Management's discussion and analysis of financial condition and results of operations

The following represents management's analysis of the financial performance and condition of OAO LUKOIL and significant trends that may affect future performance. It should be read in conjunction with our interim US GAAP consolidated financial statements and notes thereto.

References to "LUKOIL", "the Company", "the Group", "we" or "us" are references to OAO LUKOIL and its consolidated subsidiaries and associates. All dollar amounts are in millions of US dollars, unless otherwise indicated. Tonnes of crude oil produced are translated into barrels using conversion rates characterizing the density of oil from each of our oilfields. Tonnes of crude oil purchased as well as other operational indicators expressed in barrels are translated into barrels using an average conversion rate of 7.33 and billions of cubic feet into millions of oil equivalent barrels using a conversion rate of 0.167.

This report includes forward-looking statements – words such as "believes", "anticipates", "expects", "estimates", "intends", "plans", etc. - that reflect management's current estimates and beliefs, but are not guarantees of future results.

Key financial and operational results

	1st half of 2005	1st half of 2004	% change	**2nd quarter of 2005**	2nd quarter of 2004	% change
Sales (including excise and export tariffs)	**24,049**	14,477	66.1%	**13,492**	7,965	69.4%
Net Income	**2,590**	1,696	52.7%	**1,410**	877	60.8%
EBITDA	**4,298**	2,965	45.0%	**2,339**	1,553	50.6%
Earnings per share of common stock (US dollars)						
Basic earnings	**3.18**	2.07	53.6%	**1.73**	1.07	61.7%
Diluted earnings	**3.14**	2.05	53.2%	**1.71**	1.06	61.3%
Crude oil production by consolidated subsidiaries (thousands of tonnes)	**42,351**	40,552	4.4%	**21,347**	20,378	4.8%
Commercial gas production by consolidated subsidiaries (million cubic metres)	**2,618**	2,340	11.9%	**1,364**	1,117	22.1%
Refined products produced by consolidated subsidiaries (thousands of tonnes)	**21,018**	19,722	6.6%	**10,985**	10,329	6.4%

During the first half of 2005 net income was $2,590 million, which is $894 million more than in the same period of 2004.

The increase in net income resulted from favorable price conditions in the first half of 2005 and improved cost control. However, an increased tax burden has restrained growth of our profitability. These restraining factors as well as other drivers impacting the results of our operations are considered below in detail.

Segment information

Our operations are divided into three main business segments:

- **Exploration and Production** – which includes our exploration, development and production operations relating to crude oil and natural gas. These activities are primarily located within Russia, with additional activities in Azerbaijan, Kazakhstan, Uzbekistan, the Middle East, Northern Africa and Colombia

- **Refining, Marketing and Distribution –** which includes marketing and trading of crude oil, natural gas and refined products, and refining and transport operations

- **Chemicals –** which include processing and trading of petrochemical products

Other businesses include banking and finance, construction and other activities. Each of our three main segments is dependent on the other, with a portion of the revenues of one segment being a part of the costs of the other. In particular, our Refining, Marketing and Distribution segment purchases crude oil from our Exploration and Production segment. As a result of certain factors considered in the "Domestic crude oil prices" section on page 4, benchmarking crude oil market prices in Russia cannot be determined with certainty. Therefore, the prices set for inter-segment purchases of crude oil reflect a combination of market factors, primarily international crude oil market prices, transportation costs and need for investment resources at the Group's oil producing companies. Accordingly, an analysis of either of these segments on a stand-alone basis could give a misleading impression of that segment's underlying financial position and results of operations. For this reason, we do not analyze either of our main segments separately in the discussion that follows, but we do present the financial data for each in Note 17 to our consolidated financial statements.

Operating developments

Strategic Partnership with ConocoPhillips

In September 2004 LUKOIL entered into a Shareholder agreement forming a broad-based strategic alliance with ConocoPhillips. In June 2005 LUKOIL and ConocoPhillips finalized the creation of a joint venture to develop resources in the northern Timan-Pechora area. The joint venture will be governed by LUKOIL and ConocoPhillips in equal parts, but with effective ownership interests of 70% and 30%, respectively. The joint venture was formed by selling to ConocoPhillips an effective 30% interest in our wholly owned subsidiary OOO Narianmarneftegaz for $512 million. It is expected that the joint venture's crude oil production will reach approximately 200 thousand barrels per day by 2008. Crude oil production of OOO Narianmarneftegaz in the first half of 2005 was approximately 13 thousand barrels per day.

Recent developments

In July 2005 the Group acquired 66.0% of the share capital of OOO Geoilbent for $180 million. All decisions over OOO Geoilbent's financing and operating activities require approval by a 66.7% majority of voting rights. OOO Geoilbent is an exploration and production company operating in Western Siberia region of the Russian Federation.

In July 2005 LUKOIL sold a 100% stake in oil production company ZAO Arktikneft for approximately $40 million, including $20 million for settlement of Arktikneft's debt to LUKOIL. ZAO Arktikneft produced 30.3 thousand tonnes of crude oil in the first half of 2005.

In June 2005 the Company sold its 38% interest in its construction affiliate ZAO Globalstroy-Engineering – formerly ZAO LUKOIL-Neftegazstroy for $69 million.

In March 2005 we acquired 100% interest in Oy Teboil Ab and Suomen Petrooli Oy, which are incorporated in Finland, for $160 million. Oy Teboil Ab and Suomen Petrooli Oy are mainly engaged in the operation of 289 retail petrol service stations and 132 retail diesel fuel outlets, wholesale of refined oil products as well as production and sale of lubricants.

In January 2005 a Group company acquired an additional 22% interest in LUKOIL Neftochim Bourgas AD for $56 million (20.7% interest was acquired from a related party for $52 million). The acquisition increased the Group's ownership stake in LUKOIL Neftochim Bourgas AD to 93.2%.

On January 26, 2004, a Group company entered into an agreement with ConocoPhillips to purchase 308 gas stations and contracts to supply petroleum products to an additional 471 gas stations in the Northeast of the United States of America for $270 million. The transaction was finalized in May 2004.

Main macroeconomic factors affecting our results of operations

Change in the price of crude oil and refined products

The price at which we can sell crude oil and refined products is the primary driver of our revenues. During the first half of 2005 crude oil prices were steadily high due to growth of the world economy, driven mainly by the USA and China, and increased worldwide crude oil consumption. Also, during the first half of 2005, due to the continuing growth in demand in the USA and China, prolonged late winter cold snap in the US East Coast, certain geopolitical tensions, refining and distribution bottlenecks in some major consuming regions, crude oil prices reached their historical records in absolute terms. OPEC forecasts a 4.1% growth of the world economy in 2005 and estimates that the worldwide crude oil consumption will reach the level of 83.6 million barrels per day in 2005, or 1.9% more than in 2004 (data as of August, 2005). Based on OPEC's data, its actual daily production in the first half of 2005 reached 29.8 million barrels a day, or 1.3 million barrels a day more than in the same period of the 2004, which is near OPEC's full capacity. The current market situation is also influenced by high political and natural risks, which could cause crude oil production to decrease. This situation can be viewed as an indicator that crude oil prices will remain steadily high in a medium-term perspective.

Substantially all of the crude oil that we sell for export is the Urals blend. The following table shows the average crude oil export prices for respective periods of 2004 and 2005 and refined product prices based on Northern Europe averages:

	1st half of 2005	1st half of 2004	Change %	2nd quarter of 2005	2nd quarter of 2004	Change %
	(in US dollars per bbl, except for figures in percent)					
Brent crude	49.25	33.66	46.3%	50.84	35.32	43.9%
Urals crude (CIF Mediterranean)*	45.51	30.74	48.0%	47.74	32.50	46.9%
Urals crude (CIF Rotterdam)*	44.95	30.63	46.8%	47.30	32.19	46.9%
	(in US dollars per metric tonne, except for figures in percent)					
Fuel oil 3.5% (FOB Rotterdam)	201.84	147.42	36.9%	227.82	157.05	45.1%
Diesel fuel (FOB Rotterdam)	457.67	292.55	56.4%	482.07	311.26	54.9%
High-octane gasoline (FOB Rotterdam)	473.95	370.71	27.8%	510.21	408.19	25.0%

* The Company sells crude oil on foreign markets on various delivery terms. Thus, the average realized sale price of oil on international markets differs from the average prices of Urals crude on Mediterranean and Northern Europe markets.

