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

You should read the following discussion and analysis of our financial condition and results of operations for the three months ended 31 March 2010 and 2009 together with our unaudited consolidated interim condensed financial information as of and for the three months ended 31 March 2010. The unaudited consolidated interim condensed financial information has been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting*. This consolidated interim condensed financial information should be read together with the audited consolidated financial statements for the year ended 31 December 2009 prepared in accordance with International Financial Reporting Standards (IFRS).

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

OVERVIEW

We are Russia's largest independent natural gas producer and the second-largest producer of natural gas in Russia after Gazprom. In terms of proved natural gas reserves, we are the second largest holder of natural gas resources in Russia after Gazprom, under the Petroleum Resources Management System (PRMS) reserve reporting methodology.

Our exploration, development, production and processing of natural gas, gas condensate, crude oil and related oil products have been conducted primarily within the Russian Federation, and we sell our natural gas volumes exclusively in the Russian domestic market. We export our stable gas condensate directly to international markets while our liquefied petroleum gas and crude oil are generally delivered to both international (including CIS) and domestic markets. We generally sell oil products produced from our unstable gas condensate on the domestic market.

In 2009, we geographically expanded our sales of stable gas condensate through deliveries to the Asian-Pacific region. The diversification of our stable gas condensate sales provides us with revenue stability, access to new markets and opportunities for higher margins. The ability to market our stable gas condensate to various geographical regions becomes more crucial as we continue to expand the production of wet gas at our fields and increase unstable gas condensate volumes processed at the Purovsky Gas Condensate Processing Plant (Purovsky Plant).

In November 2009, we established a wholly-owned subsidiary in Poland named "Novatek Polska Sp.z.o.o." (Novatek Polska) to expand our LPG trading activities within this country. Novatek Polska commenced commercial operations in January 2010.

SELECTED DATA

millions of Russian roubles except as stated	Three months ended 31 March: 2010	2009	Change %
Financial results			
Total revenues (net of VAT and export duties)	27,742	16,981	63.4%
Operating expenses	(15,947)	(11,379)	40.1%
Profit attributable to NOVATEK shareholders	11,182	2,134	424.0%
EBITDA [(1)]	15,160	6,899	119.7%
Normalized EBITDA [(2)]	13,577	6,899	96,8%
EBITDAX [(3)]	15,291	6,998	118.5%
Earnings per share (in Russian roubles)	3.69	0.70	427.1%
Operating results			
Natural gas sales volumes (mmcm)	10,106	8,563	18.0%
Stable gas condensate sales volumes (thousand tons)	412	393	4.8%
Liquefied petroleum gas sales volumes (thousand tons)	225	156	44.2%
Crude oil sales volumes (thousand tons)	44	56	(21.4%)
Oil product sales volumes (thousand tons)	3	3	0.0%
Cash flow results			
Net cash provided by operating activities	12,454	5,432	129.3%
Capital expenditures	6,230	3,871	60.9%
Free cash flow [(4)]	6,224	1,561	298.7%

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

[(2)] Normalized EBITDA excludes one-time effect from disposal of investments.

[(3)] EBITDAX represents EBITDA as defined above excluding exploration expenses.

[(4)] Free cash flow represents the excess of Net cash provided by operating activities over Capital expenditures.

SELECTED MACRO-ECONOMIC DATA

Exchange rate of Russian rouble to US dollar	**Three months ended 31 March: 2010**	**2009**	**Change %**
At the beginning of the period	30.24	29.38	2.9%
At the end of the period	29.36	34.01	(13.7%)
Average for the period	29.89	33.93	(11.9%)

Crude oil prices, USD / bbl	**Three months ended 31 March: 2010**	**2009**	**Change %**
WTI [1]			
At the end of the period	83.8	49.7	68.6%
Average for the period	78.9	43.3	82.2%
Brent [2]			
At the end of the period	80.3	46.5	72.7%
Average for the period	76.4	44.5	71.7%
Urals [2]			
At the end of the period	78.2	45.5	71.9%
Average for the period	75.4	43.7	72.5%

(1) Based on prices quoted by New York Mercantile Exchange (NYMEX).

(2) Based on prices quoted by Intercontinental Exchange (ICE).

Export duties, USD / ton [1]	**Three months ended 31 March: 2010**	**2009**	**Change %**
Crude oil, stable gas condensate			
At the end of the period	253.6	115.3	119.9%
Average for the period	263.8	111.8	136.0%
LPG			
At the end of the period	80.0	0.0	n/a
Average for the period	63.7	0.0	n/a

(1) Export duties are determined by the government of the Russian Federation in US dollars and are paid in Russian roubles.

CERTAIN FACTORS AFFECTING OUR RESULTS OF OPERATIONS

Current financial market conditions

The ongoing financial crisis in Greece and the possibility of it spreading to other regional economies has resulted in an increasingly tight funding market and an increased risk of another global liquidity crunch. This may negatively affect all borrowers by limiting access to capital markets, despite signs of the financial markets willingness to price recent transactions. Even though expectations of a prolonged economic downturn have receded, the recent events in Greece and the fears of contagion in other economies has resulted in the possibility of a continuing period of tight credit market conditions and increasing margin spreads, although there is a willingness in the capital markets to consider quality grade issuers to access funds. Furthermore, there is a heightened awareness over excess borrowings, potential liquidity problems and the ability of a company's balance sheet to withstand a period of prolonged market turbulence.

We have continued to monitor the credit situation very closely and have taken various measures to ensure the integrity of our financial condition and mitigate counter-party credit exposure from our natural gas and liquid hydrocarbon sales. In addition, we have taken proactive steps to ensure the safety of our excess funds deposited with both domestic and international banks as well as limited our exposure from prepayments to various service providers. Presently, our cash and deposits are diversified and maintained in well capitalized banks with a minimum risk of default.

We have reviewed our capital expenditure program for the upcoming year and have concluded that we have sufficient liquidity, through current internal cash flows and short-term borrowing facilities, to adequately fund our core natural gas business operations and planned capital expenditure program. As a result of this assessment, we have not made any major adjustments to our capital expenditure program as of the 31 March 2010.

Management will continue to closely monitor the economic environment in Russia as well as the domestic and international capital markets to determine if any further corrective and/or preventive measures are required to sustain and grow our business. In addition, we will continue to assess the trends in the capital markets for opportunities to access long-term funding at a reasonable cost to the Company commensurate with our credit rating and our capital requirements.

Natural gas prices

As an independent natural gas producer, we are not subject to the Russian government's regulation of natural gas prices. Historically, we have sold most of our natural gas at prices higher than the regulated prices set by the government for Gazprom's domestic gas sales, although the prices we can achieve on the domestic market are strongly influenced by the prices regulated by the Federal Tariffs Service (FTS), a governmental agency, and present market conditions. In the three months ended 31 March 2010, the weighted average FTS price for the primary regions where we delivered our natural gas increased by RR 690 per mcm, or 43.1%, to RR 2,292 per mcm compared to RR 1,602 per mcm in the 2009 period.

The specific terms for delivery of natural gas affect our average realized prices. Natural gas sold "ex-field" is sold primarily to wholesale gas traders, in which case the buyer is responsible for the payment of gas transportation tariffs. Sales to wholesale gas traders allow us to diversify our natural gas sales without incurring additional commercial expenses. Historically we have realized higher prices and net margins for natural gas volumes sold directly to end-customers, as the gas transportation tariff is included in the contract price and no retail margin is lost to wholesale gas traders. However, the recent shift in our sales mix has demonstrated that the historical norm may or may not prevail in the present or future market situations.

