approximately 357 million or by 17% due largely to a reduction in bonus accruals for key management personnel which were offset by the increase in charitable and social programmes just mentioned.

At the end of the third quarter 2011 the company had total employee head count of approximately 3,925 employees.

We undertake various repair and maintenance activities at our production and processing site and these expenses tend to vary period on period based on rotating schedules, therefore it is not unusual to see periodic expenditures paid to maintain our asset base in working conditions and more importantly the type and frequency of the work varies depending on whether something was specifically planned to undergo repaid and maintenance or something unexpected arose that needed attention during a particular reporting period. This quarter we undertook planned various works at the Yurkharovskoye field whereas in the second quarter the repairs and maintenance activities centred mostly at the East Tarkosalinskoye and the Khancheyskoye fields.

One of the hallmarks of our success has been our low cost structure and NOVATEK continues to maintain some of the lowest operating costs in the oil and gas industry globally although periodically we experience fluctuation in specific line items based on the timing and nature of our work schedules. As a result of the factors enumerated above our EBITDA and net profit margins continue to remain robust in the reporting period achieving levels of 47.4% and 21% respectively. On an adjusted basis these reflect the recent volatility in the currency markets and to offset the non-cash foreign exchange loss from the 13.5% ruble depreciation against the dollar during the quarter, our net profit margin after this adjustment was approximately 36.8% which is consistent with our financial guidance. Naturally our earnings per share was also negatively impacted by the non-cash foreign exchange loss and thus decreased year on year by 16.8% to 2.77 rubles per share during the period but adjusting this figure to offset the forex loss, our earnings per share was higher by 54.5% year on year and 7.8% quarter on quarter.

Unfortunately we may have to continue addressing this issue on an adjusted basis until we get some economic and financial stability in the Eurozone and as a result a reduction in volatility in the currency markets.

Our balance sheet and liquidity position remained strong throughout the reporting period although we increased our overall debt portfolio this year as a result of our US dollar denominated Eurobond that we concluded in February 2011. We remain free cash flow positive during the third quarter and so far throughout all of 2011. We also received a cash payment for Total’s purchase of its 20% equity stake in Yamal LNG post the balance sheet date which effectively offsets the negative working capital during the reporting period. We will continue to fund our capital expenditure programme through internally generated cash flows and have the ability to meet all of our debt obligations in liabilities when they become mature or become due for payment.

In conclusion NOVATEK reported another strong quarter of financial and operational results despite the turmoil in the Eurozone and the increase in market volatility. We believe the company is poised to continue growth in our story and I would like to remind everyone tonight that we are planning to provide a comprehensive update to our corporate strategy reflecting the fundamental changes we see in the market as well as incorporating our new elements in our business operation such as Ust-Luga and Yamal LNG. We have set a date for 9th December at the London Stock Exchange to present our corporate strategy and we'll send out formal notifications of this even via our normal channels of communication. I would like to sincerely thank all our valued shareholders through your continued belief in the growth story of NOVATEK despite these periods of market volatility but we truly believe that the future looks quite promising to us with the portfolio of assets we currently have in the pipeline, our strong production growth profile, our increasing cash flow generation and a low risk long life reserve base that fully supports our growth strategy.

I have previously mentioned that NOVATEK has already begun its transformation process. As we migrate down the hydrocarbon value chain to increase our risk adjusted margins we will get closer to our consumer base through our regional and commercial expansion and at the same time increase our present market share. We already have an excellent set of exploration & development opportunities resident in our existing asset portfolio but we will not stand still on our quest to grow and we will continue to assess acquisitions that support our growth initiatives, expand our market reach and fill gaps in our asset portfolios. When we present our updated corporate strategy in London we will provide more concrete information on the Yamal LNG project, the challenges we face and the solutions that we have been able to achieve. We will also disclose the specific terms and conditions of the equity stake sold to Total so that our investors understand the accretive nature of this transaction towards creating shareholder value.