Domestic crude oil prices

Substantially all crude oil produced in Russia is produced by vertically integrated oil companies such as ours, as a result most transactions are between affiliated entities within vertically integrated groups. Thus, there is no concept of a benchmark domestic market price for crude oil. Essentially, crude oil prices on traditional international markets will be higher than those in Russia due to incremental transportation cost incurred to deliver the crude oil from the Russian border to the markets, and export tariffs. However, the price of crude oil that is produced but not refined or exported by one of the vertically integrated oil companies is generally determined on a transaction-by-transaction basis against a background of world market prices, but with no direct reference or correlation. At any time there may exist significant price differences between regions for similar quality crude oil as a result of the competition and economic conditions in those regions.

Domestic refined product prices

Domestic prices for refined products are determined to some extent by world market prices, but they are also directly affected by local demand and competition. In general, retail prices on refined products in Russia are comparable to those in the USA. For example, during the first half of 2005 the average retail price on regular gasoline in the USA was about 55 cents per litre, an increase of 14.4% compared to the same period of 2004. In central regions of European Russia the average retail price on gasoline of the same quality (95 octane) during the first half of 2005 was 54 cents per litre, an increase of 28.3% compared to the first half of 2004.

The table below represents average domestic wholesale prices on refined products for respective periods of 2004 and 2005.

	1st half of 2005	1st half of 2004	Change %	2nd quarter of 2005	2nd quarter of 2004	Change %
Fuel oil	90.33	67.58	33.7%	115.39	77.24	49.4%
Diesel fuel	384.72	247.04	55.7%	403.98	265.25	52.3%
High-octane gasoline (Regular)	447.28	343.45	30.2%	486.92	363.08	34.1%
High-octane gasoline (Premium)	489.30	387.25	26.4%	531.77	400.03	32.9%

Source: Kortes (excluding VAT).

Changes in the US dollar-ruble exchange rate and inflation

A substantial part of our revenues is either denominated in US dollars or is correlated to some extent with US dollar crude oil prices, while most of our costs in the Russian Federation are settled in Russian rubles. Therefore, the movements of ruble inflation and exchange rates can significantly affect the results of our operations. In particular, our operating margins are generally adversely affected by real appreciation of the ruble against the US dollar because this will generally cause our costs to increase in US dollar terms relative to our revenues.

The following table gives data on inflation in Russia, the nominal change in the ruble–dollar exchange rate, and the level of real rouble appreciation.

	1st half of 2005	1st half of 2004	2nd quarter of 2005	2nd quarter of 2004
Ruble inflation (CPI)	7.8%	6.3%	2.5%	2.5%
Nominal (devaluation)/appreciation of the exchange rate (ruble to US dollar)	(3.3)%	1.5%	(3.0)%	(1.9)%
Real appreciation/(devaluation) of the exchange rate (ruble to US dollar)	4.4%	7.8%	(0.5)%	0.6%
Average exchange rate for the period (ruble to US dollar)	27.96	28.78	28.08	28.90
Exchange rate at the end of the period (ruble to US dollar)	28.67	29.03	–	–

Change in tax rates and export tariffs

The following tables represents average enacted rates for taxes specific to the oil industry in Russia for the respective periods:

		1st half of 2005*	1st half of 2004*	Change %
Export tariffs on crude oil	$/tonne	101.51	35.15	188.8%
Export tariffs on refined products				
Light distillates (gasoline), middle distillates (jet fuel), diesel fuel and gasoils	$/tonne	68.96	30.60	125.4%
Liquid fuels (fuel oil)	$/tonne	43.29	30.60	41.5%
Excise on refined products				
High-octane gasoline	RUR/tonne	3,629.00	3,360.00	8.0%
Low-octane gasoline	RUR/tonne	2,657.00	2,460.00	8.0%
Diesel fuel	RUR/tonne	1,080.00	1,000.00	8.0%
Motor oils	RUR/tonne	2,951.00	2,732.00	8.0%
Mineral extraction tax	RUR/tonne	1,625.40	915.41	77.6%

* Average values.

		2nd quarter of 2005*	2nd quarter of 2004*	Change %
Export tariffs on crude oil	$/tonne	113.68	37.31	204.7%
Export tariffs on refined products				
Light distillates (gasoline), middle distillates (jet fuel), diesel fuel and gasoils	$/tonne	79.06	32.02	146.9%
Liquid fuels (fuel oil)	$/tonne	42.54	32.02	32.9%
Excise on refined products				
High-octane gasoline	RUR/tonne	3,629.00	3,360.00	8.0%
Low-octane gasoline	RUR/tonne	2,657.00	2,460.00	8.0%
Diesel fuel	RUR/tonne	1,080.00	1,000.00	8.0%
Motor oils	RUR/tonne	2,951.00	2,732.00	8.0%
Mineral extraction tax	RUR/tonne	1,734.64	982.41	76.6%

* Average values.

Tax rates set in rubles and translated at the average exchange rates for respective periods are as follows:

	1st half of 2005 *	1st half of 2004 *	Change %	2nd quarter of 2005 *	2 nd quarter of 2004 *	Change %
	(in US dollars per tonne)					
Excise on refined products						
High-octane gasoline	129.79	116.75	11.2%	129.24	116.27	11.2%
Low-octane gasoline	95.03	85.48	11.2%	94.62	85.12	11.2%
Diesel fuel	38.63	34.75	11.2%	38.46	34.60	11.2%
Motor oils	105.55	94.93	11.2%	105.09	94.54	11.2%
Mineral extraction tax	58.13	31.81	82.7%	61.77	33.99	81.7%

* Average values.

During the first half of 2005 our tax burden rose significantly compared to the previous year. Average crude oil export tariffs increased by 188.8% compared to the first half of 2004. Approximately 95% of the increase related to growth of crude oil prices, and the remaining 94% resulted from changes in the duty rate calculations effective June 2004 (see below). Export tariffs on gasoline, kerosene, jet fuel, diesel fuel and gasoils increased by 125.4%. Excise on refined products increased by approximately 8.0%.

The mineral extraction tax rate increased by 77.6% compared to the first half of 2004. This resulted from an increase of the Urals crude price and a change in the tax calculation method effective from January 1, 2005.

The mineral extraction tax rate is determined as follows. Effective from January 1, 2005, the base rate is set at 419 Rubles per metric tonne extracted (in the first half of 2004 – 347 rubles) and is adjusted depending on the international market price of the Urals blend and the ruble exchange rate. The tax rate is zero when the average Urals international market price for a tax period is less than or equal to $9.00 per barrel (before January 1, 2005 the lower non-taxable threshold was $8.00 per barrel). As a result each $1.00 per barrel increase in the international Urals price over the threshold ($9.00 per barrel) will effectively result in an increase of the tax rate by $1.61 per tonne extracted (or $0.22 per barrel extracted using a conversion factor of 7.33). In the first half of 2004 each $1.00 per barrel increase in the international Urals price over the threshold ($8.00 per barrel) effectively resulted in an increase of the tax rate by $1.38 per tonne extracted (or 0.19 cents per barrel extracted using a conversion factor of 7.33).

In June 2004 the Russian government introduced a new method of crude oil export duty rate calculation with a three-layer progressive scale. The rate is zero when the average Urals international market price is less than or equal to approximately $15.00 per barrel ($109.50 per metric tonne). If the Urals price is in a layer between $15.00 and $20.00 per barrel ($146.00 per metric tonne), each $1.00 per barrel increase in the Urals price over the layer's lower bound results in an increase of the crude oil export duty rate by $0.35 per barrel exported. If the Urals price is in a layer between $20.00 and $25.00 per barrel ($182.50 per metric tonne), each $1.00 per barrel increase in the Urals price over the layer's lower bound results in an increase of the crude oil export duty rate by $0.45 per barrel exported. If the Urals price is above $25.00 per barrel, each $1.00 dollar per barrel increase in the Urals price over this limit results in the increase of the crude oil export duty rate by $0.65 per barrel exported.