In November 2006, the FTS approved and published a plan to liberalize the price of natural gas sold on the Russian domestic market by the year 2011. As part of the liberalization plan, the FTS approved four quarterly increases in the regulated price for natural gas in 2009, rising by 5% in the first quarter, 7% in the second quarter, 7% in the third quarter and 6.2% in the fourth quarter. Moreover, in December 2009, the FTS approved an increase in the regulated price for natural gas by 15% effective from 1 January 2010. We expect further increases in the regulated price for natural gas as part of the Russian Federation government's efforts to liberalize the price of natural gas on the Russian domestic market. The FTS will continue to approve the effective increase on an annual basis and reserves the right to modify the percentages published as well as potentially prolong the timetable toward market price liberalization based on market conditions and other factors.

As a result of continued economic instability, in both global and domestic markets, our pricing strategy for natural gas emphasized increasing market share and maintaining production growth. In the three months ended 31 March 2010, our average natural gas price to end-customers and ex-field price increased by 28.1% and 23.1%, respectively, whereas our average natural gas netback price on end-customer sales increased by 11.0%, compared to the respective prices in the corresponding period in 2009. The slower growth in the natural gas netback price to end-customers compared to ex-field price was stipulated by our marketing policy aimed to increase the share of our deliveries to end-customers. In the three months ended 31 March 2010, we commenced deliveries to new end-customers located in more remote regions, which increased our average natural gas transportation expense (see "Transportation expenses" below).

The following table shows our average realized natural gas sales prices (net of VAT) for the three months ended 31 March 2010 and 2009:

	Three months ended 31 March:		**Change**
Russian roubles per mcm	**2010**	**2009**	**%**
Average natural gas price [(1)]:			
End-customers	*2,304*	*1,799*	*28.1%*
Traders in remote points	-	-	*n/a*
Average natural gas price to end-customers	**2,304**	**1,799**	**28.1%**
Average natural gas transportation expense:			
End-customers	*(1,099)*	*(713)*	*54.1%*
Traders in remote points	-	-	*n/a*
Average natural gas transportation expense for sales to end-customers	**(1,099)**	**(713)**	**54.1%**
Average natural gas netback price:			
End-customers	*1,205*	*1,086*	*11.0%*
Traders in remote points	-	-	*n/a*
Average natural gas netback price on end-customer sales	**1,205**	**1,086**	**11.0%**
Average natural gas price ex-field (wholesale traders)	**1,211**	**984**	**23.1%**
Total average natural gas price excluding transportation expense	**1,207**	**1,039**	**16.2%**

[(1)] Includes cost of transportation.

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

Crude oil, stable gas condensate, liquefied petroleum gas ("LPG") and oil products prices on international markets have historically been volatile depending on, among other things, the balance between supply and demand fundamentals, the ability and willingness of oil producing countries to sustain or change production levels to meet changes in global demand and potential disruptions in global crude oil supplies due to war, geopolitical developments, terrorist activities or natural disasters. Crude oil, stable gas condensate, LPG and oil products prices on the domestic market also fluctuate depending on supply and demand fundamentals amongst other factors. Crude oil that we sell bound for international markets is transported through the Transneft pipeline system where it is blended with other crude oil of varying qualities to produce an export blend commonly referred to as "Urals blend", which normally (or historically) trades at a discount to the international benchmark Brent crude oil. The actual prices we receive for our liquid hydrocarbons on both the domestic and international markets are dependent on many external factors beyond the control of management.

Volatile movements in benchmark crude oil prices can have a positive and/or negative impact on the ultimate prices we receive for our liquid volumes sold on both the domestic and international markets, amongst many other factors. In the three months ended 31 March 2010, the average benchmark crude oil prices were more than 70% higher than in the corresponding period in 2009.

Our stable gas condensate, LPG (excluding obligatory domestic deliveries at regulated prices), crude oil and oil products prices on both international and domestic markets include transportation expense in accordance with the specific terms of delivery.

In the three months ended 31 March 2010, our stable gas condensate export delivery terms were delivery to the port of destination ex-ship (DES) or priced at cost and freight (CFR), while in the corresponding period in 2009 our delivery terms were DES. Our average export stable gas condensate contract price, including export duties, in the three months ended 31 March 2010 was approximately USD 667 per ton compared to approximately USD 308 per ton in the corresponding period in 2009.

In the three months ended 31 March 2010, our crude oil export delivery terms were delivery at frontier (DAF Feneshlitke, Hungary), while in the corresponding period in 2009 our delivery terms were DAF Adamova Zastava, Germany. Our average crude oil export contract price, including export duties, was approximately USD 535 per ton compared to USD 304 per ton in the 2009 period.

In the three months ended 31 March 2010, we purchased four thousand tons of crude oil from third parties at an average price of RR 5,466 per ton and resold these volumes in the domestic market.

The following table shows our average realized stable gas condensate and crude oil sales prices (net of VAT and export duties, where applicable) for the three months ended 31 March 2010 and 2009 (prices in US dollars were translated from Russian roubles using the average exchange rate for the period):

Russian roubles (RR) or US dollars (USD) per ton	**Three months ended 31 March: 2010**	**2009**	**Change %**
Stable gas condensate			
Net export price, RR per ton	11,973	6,787	76.4%
Net export price, USD per ton	400.6	200.0	100.3%
Domestic price, RR per ton	8,475	6,189	36.9%
Crude oil			
Net export price, RR per ton	8,016	6,412	25.0%
Net export price, USD per ton	268.2	189.0	41.9%
Domestic price, RR per ton	6,843	3,668	86.6%

Our LPG export delivery terms during the three months ended 31 March 2010, were delivery at frontier (DAF) at the border of the customer's country, carriage paid to (CPT) the Port of Temryuk, southern Russia, and priced free carrier (FCA) the terminal points in Poland, compared to delivery terms of DAF (at the border of the customer's country) and CPT (the Port of Temryuk) in the corresponding period in 2009. In the three months ended 31 March 2010, our average export LPG contract price, including export duties, was approximately USD 637 per ton compared to USD 312 per ton in the corresponding period in 2009. In the three months ended 31 March 2010, we had no sales of LPG to CIS markets. In the three months ended 31 March 2009, our LPG CIS delivery terms were DAF at the border of the customer's country.

We were obliged to sell a portion of our LPG sales volumes on the domestic market at regulated prices and in the three months ended 31 March 2010, we sold a total of 11 thousand tons at the regulated price of RR 5,750 per ton in January and RR 6,613 per ton in February and March. In the 2009 period, we were not obliged to sell LPG volumes at regulated prices. The remaining portion of our LPG sales are under commercial terms on the domestic market and in the three months ended 31 March 2010, we sold 101 thousand tons at an average commercial price of RR 10,718 per ton compared to 74 thousand tons at an average commercial price of RR 5,236 per ton in the corresponding period in 2009. In addition, in the 2010 period, we sold 9 thousand tons of LPG produced at the Purovsky Plant through our wholly-owned subsidiary OOO "NOVATEK-Refuelling Complexes" at an average price of RR 11,570 per ton.

Domestic sales of oil products produced from our unstable gas condensate were priced free carrier (FCA) at the Surgut railroad station (located in the Khanty-Mansiysk Autonomous Region).

In the three months ended 31 March 2010, our wholly-owned subsidiary, OOO "NOVATEK-Refuelling Complexes" purchased 849 tons of diesel fuel and petrol from third parties and subsequently resold 790 tons through its retail stations for approximately RR 22,414 per ton. In the corresponding period in 2009, we purchased 239 tons of liquefied petroleum gas, diesel fuel and petrol, from third parties, and subsequently resold 199 tons of these volumes for approximately RR 17,579 per ton.