Finally the ministerial meetings over the past couple of days at the gas exporting countries forum in Doha confirms our previous comments that we still have strong interest in a project from other potential partners as well as Russian government's favourable view of the project.

I would like to end the conference call now and open it up to questions and answers. Thank you very much.

Operator: Thank you. If you would like to ask a question at this time please press the star or asterisk key followed by the digit 1 on your telephone. Please ensure that the mute function on your telephone is switched off to allow your signal to reach our equipment. If you find that your question has already been answered you may remove yourself from the queue by pressing *2. Again please press *1 to ask a question. We will pause for just a moment to allow everyone to signal.

We will now take our first question from Geydar Mamedov from Goldman Sachs. Please go ahead.

Geydar Mamedov: Good evening. I would like to ask two questions if possible. The first one is on the recent deal with Russian railroads. There was some information that you plan to spend 30 billion rubles on building the railroad in the Yamal-Nenets region and there were some comments around that it will be structured as a prepayment, you will get a discount from the tariffs, so I just wanted to ask about how technical, will this be a repayment on your balance sheet and will it then be offset against expenses or will it be actual capital expenditure which will result in an asset in your balance sheet? That's the first one. The second one is on the deal with Sibur on 3.5 bcm per annum purchases from 2012. Is it possible to give any guidance on the mark-up that will be used there in your resale from Sibur to Chelyabinsk region? Thank you.

Mark Gyetvay: Geydar, I'm surprised you were able to get the first question in, usually it's reserved for Oleg. To answer the first question, you're correct, we did agree with the region, the Russian railroad specifically to fund approximately 30 billion of additional railroad build-out of approximately 40 billion total capital expenditures and we did this because it has been our history to ensure that the infrastructure is in place for us to continue to grow our business. As you know as we start developing the Samburgsky licence area and other wet gas fields at SeverEnergia, we plan to significantly increase the amount of wet gas production, hence unstable gas condensate and historically what we've done, we've tried to de-bottleneck any potential problem by taking the capital expenditure ourselves such as Purovsky and our own pipeline, but in this particular case it is not going to be an asset on NOVATEK's balance sheet. It's a prepayment which we will then deduct from the favourable tariff that will be provided to us for this particular investment. Your second question on Sibur, generally speaking we don't provide individual information on each particular customer account so I would kindly refrain to answer this question. All I would say is I mentioned on this call and on the prior conference call is that we have agreed to a discount relative to the federal tariff service price and that the margin we will be making on this is sufficient for us to make this type of investment, so I'm not going to get into specific details as to what the margin is.

Geydar Mamedov: Ok, thank you for that.

Mark Gyetvay: You're welcome.

Operator: We will now take our next question from Igor Kurinnyy from ING Bank. Please go head.

Igor Kurinnyy: Good afternoon Mark, it's Igor Kurinnyy from ING Bank. I just wanted to ask about loan production growth. I know it's probably more appropriate to address this during the strategy update but given that there has already been a comment from NOVATEK about plans to double production by 2020 I just wanted to clarify those statements, basically whether you were talking about M&A growth and also Yamal LNG production. Would it on those plans or not?

Mark Gyetvay: Igor, thank you. It's a combination, again it's probably best to answer this question in more detail on the strategy presentation because we'll talk about that in specifics, but essentially what we're trying to do is reconfirm what production levels we plan to reach our target of 2015 because that is still out in the market and then what new production etc we expect to bring on stream to meet the aggressive targets that we set for ourselves to 2020. In essence effectively it is essentially a doubling of production and it will be filled by a combination of existing assets, exploration activities etc and some from Yamal LNG, so it's a combination of factors.

Igor Kurinnyy: Understood. Thank you Mark.

Operator: We will now take our next question from Karen Konstanian from Bank of America. Please go ahead.