Before June 2004 the crude oil export duty rate was calculated as follows. The rate was zero when the average Urals international market price was less than or equal to approximately $15.00 per barrel. If the Urals price was in a layer between $15.00 and $25.00 per barrel, each $1.00 per barrel increase in the Urals price over the layer's lower bound resulted in increase of the crude oil export duty rate by $0.35 per barrel exported. If the Urals price was above $25.00 per barrel, each $1.00 dollar per barrel increase in the Urals price over this limit resulted in the increase of the crude oil export duty rate by $0.40 per barrel exported.

Export duty rates on refined products are set by the Russian government. The size of export duty depends on internal demand on refined products and international crude oil market conditions. Crude oil and refined products exported to CIS countries, other than Ukraine, are not subject to export duties.

Operational highlights

Oil production

In line with our long-term strategy we increased our total daily oil production by 4.6% (including the Company's share in equity associates) compared to the first half of 2004 and produced 325.7 million barrels (44,225 thousand tonnes) during the first half of 2005.

	1st half of 2005	1st half of 2004	Change, %
Daily production of crude oil, including Company's share in Equity associates (thousand barrels per day)	1,800	1,721	4.6%
Refinery throughput (thousand barrels per day)	908	852	6.6%

	2nd quarter of 2005	2nd quarter of 2004	Change, %
Daily production of crude oil, including Company's share in Equity associates (thousand barrels per day)	1,800	1,730	4.0%
Refinery throughput (thousand barrels per day)	954	874	9.2%

The following table represents our production in the first half of 2005 and 2004 by major regions, excluding our share in equity associates:

(thousands of tonnes)	1st half of 2005	Change to 2004			1st half of 2004
		Total %	Change in structure	Organic growth	
Western Siberia	28,240	2.9%	–	783	**27,457**
Komi Republic	4,904	3.5%	–	167	**4,737**
Ural region	5,069	1.8%	–	88	**4,981**
Volga region	1,490	0.9%	–	14	**1,476**
Timan-Pechora (Nenetsky Autonomous District)	875	31.8%	11	200	**664**
Other in Russia	847	32.3%	–	207	**640**
Crude oil production in Russia	**41,425**	**3.7%**	**11**	**1,459**	**39,955**
Crude oil produced internationally	**926**	**55.1%**	**42**	**287**	**597**
Total crude oil produced	**42,351**	**4.4%**	**53**	**1,746**	**40,552**

The main oil production region of the Company is Western Siberia. In the oil fields of Western Siberia the Company produced 66.7% of its total production of crude oil in the first half of 2005 (67.7% in the first half of 2004). The increase of production in Western Siberia was 2.9%. The organic growth of oil production in traditional production regions resulted from improvement and optimization of oil production methods. As a result our average well debits increased from 10.6 tonnes a day in the first half of 2004 to 11.0 tonnes a day in the first half of 2005, or by 3.7%, and average new well debits increased up to 46.3 tonnes a day, or 7.2%. In addition to traditional regions we continue exploration and development of new promising production regions. Commencement of oil production in new oil fields in the Nenetsky Autonomous District led to an increase of oil production in this region more than 1.3 times compared to the first half of 2004. In the third quarter of 2004 we started commercial production at Kravtsovskoye (D-6), a Baltic offshore field. In the first half of 2005 we produced 208 thousand tonnes of crude oil from this field, and we expect that annual crude oil production will reach 700 thousand tonnes by 2007. The structural growth in international production volumes in the first half of 2005 was caused by consolidation of the Company's share in the Meleiha Hydrocarbon License Agreement as a result of an increase in our share of LUKAgip N.V. at the end of 2004.

In addition to our production, we purchase crude oil from third parties in Russia and on international markets. In Russia we primarily purchase crude oil from associated producing companies and other producers, including vertically integrated companies that lack refining capacity or are unable to export their crude oil. We may either refine or export purchased crude oil. Crude oil purchased on international markets is used mostly for marketing activities and, on certain occasions, for supplying our overseas refineries.

	1st half of			
	2005		2004	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Crude oil purchases in Russia	3,159	431	10,488	1,431
Crude oil purchases internationally	37,222	5,078	33,637	4,589
Total crude oil purchased	**40,381**	**5,509**	**44,125**	**6,020**

	2nd quarter of			
	2005		2004	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Crude oil purchases in Russia	1,759	240	5,996	818
Crude oil purchases internationally	22,203	3,029	17,446	2,380
Total crude oil purchased	**23,962**	**3,269**	**23,442**	**3,198**

The volume of crude oil purchased in Russia in the first half of 2005 was 1,000 thousand tonnes less than in the first half of 2004 as a result of decreases in purchases from third parties, nevertheless purchases from our associates remained on the same level. The volume of crude oil purchased internationally increased by 489 thousand tonnes because in the second quarter of 2005 we extended our marketing activity on international markets.

Gas production

In the first half of 2005 we produced 2,745 million cubic metres of commercial gas (including our share in equity associates), an increase of 11.6% compared to the first half of 2004. In April 2005 we started commercial production on the Nakhodkinskoe gas field. This is a first stage of development of the Bolshekhetskaya basin fields in the Yamalo-Nentsky Autonomous District. We estimate production output from the field will reach 11 billion cubic metres during 2005-2006 and the field's planned production capacity of 10 billion cubic metres per year will be achieved in 2007. Development of the Bolshekhetskaya basin fields is a core element of our gas business strategy.

Refining and marketing

We operate four refineries located in European Russia and three refineries located overseas – in Bulgaria, Ukraine and Romania. Our Romanian refinery, Petrotel-LUKOIL S.A., was undergoing significant upgrades until October 2004. In October 2004, we put Petrotel-LUKOIL back into operation.

In the first half of 2005 the production of refined products increased by 6.6% as compared to the same period of the previous year. Production on Russian refineries remained on the same level, while the overseas refineries increased production by 41.8% primarily due to recommencement of production by Petrotel-LUKOIL.

In the first half of 2005 we continued to expand our marketing activities in Western Europe, South-East Asia, Northern and Central America. Our marketing activities mainly include wholesale and bunkering operations in Western Europe and South-East Asia as well as supply our retail networks in the USA, Baltic states and some other regions. The total volume of refined products purchased from third parties for wholesale was 9,934 thousand tonnes or $3,671 million in the first half of 2005 (6,775 thousand tonnes or $1,681 million in the first half of 2004). The total volume of refined products purchased from third parties to supply the retail network during the first half of 2005 was 4,968 thousand tonnes or $2,554 million (2,716 thousand tonnes or $1,223 million in the first half of 2004).

In Russia we purchase refined products on occasion, primarily to manage supply chain bottlenecks.

The following tables represent volumes of refined products produced and purchased:

	1st half of 2005 (thousand of tonnes)	1st half of 2004 (thousand of tonnes)
Refined products produced at the Group refineries in Russia	16,442	16,494
Refined products produced at the Group refineries outside of Russia	4,577	3,228
Total refined products produced	**21,019**	**19,722**
Refined products purchased in Russia	590	891
Refined products purchased internationally	14,912	9,491
Total refined products purchased	**15,502**	**10,382**

	2nd quarter of 2005 (thousand of tonnes)	2nd quarter of 2004 (thousand of tonnes)
Refined products produced at the Group refineries in Russia	8,415	8,414
Refined products produced at the Group refineries outside of Russia	2,571	1,915
Total refined products produced	**10,986**	**10,329**
Refined products purchased in Russia	286	626
Refined products purchased internationally	8,087	5,056
Total refined products purchased	**8,373**	**5,682**

Export of crude oil and refined products from Russia

We transport a significant portion of our crude oil through Transneft's trunk oil pipeline system. Access to the Transneft crude oil export pipeline network is allocated quarterly, based on recent volumes produced and delivered through the pipeline and proposed export destinations. There is a constraint on the ability of Russian companies to export their crude oil due to limited capacity of Russian transportation infrastructure on the most profitable export routes.

In order to overcome such limits Transneft has extended the capacity of the Baltic Pipeline System. In the first half of 2005 it rose to 56 million tonnes of crude oil per year. This allowed us to increase the volume of crude oil exported via the Primorsk terminal in the first half of 2005 up to 4,828 thousand tonnes, or 491 thousand tonnes more than in the same period of 2004.