The following table shows our average realized liquefied petroleum gas and oil products sales prices excluding trading activities with oil products (net of VAT and export duties, where applicable) for the three months ended 31 March 2010 and 2009 (prices in US dollars were translated from Russian roubles using the average exchange rate for the period):

Russian roubles (RR) or US dollars (USD) per ton	**Three months ended 31 March: 2010**	**2009**	**Change %**
LPG			
Net export price, RR per ton	17,128	10,504	63.1%
Net export price, USD per ton	573.0	309.6	85.1%
CIS price, RR per ton	-	8,644	n/a
Domestic price, RR per ton	10,283	5,236	96.4%
Domestic price (retail and small wholesale stations), RR per ton	11,570	-	n/a
Oil products			
Net export price, RR per ton	-	9,498	n/a
Net export price, USD per ton	-	279.9	n/a
Domestic price, RR per ton	7,522	4,495	67.3%

Transportation tariffs

The methodology of calculating transportation tariffs for natural gas produced in the Russian Federation for shipments to consumers located within the customs territory of the Russian Federation and the member states of the Customs Union Agreement (Belarus, Kazakhstan, Kyrgyzstan and Tajikistan) consists of two parts: a rate for the utilization of the trunk pipeline and a transportation rate per mcm per 100 kilometers (km). The rate for utilization of the trunk pipeline is based on an "input/output" function, which is determined by where natural gas enters and exits the trunk pipeline and includes a constant rate for end-customers using Gazprom's gas distribution systems. The constant rate is deducted from the utilization rate for end-customers using non-Gazprom gas distribution systems.

In December 2008, the FTS approved four quarterly increases in the transportation tariff for natural gas in 2009 for an average total increase of 15.7% for the year, in line with the increases in natural gas prices.

In December 2009, the FTS approved a 12.3% average increase for the 2010 transportation tariff for natural gas effective 1 January 2010. The increase is applicable to both the rate for utilization of the trunk pipeline and transportation rate per mcm per 100 km, the former had a range of RR 29.21 to RR 1,630.97 (excluding VAT) per mcm and the latter was RR 9.15 (excluding VAT) per mcm per 100 km, as at 31 December 2009. Effective from 1 January 2010, the rate for utilization of the trunk pipeline has a range of RR 32.92 to RR 1,818.37 (excluding VAT) per mcm and a transportation rate of RR 10.27 (excluding VAT) per mcm per 100 km. The increases in regulated transportation tariffs are passed on to our end-customers pursuant to delivery terms in the majority of our contracts.

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

Our stable gas condensate (to the Port of Vitino on the White Sea), LPG and oil products are transported by rail which is owned and operated by Russian Railways, Russia's state-owned monopoly railway operator. Our transportation tariffs for transport by rail are also set by the FTS and vary depending on product and length of transport route. On 27 March 2009, the FTS announced specific discount co-efficients to be applied to the existing rail road transportation tariffs related to export deliveries of LPG and stable gas condensate shipped from the Limbey rail station, located in close proximity to our Purovsky Plant. We applied a co-efficient of 0.72 to the existing rail tariff for our stable gas condensate volumes shipped to export markets from 7 April 2009 and a co-efficient of 0.35 for our LPG export deliveries at the Russian Federation cross-border points for volumes in excess of 90 thousand tons which we reached in the middle of April 2009. The specific discount co-efficients remained in effect throughout 2009.

In January 2010, the FTS approved the discount co-efficients to existing rail road transportation tariffs related to export deliveries of LPG and stable gas condensate shipped from the Limbey rail station. The discount co-efficient for stable gas condensate is set at 0.89 for with annual shipped volumes of more than 2,235 thousand tons and the discount co-efficient for LPG is set at 0.35 for export volumes in excess of 105 thousand tons which we reached in the middle of April 2010. The discount co-efficients will remain in effect throughout 2010.

We deliver our stable gas condensate and oil products produced from our unstable gas condensate to international markets using the loading and storage facilities at the Port of Vitino on the White Sea and tankers for transportation to US, European and countries of the Asian-Pacific region. The costs associated with tanker transportation are determined by the distance to the final destination, tanker availability, seasonality of deliveries and standard shipping terms.

Transportation transactions with related parties

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

Our tax burden

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

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

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

OPERATIONAL HIGHLIGHTS

Hydrocarbon sales volumes

Our natural gas sales volumes increased primarily due to an increase in our production. Liquids sales volumes increased due to an increase in our unstable gas condensate production that was partially offset by an increase in liquids inventory balances.

Natural gas sales volumes

millions of cubic meters	Three months ended 31 March: 2010	2009	Change %
Production from:			
Yurkharovskoye field	5,578	4,213	32.4%
East-Tarkosalinskoye field	3,394	3,132	8.4%
Khancheyskoye field	855	824	3.8%
Other fields	20	4	400.0%
Total natural gas production	**9,847**	**8,173**	**20.5%**
Purchases from:			
Third parties	-	290	n/a
Total natural gas purchases	**-**	**290**	**n/a**
Total production and purchases	**9,847**	**8,463**	**16.4%**
Purovsky Plant and own usage	(13)	(13)	0.0%
Decrease (increase) in UGSF, UGSS and own pipeline infrastructure	272	113	140.7%
Total natural gas sales volumes	**10,106**	**8,563**	**18.0%**
Sold to end-customers	*6,110*	*4,596*	*32.9%*
Sold ex-field	*3,996*	*3,967*	*0.7%*

In the three months ended 31 March 2010, our total consolidated natural gas production increased by 1,674 mmcm, or 20.5%, compared to the 2009 period primarily due to an increase in production at our Yurkharovskoye field resulting from the launch of the second stage of the field's second phase of development in October 2009. The increase in natural gas production at the East-Tarkosalinskoye and Khancheyskoye fields was due to increased demand in the 2010 period resulting in greater utilization of these fields' production capacity. In the 2009 period, we optimized oil and gas revenues through the management of our fields' operational and production flexibility resulting in a reduction in natural gas production at the East-Tarkosalinskoye and Khancheyskoye fields enabling us to grow natural gas production at the Yurkharovskoye field, thus increasing unstable gas condensate production. The reduction in production during the 2009 period was largely due to low demand from end-customers.

In the three months ended 31 March 2010, we did not purchase natural gas from third parties due to our ability to meet domestic market demand from our own production.

Liquids sales volumes

thousands of tons	Three months ended 31 March: 2010	2009	Change %
Production from:			
Yurkharovskoye field	470	340	38.2%
East-Tarkosalinskoye field	217	219	(0.9%)
Khancheyskoye field	167	140	19.3%
Other fields	8	10	(20.0%)
Total liquids production	**862**	**709**	**21.6%**
Purchases from:			
Third parties	5	-	n/a
Total liquids purchases	**5**	**-**	**n/a**
Total production and purchases	**867**	**709**	**22.3%**
Losses and own usage [(1)]	(12)	(4)	200.0%
Decreases (increases) in liquids inventory balances	(171)	(97)	76.3%
Total liquids sales volumes	**684**	**608**	**12.5%**
Stable gas condensate export	*412*	*346*	*19.1%*
Stable gas condensate domestic	*0*	*47*	*(100.0%)*
Subtotal stable gas condensate	***412***	***393***	***4.8%***
LPG export	*104*	*77*	*35.1%*
LPG CIS	*-*	*5*	*n/a*
LPG domestic	*112*	*74*	*51.4%*
LPG sold through domestic retail and small wholesale stations	*9*	*-*	*n/a*
Subtotal LPG	***225***	***156***	***44.2%***
Crude oil export	*21*	*15*	*40.0%*
Crude oil domestic	*23*	*41*	*(43.9%)*
Subtotal crude oil	***44***	***56***	***(21.4%)***
Oil products export	*-*	*1*	*n/a*
Oil products domestic	*3*	*2*	*50.0%*
Subtotal oil products	***3***	***3***	***0.0%***

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

In the three months ended 31 March 2010, our liquids production increased by 153 thousand tons, or 21.6%, to 862 thousand tons compared to 709 thousand tons in the 2009 period, due primarily to the expansion of unstable gas condensate production capacity at our Yurkharovskoye field resulting from the launch of the second stage of the field's second phase of development in October 2009. The increase in liquids production at the Khancheyskoye field by 27 thousand tons, or 19.3%, was primarily due to a reduction in its natural gas production in the 2009 period (see "Natural gas sales volumes" above). The increases were partially offset by a decrease in crude oil production at our Ust-Purpeisky license area due to its disposal in April 2009.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED 31 MARCH 2010 COMPARED TO THE CORRESPONDING PERIOD IN 2009

The following table and discussion is a summary of our consolidated results of operations for the three months ended 31 March 2010 and 2009. Each line item is also shown as a percentage of our total revenues.

