OAO NOVATEK

IFRS CONSOLIDATED FINANCIAL STATEMENTS

AND INDEPENDENT AUDITOR'S REPORT

FOR THE YEARS ENDED 31 DECEMBER 2007 AND 2006

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INDEPENDENT AUDITOR'S REPORT

To the shareholders and directors of OAO NOVATEK:

1 We have audited the accompanying consolidated financial statements of OAO NOVATEK and its subsidiaries (the "Group") set out on pages 4 to 48 which comprise the consolidated balance sheet as at 31 December 2007 and the consolidated statement of income, consolidated statement of cash flows and consolidated statement of changes in equity for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

2 Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

3 Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

4 An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

5 We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

6 In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2007, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

Moscow, Russian Federation
18 April 2008

OAO NOVATEK
Consolidated Balance Sheet
(in millions of Russian roubles)

	Notes	At 31 December: 2007	2006
ASSETS			
Non-current assets			
Property, plant and equipment	6	82,669	66,734
Investments in associates		1,125	-
Long-term loans and receivables		681	331
Other non-current assets		2,462	1,774
Total non-current assets		**86,937**	**68,839**
Current assets			
Inventories	7	1,794	1,815
Current income tax prepayments		335	940
Trade and other receivables	8	3,267	2,213
Prepayments and other current assets	9	7,660	4,851
Cash and cash equivalents	10	3,982	5,668
Total current assets		**17,038**	**15,487**
Total assets		**103,975**	**84,326**
LIABILITIES AND EQUITY			
Non-current liabilities			
Long-term debt	11	42	543
Deferred income tax liabilities	21	8,083	8,412
Other non-current liabilities		905	816
Asset retirement obligations		1,058	781
Total non-current liabilities		**10,088**	**10,552**
Current liabilities			
Short-term debt and current portion of long-term debt	13	6,560	2,565
Trade payables and accrued liabilities	14	3,599	1,801
Current income tax payable		645	48
Other taxes payable		1,271	684
Total current liabilities		**12,075**	**5,098**
Total liabilities		**22,163**	**15,650**
Equity attributable to OAO NOVATEK shareholders			
Ordinary share capital		393	393
Additional paid-in capital		30,257	30,081
Asset revaluation surplus on acquisitions		5,617	5,617
Retained earnings		45,068	32,229
Total equity attributable to OAO NOVATEK shareholders	15	**81,335**	**68,320**
Minority interest		**477**	**356**
Total equity		**81,812**	**68,676**
Total liabilities and equity		**103,975**	**84,326**

The accompanying notes are an integral part of these consolidated financial statements.

Approved for issue and signed on behalf of the Board of Directors on 18 April 2008:

L. Mikhelson
General Director

M. Gyetvay
Financial Director

	Notes	Year ended 31 December: 2007	2006
Revenues			
Oil and gas sales	16	60,357	48,047
Sales of polymer and insulation tape		1,602	1,109
Other revenues		362	217
Total revenues		**62,321**	**49,373**
Net gain on disposal of interest in subsidiaries	5	95	9
Other income (loss)		15	(148)
Total revenues and other income		**62,431**	**49,234**
Operating expenses			
Transportation expenses	17	(14,372)	(11,362)
Taxes other than income tax	18	(6,379)	(6,223)
Materials, services and other	19	(4,924)	(3,893)
Depreciation, depletion and amortization	6	(3,668)	(3,671)
General and administrative expenses	20	(3,873)	(3,165)
Purchases of oil, gas condensate and natural gas		(3,242)	(1,805)
Exploration expenses		(486)	(459)
Net impairment expense		(153)	(100)
Changes in inventories		31	597
Total operating expenses		**(37,066)**	**(30,081)**
Profit from operations		**25,365**	**19,153**
Finance income (expense)			
Interest expense		(263)	(516)
Interest income		376	274
Foreign exchange gain (loss)		11	211
Total finance income (expense)		**124**	**(31)**
Profit before income tax		**25,489**	**19,122**
Income tax expense			
Current income tax expense		(7,301)	(5,527)
Net deferred income tax benefit		540	412
Total income tax expense	21	**(6,761)**	**(5,115)**
Profit for the year		**18,728**	**14,007**
Profit (loss) attributable to:			
Minority interest		(8)	(72)
Shareholders of OAO NOVATEK		**18,736**	**14,079**
Basic and diluted earnings per share (in Russian roubles)		6.17	4.64
Weighted average number of shares outstanding (in thousands)		*3,036,306*	*3,036,306*

The accompanying notes are an integral part of these consolidated financial statements.

(in millions of Russian roubles)

	Notes	Year ended 31 December: 2007	2006
Profit before income tax		**25,489**	**19,122**
Adjustments to profit before income tax:			
Depreciation, depletion and amortization		3,734	3,728
Net impairment expense		153	100
Net foreign exchange loss (gain)		(11)	(211)
Net loss (gain) on disposal of assets		(93)	223
Share-based compensation	25	176	176
Interest expense		263	516
Interest income		(376)	(274)
Net change in other non-current assets		(178)	(65)
Other adjustments		24	(91)
Working capital changes			
Decrease (increase) in trade and other receivables, prepayments and other current assets		(4,048)	(506)
Decrease (increase) in inventories		(94)	(409)
Increase (decrease) in trade payables and accrued liabilities, excluding interest and dividends		1,856	600
Increase (decrease) in other taxes payable		587	(217)
Total effect of working capital changes		**(1,699)**	**(532)**
Income taxes paid		(6,099)	(5,754)
Net cash provided by operating activities		**21,383**	**16,938**
Cash flows from investing activities			
Purchases of property, plant and equipment		(19,043)	(4,439)
Purchases of tangible assets		(623)	(331)
Acquisition of subsidiaries, associates and minority interests, net of cash acquired		(989)	(184)
Proceeds from disposals of subsidiaries, associates and minority interests, net of cash disposed		5	45
Interest paid and capitalized		(139)	(287)
Loans provided		(423)	(153)
Repayments of loans provided		83	39
Interest received		382	269
Net cash (used for) provided by investing activities		**(20,747)**	**(5,041)**
Cash flows from financing activities			
Proceeds from long-term debt		-	2,689
Proceeds from short-term debt		5,448	3,734
Repayments of long-term debt		(2,293)	(7,428)
Repayments of short-term debt		(862)	(4,437)
Interest paid		(111)	(305)
Dividends paid	15	(5,860)	(3,290)
Net cash (used for) provided by financing activities		**(3,678)**	**(9,037)**
Net effect of exchange rate changes on cash, cash equivalents and bank overdrafts		(12)	(148)
Net increase (decrease) in cash, cash equivalents and bank overdrafts		**(3,054)**	**2,712**
Cash and cash equivalents at beginning of the year		5,668	2,956
Cash, cash equivalents and bank overdrafts at end of the year		**2,614**	**5,668**

The accompanying notes are an integral part of these consolidated financial statements.

OAO NOVATEK
Consolidated Statement of Changes in Equity
(in millions of Russian roubles, except for number of shares)

	Number of ordinary shares (in thousands)	Ordinary share capital	Additional paid in capital	Asset revaluation surplus	Retained earnings	Equity attributable to OAO NOVATEK shareholders	Minority interest	Total equity
At 31 December 2005	***3,036,306***	**393**	**29,905**	**5,481**	**21,489**	**57,268**	**281**	**57,549**
Dividends (Note 15)	-	-	-	-	(3,258)	(3,258)	-	(3,258)
Acquisitions of subsidiaries	-	-	-	136	-	136	203	339
Purchase of minority interest	-	-	-	-	(81)	(81)	(197)	(278)
Impact of additional shares subscription in subsidiaries on minority interest	-	-	-	-	-	-	141	141
Share-based compensation funded by shareholders	-	-	176	-	-	176	-	176
Profit (loss) for the year	-	-	-	-	14,079	14,079	(72)	14,007
At 31 December 2006	***3,036,306***	**393**	**30,081**	**5,617**	**32,229**	**68,320**	**356**	**68,676**
Dividends (Note 15)	-	-	-	-	(5,860)	(5,860)	-	(5,860)
Purchase of minority interest	-	-	-	-	(37)	(37)	(111)	(148)
Impact of additional shares subscription in subsidiaries on minority interest	-	-	-	-	-	-	240	240
Share-based compensation funded by shareholders	-	-	176	-	-	176	-	176
Profit (loss) for the year	-	-	-	-	18,736	18,736	(8)	18,728
At 31 December 2007	***3,036,306***	**393**	**30,257**	**5,617**	**45,068**	**81,335**	**477**	**81,812**

The accompanying notes are an integral part of these consolidated financial statements.

1 ORGANISATION AND PRINCIPAL ACTIVITIES

OAO NOVATEK (hereinafter referred to as “NOVATEK”) and its subsidiaries (hereinafter jointly referred to as the “Group”) is an independent oil and gas company engaged in the acquisition, exploration, development, production and processing of hydrocarbons with its core operations of oil and gas properties located and incorporated in the Yamal-Nenets Autonomous Region (“YNAO”) of the Russian Federation.

The Group sells its natural gas on the Russian domestic market at both regulated and unregulated market prices, however the majority of natural gas sold on the domestic market is sold at prices regulated by the Federal Tariff Service, a governmental agency. The Group’s stable gas condensate and crude oil sales are sold on both the Russian domestic and international markets, and are subject to fluctuations in benchmark crude oil prices. Additionally, the Group’s natural gas sales fluctuate on a seasonal basis due mostly to Russian weather conditions, with sales peaking in the winter months of December and January and decreasing in the summer months of July and August. The Group’s liquids sales volumes comprising stable gas condensate, crude oil and oil products remain relatively stable from period to period.

2 BASIS OF PRESENTATION

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”). In the absence of specific IFRS guidance for oil and gas producing companies, the Group has developed accounting policies in accordance with other generally accepted accounting principles for oil and gas producing companies, mainly US GAAP, insofar as they do not conflict with IFRS principles.

The Group entities maintained their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation (“RAR”). The Group’s consolidated financial statements are based on the statutory records with adjustments and reclassifications recorded in the consolidated financial statements for the fair presentation in accordance with IFRS. The principal adjustments primarily relate to (1) depreciation, depletion and amortization, and valuation of property, plant and equipment, (2) consolidation of subsidiaries, (3) business combinations, (4) accounting for income taxes, and (5) valuation of unrecoverable assets, expense recognition and other provisions.

The consolidated financial statements have been prepared under the historical cost convention and are presented in Russian roubles. The assets and liabilities of the Group entities whose functional currency is not the Russian rouble are remeasured into Russian roubles at the exchange rate at the balance sheet date. The financial results of these entities are remeasured into Russian roubles using average exchange rates for the reporting periods. Exchange adjustments arising on the opening net assets and the profits for the reporting period are taken to a separate component of equity and reported in the consolidated statement of changes in equity.

Exchange rates, restrictions and controls. The official rate of exchange of the Russian rouble to the US dollar (“USD”) at 31 December 2007 and 2006 was 24.55 and 26.33 Russian roubles to USD 1.00, respectively. The official rate of exchange of the Russian rouble to the Euro at 31 December 2007 and 2006 was 35.93 and 34.70 Russian roubles to 1.00 Euro, respectively. Any re-measurement of Russian rouble amounts to US dollars or any other currency should not be construed as a representation that such Russian rouble amounts have been, could be, or will in the future be converted into other currencies at these exchange rates.

Through early 2006, the Russian rouble was not a convertible currency in most countries outside of the former Soviet Union and, further, the Group was required to convert 10 percent of its hard currency proceeds into Russian roubles. During the first half of 2006, substantially all restrictions for hard currency transactions were lifted and the rights of the government of the Russian Federation and those of the Central Bank of the Russian Federation to impose such restrictions were waived.

2 BASIS OF PRESENTATION (CONTINUED)

Reclassifications. The following reclassifications have been made to the comparative figures to conform to the current period presentation. Commencing January 2007, liquefied petroleum gas sales and oil products sales are presented gross of rail transportation costs. Accordingly, liquefied petroleum gas sales and oil products sales for the year ended 31 December 2006 were increased by RR 534 million and RR 25 million, respectively. Correspondingly, stable gas condensate, liquefied petroleum gas, and oil products transportation expenses by rail were increased by RR 559 million.