Karen Konstanian: Hi Mark, thank you so much for the presentation. I have one question, of the four licences that you acquired at the beginning of this year, you mentioned 6.8 billion of boe of Russian classification of reserves. Are any of those licences going to be included into the development of the Yamal LNG and as such what would be the timing of this and would any of those reserves be included into your next reserve audit? Thank you.

Mark Gyetvay: The second part of your question is easier to answer than the first. The answer on the second question is that our plan today is probably not to include it in the SEC reserves. It might be included in the PRMS reserve category because we're still working on an overall development plan, exploration programme etc as I mentioned but we know already that there is C1 and C2 reserves categories on two of the licence areas, so we know a significant amount of work has been done from an exploration perspective but we'll include that probably in 2012 reserve numbers. To go back to your first question which I said is a little more difficult, right now so that everybody understands it is not part of Yamal LNG. Those assets, those four licences are held by NOVATEK Yurkharovneftegaz and so a decision has not been made yet as to whether or not those particular licences will be part of Yamal LNG at this particular moment.

Karen Konstanian: Thanks Mark. Just to clarify, you said that part of those reserves are going to be included in 2011 reserve audit or just the 2012 reserve audit?

Mark Gyetvay: 2012.

Karen Konstanian: Just 2012. Thank you.

Mark Gyetvay: Particularly when we talk about the SEC type definition, I believe there may be some into the PRMS but I'm not certain right now. We are in discussions with DeGolyer McNaughton and our geological services here whether or not we're going to have them [reserves] appraised this year or not, but I think in all probability since we got them late in the year it's probably unlikely that we have enough work done to complete an exploration development programme to include them in the 2011 reserve works.

Karen Konstanian: OK, thank you,

Mark Gyetvay: You're welcome.

Operator; We'll now take our next question from Oswald Clint from Sanford Bernstein. Please go ahead.

Oswald Clint: Yes, good evening Mark, thank you. Just back on the exploration actually and noticing your five discoveries this quarter, I'm just curious to know what sort of size do you think is in these discoveries and how do those square up with the trend of your exploration successes over the last 12 months or the last couple of years in terms of size and/or quality? Then maybe just on the decline rates that you're discussing with the Cenomanian condensate layers, is a 5%, 6% assumption here a reasonable assumption or is there some other number you might want to point us to? Thank you.

Mark Gyetvay: In terms of the trend I think it has been relatively consistent with the exploration activities we've been doing at some of our licence areas. We have continuously expanded our Yurkharovskoye area as well as the new Yurkharov area by delineating and finding additional deposits. We've also over the last couple of years have found additional deposits in the Khancheyskoye licence as well as East Tarkosalinskoye, so I think the trend has been relatively consistent that the more exploration work we do we're able to delineate these in reasonably consistent sizes. What I'm talking about is essentially additional layers of deposits and I think it's a little early to say is it similar to a sweet spot? Obviously it's not. These may be a little more peripheral extensions of the field but nonetheless they are extensions of the field. In terms of the other question…what was the second part of your question?

Oswald Clint: You were talking about condensate declines.

Mark Gyetvay: In terms of the layers it's a natural…again I'm not sure if I can provide you with a percentage because it changes well by well. What it is historically as of the existing fields producing, when we're seeing the declines we're talking about today mostly the East Tarkosalinskoye and the Khancheyskoye field but if you look at the production capacity for example at the East Tarkosalinskoye field we're talking about relatively…11-12, 13 billion cubic metres of dry gas and approximately 2+, 2.5 bcm of wet gas, so what we're talking about is lower decline levels of the concentration in that 2.5 billion cubic metre layers and as the pressure differential changes in a well we're seeing as a natural progression of field development because now you remember East Tarkosalinskoye has been producing since 1998, we're just seeing the declines in the field based on that concentration, but it's difficult to give you a precise percentage because it changes well by well, different layers of the field. Just to clarify also, it's not coming from the Cenomanian gas. It's coming from the Valenginian layers within those two particular fields.