	Three months ended 31 March:			
Millions of Russian roubles	**2010**	**% of total revenues**	**2009**	**% of total revenues**
Total revenues (net of VAT and export duties)	**27,742**	***100.0%***	**16,981**	***100.0%***
including:				
natural gas sales	18,914	*68.2%*	12,171	*71.7%*
liquids sales	8,323	*30.0%*	4,145	*24.4%*
Operating expenses	(15,947)	*(57.5%)*	(11,379)	*(67.0%)*
Other operating income (loss)	1,578	*5.7%*	57	*0.3%*
Profit from operations	**13,373**	***48.2%***	**5,659**	***33.3%***
Finance income (expense)	612	*2.2%*	(2,908)	*(17.1%)*
Share of income (loss) of associated companies	(1)	*0.0%*	(16)	*(0.1%)*
Profit before income tax	**13,984**	***50.4%***	**2,735**	***16.1%***
Total income tax expense	(2,908)	*(10.5%)*	(596)	*(3.5%)*
Profit (loss)	**11,076**	***39.9%***	**2,139**	***12.6%***
Non-controlling interest	106	*0.4%*	(5)	*(0.0%)*
Profit attributable to NOVATEK shareholders	**11,182**	***40.3%***	**2,134**	***12.6%***

Total revenues

The following table sets forth our sales (net of VAT and export duties, where applicable) for the three months ended 31 March 2010 and 2009:

Millions of Russian roubles	Three months ended 31 March: 2010	2009	Change %
Natural gas sales	**18,914**	**12,171**	**55.4%**
End-customers	*14,075*	*8,268*	*70.2%*
Ex-field sales	*4,839*	*3,903*	*24.0%*
Stable gas condensate sales	**4,933**	**2,641**	**86.8 %**
Export	*4,932*	*2,350*	*109.9%*
Domestic	*1*	*291*	*(99.7%)*
Liquefied petroleum gas sales	**3,032**	**1,238**	**144.9%**
Export	*1,779*	*807*	*120.4%*
CIS	*-*	*44*	*n/a*
Domestic	*1,253*	*387*	*223.8%*
Crude oil sales	**325**	**243**	**33.7%**
Export	*167*	*93*	*79.6%*
Domestic	*158*	*150*	*5.3%*
Oil products sales	**33**	**23**	**43.5%**
Export	*-*	*10*	*n/a*
Domestic	*33*	*13*	*153.8%*
Total oil and gas sales	**27,237**	**16,316**	**66.9%**
Sales of polymer and insulation tape	469	397	18.1%
Other revenues	36	268	(86.6%)
Total revenues	**27,742**	**16,981**	**63.4%**

Natural gas sales

In the three months ended 31 March 2010, our revenues from sales of natural gas increased by RR 6,743 million, or 55.4%, compared to the corresponding period in 2009 largely due to an increase in natural gas prices and, to a lesser extent, an increase in sales volumes. Revenues from the sale of natural gas accounted for 68.2% and 71.7% of our total revenues in the three months ended 31 March 2010 and 2009, respectively. The decrease in natural gas sales as a percentage of total revenues was primarily due to significant increase in liquids prices.

In the three months ended 31 March 2010, our average realized natural gas price per mcm increased by RR 450 per mcm, or 31.7%, to RR 1,871 per mcm from RR 1,421 per mcm in the corresponding period in 2009. Our proportion of natural gas sold to end-customers to total natural gas sales volumes, increased from 53.7% in the reporting period in 2009 to 60.5% in the three months ended 31 March 2010 primarily due to addition of new long-term supply agreements to end-customers in the power generation sector. The average realized prices of our natural gas sold directly to end-customers (including transportation expense) and sold ex-field were higher by 28.1% and 23.1%, respectively, in the three months ended 31 March 2010 compared to the same period in 2009. In the three months ended 31 March 2010, our sales of natural gas to end-customers were primarily to energy utility companies and large industrial companies compared to deliveries to energy utility companies and regional gas distribution companies in the corresponding period in 2009.

Stable gas condensate sales

In the three months ended 31 March 2010, our revenues from sales of stable gas condensate increased by RR 2,292 million, or 86.8%, compared to the corresponding period in 2009 due to higher average realized prices resulting from an increase in benchmark crude oil prices.

In the three months ended 31 March 2010, our total stable gas condensate sales volumes increased by 19 thousand tons, or 4.8%, due to an increase in our unstable gas condensate production that was partially offset by an increase in stable gas condensate inventory balances. In the three months ended 31 March 2010, we sold 412 thousand tons of stable gas condensate, of which approximately 99.9% of our total sales volumes were exported to the United States and Europe. In the three months ended 31 March 2009, we exported 346 thousand tons of stable gas condensate, or 88.0% of our total sales volumes, to markets in the United States and the remaining 47 thousand tons were sold domestically.

We delivered our stable gas condensate to international markets using the loading and storage facilities at the Port of Vitino on the White Sea and via leased tankers.

In the three months ended 31 March 2010, our average realized price, excluding export duties, for stable gas condensate sold on the export market increased by USD 200.6 per ton, or 100.3%, to USD 400.6 per ton (DES and CFR) from USD 200.0 per ton (DES) in the 2009 period due to a 116.6% increase in our average export contract price that was partially offset by a 109.6% increase in our average export duty per ton. The increase in our average realized contract price was due to an overall increase in crude oil and related commodity prices on international markets in the 2010 period compared to the corresponding period in 2009.

Liquefied petroleum gas sales

In the three months ended 31 March 2010, our revenues from the sales of LPG increased by RR 1,794 million, or 144.9%, compared to the corresponding period in 2009, primarily due to an increase in our average realized prices and, to a lesser extent, an increase in volumes sold. In the three months ended 31 March 2010, our total LPG sales volumes increased by 69 thousand tons, or 44.2%, to 225 thousand tons from 156 thousand tons in the corresponding period in 2009.

In the three months ended 31 March 2010, we sold 104 thousand tons of LPG, or 46.2% of our total LPG sales volumes, to the export markets for an average price of USD 573.0 per ton (DAF, CPT and FCA excluding export duties), representing an increase of USD 263.4 per ton, or 85.1%, compared to the corresponding period in 2009. The increase in our average realized export prices (excluding export duties) was primarily due to a 104.2% increase in our average contract price that was partially offset by an increase in our average export duty per ton resulting from the cancellation of the zero export duty rate from 1 December 2009 (for export duty zero rate for LPG was effective from January to December 2009).

The remaining volumes of LPG were sold domestically at an average price of RR 10,379 per ton (FCA, excluding VAT) representing an increase of RR 5,143 per ton, or 98.2%, compared to the 2009 period.

In the three months ended 31 March 2009, we sold 49.4% of our LPG volumes to the export markets, 47.4% was sold domestically, and 3.2% to markets in the CIS.

Crude oil sales

In the three months ended 31 March 2010, our revenues from the sales of crude oil increased by RR 82 million, or 33.7%, compared to the 2009 period, due to an increase in our average realized prices that was partially offset by a decrease in our sales volumes.

In the three months ended 31 March 2010, our crude oil sales volumes decreased by 12 thousand tons, or 21.4%, to 44 thousand tons from 56 thousand tons in the corresponding period in 2009 due to an inventory balance increase, as well as a decrease in crude oil production. In the three months ended 31 March 2010, 52.3% of our crude oil volumes were sold domestically at an average price of RR 6,843 per ton (excluding VAT) representing an increase of RR 3,175 per ton, or 86.6%, compared to the corresponding period in 2009. The increase in our average realized price was due to the overall increase in crude oil prices in the domestic market in the 2010 period. The remaining 47.7% of our crude oil volumes were sold to the export markets at an average price of USD 268.2 per ton (DAF, excluding export duties) representing an increase of USD 79.2 per ton, or 41.9%, compared to the 2009 period. The increase in the average realized export price (excluding export duties) was the result of a 76.0% increase in our average export contract price that was partially offset by a 127.8% increase in our average export duty per ton. The increase in our average realized contract price was due to an overall increase in crude oil and related commodity prices on international markets in the 2010 period compared to the corresponding period in 2009.