The crude oil transported by Transneft is the Urals blend – a mix of crude oils of different quality, therefore Russian companies which produce crude oil of a higher quality can not obtain benefits from selling it using Transneft's pipeline.

Additional access to international markets bypassing Transneft export routes can be obtained through rail transport, by tankers or by own export infrastructure. Our export infrastructure includes the Vysotsk terminal in the Leningrad region, Varandey terminal in the Nenetsky Autonomous District and the Izhevskoye terminal in the Kaliningrad region. In the first half of 2005 the Company exported 11.8% of crude oil produced, or 5,013 thousand tonnes, by means other than Transneft (3,243 thousand tonnes in the same period of 2004), including 2,582 thousand tonnes through our own export infrastructure (762 thousand tonnes in the same period of 2004). In the third quarter of 2005 we decided to cease exporting crude oil through the Vysotsk terminal due to the increase of capacity of the Baltic Pipeline System. The terminal will be used for export of refined products.

In 2005 we began to export crude oil to China. The volume exported in the first half of 2005 was 774 thousand tonnes (in the first half of 2004 we did not export crude oil to China).

The volumes of crude oil exported from Russia by our consolidated domestic producers are summarized as follows:

	1st half of 2005		1st half of 2004	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Export of crude oil using Transneft export routs	135,972	18,550	143,960	19,640
Export of crude oil bypassing Transneft	36,745	5,013	23,772	3,243
Total crude oil export	**172,717**	**23,563**	**167,732**	**22,883**

	2nd quarter of 2005		2nd quarter of 2004	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Export of crude oil using Transneft export routs	70,310	9,592	72,324	9,867
Export of crude oil bypassing Transneft	17,086	2,331	12,748	1,739
Total crude oil export	**87,396**	**11,923**	**85,072**	**11,606**

In the first half of 2005 we exported 6.8 million tonnes of refined products, which equals the level of the same period of 2004.

Six months ended June 30, 2005 compared to the six months ended June 30, 2004

The table below details certain income and expense items from our consolidated statements of income for the periods indicated. All items are presented in millions of US dollars, except for earnings per share data and percentage of changes to the first half of 2004.

	1st half of		Change
	2005	**2004**	**%**
Revenues			
Sales (including excise and export tariffs)	24,049	14,477	66.1%
Equity share in income of affiliates	201	132	52.3%
Total revenues	**24,250**	**14,609**	**66.0%**
Costs and other deductions			
Operating expenses	(1,499)	(1,334)	12.4%
Cost of purchased crude oil, petroleum and chemical products	(8,322)	(4,328)	92.3%
Transportation expenses	(1,694)	(1,383)	22.5%
Selling, general and administrative expenses	(1,134)	(922)	23.0%
Depreciation, depletion and amortization	(601)	(514)	16.9%
Taxes other than income taxes	(2,894)	(1,558)	85.8%
Excise and export tariffs	(4,136)	(1,947)	112.4%
Exploration expenses	(183)	(87)	110.3%
Gain (loss) on disposal and impairments of assets	53	(71)	–
Income from operating activities	**3,840**	**2,465**	**55.8%**
Interest expense	(117)	(143)	(18.2)%
Interest and dividend income	37	99	(62.6)%
Currency translation (loss) gain	(85)	19	–
Other non-operating (expense) income	(6)	4	–
Minority interest	(52)	(37)	40.5%
Income before income taxes	**3,617**	**2,407**	**50.3%**
Current income taxes	(1,088)	(712)	52.8%
Deferred income taxes	61	1	–
Total income tax expense	**(1,027)**	**(711)**	**44.4%**
Net income	**2,590**	**1,696**	**52.7%**
Per share of common stock (in US dollars):			
Net income			
Basic	3.18	2.07	53.6%
Diluted	3.14	2.05	53.2%

The analysis of the main financial indicators of the financial statements is provided below.

Sales revenues

Sales breakdown	1st half of 2005		1st half of 2004	
	(millions of US dollars)			
Crude oil				
Export and sales on international markets other than CIS	7,410	30.8%	4,570	31.5%
Export and sales to CIS	191	0.8%	298	2.1%
Domestic sales	58	0.2%	101	0.7%
	7,659	**31.8%**	**4,969**	**34.3%**
Refined products				
Export and sales on international markets				
Wholesale	9,177	38.2%	4,835	33.4%
Retail	2,605	10.8%	1,488	10.3%
Domestic sales				
Wholesale	2,030	8.4%	1,416	9.8%
Retail	833	3.5%	514	3.6%
	14,645	**60.9%**	**8,253**	**57.1%**
Petrochemicals				
Export and sales on international markets	650	2.7%	451	3.1%
Domestic sales	229	1.0%	154	1.1%
	879	**3.7%**	**605**	**4.2%**
Other	**866**	**3.6%**	**650**	**4.4%**
Total sales	**24,049**	**100.0%**	**14,477**	**100.0%**

Sales volumes	1st half of 2005		1st half of 2004	
	(thousands of barrels)			
Crude oil				
Export and sales on international markets other than CIS	164,661		153,197	
Export and sales to CIS	7,754		16,903	
Domestic sales	2,661		7,550	
Crude oil	(thousands of tonnes)			
Export and sales on international markets other than CIS	22,464	38.5%	20,900	39.4%
Export and sales to CIS	1,058	1.8%	2,306	4.3%
Domestic sales	363	0.6%	1,030	1.9%
	23,885	**40.9%**	**24,236**	**45.6%**
Refined products	(thousands of tonnes)			
Export and sales on international markets				
Wholesale	21,410	36.7%	16,800	31.6%
Retail	3,284	5.6%	2,200	4.1%
Domestic sales				
Wholesale	8,218	14.1%	8,659	16.3%
Retail	1,602	2.7%	1,270	2.4%
	34,514	**59.1%**	**28,929**	**54.4%**
Total sales volume of crude oil and refined products	**58,399**	**100.0%**	**53,165**	**100.0%**

Realized average sales prices	1st half of 2005		1st half of 2004	
	($/barrel)	($/tonne)	($/barrel)	($/tonne)
Average realized price international				
Oil (excluding CIS)	45.00	329.86	29.83	218.64
Oil (CIS)	24.70	181.05	17.66	129.45
Refined products				
Wholesale		428.63		287.79
Retail		793.30		676.12
Average realized price within Russia				
Oil	21.91	160.59	13.37	98.03
Refined products				
Wholesale		247.01		163.54
Retail		520.14		405.01

During the first half of 2005 sales revenues increased by $9,572 million, or 66.1%, compared to the same period of 2004.

The total volume of crude oil and refined products sold amounted to 58.4 million tonnes, which is 9.8% more than in the first half of 2004. Our revenues from crude oil sales increased by $2,690 million, or 54.1%. Our sales of refined products increased by $6,392 million, or 77.5%.

Sales of crude oil and refined products on the international markets, including the CIS, accounted for 82.6% of total sales volume in the first half of 2005 compared to 79.4% in the first half of 2004.

The increase in sales was principally due to the following:

- favorable price conditions (see "Change in the price of crude oil and refined products" on page 4)
- increase in total volume of crude oil production (see "Oil production" on page 8)
- increase in marketing activities (see page 9)
- decrease of crude oil sales in Russia and increase in volumes exported on international markets (see "Export of crude oil and refined products from Russia" on page 10)

Sales of crude oil

During the first half of 2005 the Company decreased its sales of crude oil on the domestic market compared to the same period of the previous year by 667 thousand tonnes, or 64.8%. This change was caused by an increase in volumes exported by the Company's domestic producers and a decrease in crude oil purchases in Russia.

During the first half of 2005 we increased exports of crude oil on international markets by the Company's domestic producers by 680 thousand tonnes. The increase in export sales, along with an increase in the average realized export price of crude oil on international markets (other than CIS) from $29.83 to $45.00 per barrel, allowed us to obtain an additional $2,699 million in revenues.

Sales of refined products

Sales of refined products made up 60.9% of our total sales revenues (59.1% in terms of volumes sold) compared to 57.1% (54.4% – in terms of volumes) in the first half of 2004. The portion of our domestic refined product sales in the first half of 2005 was 16.8% of the total tonnes sold (the first half of 2004: 18.7%), but represented 11.9% of our total sales revenue (the first half of 2004: 13.4%).