At 31 December 2006, RR 331 million of materials and supplies intended for construction of fixed assets were reclassified from inventories to other non-current assets. Also, RR 664 million of recoverable value-added tax was reclassified from trade and other receivables to prepayments and other current assets. The reclassifications were made to conform to the current year presentation.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation. The accompanying consolidated financial statements include the operations of all controlled companies in which NOVATEK directly or indirectly owns more than 50 percent of the voting stock or otherwise has the power to govern the financial and operating policies. Subsidiaries are consolidated from the date on which control is obtained unless the acquisition occurred between entities under common control, which are accounted for from the beginning of the earliest period presented. Subsidiaries are no longer consolidated from the date that control ceases. Except for the acquisition of entities under common control, the purchase method of accounting is used to account for the acquisition of subsidiaries.

Upon achieving a controlling interest in an entity in which the Group previously held a non-controlling interest, the acquiree's identifiable assets, liabilities and contingent liabilities are restated to their fair values as at the date of achieving control. The effect of revaluing previously held interests to current fair values is recorded within asset revaluation surplus in the consolidated statement of changes in equity.

Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

All intercompany transactions, balances and unrealized gains on transactions between the Group entities are eliminated. Unrealized losses are also eliminated upon consolidation, but in the case where an asset is transferred with a loss amongst the Group entities, this event is considered by management as an impairment indicator for that asset.

Minority interest is that part of the net results and of the net assets of a subsidiary, including the fair value adjustments, which is attributable to interests which are not owned, directly or indirectly, by NOVATEK. Minority interest forms a separate component of the Group's equity.

Acquisition of minority interests. For accounting of acquisitions of non-controlling minority stakes, the difference between the purchase consideration and the carrying amount of minority interests acquired is recognized within retained earnings.

Investments in associates. Associated companies are entities over which the Group has significant influence, but which it does not control. Generally, significant influence exists when the Group has between 20 and 50 percent of voting rights. On acquisition of the associated company the difference between the cost of an acquisition and the share of the fair value of the associate's identifiable net assets represents goodwill. Associated companies are accounted for using the equity method and are initially recognized at cost. After the date of acquisition the carrying amount of the investment is increased or decreased to recognize the Group's share of the profit or loss of the investee. The carrying amount of associates includes goodwill identified on acquisition less accumulated impairment losses, if any. The Group's share of the post-acquisition profits or losses of associates is recorded in the consolidated statement of income, and its share of post-acquisition movements in reserves is recognized in the consolidated statement of changes in equity. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the associate.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Unrealized gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates; unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

Goodwill. Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets of the acquired subsidiary/associate at the date of acquisition. Goodwill on an acquisition of a subsidiary is included in other non-current assets and is tested annually for impairment and carried at cost less accumulated impairment losses, if any. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold. Goodwill on an acquisition of an associate is included in the investments in associates and is tested for impairment as part of the overall investment balance.

Goodwill is allocated to the cash-generating units, or Groups of cash-generating units, that are expected to benefit from the synergies of the business combination. Such units or Group of units represent the lowest level at which the Group monitors goodwill and are not larger than a segment. Gains or losses on disposal of an operation within a cash generating unit to which goodwill has been allocated include the carrying amount of goodwill associated with the operation disposed of, generally measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit which is retained.

Property, plant and equipment. Property, plant and equipment are carried at historical cost of acquisition or construction and adjusted for accumulated depreciation, depletion, amortization and impairment.

The Group follows the successful efforts method of accounting for its oil and gas properties and equipment whereby property acquisitions, successful exploratory wells, all development costs and support equipment and facilities are capitalized. Unsuccessful exploratory wells are charged to expense at the time the wells are determined to be non-productive. Production costs, overheads and all exploration costs other than exploratory drilling are charged to expense as incurred. Acquisition costs of unproved properties are evaluated periodically and any impairment assessed is charged to expense.

The Group's principal reserves have been independently estimated by internationally recognized petroleum engineers. Other oil and gas reserves of the Group have been determined based on estimates of mineral reserves prepared by management in accordance with internationally recognized definitions. The present value of the estimated costs of dismantling oil and gas production facilities, including abandonment and site restoration costs, are recognized when the obligation is incurred and are included within the carrying value of property, plant and equipment, subject to depletion using the unit-of-production method.

Costs of minor repairs and maintenance are expensed when incurred. Cost of replacing major parts or components that extend the life of property, plant and equipment items are capitalized and depreciated over their estimated useful life.

The cost of self-constructed assets includes the cost of direct materials, direct employee related costs, a pro-rata portion of depreciation of assets used for construction and an allocation of the Group's overhead costs.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

At each reporting date management assess whether there is any indication of impairment in respect of property, plant and equipment. If any such indication exists, management estimates the recoverable amount, which is determined as the higher of an asset's fair value less costs to sell and its value in use. The carrying amount is reduced to the recoverable amount and the impairment loss is recognized in the consolidated statement of income. An impairment loss recognized for an asset in prior years is reversed if there has been a change in the estimates used to determine the asset's recoverable amount.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. Gains and losses are recognized in the consolidated statement of income.

Exploration costs. Exploration costs (geological and geophysical expenditures, expenditures associated with the maintenance of non-proven reserves and other expenditures relating to exploration activity), excluding exploratory drilling expenditures and license acquisition costs, are charged to the consolidated statement of income as incurred. License acquisition costs and exploratory drilling costs are recognized as assets until it is determined whether proved reserves justifying their commercial development have been found. If no proved reserves are found, the capitalized drilling costs are charged to the consolidated statement of income. License acquisition costs and exploratory drilling costs recognized as assets are reviewed for impairment on an annual basis.

Depreciation. Depreciation, depletion and amortization of oil and gas properties and equipment (except for processing facilities) is calculated using the unit-of-production method for each field based upon proved developed reserves for development costs, and total proved reserves for costs associated with acquisitions of proved properties. Reserve amounts used for depreciation, depletion and amortization calculations include reserves expected to be produced beyond license expiry dates. Management believes that there is requisite legislation to extend mineral licenses at the initiative of the Group and, as such, intends to extend its licenses for properties expected to produce beyond the current license expiry dates.

Property, plant and equipment, other than oil and gas properties and equipment, are depreciated on a straight-line basis over their estimated useful lives. Land and assets under construction are not depreciated.

The estimated useful lives of the Group's property, plant and equipment, other than oil and gas properties and equipment, are as follows:

	Years
Machinery and equipment	5-15
Processing facilities	20-30
Buildings	25-50

Derivative instruments. The Group accounts for derivative instruments in accordance with IAS 39, *Financial Instruments: Recognition and Measurement* ("IAS 39"). All derivative instruments are recorded in the balance sheet at their fair values. Under IAS 39, in order to consider these derivative instruments as hedges for accounting purposes, management must formally designate the derivative instrument as a hedge of variability in future cash flows or fair values, normally arising from the Group's exposure to foreign currency exchange rates and oil price fluctuations. Changes in the market values of the derivative instruments treated as cash flow hedges, to the extent that they are effective hedges, are not recognized in income until the hedged item affects income. If the above designation and effectiveness criteria are not met, any unrealized gains and losses on derivative instruments are recorded immediately in the consolidated statement of income.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Adoption of IFRS 7. Effective 1 January 2007, the Group adopted IFRS 7, *Financial Instruments: Disclosures* ("IFRS 7"). IFRS 7 introduced new disclosures to improve the information about financial instruments with an emphasis on quantitative aspects of risk exposures and the methods of risk management. The quantitative disclosures provide information about the extent to which the entity is exposed to risk, based on information provided internally to the entity's key management personnel. Qualitative and quantitative disclosures cover exposure to credit risk, liquidity risk and market risk including sensitivity analysis to market risk. IFRS 7 replaced IAS 30, *Disclosures in the Financial Statements of Banks and Similar Financial Institutions*, and some of the requirements in IAS 32, *Financial Instruments: Disclosure and Presentation*. In addition, the Amendments to IAS 1, *Presentation of Financial Statement,* introduced new disclosures about the level of an entity's capital and how it manages capital.

Effective interest method. The effective interest method is a method of calculating the carrying value of a financial asset or a financial liability held at amortized costs and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts future cash payments and receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying value of the financial asset or financial liability.

Financial assets. The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss, held-to-maturity, loans and receivables, and available-for-sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition. Subsequent reclassification of financial assets is made only as a result of a change in intention or ability of management to hold the financial assets. Financial assets are recognized initially at fair value, normally being the transaction price plus, in the case of financial assets not at fair value through profit or loss, directly attributable transaction costs. The subsequent measurement of financial assets depends on their classification.

(a) Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term. Derivative instruments are also categorized as held for trading unless they are designated as hedges. Financial assets carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the consolidated statement of income. Gains or losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are presented in the consolidated statement of income within other income (loss) in the period in which they arise. Dividend income from financial assets at fair value through profit or loss is recognized in the consolidated statement of income as part of other income when the Group's right to receive payments is established.

Financial assets at fair value through profit or loss are classified as current assets. There were no financial assets designated at fair value through profit or loss held by the Group at the reporting dates.

(b) Held-to-maturity investments

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities and are classified as held-to-maturity when the Group has the positive intention and ability to hold these investments to maturity. After initial measurement held-to-maturity investments are measured at amortized cost using the effective interest method. Gains and losses are recognized in the consolidated statement of income when the investments are derecognized or impaired, as well as through the amortization process.

Held-to-maturity investments are included in current assets, except for maturities greater than 12 months after the balance sheet date. These are classified as non-current assets. There were no such investments held by the Group at the reporting dates.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Financial assets classified as loans and receivables are carried at amortized cost using the effective interest method. Gains and losses are recognized in the consolidated statement of income when the loans and receivables are derecognized or impaired, as well as through the amortization process.

Loans and receivables are included in current assets, except for maturities greater than 12 months after the balance sheet date which are classified as non-current assets.

(d) Available-for-sale financial assets

Financial assets classified as available-for-sale are non-derivatives financial assets that are either specially designated in this category or are not classified in any of the other categories. After initial recognition, financial assets classified as available-for-sale are measured at fair value, with gains and loses recognized directly in the consolidated statement of changes in equity until the investment is derecognized or determined to be impaired, at which time the cumulative gain or loss previously recorded in equity is recognized in profit or loss.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available-for-sale financial assets are analyzed between translation differences resulting from changes in amortized cost of the security and other changes in the carrying amount of the security. The translation differences on monetary securities are recognized in profit or loss, while translation differences on non-monetary securities are recognized in equity. Changes in the fair value of monetary and non-monetary securities classified as available-for-sale are recognized in equity. When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognized in equity are included in the consolidated statement of income as profit or loss on sales of available-for-sale investments.

The Group assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss (measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in profit or loss) is removed from equity and recognized in the consolidated statement of income. Impairment losses recognized in the consolidated statement of income on equity instruments are not reversed. There was no available-for-sale investments held by the Group at the reporting dates.

Financial liabilities. Financial liabilities are classified at initial recognition as either financial liabilities at fair value through profit or loss, derivative instruments designated as hedging instruments in an effective hedge or as financial liabilities measured at amortized cost. The measurement of financial liabilities depends on their classification, as follows:

(a) Financial liabilities at fair value through profit or loss

Derivative instruments, other than those designated as effective hedging instruments, are classified as held for trading and are included in this category. These financial liabilities are carried on the balance sheet at fair value with gains or losses recognized in the consolidated statement of income. There were no financial liabilities designated at fair value through profit or loss held by the Group at the reporting dates.

(b) Financial liabilities measured at amortized cost

All other financial liabilities are included in this category and initially recognized at fair value. For interest-bearing debt, the fair value of the liability is the fair value of the proceeds received net of associated issue costs. After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest method. This category of financial liabilities includes trade and other payables and debt.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Income taxes. Income taxes have been provided for in the consolidated financial statements in accordance with Russian legislation enacted or substantively enacted as of end of the reporting period. The income tax charge or benefit comprises current tax and deferred tax and is recognized in the consolidated statement of income unless it relates to transactions that are recognized, in the same or a different period, directly in equity.

Current tax is the amount expected to be paid to or recovered from the tax authorities in respect of taxable profits or losses for the current and prior periods.

Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or when the tax loss carry forwards will be utilized. Deferred tax assets and liabilities are netted only with respect to individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilized. The realization if deferred tax assets are assessed based on several interrelated factors. These factors include the Group’s expectation to generate sufficient future taxable income and the projected time period over which these deferred tax assets will be realized.

Deferred income tax is provided on post acquisition retained earnings of subsidiaries, except where the Group controls the subsidiary’s dividend policy and it is probable that the difference will not reverse through dividends or otherwise in the foreseeable future.

Inventories. Natural gas, gas condensate, crude oil and related products inventories are valued at the lower of cost or net realizable value. The cost of inventories includes applicable purchase costs of raw materials, direct operating costs, and related production overhead expenses and is recorded on a first-in-first-out (FIFO) basis. Net realizable value is the estimate of the selling price in the ordinary course of business, less selling expenses.