Oswald Clint: Ok, that's great. Thank you

Operator: As a reminder if you would like to ask a question at this time please press *1. We will now take our next question from Pavel Kushnir from Deutsche Bank. Please go ahead.

Pavel Kushnir: Good afternoon, thanks Mark for the presentation. I have a follow-up question about your Sibur contract. You will purchase gas from Sibur and then resell that gas on the Chelyabinsk market. The question is why don't you sell your own gas on the Chelyabinsk market? I'm assuming that you would be able to make much more money by gaining market share with your own natural gas volumes. The related question is on SeverEnergia liquids purchases. Gazpromneft have told us that they will sell gas condensate to you and stabilise gas condensate to you on the basis of a formula which would already take into account the price of stabilised gas condensate on international markets. Here we also see a situation when you buy gas condensate and then resell gas condensate at a small margin, at a small premium, so the question is why get involved in this activity? Thank you.

Mark Gyetvay: The answer to your first question, it's basically pure margin for us. We are able to off-take some of the associated gases being processed by Sibur and provide it into a market area where today we wouldn't have enough gas to deliver to that market area and so we're making pure cash flow on these types of trading margins. Given the opportunity to do that and lock in a particular market until such time as we can continue to increase our production and capacity makes absolute financial sense for me. On the second question in terms of…obviously I was not there to hear what the comments were made from Gazpromneft but what I can tell you is that again we're going to be purchasing stable gas condensate from the particular partners and we believe that the contract, the formula based contract that we do have we will make significant margins on them because it does take into consideration all the costs associated with processing. We are not providing free processing or free transportation. That's taken into consideration at the formula basis, so I don't know what they're telling you in terms of what type of margin, of course it's going to be based on some kind of export number but the processing and the transportation is taken into consideration because without our facilities in place today they would not be able to develop the field, so I believe that that contract is also very profitable for us and we will continue to do those types of deals if we can aggregate additional condensate in the area because remember now as we start increasing the levels of condensate either to our own production or aggregating in a market, by this time we will also have been expanding Purovsky Processing from 5 to 8 and 8 to 11, going from 5 to 8 by 2013 and from 8 to 11 by 2015 but we're also next year going to launch the first phase of our Ust-Luga project, so the more condensate that we get for the system, I believe it's good for us to be the aggregator at this particular juncture in the marketplace. Also I think that if you go back to the Sibur contract for a second, don't lose sight that in addition to this contract that you say why are we doing this and I am telling you that it's a pure cash margin for us which we think is an acceptable risk for taking on these particular clients. We are also going to supply them with about 2 billion cubic metres of additional equity production in facilities that we currently don't provide gas, in markets we don't provide to that region which provides certain stability in our production, so the Sibur contract is perfectly good for us from a financial perspective.

Pavel Kushnir: Thank you very much.

Operator: We will now take our next question from Vadim Mitrosin from Okirite Capital. Please go ahead.

Vadim Mitrosin: Yes, good afternoon. Thanks Mark for your presentation. I have a couple of small follow-ups. First of all on this contract with the Russian railroads and your advanced payment, 30 billion rubles seems to be a very big number. I wonder over what period of time do you plan to make this expenditure and in relation to this how long it will take for you to compensate for this amount? What number of years do you project to cover this expense?