Oil products sales

In the three months ended 31 March 2010, our revenue from the sales of oil products increased by RR 10 million, or 43.5%, compared to the 2009 period, primarily due to an increase in our average realized prices.

In the three months ended 31 March 2010, we had no deliveries of oil products to export markets, while in the corresponding period in 2009 we sold one thousand tons of oil products (light distillate) produced from our unstable gas condensate to the international market through our foreign trading subsidiary at an average realized price, excluding export duties, of USD 279.9 per ton (FOB Vitino).

In the three months ended 31 March 2010, our revenues from oil products produced at the Surgutsky refinery increased to RR 16 million from RR 10 million in the 2009 period. Oil products sales volumes produced from our unstable gas condensate amounted to two thousand tons in both periods. Our average oil products sales price increased by RR 3,027 per ton, or 67.3%, to RR 7,522 per ton in the 2010 period from RR 4,495 per ton in the corresponding period in 2009 primarily due to an overall increase in oil products prices in the domestic market in the 2010 period.

In the three months ended 31 March 2010, our revenues from oil products trading operations sold through our retail stations on the domestic market amounted to RR 18 million compared to RR three million in the corresponding period in 2009. In the three months ended 31 March 2010, we sold approximately one thousand tons of oil products (diesel fuel and petrol) for an average price of RR 22,414 per ton through our retail stations compared to 199 tons of oil products for an average price of RR 17,579 per ton in the corresponding period in 2009.

Sales of polymer and insulation tape

Our revenues from the sales of polymer and insulation tape increased by RR 72 million, or 18.1%, to RR 469 million in the three months ended 31 March 2010 compared to RR 397 million in the 2009 period due to an increase in both polymer products production volumes and average realized prices.

Revenues from our sales of BOPP film wrap increased by RR 69 million, or 27.6%, from RR 250 million in the three months ended 31 March 2009 to RR 319 million in the 2010 period due to low demand in the 2009 period. The proportion of BOPP film wrap sales to total sales of polymer and insulation tape increased by 5.0% to 68.0% in the three months ended 31 March 2010 compared to 63.0% in the 2009 period.

Our revenues from pipe insulation product sales increased by RR 15 million, or 12.5%, from RR 120 million in the 2009 period to RR 135 million in the three months ended 31 March 2010 due to an increase in volumes sold. Revenues from polymer pipes sales decreased by RR 7 million, or 35.0%, from RR 20 million in the 2009 period to RR 13 million in the 2010 period due to a decrease in volumes sold. The remaining RR 2 million and RR 7 million in the three months ended 31 March 2010 and 2009, respectively, related to sales of other polymer products.

Other revenues

Other revenues include geological and geophysical research services, rent and other services sales. In the three months ended 31 March 2010, other revenues decreased by RR 232 million, or 86.6%, to RR 36 million from RR 268 million in the corresponding period in 2009. The decrease in other revenues was primarily related to a RR 236 million, or 100.0%, decrease in revenues from geological and geophysical research services provided to our associates. The decrease was due to the February 2010 acquisition of a controlling interest in our associated companies and the subsequent consolidation of their activities and elimination of intercompany operations. The remaining increase of RR 4 million in other revenues was composed of various immaterial items.

Operating expenses

In the three months ended 31 March 2009, our total operating expenses increased by RR 4,568 million, or 40.1%, to RR 15,947 million compared to RR 11,379 million in the 2009 period, largely due to an increase in transportation expenses. As a percentage of total operating expenses, our non-controllable expenses, such as transportation and taxes other than income tax, increased by 8.8% in the three months ended 31 March 2010 to 72.0% compared to 63.2% in the corresponding period in 2009. Total operating expenses decreased as a percentage of total revenues to 57.5% in the three months ended 31 March 2010 compared to 67.0% in the corresponding period in 2009, as shown in the table below. The decrease in our operating expenses as a percent of total revenues was primarily due to an increase in our natural gas prices and sales volumes, as well as an increase in liquids prices.

	Three months ended 31 March:			
millions of Russian roubles	**2010**	**% of total revenues**	**2009**	**% of total revenues**
Transportation expenses	9,063	*32.7%*	5,273	*31.1%*
Taxes other than income tax	2,424	*8.7%*	1,921	*11.3%*
Subtotal non-controllable expenses	**11,487**	***41.4%***	**7,194**	***42.4%***
Depreciation, depletion and amortization	1,602	*5.8%*	1,182	*7.0%*
Materials, services and other	1,548	*5.6%*	1,492	*8.8%*
General and administrative expenses	1,463	*5.3%*	1,100	*6.5%*
Exploration expenses	131	*0.5%*	99	*0.6%*
Purchases of natural gas and liquid hydrocarbons	38	*0.1%*	293	*1.7%*
Net impairment expense (reversal)	26	*n/m*	(1)	*n/m*
Change in natural gas, liquid hydrocarbons, and polymer products and work-in-progress	(348)	*n/m*	20	*n/m*
Total operating expenses	**15,947**	***57.5%***	**11,379**	***67.0%***

Non-controllable expenses

A significant proportion of our operating expenses are characterized as non-controllable expenses since we are unable to influence the increase in regulated tariffs for transportation of our hydrocarbons or the rates imposed by federal, regional or local tax authorities. In the three months ended 31 March 2010, non-controllable expenses of transportation and taxes other than income tax increased by RR 4,293 million, or 59.7%, to RR 11,487 million from RR 7,194 million in the corresponding period in 2009. The change in transportation expenses was primarily due to an increase in the natural gas transportation tariff and volumes delivered to end-customers. Taxes other than income tax increased primarily due to higher unified natural resources production tax expense for natural gas. As a percentage of total revenues our non-controllable expenses decreased by 1.0% to 41.4% in the three months ended 31 March 2010 compared to 42.4% in the corresponding period in 2009.

Transportation expenses

In the three months ended 31 March 2010, our total transportation expenses increased by RR 3,790 million, or 71.9%, compared to the corresponding period in 2009.

	Three months ended 31 March:		Change
millions of Russian roubles	**2010**	**2009**	**%**
Natural gas transportation to customers	6,712	3,277	104.8%
Stable gas condensate, liquefied petroleum gas and oil products transportation by rail	1,628	1,332	22.2%
Stable gas condensate transported by tankers	551	547	0.7%
Unstable gas condensate transportation from the fields to the processing facilities through third party pipelines	119	78	52.6%
Crude oil transportation to customers	48	37	29.7%
Other transportation costs	5	2	150.0%
Total transportation expenses	**9,063**	**5,273**	**71.9%**

In the three months ended 31 March 2010, our transportation expenses for natural gas increased by RR 3,435 million, or 104.8%, to RR 6,712 million from RR 3,277 million in the corresponding period in 2009. The increase was due to a 32.9% increase in our sales volumes of natural gas delivered directly to end-customers, where the cost of transportation is included in the sales price, as well as increases in the natural gas transportation tariff (see “Transportation tariffs” above) and, to a lesser extent, deliveries to more distant regions from our fields compared to the period in 2009. Our average transportation distance for natural gas sold to end-customers fluctuates period-to-period and depends on the location of end-customers and the specific routes of transportation.

Total expenses for transportation by rail increased by RR 296 million, or 22.2%, primarily due to higher liquids volumes sold. In the three months ended 31 March 2010, our combined volumes of stable gas condensate, LPG and oil products sold and transported via rail increased by 75 thousand tons, or 13.6%, to 626 thousand tons from 551 thousand tons in the corresponding period in 2009.