Starting from 1 January 2007, the Group changed its accounting policy for accounting of inventories cost from the weighted average method to FIFO. The cumulative effect of the retrospective application of the new policy was not material. Management believes that the new inventory methodology is more precise in transferring costs of inventory purchases to the consolidated statement of income and more fairly presents the reported inventory balances in the consolidated balance sheet of the Group.

Materials and supplies inventories are carried at amounts which do not exceed their respective recoverable amounts in the normal course of business.

Trade and other receivables. Trade receivables are represented by amounts due from regular customers in the ordinary course of business (production and marketing of natural gas, gas condensate, crude oil and related products; production and marketing of polymer and insulation tape products). Trade and other receivables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method and include value-added taxes. Trade receivables are analyzed for impairment on a debtor by debtor basis. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the asset’s carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The amount of the provision is recognized in the consolidated statement of income within operating expenses. Subsequent recoveries of amounts previously written off are credited against amount of the provision in the consolidated statement of income.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and cash equivalents. Cash and cash equivalents comprises cash on hand, cash deposits held with banks, investments which are readily convertible to known amounts of cash and which are not subject to significant risk of change in value and have an original maturity of three months or less. For purposes of the presentation of the statement of cash flows, bank overdrafts are deducted from cash and cash equivalents.

Treasury shares. Repurchased shares of NOVATEK are classified as treasury shares and are presented in the consolidated balance sheet as a deduction from total equity. Treasury shares are recorded at weighted average cost, gains or losses resulting from subsequent sales of shares are recorded in the consolidated statement of changes in equity, net of associated costs including taxation. There were no treasury shares held by the Group at the reporting dates.

Dividends. Dividends are recognized as a liability and deducted from shareholders' equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the consolidated financial statements are authorized for issue.

Value added tax (VAT). Output VAT related to sales is payable to the tax authorities on the earlier of (a) collection of the receivables from customers or (b) delivery of the goods or services to customers. Input VAT related to purchases is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis. VAT related to sales and purchases which is not settled or recovered at the balance sheet date (VAT payable and VAT recoverable) is recognized on a gross basis and disclosed separately as current asset and current liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

Borrowings. Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the consolidated statement of income over the period of the borrowings using the effective interest method.

Interest costs on borrowings to finance the construction of property, plant and equipment are capitalized during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

Trade and other payables. Trade payables are accrued when the counterparty performed its obligations under the contract. Trade payables are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

Provisions for liabilities and charges. Provisions are recognized when the Group has a present legal or constructive obligation as a result of past events and when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognized even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be low.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. Provisions are reassessed at each reporting date and changes in the provisions resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Where the Group expects a provision to be reimbursed, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Asset retirement obligations. An asset retirement obligation is recognized when the Group has a present legal or constructive obligation to dismantle, remove and restore items of property, plant and equipment. The amount of the obligation is the present value of the estimated expenditures expected to be required to settle the obligation, determined using discount rates reflecting adjustments for risks specific to the obligation. Changes in the obligation resulting from the passage of time are recognized in the consolidated statement of income as interest expense. Changes in the obligation, reassessed at each balance sheet date, related to a change in the expected pattern of settlement of the obligation, or in the estimated amount of the obligation or in the discount rates, are treated as a change in an accounting estimate in the period. Such changes are reflected as adjustments to the carrying value of property, plant and equipment and the corresponding liability.

Foreign currency transactions. Transactions denominated in foreign currencies are converted into the functional currency of each entity of the Group at the exchange rates prevailing on the date of transactions. Exchange gains and losses resulting from foreign currency remeasurement into the functional currencies are included in the determination of profit for the reporting period.

Monetary assets and liabilities denominated in foreign currencies are converted into the functional currency of each entity of the Group by applying the year end exchange rate and the effect is stated in the consolidated statement of income. Non-monetary assets and liabilities denominated in foreign currencies valued at cost are converted into the functional currency of each entity of the Group at the initial exchange rate. Non-monetary assets that are remeasured to fair value, recoverable amount or realizable value, are translated at the exchange rate applicable to the date of remeasurement.

Revenue recognition. Revenues represent the amounts receivable for goods and services provided in the normal course of business, net of discounts, value-added tax and export duties.

Revenues from oil and gas sales and sales of polymer and insulation tape are recognized when such products are shipped or delivered to customers in accordance to the contract terms and the title has transferred. Services are recognized in the period in which the services are rendered.

Interest income is recognized as the interest accrues as related to the net carrying amount of the financial asset.

General and administrative expenses. General and administrative expenses represent overall corporate management and other expenses related to the general management and administration of the business unit as a whole. They include management and administrative compensation, certain legal and other advisory expenses, insurance of properties, social expenses and other expenses necessary for the administration of the Group.

Employee benefits. Wages and salaries, bonuses, voluntary medical insurance, paid annual and sick leaves are accrued in the period in which the associated services are rendered by the employees of the Group. Compensation at dismissals, vocational support payments, and other allowances are expensed when incurred.

The Group contributes to the Russian Federation State social insurance fund and State pension plan on behalf of its employees. Mandatory contributions to the State social insurance fund and the State pension plan, which is a defined contribution plan, are expensed when incurred and are included in payroll expenses.

The Group also incurs employee costs related to the provision of benefits such as health and social infrastructure and services, employees meals, transportation, and other services. These amounts principally represent an implicit cost of employing production workers and, accordingly, are charged to payroll expenses in the consolidated statement of income.

3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Share based compensation. The Group accounts for share-based compensation in accordance with IFRS 2, *Share-based Payment* ("IFRS 2"). The fair value of the employee services received in exchange for the grant of the equity instruments is recognized as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the instruments granted measured at the grant date. For share-based compensation made to employees by shareholders, an increase to additional paid in capital is recorded equal to the associated compensation expense each period.

Pension obligations. The Group operates a non-contributory post-employment defined benefit plan based on employees' years of service and average salary (Note 12).

The liability recognized in the consolidated balance sheet in respect of the defined benefit pension plan is the present value of the defined benefit obligations at the balance sheet date, together with adjustments for unrecognized past service costs. The present value of the pension obligations are determined by discounting the estimated future cash outflows. The defined benefit obligations are calculated annually by independent actuaries using the projected unit credit method. The discount rate was determined by reference to Russian rouble denominated bonds issued by the Government of the Russian Federation chosen to match the duration of the post-employment benefit obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are recorded to the consolidated statement of income in the period in which they arise. Past-service costs are amortized on a straight-line basis over the vesting period.

Earnings per share. Earnings per share are determined by dividing the profit or loss attributable to shareholders of NOVATEK by the weighted average number of shares outstanding during the reporting period.

Segment reporting. A segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment) or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. Segments with a majority of revenues earned from sales to external customers and whose revenues, results or assets are ten percent or more of all the segments are reported separately.

The Group's primary format for reporting segment information is business segments and the secondary format is geographical segments. The risks and returns of the Group's operations are primarily determined by the nature of the different activities that the Group engages in, rather than the geographical location of these operations. This is reflected by the Group's organizational structure.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Consolidated financial statements prepared in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period.

Management reviews these estimates and assumptions on a continuous basis, by reference to past experiences and other factors considered as reasonable which form the basis for assessing the book values of assets and liabilities. Adjustments to accounting estimates are recognized in the period in which the estimate is revised if the change affects only that period or in the period of the revision and subsequent periods, if both periods are affected. Management also makes certain judgments, apart from those involving estimations, in the process of applying the Group's accounting policies. Actual results may differ from such estimates if different assumptions or circumstances apply; however, management considers that the effect of any changes in these estimates would not be significant.

Judgments and estimates that have the most significant effect on the amounts reported in these consolidated financial statements and within the next financial year are described below.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Useful lives of property, plant and equipment. Management assesses the useful life of an asset by considering the expected usage, estimated technical obsolescence, residual value, physical wear and tear and the operating environment in which the asset is located. Differences between such estimates and actual results may have a material impact on the amount of the carrying values of the property, plant and equipment and may result in adjustments to future depreciation rates and expenses for the period.

Fair values of financial assets and liabilities. The fair value of financial assets and liabilities, other than financial instruments that are traded in an active market, is determined by applying various valuation methodologies. Management uses its judgment to make assumptions based on market conditions existing at each balance sheet date. Discounted cash flow analysis is used for various loans and receivables as well as debt instruments that are not traded in active markets. The effective interest rate is determined by reference to the interest rates of instruments available to the Group in active markets. In the absence of such instruments, the effective interest rate is determined by reference to the interest rates of active market instruments available adjusted for the Group's specific risk premium estimated by management.

Deferred income tax asset recognition. Management assesses deferred income tax assets at each balance sheet date and determines the amount recorded to the extent that realization of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments and applies estimation based on prior years taxable profits and expectations of future income that are believed to be reasonable under the circumstances.

Estimation of oil and gas reserves. Engineering estimates of oil and gas reserves are inherently uncertain and are subject to future revisions. The Group estimates its oil and gas reserves in accordance with guidelines promulgated by the Securities and Exchange Commission (SEC) for proved reserves. Accordingly, accounting measures such as depreciation, depletion and amortization charges and asset retirement obligations that are based on the estimates of proved reserves are also subject to change.

Proved reserves are estimated by reference to available reservoir and well information, including production and pressure trends for producing reservoirs. Furthermore, estimates of proved reserves only include volumes for which access to market is assured with reasonable certainty. All proved reserves estimates are subject to revision, either upward or downward, based on new information, such as from development drilling and production activities or from changes in economic factors, including product prices, contract terms or development plans.

In general, estimates of reserves for undeveloped or partially developed fields are subject to greater uncertainty over their future life than estimates of reserves for fields that are substantially developed and depleted. As those fields are further developed, new information may lead to further revisions in reserve estimates.

Oil and gas reserves have a direct impact on certain amounts reported in the consolidated financial statements, most notably depreciation, depletion and amortization as well as impairment expenses. Depreciation rates on oil and gas assets using the units-of-production method for each field are based on proved developed reserves for development costs, and total proved reserves for costs associated with the acquisition of proved properties. Assuming all variables are held constant, an increase in proved developed reserves for each field decreases depreciation, depletion and amortization expenses. Conversely, a decrease in the estimated proved developed reserves increases depreciation, depletion and amortization expenses. Moreover, estimated proved reserves are used to calculate future cash flows from oil and gas properties, which serve as an indicator in determining whether or not property impairment is present.

Although the possibility exists for changes or revisions in estimated reserves to have a critical effect on depreciation, depletion and amortization charges and, therefore, reported net profit for the year, it is expected that in the normal course of business the diversity of the Group's asset portfolio will mitigate the likelihood of this occurring.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Impairment of non-financial assets. Management assesses whether there are any indicators of possible impairment of all non-financial assets at each reporting date based on events or circumstances that indicate the carrying value of assets may not be recoverable. Such indicators include changes in the Group's business plans, changes in commodity prices leading to unprofitable performances, changes in product mixes, and for oil and gas properties, significant downward revisions of estimated proved reserves. Goodwill and other indefinite life intangibles are tested for impairment annually and at other times when impairment indicators exist. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable.

When value in use calculations are undertaken, management estimates the expected future cash flows from the asset or cash generating unit and chooses a suitable discount rate in order to calculate the present value of those cash flows.

Impairment provision for trade receivables. The impairment provision for trade receivables is based on management's assessment of the probability of collection of individual customer accounts receivable. Significant financial difficulties of the customer, probability that the customer will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the receivable is potentially impaired. Actual results could differ from these estimates if there is deterioration in a major customer's creditworthiness or actual defaults are higher than the estimates.

When there is no expectation of recovering additional cash for an amount receivable, amount receivable is written off against associated provision.

Future cash flows of trade receivables that are evaluated for impairment are estimated on the basis of the contractual cash flows of the assets and the experience of management in respect of the extent to which amounts will become overdue as a result of past loss events and the success of recovery of overdue amounts. Past experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect past periods and to remove the effects of past conditions that do not exist currently.

Pension obligations. The cost of defined benefit pension plans and related current service costs are determined using actuarial valuations. The actuarial valuations involve making demographic assumptions (mortality rates, age of retirement, employee turnover and disability) as well as financial assumptions (discount rates, expected rates of return on assets, inflation forecasts, future salary and pension increases). Due to the long term nature of these plans, such estimates are subject to significant uncertainty.