The average realized wholesale price on refined products outside of Russia increased by $140.84 per tonne, or 48.9%, compared to the first half of 2004. Volumes of refined products sold outside of Russia increased by 4,610 thousand tonnes, or 27.4% (see also "Refining and marketing" on page 9). As a result, our revenues from wholesale of refined products outside of Russia increased by $4,342 million, or 89.8%.

In the first half of 2005 retail sales of refined products outside of Russia increased by 1,084 thousand tonnes, or by 49.3%, compared to the same period of 2004. The increase was a result of continuing development of the existing retail chains outside of Russia and structural changes in the retail network we operate. In particular, in May 2004 we acquired an additional retail network in the USA, and in March 2005 we acquired a retail network in Finland. Average retail prices increased up to $793.30 per tonne, or by 17.3%. As a result, our revenues from retail sales increased by $1,117 million, or 75.1%. In the first half of 2005 revenue from retail sales was 22.1% of total sales of refined products outside of Russia. Our international retail sales include supplies of refined products to third parties' retail networks within the bounds of long-term contracts with pricing similar to retail pricing.

Wholesale of refined products within Russia in the first half of 2005 decreased by 441 thousand tonnes, or 5.1%, as compared to the same period in 2004. The average domestic realized price on refined products increased by $83.47 per tonne, or 51.0%. As a result, our revenues from wholesale of refined products on the domestic market increased by $614 million, or 43.4%.

Retail sales within Russia in the first half of 2005 increased by 332 thousand tonnes, or 26.1%, compared to the same period in 2004. Average retail prices increased up to $520.14 per tonne, or by 28.4%. As a result, our revenues from retail sales increased by $319 million, or 62.1%. Revenue from retail sales was 29.1% of total sales of refined products in Russia in the first half of 2005.

Sales of petrochemical products

Revenues from sales of petrochemical products increased by $274 million, or 45.3%, during the first half of 2005. This was mainly due to an increase of production volume up to 1,195 thousand tonnes, or by 10.4%, compared to the same period in 2004, and an increase in average realized prices.

Sales of other products

Other sales increased by $216 million, or 33.2%, as a result of sales of other products produced by the Company, and also increased activity in providing other services to third parties.

Equity share in income of affiliates

Our share in the income of affiliates in the first half of 2005 increased by $69 million, or 52.3%, compared to the first half of 2004, primarily due to an increase in the net income of ZAO Turgai-Petroleum. ZAO Turgai-Petroleum, our 50% interest affiliate company, is a partner in the Turgai-Petroleum joint venture developing the Kumkol oil field in Kazakhstan. The Group's share in the net income of ZAO Turgai-Petroleum in the first half of 2005 amounted $113 million, which represents an increase of $64 million as compared to the same period of the previous year.

Operating expenses

Operating expenses include the following types of costs:

	1st half of 2005	1st half of 2004
	(millions of US dollars)	
Extraction expenses	835	752
Refining expenses	329	253
Petrochemical expenses	96	89
Other operating expenses	239	240
Total operating expenses	**1,499**	**1,334**
Cost of purchased crude oil, petroleum and chemical products	**8,322**	**4,328**

Compared to the first half of 2004, operating expenses increased by $165 million, or 12.4%.

Extraction expenses. Our extraction expenses include expenditures related to repairs of extraction equipment, labor costs, expenses of artificial stimulation of reservoirs, fuel and electricity costs, property insurance of extraction equipment and other similar costs.

Expenses of the Company's oil production enterprises related to the sale of services and goods (such as electricity, heat, etc.) that do not relate to core activities have been excluded from extraction expenses and are included in other operating costs.

In the first half of 2005 our extraction expenses rose by $83 million, or 11.0%, compared to the same period of 2004. The increase resulted from growth of crude oil produced by our subsidiaries up to 42.4 million tonnes, or by 4.4%, compared to the first half of 2004, and additional expenses on repairs and overhaul in our production subsidiaries and increased expenses of artificial stimulation of reservoirs in the second quarter of 2005. Moreover, extraction costs were affected by real ruble appreciation of 14.7% during the year ended June 30, 2005. However, the impact of these factors was mitigated by an increase of average well debits from 10.6 tonnes a day in the first half of 2004 to 11.0 tonnes a day in the first half of 2005 and improved cost control. As a result our average extraction cost per barrel increased from $2.53 to $2.69 per barrel, or by 6.3% (average extraction cost calculated using an average tonnes to barrels conversion rate of 7.33).

Refining expenses at our refineries increased by $76 million, or 30.0%, in the first half of 2005 compared to the first half of 2004.

Refining expenses of our domestic refineries increased by 20.2%, or $37 million, primarily as a result of real ruble appreciation. Moreover, in late 2004 we began changing product mix in order to produce higher quality and more profitable products (in particular, Euro 4 quality standard diesel fuel) which led to an increase of our refinery expenses.

Refining expenses of our international refineries increased by 55.7%, or $39 million, as a result of an overall increase in volumes produced and the recommencement of operations of our Romanian refinery Petrotel-LUKOIL after modernization.

Operating expenses of petrochemical companies increased by $7 million, or 7.9%, compared to the first half of 2004, as result of an increase in volumes produced.

Other operating expenses include the costs of other services provided and goods not related to primary activities (such as electricity, heat, etc.) sold by our production companies, and operating expenses of other non-core businesses of the Group. Other operating expenses also include costs associated with the delivery of crude oil from the Group's exploration and production entities to the Group's refineries, as well as the amount of the change in crude oil and refined products inventory originated within the Group. Other operating expenses remained on the same level as compared to the first half of 2004.

Cost of purchased crude oil, petroleum and chemical products increased by $3,994 million in the first half of 2005, or 92.3%, compared to the same period of the previous year due to a significant increase in volumes of sales of purchased crude oil and refined products in the first half of 2005 by 4,633 thousand tonnes compared to the same period of 2004 and growth of market prices on crude oil and petroleum products.

Transportation expenses

The increase in the total volume of sales together with the increase in transportation tariffs led to growth of transportation expenses in the first half of 2005 by $311 million, or 22.5%, compared to the first half of 2004.

According to the Federal Statistics Service of the Russian Federation, during the twelve months ended June 30, 2005 transportation tariffs increased as follows: transportation of oil by pipeline transport – 34.8% (including certain specific tariffs established for individual parts of the Transneft pipeline which did not have a material impact on transportation expenses of the Group), transportation of refined products by pipeline transport – 30.1%, railway transport – 8.8%. Sea shipping tariffs decreased by 5.1% (weighted average by volumes transported to different locations).

Selling, general and administrative expenses

Our selling, general and administrative expenses increased by $212 million, or 23.0%, compared to the first half of 2004. The above-mentioned expenses include general business expenses, payroll costs (excluding extraction entities' and refineries' production staff cost), insurance costs (except for property insurance related to oil and gas, and refinery equipment), costs of maintenance of social infrastructure, movement in bad debt provision and other expenses.

The increase in selling, general and administrative expenses was a result of general expansion of our operations. Also, the expenses were affected by real ruble appreciation of 14.7% during the twelve months ended June 30, 2005, and an increase in expenses related to a share-based compensation program for management in the first half of 2005, which was $88 million compared to $31 million in the same period of 2004. At the same time, these were compensated by a decrease in bad debt provision expense. During the first half of 2005 the bad debt expense was $12 million, while for the same period of 2004 the bad debt expense amounted to $27 million.

Selling, general and administrative expenses for the six months ended June 30, 2005 also included $23 million of expenses related to our Finnish subsidiaries acquired in March 2005 (see page 2).

Depreciation, depletion and amortization

Depreciation, depletion and amortization expenses include depletion of assets fundamental to production, depreciation of other productive and non-productive assets and certain intangible assets. Our depreciation, depletion and amortization expenses increased by $87 million, or 16.9%, compared to the first half of 2004. The increase was a result of the Company's capital expenditure program and corresponding growth of depreciable assets. This increase was partly compensated by upward revisions of the Company's proved reserves and, consequently, an increase in estimated useful economic life of fixed assets.

Taxes other than income taxes

Taxes other than income taxes include mineral extraction tax, property tax and social taxes.