Our expense for stable gas condensate transported by rail to export markets increased by RR 143 million, or 24.2% to RR 733 million from RR 590 million in the three months ended 31 March 2009 due to a 19.1% increase in volumes sold. In the three months ended 31 March 2010, our average transportation rate per ton for stable gas condensate transported by rail to export markets increased by 4.5% to RR 1,781 from RR 1,704 in the corresponding period in 2009, primarily due to increases in rail tariffs by 5.7% effective 1 July 2009 and by a further 9.4% effective 1 January 2010. The increases in the rail tariff were partially offset by the application of a co-efficient of 0.89 to the existing rail tariff for SGC deliveries to export markets from February 2010 compared to co-efficient of 0.72 applicable from 7 April 2009 (see “Transportation tariffs” above).

In the three months ended 31 March 2010, our expense for LPG transported by rail increased by RR 220 million, or 32.8%, primarily due to an increase in volumes sold. In the three months ended 31 March 2010, our expense for LPG transported by rail amounted to RR 890 million, of which RR 591 million was related to export sales and RR 299 million to domestic sales, or RR 5,691 per ton and RR 2,729 per ton, respectively. In the three months ended 31 March 2009, transportation expenses for LPG transported by rail amounted to RR 670 million, of which RR 471 million was related to export sales, RR 16 million to CIS sales, and RR 183 million to domestic sales, or RR 6,127 per ton, RR 3,203 per ton and RR 2,479 per ton, respectively. We began applying a co-efficient of 0.35 to the existing rail tariff for LPG export deliveries at the cross-border points of the Russian Federation for volumes in excess of 105 thousand tons in 2010 and 90 thousand tons in 2009 which we reached in the middle of April in both years (see “Transportation tariffs” above).

In the three months ended 31 March 2010, we incurred RR 0.3 million of railroad transportation expenses related to the domestic sales of stable gas condensate compared to RR 68 million in the 2009 period. The remaining RR 5 and RR 4 million of transportation expenses by rail in the 2010 and 2009 periods, respectively, were related to the transportation of oil products sold on the domestic market and other railroad services not allocated between products.

Total transportation expense for delivery of stable gas condensate by tanker to international markets increased by RR 4 million, or 0.7%, to RR 551 million in 2010 from RR 547 million in the 2009 period. The change was primarily due to a 19.1% increase in volumes sold that was partially offset by a decrease in average freight rates. In the three months ended 31 March 2010, we delivered 85.4% of our stable gas condensate export volumes to United States markets compared to 100.0% in the 2009 period.

Taxes other than income tax

millions of Russian roubles	**Three months ended 31 March: 2010**	**2009**	**Change %**
Unified natural resources production tax (UPT)	2,018	1,635	23.4%
Property tax	336	255	31.8%
Other taxes	70	31	125.8%
Total taxes other than income tax	**2,424**	**1,921**	**26.2%**

In the three months ended 31 March 2010, taxes other than income tax increased by RR 503 million, or 26.2%, primarily due to an increase in unified natural resources production tax expense.

In the three months ended 31 March 2010, our UPT for natural gas and gas condensate increased by RR 246 million, or 20.5%, and RR 91 million, or 25.2%, respectively, due to an increase in our production volumes. The increase in our UPT for crude oil of RR 46 million was due to an increase in our average crude oil production tax rate, which is linked to the Urals benchmark crude oil price, which was partially offset by a decrease in our crude oil production. Our average UPT rate for crude oil increased from RR 1,527 per ton in the three months ended 31 March 2009 to RR 2,878 per ton in the 2010 period. The natural gas production tax rate in the 2010 and 2009 periods remained unchanged at RR 147 per mcm.

In the three months ended 31 March 2010, our property tax expense increased by RR 81 million, or 31.8%, to RR 336 million from RR 255 million in the corresponding period in 2009, primarily due to additions of property, plant and equipment (PPE) at our production subsidiaries.

In the three months ended 31 March 2010, other taxes increased by RR 39 million, or 125.8%, primarily due to excise tax and fuel tax payments at the custom border of Poland in case of our LPG export sales through our wholly-owned subsidiary Novatek Polska.

Depreciation, depletion and amortization

In the three months ended 31 March 2010, our depreciation, depletion and amortization ("DDA") expense increased by RR 420 million, or 35.5%, compared to the corresponding period in 2009 primarily due to an increase in depreciation and depletion of our oil and gas properties accrued using the "units of production" method by RR 387 million, or 38.1%, as a result of an increase in our depletable cost base as well as a 20.8% increase in our hydrocarbon production in barrels of oil equivalent (boe).

In the three months ended 31 March 2010, our DDA per boe was RR 19.6 compared to RR 17.1 in the corresponding period in 2009. The increase in our DDA charge calculated on a boe basis was primarily due to an increase in our depletable cost base as a result of completing the capital expansion program related to the second stage of the second phase of development at the Yurkharovskoye field in October 2009.

Our reserve base used as the denominator in the calculation of the DDA charge under the "units of production" method is only appraised on an annual basis and does not fluctuate during the year, whereas our depletable cost base does change each quarter due to the ongoing capitalization of our costs throughout the year.

Materials, services and other

In the three months ended 31 March 2010, our materials, services and other expenses increased by RR 56 million, or 3.8%, to RR 1,548 million compared to RR 1,492 million in the 2009 period. The main components of this expense were employee compensation and materials and supplies, which comprised 41.5% and 23.3%, respectively, of total materials, services and other expenses in the 2010 period.

millions of Russian roubles	**Three months ended 31 March: 2010**	**2009**	**Change %**
Employee compensation	642	612	4.9%
Materials and supplies	361	234	54.3%
Tolling and processing fees	204	122	67.2%
Repair and maintenance services	124	129	(3.9%)
Electricity and fuel	98	86	14.0%
Fire safety and security expense	40	46	(13.0%)
Other	78	42	85.7%
Subtotal materials, services and other	**1,547**	**1,271**	**21.7%**
Operator services expense	1	221	(99.5%)
Total materials, services and other	**1,548**	**1,492**	**3.8%**

In the three months ended 31 March 2010, our materials, services and other expenses, excluding operator services expense, increased by RR 276 million, or 21.7%, to RR 1,547 million compared to RR 1,271 million in the corresponding period in 2009.

Our employee compensation increased by RR 30 million, or 4.9%, to RR 642 million compared to RR 612 million in the 2009 period due primarily to an increase in the average number of employees by 6.4%. The increase in additional staffing was primarily due to the growth in activities at the Yurkharovskoye field and the acquisition of OAO “Yamal LNG” in the second quarter 2009.

Materials and supplies expense increased by RR 127 million, or 54.3%, mainly due to an increase in production of polymers and insulation tape products and the associated increase in purchases of raw materials, which accounted for RR 120 million, or 94.5%, of the total increase in materials and supplies expense.

Tolling and processing fees increased by RR 82 million, or 67.2%, primarily due to an increase in third party services related to de-ethanization of unstable gas condensate, which accounted for RR 54 million of the total increase in tolling and processing fees. The increase in de-ethanization costs was due to a 38.2% increase in volumes of unstable gas condensate produced at the Yurkharovskoye field. In addition, in the three months ended 31 March 2010, we incurred RR 27 million in costs related to the preparation of crude oil produced at our East-Tarkosalinskoye field for transportation. Tolling and processing fees at the Surgutsky refinery increased by RR 1 million.

Electricity and fuel expenses increased by RR 12 million, or 14.0%, from RR 86 million in the three months ended 31 March 2009 to RR 98 million in the 2010 period primarily due to an increase in energy consumption at OOO “NOVATEK-Polimer” resulting from an increase in polymer products production.

Our fire safety and security expenses decreased by RR 6 million, or 13.0%, to RR 40 million from RR 46 million in the three months ended 31 March 2009, primarily due to a reduction in fire safety services provided by third parties at our production subsidiary OOO “NOVATEK-Yurkharovneftegas”, which completed the organization of its own fire safety department at the end of 2009 to meet overall fire safety requirements as well as to optimize costs by providing these services in-house.