Asset retirement obligations. Management makes provision for the future costs of decommissioning oil and gas production facilities, pipelines and related support equipment based on the best estimates of future cost and economic lives of those assets. Estimating future asset retirement obligations is complex and requires management to make estimates and judgments with respect to removal obligations that will occur many years in the future. Changes in the measurement of existing obligations can result from changes in estimated timing, future costs or discount rates used in valuation.

The Group also assesses it liabilities for site restoration at each balance sheet period in accordance with the guidelines of IFRIC 1, *Changes in Existing Decommissioning, Restoration and Similar Liabilities*. The amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the balance sheet date based on current legislation where the Group's respective operating assets are located, and is also subject to change because of modifications, revisions and changes in laws and regulations and their interpretation thereof. As a result of the subjectivity of these provisions there is uncertainty regarding both the amount and estimated timing of incurring such costs.

4 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (CONTINUED)

Taxes. Management reduces deferred tax assets to the amount that is more likely than not to be realized. In the event that management determines that it would be able to realize deferred tax assets in the future in excess of the net recorded amount, an adjustment to the deferred tax asset valuation allowance would increase income in the period such determination was made. Likewise, should management determine that it would not be able to realize all or part of Group's deferred tax assets in the future, an adjustment to the deferred tax assets would be charged to income in the period such determination was made. Currently, management expects to generate future taxable income to realize the benefits of the Group's net deferred tax assets.

5 ACQUISITIONS AND DISPOSAL

In July 2007, the Group acquired 25 percent participation interests in OOO Oiltechproduct-Invest, OOO Petra Invest-M and OOO Tailiksneftegas. These entities hold exploration licenses for the Sredniy Chaselskiy, Severo Russkiy, Yuzhno-Zapolyarniy, Zapadno-Tazovskiy, and Anomalniy license areas which expire in 2010 and 2011 and the Severo-Yamsoveskiy license area, which expires in 2009. The cost of these participation interests was RR 1,125 million, of which RR 108 million were payable at 31 December 2007. The Group has an option to purchase an additional 25 percent participation interests in the aforementioned companies after they are granted production licenses and if the license areas are deemed economically viable. Purchase prices for these entities approximate their fair value. The financial and operational activities of the acquirees were not material to the Group's assets, liabilities, revenues and results of operations as at and for the year ended 31 December 2007.

In September 2007, the Group acquired a 50 percent working interest in the Concession Agreement for Gas and Crude Oil Exploration and Exploitation in El Arish Offshore Area (hereinafter referred to as the "Concession Agreement") in the Arab Republic of Egypt. The remaining working interest is held by Tharwa Petroleum S.A.E. Pursuant to the Concession Agreement the Group is committed to spend a minimum of USD 40 million on exploration operations during the initial exploration period of four years.

In November 2007, the Group disposed of its non-core subsidiary, OAO "Geolog Yamala", to third parties for RR 175 million payable in three equal annual installments, recognizing a gain on sale of RR 85 million, net of associated income tax of RR 10 million. The Group included balances and results of the operations of the disposed subsidiary within "other" in the Group's segment information.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

6 PROPERTY, PLANT AND EQUIPMENT

Movements in property, plant and equipment, for the years ended 31 December 2007 and 2006 are as follows:

	Oil and gas properties and equipment	Assets under construction	Other	Total
Cost	62,341	4,174	3,482	69,997
Accumulated depreciation, depletion and amortization	(4,065)	-	(257)	(4,322)
Net book value at 1 January 2006	**58,276**	**4,174**	**3,225**	**65,675**
Acquisition of subsidiaries	741	-	-	741
Additions	469	4,227	7	4,703
Transfers	3,280	(3,711)	431	-
Depreciation, depletion and amortization	(3,490)	-	(238)	(3,728)
Disposals, net	(250)	(173)	(234)	(657)
Cost	66,555	4,517	3,643	74,715
Accumulated depreciation, depletion and amortization	(7,529)	-	(452)	(7,981)
Net book value at 31 December 2006	**59,026**	**4,517**	**3,191**	**66,734**
Acquisition of subsidiaries	-	-	254	254
Additions	2,136	17,324	6	19,466
Transfers	2,716	(2,999)	283	-
Depreciation, depletion and amortization	(3,478)	-	(260)	(3,738)
Disposal of subsidiaries, net	-	-	(18)	(18)
Disposals, net	(2)	-	(27)	(29)
Cost	71,404	18,842	4,098	94,344
Accumulated depreciation, depletion and amortization	(11,006)	-	(669)	(11,675)
Net book value at 31 December 2007	**60,398**	**18,842**	**3,429**	**82,669**

Included within the oil and gas properties and equipment balance at 31 December 2007 and 2006 are proved properties of RR 28,222 million and RR 28,168 million, net of accumulated depreciation, depletion and amortization of RR 4,908 million and RR 3,225 million, respectively.

Included within general and administrative expenses are RR 66 million and RR 57 million of depreciation of administrative buildings for the years ended 31 December 2007 and 2006, respectively (see Note 20).

Included in additions to property, plant and equipment for the years ending 31 December 2007 and 2006 is capitalized interest of RR 139 million and RR 287 million, respectively. The interest capitalization rates for 2007 and 2006 used for additions were 6.0 percent and 6.2 percent, respectively.

Asset retirement obligations. Estimated costs of dismantling oil and gas production facilities, pipelines and related processing facilities, including abandonment and site restoration costs, amounting to RR 618 million and RR 424 million at 31 December 2007 and 2006, respectively, are included in the cost of oil and gas properties and equipment. The Group has estimated its liability based on current legislation using estimated costs and timing of when the expenses are expected to be incurred between the end of the reporting period and 2051. Governmental authorities are continually reviewing regulations and their enforcement. Consequently, the Group's ultimate liabilities may differ from the recorded amounts.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

7 INVENTORIES

	At 31 December: 2007	2006
Materials and supplies at net realizable value (net of provisions of RR 45 million and RR 46 million at 31 December 2007 and 2006, respectively)	280	332
Materials and supplies at cost	438	432
Natural gas and hydrocarbon liquids	799	814
Polymer and insulation tape products (net of provisions of RR 10 million and RR 33 million at 31 December 2007 and 2006, respectively)	177	147
Other inventories	100	90
Total inventories	**1,794**	**1,815**

The Group recorded an expense of RR 101 million and RR 64 million during the years ended 31 December 2007 and 2006, respectively, to write-down the carrying value of inventory due to obsolescence.

8 TRADE AND OTHER RECEIVABLES

	At 31 December: 2007	2006
Trade receivables (net of provision of RR 8 million and RR 16 million at 31 December 2007 and 2006, respectively)	2,947	1,843
Interest on loans receivable	3	26
Other receivables (net of provision of RR 47 million and RR 59 million at 31 December 2007 and 2006, respectively)	317	344
Total trade and other receivables	**3,267**	**2,213**

The carrying values of trade and other receivables approximate their fair value. The maximum exposure to credit risk at the balance sheet date is the carrying value of each class of receivables mentioned above. The Group does not hold any collateral as security for trade and other receivables (see Note 22 for credit risk disclosures).

Trade and other receivables that are less than three months past due are generally not considered for impairment unless other indicators of impairment exist. Trade and other receivables of RR 81 million and RR 69 million at 31 December 2007 and 2006, respectively were past due but not impaired. These relate to a number of independent customers for whom there is no recent history of default. The ageing analysis of these past due but not impaired trade and other receivables are as follows:

	At 31 December: 2007	2006
Up to 90 days past-due	19	15
91 to 360 days past-due	55	39
Over 360 days past-due	7	15
Total past due but not impaired	**81**	**69**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

8 TRADE AND OTHER RECEIVABLES (CONTINUED)

Movements on the Group provision for impairment of trade and other receivables are as follows:

	Year ended 31 December:	
	2007	2006
At 1 January	**75**	**121**
Additional provision recorded	23	33
Receivables written off as uncollectible	(43)	(70)
Provision amount reversed into income	-	(9)
At 31 December	**55**	**75**

The provision for impaired receivables has been included in the consolidated statement of income in net impairment expense.

9 PREPAYMENTS AND OTHER CURRENT ASSETS

	At 31 December:	
	2007	2006
Financial assets		
Short-term loans receivable	36	20
Short-term bank deposits	-	50
Non-financial assets		
Recoverable value-added tax	2,668	664
Prepayments and advances to suppliers (net of provision of RR 4 million and RR 11 million at 31 December 2007 and 2006, respectively)	2,413	1,143
Deferred export duties for stable gas condensate	1,069	924
Prepaid taxes other than income tax	974	777
Deferred transportation expense for stable gas condensate	334	306
Deferred transportation expense for natural gas	55	874
Other current assets	111	93
Total prepayments and other current assets	**7,660**	**4,851**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

10 CASH AND CASH EQUIVALENTS

	At 31 December: 2007	2006
Cash at current bank accounts	1,787	1,522
Russian rouble denominated deposits (average interest rate 3% p.a. and 4% p.a. for 2007 and 2006, respectively)	2,195	3,757
US dollar denominated deposits (average interest rate 5% p.a. for 2006)	-	389
Total cash and cash equivalents	**3,982**	**5,668**

All deposits have original maturities of less than three months (see Note 22 for credit risk disclosures).

Cash, cash equivalents and bank overdrafts include the following for the purposes of the cash flow statement:

	At 31 December: 2007	2006
Cash and cash equivalents per the consolidated balance sheet	3,982	5,668
Less: bank overdrafts (Note 13)	(1,368)	-
Cash, cash equivalents and bank overdrafts per the consolidated statement of cash flows	**2,614**	**5,668**

11 LONG-TERM DEBT

	At 31 December: 2007	2006
US dollar denominated loans	54	2,153
Euro denominated loans	270	507
Total	324	2,660
Less: current portion of long-term debt	(282)	(2,117)
Total long-term debt	**42**	**543**

At 31 December 2007 and 2006, the Group's long-term debt by facility is as follows:

	At 31 December: 2007	2006
BNP PARIBAS Bank	-	1,975
Other loans	324	685
Total	324	2,660
Less: current portion of long-term debt	(282)	(2,117)
Total long-term debt	**42**	**543**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

11 LONG-TERM DEBT (CONTINUED)

Other loans. At 31 December 2007 and 2006, other loans included US dollar denominated loans totaling RR 54 million (USD 2.2 million) and RR 178 million (USD 6.8 million), respectively, with a weighted average interest rate of 10.8 percent and 10.3 percent, respectively. These loans mature between 2008 and 2009. At 31 December 2007 and 2006, other loans also included Euro denominated loans totaling RR 270 million (Euro 7.5 million) and RR 507 million (Euro 14.6 million), respectively, with a weighted average effective interest rate of 13.6 percent and 13.5 percent, respectively. These loans mature between 2008 and 2009.

The carrying values of long-term debt approximate their fair value.

12 PENSION OBLIGATIONS

In February 2007, the Group announced the implementation of a post-employment benefit program. Under the pension program, employees who are employed by the Group for more than three years and retire from the Group on or after the statutory retirement age will receive monthly payments from NOVATEK for life unless they are actively employed. The amount of payments to be disbursed depends on the average salary, duration and location of employment. The program is effective from 1 January 2007 and applies to employees who retire after that date.

The program represents an unfunded defined benefit plan and is accounted for as such under provisions of IAS 19, *Employee Benefits*. The impact of the program on the consolidated financial statements is disclosed below.

The amounts recognized in the consolidated balance sheet and included in other non-current liabilities are determined as follows:

	At 31 December 2007
Present value of the defined benefit obligations	492
Unrecognized past service cost	(276)
Defined benefit plan liability recognized in the consolidated balance sheet	**216**

The movements in the present value of the defined benefit obligations are as follows:

	Year ended 31 December 2007
At 1 January	**-**
Past service cost	293
Interest cost	18
Current service cost	60
Actuarial loss	121
At 31 December	**492**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

12 PENSION OBLIGATIONS (CONTINUED)

The amounts recognized in the consolidated statement of income are as follows:

	Year ended 31 December 2007
Current service cost	60
Interest cost	18
Actuarial loss	121
Amortization of past service cost	17
Defined benefit plan costs recognized in operating expenses	**216**
of which the following amounts were included as employee compensation in:	
Materials, services and other	106
General and administrative expenses	110

As a result of experience adjustments on plan liabilities the Group recognized a loss of RR 77 million included in actuarial loss.

The principal actuarial assumptions used at 31 December 2007 are as follows:

Weighted average discount rate	6.4%
Projected annual increase in employee compensation	10%
Expected increases to pension benefits occurring every third year	10%

The assumed average salary and pension payment increases for Group employees have been calculated on the basis of inflation forecasts, analysis of increases of past salaries and the general salary policy of the Group. It is assumed that the thresholds for the minimum and maximum amount of monthly pension payments would increase by 10 percent every third year.