	1st half of			
	2005		2004	
	In Russia	International	In Russia	International
	(millions of US dollars)			
Mineral extraction tax	2,401	–	1,275	–
Social security taxes and contributions	160	17	160	13
Property tax	119	11	61	9
Other taxes	171	15	27	13
	2,851	**43**	**1,523**	**35**
Total		**2,894**		**1,558**

The increase in taxes other than income taxes resulted primarily from a $1,126 million increase in mineral extraction tax, which is linked to international crude oil prices (see "Change in tax rates and export tariffs" on page 5). Property tax in Russia increased by $58 million primarily due to recalculation of domestic property tax related to 2002 and 2003. In the first half of 2005 the Group also accrued a provision in relation to the results of tax audits of the Group companies for periods prior to the 2004 financial year. The amount of provision related to taxes other than income taxes was approximately $150 million.

Excise and export tariffs

Our excise and export tariffs include duties on sales of refined products and export tariffs on export of crude oil and refined products. Excise and export tariffs increased by $2,189 million, or 112.4%, compared to the first half of 2004. The increase in export tariff expenses resulted from an increase in export tariff rates (see "Change in tax rates and export tariffs" on page 5) and also an increase in volumes exported. The increase in international excise taxes on refined products resulted from an increase in volumes of products sold across our international group, primarily in the USA, and due to commencement of our operations in Finland.

	1st half of			
	2005		2004	
	In Russia	International	In Russia	International
	(millions of US dollars)			
Excise tax and sales taxes on refined products	307	1,235	250	756
Export tariffs	2,592	2	935	6
	2,899	**1,237**	**1,185**	**762**
Total		**4,136**		**1,947**

Exploration expenses

The costs we incur in our exploratory drilling efforts are capitalized to the extent that our exploration efforts are successful and otherwise are charged to expenses of the current period. During the first half of 2005 the amount charged to exploration expense increased in comparison with the same period of the previous year by $96 million, or by 110.3%. This is attributable to the fact that during the first half of 2005 the Group completed drilling the first exploratory wells of the Yalama (D-222) and Tyub-Karagan exploration projects. Both exploratory wells were dry and their costs in the amount of $102 million were charged to expense. Notwithstanding the fact that the initial exploratory wells were not successful, the Group continues to perform further geological studies and is using the results of the first exploratory drilling in its analysis to assess potential placement of hydrocarbon deposits and to determine drilling programs for the second exploratory wells in both fields. The Group expects to complete this assessment by the end of 2005.

Gain on disposal and impairment of assets

Gain on disposal and impairment of assets in the first half of 2005 amounted to $53 million compared to $71 million loss in the first half of 2004.

In the first half of 2005 we recognized an $87 million gain on the sale our 30% interest in OOO Narianmarneftegaz to ConocoPhillips. We also recognized a gain of $4 million on the sale of our 38% interest in ZAO Globalstroy-Engineering.

In the first half of 2004 we recognized an impairment loss in relation to our decision to sell our ownership interests in OAO Bank Petrocommerce in amount of $35 million.

Interest expense

Interest expense in the first half of 2005 decreased by $26 million compared to the same period of 2004 primarily due to the sale of our ownership interest in OAO Bank Petrocommerce in the third quarter of 2004.

Income taxes

Our total income tax expense increased by $316 million, or 44.4%, compared to the same period of 2004, due to an increase of income before income tax by $1,210 million, or 50.3%.

Our effective tax rate in the first half of 2005 was 28.4% (in the first half of 2004 it was 29.5%), which is higher than the maximum statutory rate for the Russian Federation (24%). This is attributable to the fact that some costs incurred during the period are not tax deductible or only deductible to a certain limit.

Liquidity and capital resources

	1st half of 2005	1st half of 2004
	(million US dollars)	
Net cash provided by operating activities	2,420	1,360
Net cash used in investing activities	(1,818)	(2,141)
Net cash (used in) provided by financing activities	(313)	582
Net debt	2,025	4,139
Current ratio	1.70	1.43
Total debt to equity	16%	28%
Long term debt to long term debt and equity	10%	12%

Our primary source of cash flow is funds generated from our operations. During the first half of 2005 cash generated by operating activities was $2,420 million, an increase of $1,060 million compared to the first half of 2004. In the first half of 2005 cash inflow from operating activity was impacted by the following factors:

- increase in revenue
- increase in amount of income tax paid
- increase in volume of export sales and, consequently, prepayment of custom fees, export duties and transportation tariffs.

Moreover, in the first half of 2005 our operating cash inflows was significantly affected by an increase of working capital (excluding effect of acquisitions) by $506 million compared to January 1, 2005. This was mainly caused by:

- increase in trade accounts and notes receivable by $444 million resulted from an increase in the price of crude oil and refined products and expansion of marketing activities
- growth of inventory by $662 million resulted from increased volumes of crude oil and refined products in stock, and increased purchase prices.

At the same time, this change in working capital was partly compensated by:

- an increase in accounts payable related to mineral extraction tax by $228 million due to rise of the tax rate
- increase in trade accounts and notes payable by $297 million resulted from an increase in volumes of purchased crude oil and refined products and growth of related prices.

During the first half of 2005 the Company spent $2,302 million on capital investments and acquisitions of interests in other companies, which was $460 million more than in the first half of 2004. The increase was due to acquisitions of shares in Oy Teboil Ab and Suomen Petrooli Oy, increase of our share in LUKOIL Neftochim Burgas AD and prepayment of $180 million for a 66% equity interest in OOO Geoilbent. Capital expenditures, including non-cash transactions during the first half of 2005 amounted to $1,983 million, which was $387 million more than in the same period of the previous year. The growth in capital expenditures in new regions amounted to $182 million.

Cash flows from investing activities include $532 million of cash received from the sale of 30% interests in OOO Narianmarneftegaz for $512 million and in ZAO Globalstroy-Engineering.

In the first half of 2005 cash outflows related to financing activities were $313 million, compared to an inflow of $582 million in the same period of the previous year. The reason for this change is an overall decrease of our indebtedness.

Analysis of capital expenditures

	1st half of		2nd quarter of	
	2005	2004	2005	2004
	(millions of US dollars)		(millions of US dollars)	
Exploration and production				
Russia	1,199	949	628	482
International	187	72	104	31
Total exploration and production	1,386	1,021	732	513
Refining, marketing and distribution				
Russia	319	345	162	193
International	211	191	108	103
Total refining, marketing and distribution	530	536	270	296
Chemicals				
Russia	25	12	20	7
International	5	5	–	2
Total chemicals	30	17	20	9
Other	37	22	23	17
Total capital expenditures*	**1,983**	**1,596**	**1,045**	**835**
Acquisitions of subsidiaries**				
Exploration and production				
Russia	199	–	199	–
International	–	–	–	–
Total exploration and production	199	–	199	–
Refining, marketing and distribution				
Russia	1	5	–	5
International	219	289	–	289
Total refining, marketing and distribution	220	294	–	294
Chemicals				
Russia	–	–	–	–
International	–	–	–	–
Total chemicals	–	–	–	–
Other	–	–	–	–
Less cash acquired	(10)	–	–	–
Total acquisitions of subsidiaries	**409**	**294**	**199**	**294**

* Including non-cash transactions.
** Including advances related to acquisitions

The table below shows our capital expenditures included in exploration and production expenditures above on new promising oil regions.

Exploration and production

	1st half of		2nd quarter of	
	2005	2004	2005	2004
	(millions of US dollars)		(millions of US dollars)	
Northern Timan-Pechora	293	183	152	99
Yamal	163	205	77	107
Caspian region	141	27	80	9
Total	**597**	**415**	**309**	**215**

Reconciliation of income before income tax to EBITDA (earnings before interest, taxes, depreciation and amortization)

	1st half of	
	2005	**2004**
Income before income taxes	**3,617**	**2,407**
Add back:		
Depreciation and amortization	601	514
Interest expense	117	143
Interest and dividend income	(37)	(99)
EBITDA	**4,298**	**2,965**

Three months ended June 30, 2005 compared to three months ended June 30, 2004

The table below details certain income and expense items from our consolidated statements of income for the periods indicated. All items are presented in millions of US dollars, except for earnings per share data and percentage of changes to the second quarter of 2004.