Operator services expenses mainly referre to the geological and geophysical research provided to our associated companies. In the three months ended 31 March 2010, operator services expenses decreased by RR 220 million, or 99.5%, due to the acquisition in February 2010 of additional an 26 percent participation interests in our associates OOO “Oiltechproduct-Invest”, OOO “Petra Invest-M” and OOO “Tailiksneftegas” and the subsequent consolidation of these companies activities.

General and administrative expenses

In the three months ended 31 March 2010, our general and administrative expenses increased by RR 363 million, or 33.0%, to RR 1,463 million compared to RR 1,100 million in the corresponding period in 2009. The main components of these expenses were employee compensation and charitable contributions, which, on aggregate, comprised 70.7% and 65.0% of total general and administrative expenses in the three months ended 31 March 2010 and 2009, respectively.

	Three months ended 31 March:		**Change**
millions of Russian roubles	**2010**	**2009**	**%**
Employee compensation	838	555	51.0%
Charitable contributions	196	160	22.5%
Legal, audit, and consulting services	86	54	59.3%
Rent expense	63	56	12.5%
Business trip expenses	45	24	87.5%
Fire safety and security expense	38	34	11.8%
Depreciation – administrative buildings	36	34	5.9%
Concession management services	35	95	(63.2%)
Insurance expense	19	17	11.8%
Other	107	71	50.7%
Total general and administrative expenses	**1,463**	**1,100**	**33.0%**

Our employee compensation increased by RR 283 million, or 51.0%, to RR 838 million in the three months ended 31 March 2010 as compared to RR 555 million in the corresponding period in 2009 primarily due to an increase by RR 219 million in the accrual of bonuses dependant on the Group’s financial results.

In the three months ended 31 March 2010, our charitable contributions increased by RR 36 million, or 22.5%, to RR 196 million compared to RR 160 million in the corresponding period in 2009, and were primarily related to our donations to sport clubs and activities as well as continued support for charities and social programs in the regions where we operate. Charitable contributions will continue to fluctuate period-on-period depending on the funding needs and the implementation schedule of specific programs we support.

Legal, audit, and consulting services expenses increased by RR 32 million, or 59.3%, to RR 86 million compared to RR 54 million in the 2009 period largely due to an increase in expenses on information technology system support and maintenance expense.

In the three months ended 31 March 2010, our rent expense increased by RR 7 million, or 12.5%, primarily due to an increase in rental rates for our Moscow office effective from July 2009.

Fire safety and security expenses increased by RR 4 million, or 11.8%, due to an increase in the service rates of security companies starting from 1 January 2010.

Concession management services represent administrative expenses incurred by Tharwa Petroleum Company S.A.E (the operator of the El Arish concession area located in Egypt). In the three months ended 31 March 2010, our expenses related to concession management services decreased by RR 60 million, or 63.2%, compared to the 2009 period. The lower level of concession management services in the 2010 period is in line with our business-plan.

In the three months ended 31 March 2010, other general and administrative expenses increased by RR 36 million, or 50.7%, compared to the corresponding period in 2009, of which an increase of RR 23 million related to bank guarantee services. The remaining increase of RR 13 million was allocated amongst different expense categories within other general and administrative expenses which, taken individually, increased immaterially.

Purchases of natural gas and liquid hydrocarbons

Purchases of natural gas and liquid hydrocarbons decreased by RR 255 million, or 87.0%, to RR 38 million in the three months ended 31 March 2010, from RR 293 million in the corresponding period in 2009, primarily due to a decrease in natural gas purchases from third parties by RR 290 million, or 100.0%. The decrease was partially offset by an increase in crude oil and oil products purchases by RR 35 million.

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

In the three months ended 31 March 2010, we recorded a reversal of RR 348 million to change in inventory expense as compared to a charge of RR 20 million in the corresponding period in 2009:

	Three months ended 31 March:	
millions of Russian roubles	**2010**	**2009**
Natural gas	110	42
Stable gas condensate	(395)	(136)
Polymer and insulation tape	(1)	91
Other	(62)	23
Increase (decrease) in operating expenses due to change in inventory balances	**(348)**	**20**

In the three months ended 31 March 2010, we recorded a charge to our operating expenses of RR 110 million due to a decrease in our natural gas inventory balance by 272 mmcm. Our volumes of natural gas injected into Gazprom’s underground gas storage facilities (UGSF) fluctuate period-to-period depending on market conditions, storage capacity constraints and our development plans to sustain and/or grow production during periods of seasonality.

In addition, in the three months ended 31 March 2010, we recorded a reversal of RR 395 million to our operating expenses due to an increase in our inventory balance of stable gas condensate in transit and storage by 166 thousand tons.

	2010			2009		
Inventory balances in transit or in storage	**At 1 January**	**At 31 March**	**Increase / (decrease)**	**At 1 January**	**At 31 March**	**Increase / (decrease)**
Natural gas (millions of cubic meters)	**744**	**472**	**(272)**	**372**	**259**	**(113)**
including Gazprom's UGSF	*584*	*405*	*(179)*	*300*	*137*	*(163)*
Liquid hydrocarbons (thousand tons)	**151**	**322**	**171**	**259**	**356**	**97**
including stable gas condensate	*111*	*277*	*166*	*220*	*313*	*93*

Other operating income (loss) and net gain (loss) on disposals

In the three months ended 31 March 2010, we realized RR 1,583 million of gain on disposal of 49 percent participation interest in our subsidiary ZAO "Terneftegas" to TOTAL Termokarstovoye B.V., which is represented by a net income on disposal of RR 776 million and a gain of RR 807 million due to revaluation to fair value of the remaining 51 percent participation interest. In the three months ended 31 March 2010, other other operating loss of RR 5 million was related to the disposals of fixed assets, equipment and materials.

In the three months ended 31 March 2009, we realized other operating income of RR 57 million, of which RR 22 million was related to commodity derivative instruments that did not qualify as hedge transactions under IAS 39, *Financial Instruments: Recognition and Measurement* ("IAS 39"); other income of RR 20 million was related to penalties from our equipment suppliers due to non-compliance of their contractual obligations, and the remaining RR 15 million of other operating income was related to the disposals of fixed assets, equipment and materials.

Profit from operations

As a result of the factors discussed above, our profit from operations increased by RR 7,714 million, or 136.3%, to RR 13,373 million in the three months ended 31 March 2010, compared to RR 5,659 million in the corresponding period in 2009. In the three months ended 31 March 2010, our profit from operations as a percentage of total revenues increased to 48.2% compared to 33.3% in the 2009 period due to higher natural gas and liquids prices and sales volumes that was partially offset by an increase in natural gas transportation expense.

Finance income (expense)

In the three months ended 31 March 2010, we recorded net finance income of RR 612 million which was due primarily to foreign exchange gains resulted from the strengthening of the Russian rouble relative to the US dollar compared to net finance expense of RR 2,908 million in the corresponding period in 2009 due to significant foreign exchange loss resulted from the devaluation of the Russian rouble relative to the US dollar.

In the three months ended 31 March 2010, our total accrued interest expense increased to RR 672 million compared to RR 352 million in the corresponding period in 2009 as a result of an increase in our average borrowings and higher average financing rates on Russian rouble denominated borrowings. During the 2010 and 2009 periods RR 523 and RR 289 million respectively were capitalized in cost of additions to property, plant and equipment in accordance with the Group's accounting policy.

In the three months ended 31 March 2010, interest income decreased by RR 65 million, or 36.1%, primarily due to a decrease in interest income received on funds held on account as bank deposits.

We recorded a net foreign exchange gain of RR 646 million as compared to a net loss RR 3,025 million in the 2009 period due to a 2.9% appreciation and 15.8% depreciation of the Russian rouble against the US dollar in the three months ended 31 March 2010 and 2009, respectively, and its effect on our foreign currency denominated borrowings.