Mortality assumptions are based on the Russian mortality tables published by the State Statistics Committee from the years 1986 to 1987, which management believes are the most conservative and prudent Russian whole-population mortality tables available.

Management has assessed that reasonable changes in the most significant actuarial assumptions will not have a significant impact on the consolidated statement of income or the liability recognized in the consolidated balance sheet.

13 SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT

	At 31 December:	
	2007	2006
US dollar denominated loans	4,910	448
US dollar denominated bank overdrafts	1,368	-
Total	6,278	448
Add: current portion of long-term debt	282	2,117
Total short-term debt and current portion of long-term debt	**6,560**	**2,565**

US dollar denominated loans. At 31 December 2007, the US dollar denominated loans included a loan from BNP PARIBAS Bank in the amount RR 2,455 million (USD 100 million) with annual interest of LIBOR plus 0.75 percent (5.8 percent at 31 December 2007). The loan is repayable in September 2008.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

13 SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT (CONTINUED)

At 31 December 2007, the US dollar denominated loans included loans from CALYON S.A. and CALYON RUSBANK Corporate and Investment Bank in the total amount RR 2,455 million (USD 100 million) with annual interest of LIBOR plus 0.85 percent (5.9 percent at 31 December 2007). The loans are repayable in May 2008.

The carrying values of the short-term debt approximate their fair value.

Available credit facilities and bank overdrafts. At 31 December 2007 and 2006, the Group used RR 1,368 million and nil of its credit facilities as bank overdrafts, respectively. Available funds under these short-term credit lines with various international banks were in total RR 4,148 million (USD 169 million) and RR 6,135 million (USD 233 million) at 31 December 2007 and 2006, respectively, on either fixed or variable interest rates subject to the specific type of credit facility.

In November 2007, the Group obtained a two year credit line facility with International Moscow Bank (from December 2007 – "UniCredit Bank") up to the maximum amount of RR 2,455 million (USD 100 million) with interest rates negotiated on each withdrawal dates.

14 TRADE PAYABLES AND ACCRUED LIABILITIES

	At 31 December:	
	2007	**2006**
Financial liabilities		
Trade payables	1,327	677
Other payables	375	40
Interest payable	9	7
Non-financial liabilities		
Advances from customers	1,535	961
Salary payables	352	115
Other payables	1	1
Trade payables and accrued liabilities	**3,599**	**1,801**

15 SHAREHOLDERS' EQUITY

Ordinary share capital. Share capital issued and paid-in consisted of 3,036,306,000 ordinary shares at 31 December 2007 and 2006 with a par value of RR 0.1 each. The total authorized number of ordinary shares was 10,593,682,000 shares at both dates.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

15 SHAREHOLDERS' EQUITY (CONTINUED)

Dividends. Dividends declared and paid are as follows:

	Year ended 31 December:	
	2007	2006
Dividends payable at 1 January	1	33
Total dividends declared	5,860	3,258
Dividends paid	(5,860)	(3,290)
Dividends payable at 31 December	**1**	**1**
Dividends per share declared during the year (in Russian roubles)	1.93	1.07
Dividends per GDR declared during the year (in Russian roubles)	19.3	10.7

The Group declares and pays dividends in Russian roubles. Dividends declared in 2007 and 2006 were as follows:

Final for 2006: RR 1.10 per share or RR 11.0 per GDR declared in May 2007	3,340
Interim for 2007: RR 0.83 per share or RR 8.30 per GDR declared in October 2007	2,520
Total dividends declared in 2007	**5,860**
Final for 2005: RR 0.52 per share or RR 5.20 per GDR declared in June 2006	1,588
Interim for 2006: RR 0.55 per share or RR 5.50 per GDR declared in September 2006	1,670
Total dividends declared in 2006	**3,258**

Share-based compensation. In 2005, certain shareholders provided share-based compensation to key members of the Group's management team. The fair value of the awards of RR 879 million is being recognized as compensation expense evenly over their five year vesting period beginning the second quarter of 2005. A corresponding increase is recorded to additional paid in capital as expense is recognized to reflect the shareholders contribution in providing the award. The fair value of the awards was determined by reference to the fair value of the limited liability company's net assets estimated by its owners.

Distributable retained earnings. In accordance with Russian legislation, NOVATEK distributes profits as dividends or transfers them to reserves (fund accounts) on the basis of financial statements prepared in accordance with Russian Accounting Rules. Russian legislation identifies the net profit as basis of distribution. For 2007, net statutory profit of NOVATEK as reported in the published annual statutory reporting forms was RR 16,242 million (2006: RR 12,946 million) and the closing balance of the accumulated profit including the current year net statutory profit totalled RR 41,213 million (2006: RR 30,830 million).

16 OIL AND GAS SALES

	Year ended 31 December:	
	2007	2006
Natural gas	35,605	28,048
Stable gas condensate	17,106	13,768
Liquefied petroleum gas	4,926	3,804
Crude oil	1,753	1,928
Oil products	967	499
Total oil and gas sales	**60,357**	**48,047**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

17 TRANSPORTATION EXPENSES

	Year ended 31 December:	
	2007	2006
Natural gas transportation to customers	9,077	6,934
Stable gas condensate and liquefied petroleum gas transportation by rail	3,376	2,753
Stable gas condensate transportation by tankers	1,690	1,484
Unstable gas condensate transportation from the fields to the processing facilities through third party pipelines	115	78
Crude oil transportation to customers	78	93
Insurance expense	7	8
Other	29	12
Total transportation expenses	**14,372**	**11,362**

18 TAXES OTHER THAN INCOME TAX

The Group is subject to a number of taxes other than income tax, which are detailed as follows:

	Year ended 31 December:	
	2007	2006
Unified natural resources production tax	5,703	5,556
Property tax	544	483
Excise tax	36	80
Other taxes	96	104
Total taxes other than income tax	**6,379**	**6,223**

In 2007 and 2006, the unified natural resources production tax for natural gas production was fixed at a rate of RR 147 per thousand cubic meters.

The unified natural resources production tax rate for gas condensate is set at 17.5 percent of gas condensate revenues recognized by the producing entities.

Under the Tax Code of the Russian Federation, the tax rate for the unified natural resources production tax for crude oil is calculated by reference to an average price for Urals oil mix and an average exchange rate over the relevant tax period. Beginning 1 January 2005, the base rate was set at RR 419 per metric ton of crude oil.

19 MATERIALS, SERVICES AND OTHER

	Year ended 31 December:	
	2007	2006
Employee compensation	1,897	1,351
Materials and supplies	1,521	1,219
Repair and maintenance services	367	333
Fire safety and security expense	263	254
Electricity and fuel	216	192
Tolling and processing fees	213	226
Other	447	318
Total materials, services and other	**4,924**	**3,893**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

20 GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December:	
	2007	**2006**
Employee compensation	1,961	1,476
Maintenance of social infrastructure and charitable contributions	559	491
Legal, audit, and consulting services	404	256
Business trips expense	199	166
Rent expense	146	123
Insurance expense	117	225
Depreciation - administrative buildings	66	57
Other	421	371
Total general and administrative expenses	**3,873**	**3,165**

Auditors' fees and services. ZAO PricewaterhouseCoopers Audit has served as the Group's independent external auditors for each of the financial years. The independent external auditors are subject to re-appointment at the Annual General Meeting of shareholders based on the recommendations from the Board of Directors. The following table presents the aggregate fees for professional services and other services rendered by ZAO PricewaterhouseCoopers Audit to the Group included within legal, audit, and consulting services:

	Year ended 31 December:	
	2007	**2006**
Audit services fee (audit of the Group's consolidated financial statements and the statutory audit of the parent company)	28	28
Non-audit services (tax services and other)	3	1
Total auditors' fees and services	**31**	**29**

21 INCOME TAX

Reconciliation of income tax. The table below reconciles actual income tax expense and theoretical income tax, determined by applying the statutory tax rate to profit before income tax and share of income in associates.

	Year ended 31 December:	
	2007	**2006**
Profit before income tax	25,489	19,122
Theoretical income tax expense at statutory rate of 24 percent	6,117	4,589
Increase (decrease) due to:		
Non-deductible expenses	364	403
Foreign entities' taxation at lower income tax rate	(107)	(65)
Withholding tax on dividends distributed between parent and subsidiaries	193	-
Other non-temporary differences	194	188
Total income tax expense	**6,761**	**5,115**

Effective income tax rate. The Group's Russian statutory income tax rate in 2007 and 2006 was 24.0 percent. For the years ended 31 December 2007 and 2006, the Group's effective income tax rate was 26.5 percent and 26.7 percent, respectively.

Deferred income tax. Differences between IFRS and Russian statutory tax regulations give rise to certain temporary differences between the carrying value of certain assets and liabilities for financial reporting purposes and for income tax purposes.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

21 INCOME TAX (CONTINUED)

Deferred income tax balances are presented in the consolidated balance sheets as follows:

	At 31 December: 2007	At 31 December: 2006
Long-term deferred income tax asset (other non-current assets)	532	321
Long-term deferred income tax liability	(8,083)	(8,412)
Net deferred income tax liability	**(7,551)**	**(8,091)**

Deferred income tax assets expected to be realized within twelve months of 31 December 2007 and 2006 were RR 608 million and RR 387 million, respectively. Deferred tax liabilities expected to be reversed within twelve months of 31 December 2007 and 2006 were RR 348 million and RR 376 million, respectively.

Movements in deferred income tax assets and liabilities during the years ended 31 December 2007 and 2006 are as follows:

	At 31 December 2007	Statement of Income effect	At 31 December 2006	Statement of Income effect	Acquisitions	At 31 December 2005
Liabilities						
Property, plant and equipment	(8,720)	226	(8,946)	496	(180)	(9,262)
Inventories	(43)	(3)	(40)	(16)	-	(24)
Other current assets	(312)	17	(329)	(329)	-	-
Trade payables and accrued liabilities	(3)	13	(16)	(6)	-	(10)
Total deferred income tax liabilities	(9,078)	253	(9,331)	145	(180)	(9,296)

	At 31 December 2007	Statement of Income effect	At 31 December 2006	Statement of Income effect	Acquisitions	At 31 December 2005
Assets						
Inventories	561	170	391	205	33	153
Trade and other receivables	24	1	23	(13)	-	36
Trade payables and accrued liabilities	585	69	516	(84)	-	600
Tax losses carried forward	319	81	238	143	19	76
Other	38	(34)	72	16	-	56
Total deferred income tax assets	1,527	287	1,240	267	52	921
Net deferred income tax liabilities	**(7,551)**	**540**	**(8,091)**	**412**	**(128)**	**(8,375)**

At 31 December 2007, the Group had recognized deferred income tax assets of RR 319 million (31 December 2006: RR 238 million) in respect of unused tax loss carry forwards of RR 1,329 million (31 December 2006: RR 992 million). Tax losses can be carried forward for relief against taxable profits for 10 years after they are incurred, subject to certain limitations. In determining future taxable profits and the amount of tax benefits that are probable in the future management makes judgments including expectations regarding the Group's ability to generate sufficient future taxable income and the projected time period over which deferred tax benefits will be realized.

At 31 December 2007 and 2006, the Group had not recorded a deferred tax liability in respect of taxable temporary differences of RR 8,614 million and RR 7,577 million, respectively, associated with investments in subsidiaries as the Group is able to control the timing of the reversal of those temporary differences and does not intend to reverse them in the foreseeable future.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

22 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS

The accounting policies for financial instruments have been applied to the line items below:

Financial assets	*Loans and receivables* At 31 December: 2007	2006
Non-current		
Long-term loans receivable	412	102
Trade and other receivables	269	229
Letters of credit	175	-
Current		
Short-term loans receivable	36	20
Trade and other receivables	3,267	2,213
Short-term bank deposits	-	50
Cash and cash equivalents	3,982	5,668
Total carrying amount	**8,141**	**8,282**

Financial liabilities	*Measured at amortized cost* At 31 December: 2007	2006
Non-current		
Long-term debt	42	543
Current		
Current portion of long-term debt	282	2,117
Short-term debt	6,278	448
Trade and other payables	1,711	724
Total carrying amount	**8,313**	**3,832**

Financial risk management objectives and policies. In the ordinary course of business, the Group is exposed to market risks from fluctuating prices on commodities purchased and sold, prices of other raw materials, currency exchange rates and interest rates. Depending on the degree of price volatility, such fluctuations in market prices may create volatility in the Group's financial results. To effectively manage the variety of exposures that may impact financial results, the Group's overriding strategy is to maintain a strong financial position.