Mark Gyetvay: Again what you're asking and I appreciate your question Vadim, what you're asking, do we take the risk that absent our investments pre-payment that the Russian railroad will not make their investment and hence we don't have transportation for our increased volumes of stable gas condensate and I will tell you right now again if you look historically what we've done at NOVATEK and I can take you back to our investment into Purovsky Processing Plant and the relative quick payback, but that was done because we knew that there was a bottleneck in the structure at [Surgutsky Refinery] and we knew that we would increase our levels of condensate via the wet gas production at the Yurkharovskoye field. The same thing with the transportation of the pipeline, we built the 326 km pipeline. People are saying why are you making this capital investment when the fact that you have Gazprom's pipeline structure, well the fact of the matter is we wouldn't have it forever and it's prudent for us to ensure that these assets, these transportation structures or these processing facilities are available for us, no different than a Russian railroad. 30 billion rubles over a period of 3, 5 years, whatever that investment will be spread out is a very acceptable investment for us to make as a prepayment because it will be a prepayment and a discounted tariff to ensure that these investments are being made by the Russian railroad so that we can increase the level of condensate being transported through the infrastructure. Absent that we're not getting into the railroad business, so we're not going to build our own separate railroad lines, so I think this is an absolute prudent way to invest capital to ensure that this infrastructure is in place and we can continue growing because the trade off is high value liquid products in the market versus a relatively small investment which will be just a prepayment on a discounted tariff version. Again I would do that investment any day.

Operator: We will now take our next question from Nadia Kazakova from JP Morgan. Please go ahead.

Nadia Kazakova: Thank you. Could I ask two questions please? The first one just to clarify the capacity number you've given to us, you said that by the end of 2012 I understand production capacity at the major field will be 57 bcm; then you mentioned the 67 bcm number as an overall capacity. Have I misheard or are they actual numbers, 57 organic capacity and 67 overall capacity? That's the first question. The second question, can you give us production targets for liquids please for this year/next year? Thank you.

Mark Gyetvay: Ok. To clarify the first question it's 57 billion cubic metres of production capacity. That is all organic production capacity. That takes into consideration the Yurkharovskoye upgrade, the East Tarkosalinskoye, Khancheyskoye etc. That's the 57. The 67 that I mentioned bcm is our infrastructure that we built out, so we're building out infrastructure on the field for future ramp-up of additional production capacity and we're doing that now and so I'm saying is that the overall infrastructure capacity at the field will be 67 bcm. It's similar to the situation we had when we built for example; we built a pipeline at the Yurkharovskoye field. The infrastructure that we laid on the pipeline structure was about 34 billion cubic metres of gas, although we were only producing at the field 20 something billion cubic metres, because we knew that we were going to incrementally grow our production over time, when we make this investment in infrastructure we just increased it, so it's essentially a difference between production capacity at 57 and infrastructure capacity at 67. To answer your second question I don't have a liquid number to present today or I would have provided that number on the conference call.

Operator: As a final reminder if you would like to ask a question please press *1 on your telephone keypad. We will now take our next question from John Armitage from Egerton Capital. Please go ahead.

John Armitage: Hi Mark. Congratulations on the numbers and congratulations on everything you're doing. Just to clarify this railway expenditure, so it's 30 billion rubles and we should see that essentially as a prepayment against future tariffs?

Mark Gyetvay: John, that's correct. Future tariffs will be a discounted tariff to us but I don't have the discount number to you today but obviously you'll see it when we start reporting, but it will be a discounted tariff for the cost of capital to do this investment.

John Armitage: Is it a greater expenditure than you would expect to spend on railway transport?

Mark Gyetvay: No, that's all been taken into consideration. We are talking about essentially a long term…we're talking about essentially building, providing the Russian railroad who doesn't have the money to make these capital investments into rail tracks etc that will be servicing our production growth, so if you assume our production to be 10, 15, 20 years, we're going to have…it'll be amortised over a series of productions and transport fees over time.

John Armitage: So in other words based on your production plans in the medium and long term, you would have been spending 30 billion rubles on railway transport?

Mark Gyetvay: Absolutely.

John Armitage: OK, great. Thanks a lot.

Operator: We will now take our next question from Apostolos Pansis from Commerzbank.

Apostolos Pansis: Hello Mark, this is Apostolos from Commerzbank. I understand that you are planning to lay out a lot more details on your capex and acquisitions plans at the upcoming strategy update, however I was wondering if at this stage you are able to comment a bit on the company's leverage policy targets as well as future funding strategy and if there any plans on the near term or early next year to visit the Eurobond market? There's good performance on the current issues with your yields very close to Gazprom.