Share of income (loss) of associated companies

In the three months ended 31 March 2010, our proportionate share in the loss of associated companies amounted to RR 1 million compared to a loss of RR 16 million recorded in the 2009 period. The loss recognized by our associated companies was due to the expensing of geological and geophysical research expenditures under the successful efforts accounting policy.

Income tax expense

Our overall consolidated effective income tax rates (total income tax expense calculated as a percentage of our reported IFRS profit before income tax) were 20.8% and 21.7% for the three months ended 31 March 2010 and 2009, respectively. Our effective income tax rate, after excluding the effect of foreign subsidiaries, was 21.4% and 21.8% in the 2010 and 2009 periods, respectively. The Russian statutory income tax rate for both periods was 20%. The difference between our effective and statutory income tax rates is primarily due to certain non-deductible expenses.

Profit attributable to shareholders and earnings per share

As a result of the factors discussed above, profit for the period increased by RR 8,937 million, or 417.8%, to RR 11,076 million in the three months ended 31 March 2010 from RR 2,139 million in the corresponding period in 2009. The profit attributable to NOVATEK shareholders increased by RR 9,048 million, or 424.0%, to RR 11,182 million in the three months ended 31 March 2010 from RR 2,134 million in the corresponding period in 2009.

Our weighted average basic and diluted earnings per share, calculated from the profit attributable to NOVATEK shareholders, increased by RR 2.99 per share, or 427.1%, to RR 3.69 per share in the 2010 period from RR 0.70 per share in corresponding period in 2009.

LIQUIDITY AND CAPITAL RESOURCES

The following table shows our net cash flows from operating, investing and financing activities for the three months ended 31 March 2010 and 2009:

millions of Russian roubles	Three months ended 31 March: 2010	2009	Change %
Net cash provided by operating activities	12,454	5,432	129.3%
Net cash used in investing activities	(6,467)	(3,977)	62.6%
Net cash used in financing activities	(4,895)	(83)	n/m

Liquidity ratios	31 March 2010	31 December 2009	Change, %
Current ratio	0.98	1.14	(14.0%)
Total debt to equity	0.27	0.33	(18.2%)
Long-term debt to long term debt and equity	0.11	0.17	(35.3%)
Net debt to total capitalization (1)	0.13	0.17	(23.5%)

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

Net cash provided by operating activities

In the three months ended 31 March 2010, our net cash provided by operating activities increased by RR 7,022 million, or 129.3%, to RR 12,454 million compared to RR 5,432 million in the corresponding period in 2009 due to the growth in natural gas and liquids prices and sales volumes.

Net cash used in investing activities

In the three months ended 31 March 2010, our net cash used in investing activities increased by RR 2,490 million, or 62.6%, to RR 6,467 million as compared to RR 3,977 million in the corresponding period in 2009. In the three months ended 31 March 2010, we spent RR 4,822 million for ongoing work at our Yurkharovskoye field compared to RR 1,912 million in the corresponding period in 2009. In addition, in the 2010 period, we paid RR 1,297 million for an additional 26 percent participation interest in our three associated companies and received RR 483 million in cash for the disposal of our 49 percent participation interest in ZAO “Terneftegas”.

Net cash used in financing activities

In the three months ended 31 March 2010, our net cash used in financing activities increased to RR 4,895 million from RR 83 million in the corresponding period in 2009 due to an increase in the repayment of long-term and short-term borrowings.

Working capital

Our net working capital position (current assets less current liabilities) at 31 March 2010 was a negative RR 674 million compared to a positive RR 3,274 million at 31 December 2009. The change in our net working capital position was mainly due to an increase in the current portion of our long-term debt, as well as a decrease in trade and other receivables that were partially offset by an increase in prepayments and other current assets. The decrease in our net working capital position resulted from the acquisition of our associated companies in the first quarter 2010 and an increase in capital expenditures. In April 2010, the Group repaid USD 114 million of the syndicated term-loan as scheduled.

The Group’s management believes that it has and will have the ability to generate sufficient cash flows (from operating and financing activities) to repay all current liabilities and finance the Company’s capital construction programs.

Capital expenditures

Total capital expenditures on property, plant and equipment for the three months ended 31 March 2010 and 2009 were as follows:

millions of Russian roubles	Three months ended 31 March: 2010	2009	Change %
Exploration, production and marketing	6,141	3,870	58.7%
Polymer production and marketing	89	1	n/m
Total	**6,230**	**3,871**	**60.9%**

Exploration, production and marketing expenditures represent our investments in exploring for and developing our oil and gas properties. During both reporting periods, the majority of our capital expenditures related to ongoing development and exploration activities at our three core fields and at our Purovsky Plant. In the three months ended 31 March 2010, we spent RR 5 million, RR 204 million and RR 4,822 million for further field development at the Khancheyskoye, East-Tarkosalinskoye and Yurkharovskoye fields, respectively, and RR 234 million on further construction work at the Purovsky Plant.

Debt obligations

At 31 March 2010, the Group had available funds under short-term credit lines with various international banks in the aggregate amount of RR 4,405 million (USD 150 million) on either fixed or variable interest rates subject to the specific type of credit facility.

In addition, the Group has available funds under two credit line facilities with UniCredit Bank up to the maximum amount of RR 2,936 million (USD 100 million) with interest rate negotiated at time of each withdrawal and of RR 5,873 million (USD 200 million) with interest rate LIBOR plus 4.65 percent until May 2010 and October 2012, respectively. However, total funds that can be withdrawn under these two credit line facilities cannot exceed the combined maximum amount of USD 250 million. In October 2009, the Group withdrew USD 200 million under these facilities as long-term borrowings at initial interest rate of LIBOR plus 6.5 percent, which was subsequently reduced to LIBOR plus 4.65 percent from 25 February 2010 (4.88 percent at 31 March 2010).

The Group also has funds available under an agreement with CALYON RUSBANK Corporate and Investment Bank in the amount of USD 100 million until June 2010 with the interest rate to be negotiated at the time of each withdrawal and with Gazprombank in the amount of RR 3,894 million until November 2012 with an annual interest rate of 9.5 percent.

Management believes it has sufficient internally generated cash flows as well as access to available external borrowings (both short- and long-term) to fund its capital expenditure program, service its existing debt and meet its current obligations as they become due.

QUALITATIVE AND QUANTITATIVE DISCLOSURES AND MARKET RISKS

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

Foreign currency risk

Our principal exchange rate risk involves changes in the value of the Russian rouble relative to the US dollar and Euro. As of 31 March 2010, RR 9,141 million, or 27.2%, of our long-term debt was denominated in US dollars (out of RR 33,613 million of our total borrowings at that date). Changes in the value of the Russian rouble relative to the US dollar will impact our foreign currency-denominated costs and expenses and our debt service obligations for foreign currency-denominated borrowings in Russian rouble terms as well as receivables at our foreign subsidiaries. We believe that the risks associated with our foreign currency exposure are mitigated by the fact that a portion of our total revenues, approximately 24.8% in the three months ended 31 March 2010, is denominated in US dollars. As of 31 March 2010, the Russian rouble had appreciated by approximately 2.9% against the US dollar since 1 January 2010.

A hypothetical and instantaneous 10% strengthening in the Russian rouble in relation to the US dollar as of 31 March 2010 would have resulted in an estimated foreign exchange gain of approximately RR 2,256 million on foreign currency denominated borrowings held at that date.

Commodity risk

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

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

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

Pipeline access

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

Ability to reinvest

Our business requires significant ongoing capital expenditures in order to grow our production. An extended period of reduced demand for our hydrocarbons available for sale and the corresponding revenues generated from these sales would limit our ability to maintain an adequate level of capital expenditures, which in turn could limit our ability to increase or maintain current levels of production and deliveries of natural gas, gas condensate, crude oil and other associated products; thereby, adversely affecting our financial and operating results.

Off balance sheet activities

As of 31 March 2010, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which are typically established for the purpose of facilitating off-balance sheet arrangements.