The Group's principal risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to these limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

Market risk. Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates, commodity prices and equity prices, will affect the Group's financial results or the value of its holdings of financial instruments. The primary objective of mitigating these market risks is to manage and control market risk exposures, while optimizing the return on risk.

The Group is exposed to market price movements relating to changes in commodity prices such as crude oil, gas condensate, liquefied petroleum products and natural gas (commodity price risk), foreign currency exchange rates, interest rates, equity prices and other indices that could adversely affect the value of the Group's financial assets, liabilities or expected future cash flows.

(a) Foreign exchange risk

The Group is exposed to foreign exchange risk arising from various exposures in the normal course of business, primarily with respect to the US dollar and the Euro. Foreign exchange risk arises primarily from future commercial transactions, recognized assets and liabilities when assets and liabilities are denominated in a currency other than the functional currency.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

22 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The Group's overall strategy is to have no significant net exposure in currencies other than the Russian rouble or the US dollar. Foreign currency derivative instruments may be utilized to manage the risk exposures associated with fluctuations on certain firm commitments for sales and purchases, debt instruments and other transactions that are denominated in currencies other than the Russian rouble, and certain non-Russian rouble assets and liabilities.

The carrying amounts of the Group's financial instruments are denominated in the following currencies:

At 31 December 2007	**Russian rouble**	**US dollar**	**Euro**	**Other**	**Total**
Financial assets					
Non-current					
Long-term loans receivable	412	-	-	-	412
Trade and other receivables	269	-	-	-	269
Letters of credit	169	-	6	-	175
Current					
Short-term loans receivable	36	-	-	-	36
Trade and other receivables	1,913	1,350	-	4	3,267
Cash and cash equivalents	3,763	189	7	23	3,982
Financial liabilities					
Non-current					
Long-term debt	-	(4)	(38)	-	(42)
Current					
Current portion of long-term debt	-	(50)	(232)	-	(282)
Short-term debt	-	(6,278)	-		(6,278)
Trade and other payables	(1,657)	(31)	(16)	(7)	(1,711)
Net exposure at 31 December 2007	**4,905**	**(4,824)**	**(273)**	**20**	**(172)**

At 31 December 2006	**Russian rouble**	**US dollar**	**Euro**	**Other**	**Total**
Financial assets					
Non-current					
Long-term loans receivable	102	-	-	-	102
Trade and other receivables	229	-	-	-	229
Current					
Short-term loans receivable	20	-	-	-	20
Short-term bank deposits	50	-	-	-	50
Trade and other receivables	1,272	932	-	9	2,213
Cash and cash equivalents	4,907	748	-	13	5,668
Financial liabilities					
Non-current					
Long-term debt	-	(275)	(268)	-	(543)
Current					
Current portion of long-term debt	-	(1,878)	(239)	-	(2,117)
Short-term debt	-	(448)	-	-	(448)
Trade and other payables	(635)	(34)	(47)	(8)	(724)
Net exposure at 31 December 2006	**5,945**	**(955)**	**(554)**	**14**	**4,450**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

22 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

In accordance with IFRS requirements the Group has chosen to provide information about market risk and potential exposure to hypothetical loss from its use of financial instruments through sensitivity analysis disclosures.

The sensitivity analysis depicted in the table below reflects the hypothetical loss that would occur assuming a 10 percent change in exchange rates and no changes in the portfolio of instruments and other variables at 31 December 2007 and 2006, respectively.

		At 31 December:	
Effect on pre-tax profit	**Increase in exchange rate**	**2007**	**2006**
RUR / USD	10%	(482)	(95)
RUR / EUR	10%	(27)	(55)

The effect of a corresponding 10 percent decrease in exchange rate is approximately equal and opposite.

(b) Commodity price risk

The Group's overall commercial trading strategy in natural gas, stable gas condensate and crude oil and related products is centrally managed. Changes in commodity prices could negatively or positively affect the Group's results of operations. The Group manages the exposure to commodity price risk by optimizing its core activities to achieve stable price margins.

Natural gas. As an independent natural gas producer, the Group is not subject to the government's regulation of natural gas prices. Nevertheless, the Group's prices are strongly influenced by the prices regulated by the Federal Tariffs Service (FTS), a governmental agency. 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 this program, the FTS approved a 25% increase in the regulated price effective 1 January 2008 for the year 2008. Management believes it has limited downside commodity price risk for natural gas and does not use commodity derivative instruments for trading purposes. However, to effectively manage the margins achieved through its natural gas trading activities, management has established targets for volumes sold to wholesale traders, end-customers and the natural gas exchange.

Liquid hydrocarbons. The Group sells all its crude oil and related products and gas condensate under spot contracts. Gas condensate volumes sold to the US and European markets are based on benchmark reference crude oil prices of WTI and Brent dated, respectively, plus a margin or discount, depending on current market situation. Crude oil sold internationally are based on benchmark reference crude oil prices of Brent dated, plus a discount and on a transaction-by-transaction basis for volumes sold domestically. As a result, the Group's revenues from the sales of liquid hydrocarbons are subject to commodity price volatility based on fluctuations or changes in the crude oil benchmark reference prices. Presently, the Group does not use commodity derivative instruments for trading purposes to mitigate price volatility.

(c) Cash flow and fair value interest rate risk

The Group is subject to interest rate risk on financial liabilities with variable interest rates. To mitigate this risk, the Group's treasury function performs periodic analysis of the current interest rate environment and depending on that analysis management makes decisions whether it would be more beneficial to obtain financing on a fixed-rate or variable-rate basis. In cases where the change in the current market fixed or variable interest rates is considered significant management may consider refinancing a particular debt on more favorable interest rate terms.

Changes in interest rates impact primarily debt by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new debts management uses its judgment to decide whether it believes that a fixed or variable rate would be more favorable over the expected period until maturity.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

22 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

	At 31 December:	
	2007	**2006**
At variable rate	6,278	448
At fixed rate	324	2,660
Total debt	**6,602**	**3,108**

The Group centralizes the cash requirements and surpluses of controlled subsidiaries and the majority of their external financing requirements, and applies, on its consolidated net debt position, a funding policy to optimize its financing costs and manage the impact of interest-rate changes on its financial results in line with market conditions. In this way, the Group is able to ensure that the balance between the floating rate portion of its debt and its cash surpluses has a low level of exposure to any change in interest rates over the short term. This policy makes it possible to significantly limit the Group's sensitivity to interest-rate volatility.

The Group's financial results are sensitive to changes in interest rates on the floating rate portion of the Group's debt portfolio. If the interest rates applicable to floating rate debt were to increase by 100 basis points at the reporting dates, assuming all other variables remain constant, it is estimated that the Group's profit before taxation for 2007 would decrease by the amounts shown below.

	At 31 December:	
Effect on pre-tax profit	**2007**	**2006**
Increase by 100 basis points	63	4

The effect of a corresponding 100 basis points decrease in exchange rate is approximately equal and opposite.

Credit risk. Credit risk refers to the risk exposure that a potential financial loss to the Group may occur if a counterparty defaults on its contractual obligations.

Credit risk is managed on a Group level and arises from cash and cash equivalents, including short-term deposits with banks, as well as credit exposures to customers, including outstanding trade receivables and committed transactions. Cash and cash equivalents are deposited only with banks that are considered by the Group at the time of deposit to minimal risk of default.

The Group's trade and other receivables consist of a large number of customers, spread across diverse industries and geographical areas. Most of the Group's international liquid sales are made to customers with independent external ratings. All domestic sales of liquid hydrocarbons are made on a 100 percent prepayment basis. The Group also requires 100 percent prepayments from small customers for natural gas deliveries and partial advances from others. Although the Group does not require collateral in respect of trade and other receivables, it has developed standard credit payment terms and constantly monitors the status of trade receivables and the creditworthiness of the customers.

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

22 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

The table below highlights the Group's trade and other receivables to published credit ratings of its counterparties.

	At 31 December:	
Moody's and/or Fitch	**2007**	**2006**
Investment grade rating	499	395
Non-investment grade rating	1,071	859
No external rating	1,697	959
Total trade and other receivables	**3,267**	**2,213**

The table below highlights the Group's cash balances to published credit ratings of its banks.

	At 31 December:	
Moody's and/or Fitch	**2007**	**2006**
Investment grade rating	2,528	4,036
Non-investment grade rating	1,303	1,418
No external rating	151	214
Total cash and cash equivalents	**3,982**	**5,668**

Liquidity risk. Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation. In managing its liquidity risk, the Group maintains adequate cash reserves and debt facilities, continuously monitors forecast and actual cash flows and matches the maturity profiles of financial assets and liabilities.

The Group prepares various financial plans (monthly, quarterly and annually) which ensures that the Group has sufficient cash on demand to meet expected operational expenses, financial obligations and investing activities for a period of 30 days or more. The Group has entered into a number of short-term credit facilities. Such credit lines and overdraft facilities can be drawn down to meet short-term financing needs. To fund cash requirements of a more permanent nature, the Group will normally raise long-term debt in available international and domestic markets.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

22 FINANCIAL INSTRUMENTS AND FINANCIAL RISK FACTORS (CONTINUED)

All of the Group's financial liabilities represent non-derivative financial instruments. The following tables summarize the maturity profile of the Group's financial liabilities based on contractual undiscounted payments, including interest payments:

At 31 December 2007	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Total
Debt at fixed rate				
Principal	282	42	-	324
Interest	41	2	-	43
Debt at variable rate				
Principal	6,278	-	-	6,278
Interest	157	-	-	157
Trade and other payables	1,711	-	-	1,711
Total financial liabilities	**8,469**	**44**	**-**	**8,513**

At 31 December 2006	Less than 1 year	Between 1 and 2 years	Between 2 and 5 years	Total
Debt at fixed rate				
Principal	2,117	501	42	2,660
Interest	190	45	2	237
Debt at variable rate				
Principal	448	-	-	448
Interest	26	-	-	26
Trade and other payables	724	-	-	724
Total financial liabilities	**3,505**	**546**	**44**	**4,095**

Capital management. The primary objectives of the Group's capital management policy is to ensure a strong capital base to fund and sustain its business operations through prudent investment decisions and to maintain investor, market and creditor confidence to support its business activities.

The Group presently has an investment grade credit rating of Baa3 (stable outlook) by Moody's Investor Services and is rated BB (positive) by Standard & Poors. To maintain its credit rating, the Group has established certain financial targets and coverage ratios that it monitors on a quarterly and annual basis.

The Group manages its liquidity on a corporate-wide basis to ensure adequate funding to sufficiently meet group operational requirements. All external debts are centralized at the Parent level, and all financing to Group entities is facilitated through inter-company loan arrangements.

The Group has a stated dividend policy that distributes at least 30 percent of its parent company non-consolidated statutory net profit determined according to Russian accounting standards. The dividend for a specific year is determined after taken into consideration future earnings, capital expenditure requirements, future business opportunities and the Group current financial position. Dividends are recommended by the Board of Directors and approved by the NOVATEK's shareholders.

There were no changes to the Group's approach to capital management during the year.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 CONTINGENCIES AND COMMITMENTS

Operating environment. The Russian Federation continues to display some characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is in practice not convertible in most countries outside of the Russian Federation, and relatively high inflation. The tax and customs legislation within the Russian Federation is subject to varying interpretations and changes that can occur frequently.

While there have been significant improvements in the macro-economic environment of the Russian Federation, the future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the government, together with tax, legal, regulatory, and political developments.

Commitments. At 31 December 2007, the Group had contractual capital expenditures commitments aggregating approximately RR 21,744 million (at 31 December 2006: RR 5,200 million) for phase two development of the Yurkharovskoye field (through 2009), development of the East-Tarkosalinskoye and Khancheiskoye fields (through 2008 and 2010, respectively) and for continuation of phase two construction of the Purovsky Gas Condensate Plant (through 2008).

Taxation. Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activities of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in its interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years proceeding the year of review. Under certain circumstances reviews may cover longer periods.

As at 31 December 2007, management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. Where management believes it is probable that a position cannot be sustained, an appropriate amount has been accrued.

Mineral licenses. The Group is subject to periodic reviews of its activities by governmental authorities with respect to the requirements of its mineral licenses. Management cooperates with governmental authorities to agree on remedial actions necessary to resolve any findings resulting from these reviews. Failure to comply with the terms of a license could result in fines, penalties or license limitation, suspension or revocation. The Group's management believes any issues of non-compliance will be resolved through negotiations or corrective actions without any material adverse effect on the Group's financial position, statement of income or of cash flows.