Mark Gyetvay: The second question is a little trickier because obviously if the need is there and we have a specific use of proceeds we will definitely consider going out to the bond market. The other thing is really the financial policies that we have in place and the company just for your information is one of the early companies that actually published our whole set of financial policies etc before we even went to the capital markets and we did that because we wanted to make sure that everybody had some transparency in our overall objectives, policies and we wanted to give everybody a chance to actually go back and look at what we've done relative to these policies and you can see that on some of our presentation materials. Essentially what our target is to generally maintain a net debt to EBITDA of one times over a cycle and we have asked the credit rating agencies to provide us with some flexibility of 1.5 to 2 times over this 3-5 year cycle period specifically related to any M&A transactions. We generally maintain EBITDA net interest coverage of 10-15 times. We have certain cash balances on the balance sheet; we try to maintain at least 100-150 million of reserves. We have been carrying I think as of the third quarter we were about almost 500 million on the balance sheet. We try to avoid concentrations of bank accounts. We have cash held in 12 banks. We have available lines of credit between 300-500 million. As of this date we have 495 million of unused funding. All financing funding is done at a central basis. We don't allow our subsidiary companies to raise money. We maintain or aim to maintain secure debt below 15% of the total debt target. We have zero today, so the credit policies are out there for people to look at and I think if you look at some of our presentations that we have on our website where we actually show you the metrics relative to the credit policy you'll see that we have been in line with those policies since we went public.

Apostolos Pansis: Fair enough, thank you very much.

Mark Gyetvay: You're welcome.

Operator: We will now take our next question from Constantine Cherepanov from UBS. Please go ahead.

Constantine Cherepanov: Yes, good evening Mark. My question is about the selling of a 20% stake in Yamal LNG to Total, so the question is will you recognise any profits from this transaction in the fourth quarter? Could you give us guidance for this amount it would be very useful? Thank you.

Mark Gyetvay: Obviously there will be some profit on it but it will be relatively minimal considering…when we get to that point in the fourth quarter and do the calculations etc, it may be one of the things…I understand it's very difficult for you to calculate that. We might provide some extra pre-earnings release information so that you have that number in place because we're not here to surprise anybody. Let me just clarify a couple of points on the transaction so that everybody gets a general sense of what we've done. Effectively we were not interested in making huge cash transaction on the initial sale of the options. Our interest and our aim was to ensure that we maximise the total amount of capital carry or proportional finance into the project which we now say will be a contribution to the chart of capital to Yamal LNG rather than worrying about crystallising some profits on the balance sheet date we sold due to the fact that the value we received…because many people were thinking that we would send…at least receive a large cash payment and our goal like I said is not to crystallise huge profits on the actual sale but to ensure over time that the amount of financing that NOVATEK specifically has to contribute into the Yamal LNG project was reduced by the carried interest.

Operator: As we have no further questions at this time I would like to turn the call over to Mark Gyetvay. Please go ahead.

Mark Gyetvay: Again thank you very much and we look forward to seeing everybody, whether or not you can physically visit the London Stock Exchange on 9th December or through the traditional means of a conference call, we look forward to that presentation because I think there's going to be some exciting information on the prospects of NOVATEK going forward and hopefully it answers a lot of these questions in terms of the transaction itself, potential strategic partners, some of the things that we're doing with the Yamal LNG project, as I mentioned some of the challenges and solutions that we have already achieved already and at the same time provide you with some more information as we move forward into our marketing aim where we see both on the global gas business and the Russian domestic market that we believe that we're well positioned to continue growing our market share here on the Russian domestic market and I believe the news flow that you've seen probably today or yesterday, or over the last couple of days from this conference clearly shows you that there's still significant partner interest in our project and we believe hopefully by the strategy presentation we can make some further announcements, but again thank you very much and we look forward to addressing you in December.

Operator: That will conclude today's conference call. Thank you for your participation ladies and gentlemen, you may now disconnect.