	2nd quarter of		Change
	2005	**2004**	**%**
Revenues			
Sales (including excise and export tariffs)	13,492	7,965	69.4%
Equity share in income of affiliates	142	62	129.0%
Total revenues	**13,634**	**8,027**	**69.9%**
Costs and other deductions			
Operating expenses	(717)	(674)	6.4 %
Cost of purchased crude oil, petroleum and chemical products	(4,942)	(2,501)	97.6%
Transportation expenses	(857)	(734)	16.8 %
Selling, general and administrative expenses	(622)	(451)	37.9 %
Depreciation, depletion and amortization	(317)	(266)	19.2 %
Taxes other than income taxes	(1,597)	(818)	95.2 %
Excise and export tariffs	(2,361)	(1,090)	116.6 %
Exploration expense	(147)	(57)	157.9 %
Gain (loss) on disposal and impairment of assets	70	(46)	–
Income from operating activities	**2,144**	**1,390**	**54.2%**
Interest expense	(62)	(75)	(17.3)%
Interest and dividend income	19	57	(66.7)%
Currency translation loss	(73)	(40)	82.5 %
Other non-operating loss	(19)	(42)	(54.8)%
Minority interest	(30)	(21)	42.9 %
Income before income taxes	**1,979**	**1,269**	**55.9%**
Current income taxes	(598)	(401)	49.1%
Deferred income taxes	29	9	–
Total income tax expense	**(569)**	**(392)**	**45.2%**
Net income	**1,410**	**877**	**60.8%**
Per share of common stock (in US dollars):			
Net income			
Basic	1.73	1.07	61.7%
Diluted	1.71	1.06	61.3%

The analysis of the main financial indicators of the financial statements is provided below.

Sales revenues

Sales breakdown	2nd quarter of 2005		2004	
	(millions of US dollars)			
Crude oil				
Export and sales on international markets other than CIS.........	3,996	29.6%	2,481	31.2%
Export and sales to CIS..	140	1.0%	130	1.6%
Domestic sales	49	0.4%	33	0.4%
	4,185	**31.0%**	**2,644**	**33.2%**
Refined products				
Export and sales on international markets				
Wholesale..	5,289	39.1%	2,757	34.6%
Retail..	1,581	11.7%	868	10.9%
Domestic sales				
Wholesale..	1,088	8.1%	789	9.9%
Retail..	466	3.5%	285	3.6%
	8,424	**62.4%**	**4,699**	**59.0%**
Petrochemicals				
Export and sales on international markets................................	319	2.4%	232	2.9%
Domestic sales	116	0.9%	82	1.0%
	435	**3.3%**	**314**	**3.9%**
Other	**448**	**3.3%**	**308**	**3.9%**
Total sales	**13,492**	**100.0%**	**7,965**	**100.0%**

Sales volumes	2nd quarter of 2005		2004	
	(thousands of barrels)			
Crude oil				
Export and sales on international markets other than CIS.........	83,452		78,717	
Export and sales to CIS..	5,049		7,073	
Domestic sales	1,935		2,280	
Crude oil	(thousands of tonnes)			
Export and sales on international markets other than CIS.........	11,385	37.2%	10,739	39.4%
Export and sales to CIS..	689	2.3%	965	3.5%
Domestic sales	264	0.9%	311	1.1%
	12,338	**40.4%**	**12,015**	**44.0%**
Refined products	(thousands of tonnes)			
Export and sales on international markets				
Wholesale..	11,654	38.1%	9,044	33.1%
Retail..	1,870	6.1%	1,232	4.5%
Domestic sales				
Wholesale..	3,821	12.5%	4,337	15.9%
Retail..	888	2.9%	694	2.5%
	18,233	**59.6%**	**15,307**	**56.0%**
Total sales volume of crude oil and refined products..........	**30,571**	**100.0%**	**27,322**	**100.0%**

Realized average sales prices	2nd quarter of			
	2005		2004	
	($/barrel)	($/tonne)	($/barrel)	($/tonne)
Average realized price international				
Oil (excluding CIS)	47.88	350.98	31.51	231.00
Oil (CIS)	27.87	204.26	18.44	135.18
Refined products				
Wholesale		453.76		304.76
Retail		845.73		705.03
Average realized price within Russia				
Oil	25.40	186.19	14.67	107.52
Refined products				
Wholesale		284.79		182.08
Retail		524.81		410.65

During the second quarter of 2005 sales revenues increased by $5,527 million, or 69.4%, compared to the same period of 2004.

The total volume of crude oil and refined products sold amounted to 30.6 million tonnes, which is 11.9% more than that sold in the second quarter of 2004. Our revenues from crude oil sales increased by $1,541 million, or 58.3%. Our sales of refined products increased by $3,725 million, or 79.3%.

Sales of crude oil and refined products on the international markets, including the CIS, accounted for 83.7% of total sales volume in the second quarter of 2005 compared to 80.5% in the second quarter of 2004.

The increase in sales was principally due to the following:

- favorable price conditions (see “Change in the price of crude oil and refined products” on page 4)
- increase in total volume of crude oil production (see “Oil production” on page 8)
- increase in marketing activities (see page 9)
- decrease of crude oil sales in Russia and increase in volumes exported on international markets (see “Export of crude oil and refined products from Russia” on page 10)

Sales of crude oil

During the second quarter of 2005 the Company decreased its sales of crude oil on the domestic market compared to the same period of the previous year by 47 thousand tonnes, or 15.1%. This change was caused by an increase in volumes exported by the Company’s domestic producers and a decrease in crude oil purchases in Russia.

During the second quarter of 2005 we increased exports of crude oil on international markets by the Company’s domestic producers by 317 thousand tonnes. The increase in export sales, along with an increase in the average realized export price of crude oil on international markets (other than CIS) from $31.51 to $47.88 per barrel, allowed us to obtain an additional $1,428 million in revenues.

Sales of refined products

Sales of refined products made up 62.4% of our total sales revenues (59.6% in terms of volumes sold) compared to 59.0% (56.0% – in terms of volumes) in the second quarter of 2004. The portion of our domestic refined product sales in the second quarter of 2005 was 15.4% of total tonnes sold (the second quarter of 2004: 18.4%), but represented 11.6% of our total sales revenue (the second quarter of 2004: 13.5%).

The average realized wholesale price on refined products outside of Russia increased by $149.00 per tonne, or 48.9%, compared to the second quarter of 2004. Volumes of refined products sold outside of Russia increased by 2,610 thousand tonnes, or 28.9% (see also “Refining and marketing” on page 9). As a result, our revenues from wholesale of refined products outside of Russia increased by $2,532 million, or 91.8%.

In the second quarter of 2005 retail sales of refined products outside of Russia increased by 638 thousand tonnes, or by 51.8%, compared to the same period of 2004. The increase was a result of continuing development of the existing retail chains outside of Russia and structural changes in the retail network we operate. In particular, in May 2004 we acquired an additional retail network in the USA, and in March

2005 we acquired retail network in Finland. Average retail prices increased up to $845.73 per tonne, or by 20.0%. As a result, our revenues from retail sales increased by $713 million, or 82.1%. In the second quarter of 2005 revenue from retail sales was 23.0% of total sales of refined products outside of Russia. Our international retail sales include supplies of refined products to third parties' retail networks within the bounds of long-term contracts with pricing similar to retail pricing.

Wholesale of refined products within Russia in the second quarter of 2005 decreased by 516 thousand tonnes, or 11.9%, as compared to the same period in 2004. The average domestic realized price on refined products increased by $102.71 per tonne, or 56.4%. As a result, our revenues from wholesale of refined products on the domestic market increased by $299 million, or 37.9%.

Retail sales within Russia in the second quarter of 2005 increased by 194 thousand tonnes, or 28.0%, compared to the same period in 2004. Average retail prices increased up to $524.81 per tonne, or by 27.8%. As a result, our revenues from retail sales increased by $181 million, or 63.5%. Revenue from retail sales was 30.0% of total sales of refined products in Russia in the second quarter of 2005.