The Group's oil and gas fields and license areas are situated on land located in the Yamal-Nenets Autonomous Region. Licenses are issued by the Federal Agency for the Use of Natural Resources under the Ministry of Natural Resources and the Group pays unified natural resources production tax to produce oil and gas from these fields and contributions for exploration of license areas. The principal licenses of the Group and their expiry dates are:

Field	License holder	License expiry date
Yurkharovskoye	OOO NOVATEK-YURKHAROVNEFTEGAS	2034
East-Tarkosalinskoye	OOO NOVATEK-TARKOSALENEFTEGAS	2043
Khancheiskoye	OOO NOVATEK-TARKOSALENEFTEGAS	2019
Sterkhovoye (within the Olympinsky license area)	OOO PurNovaGas	2026
Termokarstovoye	OOO Terneftegas	2021

Management believes the Group has the right to extend its licenses beyond the initial expiration date under the existing legislation and intends to exercise this right on all of its fields. In December 2007, the Group was successful in extending the license for the East-Tarkosalinskoye field from 2018 to 2043. The Group has plans to submit the appropriate application with the respective Agency for the Use of Natural Resources for the extension of the terms of the licenses for Khancheiskoye field.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

23 CONTINGENCIES AND COMMITMENTS (CONTINUED)

Environmental liabilities. The Group and its predecessor entities have operated in the oil and gas industry in the Russian Federation for many years. The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations and, as obligations are determined, they are recognized as an expense immediately if no future benefit is discernible. Potential liabilities which might arise as a result of a change in interpretation of existing regulations, civil litigation or changes in legislation cannot be estimated. Under existing legislation, management believes that there are no probable liabilities which will have a material adverse effect on the Group's financial position, statement of income or of cash flows.

Legal contingencies. The Group is subject of, or party to a number of court proceedings (both as a plaintiff and a defendant) arising in the ordinary course of business. In the opinion of management, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Group and which have not been accrued or disclosed in the consolidated financial statements.

24 SUBSIDIARIES AND ASSOCIATES

The most important subsidiaries and associates of the Group at 31 December 2007 and respective ownership in the ordinary share capital are set out below.

	Ownership interest at 31 December 2007	Country of incorporation	Principal activities
Subsidiaries			
OOO NOVATEK-YURKHAROVNEFTEGAS	100.0%	Russia	Exploration and production
OOO NOVATEK-TARKOSALENEFTEGAS	100.0%	Russia	Exploration and production
OOO Terneftegaz	100.0%	Russia	Exploration and production
OOO NOVATEK-PUROVSKY ZPK	100.0%	Russia	Gas Condensate Plant
OOO NOVATEK-TRANSERVICE	100.0%	Russia	Transportation services
OOO NOVASIB	100.0%	Russia	Exploration activities
OOO NOVATEK-Refuelling Complexes	100.0%	Russia	Wholesale and retail trading
OOO NOVATEK North-West	100.0%	Russia	Trading and marketing
OOO NOVATEK-Polymer	100.0%	Russia	Production of polymer and insulation tape
OOO PurNovaGaz	100.0%	Russia	Exploration and production
OOO Purneft	100.0%	Russia	Exploration and production
OOO NOVATEK-Ust-Luga	100.0%	Russia	Construction of sea terminal
OOO Purovsky Terminal	83.85%	Russia	Transport / handling services
OOO YARGEO	51.0%	Russia	Exploration activities
Novatek Overseas AG	100.0%	Switzerland	Holding company
Runitek GmbH	100.0%	Switzerland	Trading and marketing
Novatek Overseas Exploration & Production GmbH	100.0%	Switzerland	Exploration and production
Associates			
OOO Oiltechproduct-Invest	25.0%	Russia	Exploration activities
OOO Petra Invest-M	25.0%	Russia	Exploration activities
OOO Tailiksneftegas	25.0%	Russia	Exploration activities

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

25 RELATED PARTY TRANSACTIONS

For the purposes of these consolidated financial statements, parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial and operational decisions. Management has used reasonable judgments in considering each possible related party relationship with attention directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be affected on the same terms, conditions and amounts as transactions between unrelated parties. The Group enters into transactions with related parties based on market or regulated prices.

All natural gas producers and wholesalers operating in Russia transport their natural gas volumes through the Unified Gas Supply System (UGSS), which is owned and operated by OAO Gazprom, a State monopoly. As an independent natural gas producer, the Group utilizes the UGSS to transport natural gas to end-consumers at the tariff established by the Federal Tariff Service. Transactions only with Gazprom group parent company – OAO Gazprom, a shareholder of NOVATEK from October 2006, are presented below. The difference with the expenses for natural gas transportation as disclosed in Note 17 relates to volumes sold on electronic trading facilities of Mezhregiongaz, a subsidiary of OAO Gazprom.

	As at and for the year ended 31 December	
OAO Gazprom	2007	2006
Transactions		
Purchases of natural gas	1,282	237
Natural gas transportation to customers	8,939	1,932
Balances		
Prepayments and other current assets	835	-
Trade and other payables	152	163

	As at and for the year ended 31 December	
Related parties – associates	2007	2006
Transactions		
Other revenues	22	-
Interest income	16	-
Balances		
Long-term loans receivable	409	-
Interest on long-term loans receivable	16	-
Trade payables and accrued liabilities	324	-

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

25 RELATED PARTY TRANSACTIONS (CONTINUED)

During 2006, the Group had transactions with entities controlled by the Group's significant shareholders. Starting October 2006, these entities were no longer considered to be related parties of the Group.

	Year ended 31 December	
Related parties - subject to control by significant shareholders	**2007**	**2006**
Transactions		
Sales of inventory and oil products	-	54
Purchases of construction services	-	656
Materials, services and other	-	176
Interest income	-	17

Key management compensation. During 2007 and 2006, the Group paid to the key management personnel (the members of the Board of Directors and the Management Board, some of whom have also direct and indirect interests in the Group) short-term compensation, including salary, bonuses, excluding dividends the total of RR 403 million and RR 364 million in cash, respectively. Such amounts include personal income tax and are net of unified social tax. The remuneration for serving on the Board of Directors is subject to approval by the General Meeting of Shareholders. Key management personnel also receive certain short-term benefits related to healthcare. In addition, during 2007 and 2006, RR 176 million for each year, were recognized as part of the share-based compensation program (Note 15) and included in general and administrative expense.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

26 SEGMENT INFORMATION

The Group's primary format for reporting segment information is business segments and the secondary format is geographical segments.

Business Segments. The Group evaluates performance and makes investment and strategic decisions based upon a review of profitability for the Group as a whole. However, the Group's activities are considered by management to comprise the following business segments:

- Exploration and production – acquisitions, exploration, development, production, processing, marketing and transportation of natural gas, gas condensate, crude oil and related products;
- Corporate and other – other activities, including head-office, certain general and administrative services, polymer and tape insulation.

Segment information as at 31 December 2007 and 2006 is as follows:

At 31 December 2007	**Exploration and production**	**Corporate and other**	**Total**
Segment assets	92,965	4,344	97,309
Investment in associates	1,125	-	1,125
Unallocated assets:			
Current and deferred income tax			868
Long-term loans receivable			412
Trade and other receivables			3
Other non-current assets			191
Prepayments and other current assets			85
Cash and cash equivalents			3,982
Total assets			**103,975**
Segment liabilities	6,728	94	6,822
Unallocated liabilities:			
Current and deferred income tax			8,728
Long-term and short term debt			6,602
Trade payable and accrued liabilities			11
Total liabilities			**22,163**

At 31 December 2006	**Exploration and production**	**Corporate and other**	**Total**
Segment assets	73,608	3,545	77,153
Unallocated assets:			
Current and deferred income tax			1,261
Long-term loans receivable			102
Trade and other receivables			29
Prepayments and other current assets			113
Cash and cash equivalents			5,668
Total assets			**84,326**
Segment liabilities	3,968	106	4,074
Unallocated liabilities:			
Current and deferred income tax			8,460
Long-term and short term debt			3,108
Trade payable and accrued liabilities			8
Total liabilities			**15,650**

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

26 SEGMENT INFORMATION (CONTINUED)

Segment information for the years ended 31 December 2007 and 2006 is as follows:

Year ended 31 December 2007	Exploration and production	Corporate and other	Total
Segment revenues			
External revenues and other income	60,478	1,858	62,336
Inter-segment sales	11	51	62
Total segment revenues	**60,489**	**1,909**	**62,398**
Segment expenses			
External expenses	(32,510)	(4,556)	(37,066)
Inter-segment expenses	(51)	(11)	(62)
Total segment expenses	**(32,561)**	**(4,567)**	**(37,128)**
Segment result	**27,928**	**(2,658)**	**25,270**
Unallocated gains on sales of investments			95
Profit from operations			**25,365**
Finance income (expense), net			124
Profit before income tax			**25,489**
Income tax expense			(6,761)
Profit for the year			**18,728**
Acquisition of subsidiaries	-	254	254
Capital expenditures	18,382	1,084	19,466
Depreciation, depletion and amortization	(3,516)	(218)	(3,734)
Impairment charges	(30)	(123)	(153)

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

26 SEGMENT INFORMATION (CONTINUED)

Year ended 31 December 2006	Exploration and production	Corporate and other	Total
Segment revenues			
External revenues and other income	47,972	1,251	49,223
Inter-segment sales	10	18	28
Total segment revenues	**47,982**	**1,269**	**49,251**
Segment expenses			
External expenses	(26,413)	(3,668)	(30,081)
Inter-segment expenses	(18)	(10)	(28)
Total segment expenses	**(26,431)**	**(3,678)**	**(30,109)**
Segment result	**21,551**	**(2,409)**	**19,142**
Unallocated gains on sales of investments			11
Profit from operations			**19,153**
Finance income (expense), net			(31)
Profit before income tax			**19,122**
Income tax expense			(5,115)
Profit for the year			**14,007**
Acquisition of subsidiaries	741	-	741
Capital expenditures	4,347	356	4,703
Depreciation, depletion and amortization	(3,565)	(163)	(3,728)
Impairment charges	(32)	(68)	(100)

Capital expenditures include purchases of property, plant, and equipment. Charges for impairment above include impairment provisions for accounts and loans receivable and inventories.

The inter-segment sales mainly consist of:

- Exploration and production – sale of gas and oil products to the other segments, for which prices are based on market prices; and
- Corporate and other – rendering rent services, transportation sales and sales of polymer to the other segments, for which prices are based on market prices.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

26 SEGMENT INFORMATION (CONTINUED)

Geographical segments. The Group's two business segments operate in three major geographical areas of the world. In the Russian Federation, its home country, the Group is mainly engaged in the exploration, development, extraction and sales of natural gas, crude oil, gas condensate and related products and sales of polymer and insulation tape. Activities outside the Russian Federation are conducted in the United States (sales of stable gas condensate), in Europe (sales of stable gas condensate, liquefied petroleum gas and crude oil) and other areas (sales of liquefied petroleum gas and sales of polymer and insulation tape). Information for the main geographical segments of the Group is set out below.

At 31 December 2007 and for the year then ended	Russia	Europe	USA	Other	Total
Total segment assets	94,353	1,416	1,540	-	97,309
Investment in associates	1,125	-	-	-	1,125
External revenues and other income	42,201	5,693	13,377	1,065	62,336
Unallocated gain on sales of investments					95
Total revenues and other income as per consolidated statement of income					**62,431**
Acquisition of subsidiaries	254	-	-	-	254
Capital expenditures	19,440	-	-	26	19,466

At 31 December 2006 and for the year then ended	Russia	Europe	USA	Other	Total
Total segment assets	75,260	1,893	-	-	77,153
External revenues and other income	33,790	9,410	5,481	542	49,223
Unallocated gain on sales of investments					11
Total revenues and other income as per consolidated statement of income					**49,234**
Acquisition of subsidiaries	741	-	-	-	741
Capital expenditures	4,699	4	-	-	4,703

Segment revenue from external customers is based on the geographical location of customers. Segment assets are based on the geographical location of the assets. Capital expenditure is based on the geographical location of the Group's assets.

(in Russian roubles, [tabular amounts in millions] unless otherwise stated)

27 EXPLORATION FOR AND EVALUATION OF MINERAL RESOURCES

The amounts included within the consolidated financial statements associated with the exploration for and evaluation of mineral resources for the years ended 31 December 2007 and 2006 is as follows:

	At 31 December and for the year then ended:	
	2007	**2006**
Assets	3,881	1,395
Liabilities	(12)	(23)
Expenses	(486)	(459)
Cash flows used for operating activities	(449)	(335)
Cash flows used for investing activities	(2,463)	(1,309)

Assets include uncompleted cost of drilling and equipping of exploratory wells on unproved reserves and participation payment for the rights to purchase oil and gas exploration and production licenses. Liabilities include unpaid obligations under the contracts for drilling and equipping exploratory wells. Exploration costs include geological and geophysical expenditures, expenditures associated with the maintenance of non-proven reserves and other expenditures relating to exploration activity. Cash flows used for operating activities and for investing activities include cash paid for geological and geophysical studies performed and cash paid for drilling and equipping exploratory wells and acquiring the right for mineral recourses, respectively.