Sales of petrochemical products

Revenues from sales of petrochemical products increased by $121 million, or 38.5%, during the second quarter of 2005. This was mainly due to an increase of production volume up to 573 thousand tonnes, or by 8.3%, compared to the same period in 2004, and an increase in average realized prices.

Sales of other products

Other sales increased by $140 million, or 45.5%, as a result of sales of other products produced by the Company, and also increased activity in providing other services to third parties.

Equity share in income of affiliates

Our share in the income of affiliates in the second quarter of 2005 increased by $80 million, or 129.0%, compared to the second quarter of 2004, primarily due to an increase in the net income of ZAO Turgai-Petroleum. ZAO Turgai-Petroleum, our 50% interest affiliate company, is a partner in the Turgai-Petroleum joint venture developing the Kumkol oil field in Kazakhstan. The Group's share in the net income of ZAO Turgai-Petroleum in the second quarter of 2005 amounted $102 million that represents an increase of $74 million as compared to the same period of the previous year.

Operating expenses

Operating expenses include the following types of costs:

	2nd quarter of	
	2005	**2004**
	(millions of US dollars)	
Extraction expenses	434	381
Refining expenses	174	123
Petrochemical expenses	45	44
Other operating expenses	64	126
Total operating expenses	**717**	**674**
Cost of purchased crude oil, petroleum and chemical products	**4,942**	**2,501**

Compared to the second quarter of 2004, operating expenses increased by $43 million, or 6.4%.

In the second quarter of 2005 our **extraction expenses** rose by $53 million, or 13.9%, compared to the same period of 2004. The increase resulted from growth of crude oil produced by our subsidiaries up to 21.3 million tonnes, or by 4.8%, compared to the second quarter of 2004, and additional expenses on repairs and overhaul in our production subsidiaries and increased expenses of artificial stimulation of reservoirs in the second quarter of 2005. Moreover, extraction costs were affected by real ruble appreciation of 14.7% during the year ended June 30, 2005. However, the impact of these factors was mitigated by an increase of average well debits from 10.6 tonnes a day in the first half of 2004 to 11.0 tonnes a day in the first half of 2005 and improved cost control. As a result our average extraction cost per barrel increased from $2.55 to $2.77 per barrel, or by 8.6% (average extraction cost calculated using an average tonnes to barrels conversion rate of 7.33).

Refining expenses at our refineries increased by $51 million, or 41.5%, in the second quarter of 2005 compared to the second quarter of 2004.

Refining expenses of our domestic refineries increased by 27.8%, or $25 million, primarily as a result of real ruble appreciation. Moreover in late 2004 we began changing product mix in order to produce higher quality and more profitable products (in particular, Euro 4 quality standard diesel oil) which led to an increase of our refinery expenses.

Refining expenses of our international refineries increased by 78.8%, or $26 million, as a results of an overall increase in volumes produced and the recommencement of operations of our Romanian refinery Petrotel-LUKOIL after modernization.

Operating expenses of petrochemical companies increased by $1 million, or 2.3%, compared to the second quarter of 2004.

Other operating expenses decreased by $62 million, or 49.2%, as compared to the second quarter of 2004 primarily as a result of change in crude oil and refined products inventory originated within the Group in the second quarter of 2005.

Cost of purchased crude oil, petroleum and chemical products increased by $2,441 million in the second quarter of 2005, or 97.6%, compared to the same period of the previous year due to a significant increase in volumes of crude oil and refined products purchased for resale in the second quarter of 2005 by 3,005 thousand tonnes and growth of market prices on crude oil and petroleum products.

Transportation expenses

The increase in the total volume of sales together with the increase in transportation tariffs led to growth of transportation expenses in the second quarter of 2005 by $123 million, or 16.8%, compared to the second quarter of 2004.

Selling, general and administrative expenses

Our selling, general and administrative expenses increased by $171 million, or 37.9%, compared to the second quarter of 2004 as a result of general expansion of our operations and real ruble appreciation of 14.7% during the twelve months period ended June 30, 2005. Also, in the second quarter of 2005 the Company accrued $55 million of compensation to management in relation to its share-based compensation program, compared to $14 million in the same period of 2004.

Also, selling, general and administrative expenses for the three months ended June 30, 2005 included $23 million of expenses related to our Finnish subsidiaries acquired in March 2005 (see page 2).

Depreciation, depletion and amortization

Depreciation, depletion and amortization expenses increased by $51 million, or 19.2%, compared to the second quarter of 2004. The increase was a result of the Company’s capital expenditure program and corresponding growth of depreciable assets. This increase was partly compensated by upward revisions of the Company’s proved reserves and, consequently, an increase in estimated useful economic life of fixed assets.

Taxes other than income taxes

The increase in taxes other than income taxes resulted primarily from a $604 million increase in mineral extraction tax, which is linked to international crude oil prices (see "Change in tax rates and export tariffs" on page 5). In the first half of 2005 the Group accrued a provision in relation to the results of tax audits of the Group companies for periods prior to the 2004 financial year. The amount of provision related to taxes was approximately $150 million.

	2nd quarter of			
	2005		2004	
	In Russia	International	In Russia	International
	(millions of US dollars)			
Mineral extraction tax	1,284	–	680	–
Social security taxes and contributions	86	9	73	5
Property tax	39	6	30	5
Other taxes	164	9	18	7
	1,573	**24**	**801**	**17**
Total		**1,597**		**818**

Excise and export tariffs

Excise and export tariffs increased by $1,271 million, or 116.6%, compared to the second quarter of 2004. The increase in export tariff expenses resulted from an increase in export tariff rates (see "Change in tax rates and export tariffs" on page 5) and also an increase in volumes exported. The increase in international excise taxes on refined products resulted from an increase in volumes of products sold across our international group, primarily in the USA, and due to commencement of our operations in Finland.

	2nd quarter of			
	2005		2004	
	In Russia	International	In Russia	International
	(millions of US dollars)			
Excise tax and sales taxes on refined products	163	728	132	436
Export tariffs	1,469	1	519	3
	1,632	**729**	**651**	**439**
Total		**2,361**		**1,090**

Exploration expenses

During the second quarter of 2005 the amount charged to exploration expense increased in comparison with the same period of the previous year by $90 million, or by 157.9%. This is attributable to the fact that during the second quarter of 2005 the Group completed drilling the first exploratory wells of the Yalama (D-222) and Tyub-Karagan exploration projects. Both exploratory wells were dry and their costs in amount of $102 million were charged to expense. Notwithstanding the fact that the initial exploratory wells were not successful, the Group continues to perform further geological studies and is using the results of the first exploratory drilling in its analysis to assess potential placement of hydrocarbon deposits and to determine drilling programs for the second exploratory wells in both fields. The Group expects to complete this assessment by the end of 2005.

Gain on disposal and impairment of assets

Gain on disposal and impairment of assets in the second quarter of 2005 was $70 million compared to $46 million loss in the second quarter of 2004.

In the second quarter of 2005 we recognized a gain of $87 million on the sale of 30% of our shares in OOO Narianmarneftegaz to ConocoPhillips. In the second quarter of 2005 the Group also recognized a gain of $4 million in relation to sale of its 38% interest in ZAO Globalstroy-Engineering.

In the second quarter of 2004 we recognized an impairment loss in relation to our decision to sell our ownership interests in OAO Bank Petrocommerce in the amount of $35 million.

Interest expense

Interest expense in the second quarter of 2005 decreased by $13 million compared to the same period of 2004 primarily due to the sale of our ownership interest in OAO Bank Petrocommerce in the third quarter of 2004.

Income taxes

Our total income tax expense increased by $177 million, or 45.2%, compared to the same period of 2004, due to an increase of income before income tax by $710 million, or 55.9%.

Our effective tax rate in the second quarter of 2005 was 28.8% (in the second quarter of 2004 it was 30.9%), which is higher than the maximum statutory rate for the Russian Federation (24%). This is attributable to the fact that some costs incurred during the period are not tax deductible or only deductible to a certain limit.

Reconciliation of income before income tax to EBITDA (earnings before interest, taxes, depreciation and amortization)

	2nd quarter of	
	2005	**2004**
Income before income taxes	**1,979**	**1,269**
Add back:		
Depreciation and amortization	317	266
Interest expense	62	75
Interest and dividend income	(19)	(57)
EBITDA	**2,339**	**1,553**