28 SUBSEQUENT EVENTS

On 11 February 2008, the Group’s Board of Directors approved the purchase of up to, but not more than, 3.0 percent of NOVATEK’s ordinary shares outstanding, in the form of GDR’s, as part of a share buy back program. The program will be carried out on a long-term basis. NOVATEK plans to use the buy back program for possible future financing activities and for the Company’s ongoing implementation of a compensation and incentive program.

29 NEW ACCOUNTING PRONOUNCEMENTS

Beginning 1 January 2007, the Group has adopted the following interpretations:

- IFRIC 7, *Applying the Restatement Approach under IAS 29* (effective for periods beginning on or after 1 March 2006). IFRIC 7 clarifies the requirements under IAS 29, *Financial Reporting in Hyperinflationary Economies* relating to how comparative amounts in financial statements should be restated when an entity identifies the existence of hyperinflation in the economy of the currency in which its financial statements are measured; and how deferred tax items in the opening balance sheet should be restated;

- IFRIC 8, *Scope of IFRS 2* (effective for periods beginning on or after 1 May 2006). IFRIC 8 clarifies that the accounting standard IFRS 2, *Shared-based Payment* applies to arrangements where an entity makes share-based compensation for apparently no or inadequate consideration;

- IFRIC 9, *Reassessment of Embedded Derivatives* (effective for annual periods beginning on or after 1 June 2006). IFRIC 9 requires an entity to assess whether an embedded derivative is required to be separated from the host contract and accounted for as a derivative when the entity first becomes a party to the contract. Subsequent reassessment is prohibited unless there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract, in which case reassessment is required; and

- IFRIC 10, *Interim Financial Reporting and Impairment* (effective for annual periods beginning on or after 1 November 2006). IFRIC 10 prohibits the impairment losses recognized in an interim period on goodwill, investments in equity instruments and investments in financial assets carried at cost to be reversed at a subsequent balance sheet date.

The adoption of these interpretations, if applicable, had an insignificant effect on the Group's consolidated financial statements.

Recently, the International Accounting Standards Board published the following new standards and interpretations which have not been early adopted by the Group.

- IFRS 8, *Operating Segments* (effective for annual periods beginning on or after 1 January 2009). IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information;

- IAS 1, *Presentation of Financial Statements* (revised September 2007); effective for annual periods beginning on or after 1 January 2009). The main change in IAS 1 is the replacement of the income statement by a statement of comprehensive income which will also include all non-owner changes in equity, such as the revaluation of available-for-sale financial assets. Alternatively, entities will be allowed to present two statements: a separate income statement and a statement of comprehensive income. The revised IAS 1 also introduces a requirement to present a statement of financial position (balance sheet) at the beginning of the earliest comparative period whenever the entity restates comparatives due to reclassifications, changes in accounting policies, or corrections of errors. The Group expects the revised IAS 1 to affect the presentation of its financial statements but to have no impact on the recognition or measurement of specific transactions and balances;

- Amendment to IAS 32 and IAS 1, *Puttable financial instruments and obligations arising on liquidation* (effective from 1 January 2009). The amendment requires classification as equity of some financial instruments that meet the definition of a financial liability;

- IAS 27, *Consolidated and Separate Financial Statements* (revised January 2008; effective for annual periods beginning on or after 1 July 2009). The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously "minority interests") even if this results in the non-controlling interests having a deficit balance (the current standard requires the excess losses to be allocated to the owners of the parent in most cases). The revised standard specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. At the date when control is lost, any investment retained in the former subsidiary will have to be measured at its fair value;

29 NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

- IFRS 3, *Business Combinations* (revised January 2008; effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009). The revised IFRS 3 will allow entities to choose to measure non-controlling interests using the existing IFRS 3 method (proportionate share of the acquiree's identifiable net assets) or on the same basis as US GAAP (at fair value). The revised IFRS 3 is more detailed in providing guidance on the application of the purchase method to business combinations. The requirement to measure at fair value every asset and liability at each step in a step acquisition for the purposes of calculating a portion of goodwill has been removed. Instead, goodwill will be measured as the difference at acquisition date between the fair value of any investment in the business held before the acquisition, the consideration transferred and the net assets acquired. Acquisition-related costs will be accounted for separately from the business combination and therefore recognized as expenses rather than included in goodwill. An acquirer will have to recognize at the acquisition date a liability for any contingent purchase consideration. Changes in the value of that liability after the acquisition date will be recognized in accordance with other applicable IFRSs, as appropriate, rather than by adjusting goodwill. The revised IFRS 3 brings into its scope business combinations involving only mutual entities and business combinations achieved by contract alone;

- Amendment to IFRS 2, *Share-based Payment* (issued in January 2008; effective for annual periods beginning on or after 1 January 2008). The amendment clarifies that only service conditions and performance conditions are vesting conditions. Other features of a share-based payment are not vesting conditions. The amendment specifies that all cancellations, whether by the entity or by other parties, should receive the same accounting treatment;

- IAS 23 (Revised), *Recognition of Borrowing Costs*. The revision removed the option of immediately recognizing as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. The revised standard applies to borrowing costs relating to qualifying assets for which the commencement date for capitalization is on or after 1 January 2009;

- IFRIC 11, *IFRS 2 – Group and Treasury Share Transactions* (effective for annual periods beginning on or after 1 March 2007). IFRIC 11 addresses accounting for certain transactions an entity may enter into to satisfy rights to equity instruments previously granted to employees. Additionally it provides guidance on accounting for rights to equity instruments of a parent company granted for employees of a subsidiary in the subsidiary's separate financial statements;

- IFRIC 12, *Service Concession Arrangements* (effective for annual periods beginning on or after 1 January 2008). IFRIC 12 gives guidance on the accounting by operators for public-to-private service concession arrangements;

- IFRIC 13, *Customer Loyalty Programs* (effective for annual periods beginning on or after 1 July 2008). IFRIC 13 provides guidance on the recognition and measurement of award credits which a company grants to its customers; and

- IFRIC 14, *IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction* (effective for annual periods beginning on or after 1 January 2008). IFRIC 14 addresses the measurement of defined benefit plan assets and accounting for an obligation under a minimum funding requirement.

Unless otherwise described above, the new standards and interpretations are not expected to significantly affect the Group's financial statements.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES

The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). In the absence of specific IFRS guidance, the Group has reverted to other relevant disclosure standards, mainly US GAAP, that are consistent with norms established for the oil and gas industry. While not required under IFRS, this section provides unaudited supplemental information on oil and gas exploration and production activities but excludes disclosures regarding the standardized measures of discounted cash flows related to oil and gas activities.

The Group's exploration and production activities are presently exclusively within the Russian Federation; therefore, all of the information provided in this section pertains to this country. The Group operates through various oil and gas production subsidiaries. The Group also has an interest in oil and gas companies that are accounted for under the equity method. These associates have no proved reserves and immaterial capitalized costs.

Oil and Gas Exploration and Development Costs

The following tables set forth information regarding oil and gas acquisition, exploration and development activities. The amounts reported as costs incurred include both capitalized costs and costs charged to expense during the years ended 31 December 2007 and 2006 (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2007	**2006**
Costs incurred in exploration and development activities		
Acquisition cost	2,835	741
Exploration costs	1,605	740
Development costs	16,077	3,883
Total costs incurred in exploration and development activities	**20,517**	**5,364**

	At 31 December:	
	2007	**2006**
Capitalized costs relating to oil and gas producing activities		
Wells and related equipment and facilities	60,674	56,171
Support equipment and facilities	9,824	9,740
Uncompleted wells, equipment and facilities	18,312	4,165
Total capitalized costs relating to oil and gas producing activities	88,810	70,076
Less: accumulated depreciation, depletion and amortization	(10,909)	(7,471)
Net capitalized costs relating to oil and gas producing activities	**77,901**	**62,605**

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Results of Operations for Oil and Gas Producing Activities

The Group's results of operations for oil and gas producing activities are shown below. The results of operations for oil and gas producing activities do not include general corporate overhead or its associated tax effects. Income tax is based on statutory rates. In the following table both transportation and processing costs are included in Revenues from oil and gas sales (amounts in millions of Russian roubles).

	Year ended 31 December:	
	2007	2006
Revenues from oil and gas sales	60,357	48,047
Production costs	(3,072)	(1,729)
Long-term supply purchases	(3,242)	(1,805)
Transportation expenses	(14,358)	(11,342)
Taxes other than income tax	(6,222)	(6,019)
Depreciation, depletion and amortization	(3,446)	(3,466)
Exploration expenses	(486)	(459)
Results of operations for oil and gas producing activities before income tax	29,531	23,227
Less: related income tax expense	(7,087)	(5,574)
Results of operations for oil and gas producing activities	**22,444**	**17,653**

Proved Oil and Gas Reserves

The Group's oil and gas reserves estimation and reporting process involves an annual independent third party reserve appraisal as well as internal technical appraisals of reserves. The Group maintains its own internal reserve estimates that are calculated by technical staff working directly with the oil and gas properties. The Group's technical staffs periodically updates reserve estimates during the year based on evaluations of new wells, performance reviews, new technical information and other studies.

The oil and gas reserve estimates reported below are determined by the Group's independent petroleum reservoir engineers, DeGolyer and MacNaughton ("D&M"), for the Group's fields – Yurkharovskoye, East-Tarkosalinskoye, Khancheiskoye, Sterkhovoye, Termokarstovoye, Urengoyskoe and North Khancheiskoye. The Group provides D&M annually with engineering, geological and geophysical data, actual production histories and other information necessary for the reserve determination. The Group's and D&M's technical staffs meet to review and discuss the information provided, and upon completion of this process, senior management reviews and approves the final reserve estimates issued by D&M.

The following reserve estimates were prepared using standard geological and engineering methods generally accepted by the petroleum industry. The method or combination of methods used in the analysis of each reservoir is tempered by experience with similar reservoirs, stages of development, quality and completeness of basic data, and production history.

The following information presents the quantities of proved oil and gas reserves and changes thereto as at and for the years ended 31 December 2007 and 2006.

Extensions of production licenses are assumed to be at the discretion of the Group. Management believes that proved reserves should include quantities which are expected to be produced after the expiry dates of the Group's production licenses. The Group's licenses expire between 2018 and 2043, with the most significant license, Yurkharovskoye field and East-Tarkosalinskoye field, expiring in 2034 and 2043, respectively. Management believes that there is requisite legislation to extend mineral licenses at the initiative of the Group and, as such, intends to extend its licenses for properties expected to produce beyond the license expiry dates.

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

The Group has disclosed information on proved oil and gas reserve quantities for periods up to and past the license expiry dates separately.

Proved reserves are defined as the estimated quantities of oil and gas which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic conditions. In some cases, substantial new investment in additional wells and related support facilities and equipment will be required to recover such proved reserves. Due to the inherent uncertainties and the limited nature of reservoir data, estimates of underground reserves are subject to change over time as additional information becomes available.

Proved developed reserves are those reserves which are expected to be recovered through existing wells with existing equipment and operating methods. Undeveloped reserves are those reserves which are expected to be recovered as a result of future investments to drill new wells, to re-complete existing wells and/or install facilities to collect and deliver the production.

Net reserves exclude quantities due to others when produced.

The reserve quantities below include 100 percent of the net proved reserve quantities attributable to the Group's consolidated subsidiaries. A portion of the Group's total proved reserves are classified as either developed non-producing or undeveloped. Of the non-producing reserves, a portion represents existing wells which are to be returned to production at a future date.

Additions represent two more fields, North Khancheiskoye and Urengoyskoe, appraised by D&M in 2007. For convenience, volumes are provided both in English and metric units.

Net proved reserves of natural gas are presented below.

	Net proved reserves of natural gas recoverable up to license expiry dates		**Net proved reserves of natural gas recoverable past license expiry dates**		**Total net proved reserves of natural gas**	
	Billions of cubic feet	***Billions of cubic meters***	***Billions of cubic feet***	***Billions of cubic meters***	***Billions of cubic feet***	***Billions of cubic meters***
Reserves at 31 December 2005	**18,949**	**537**	**3,685**	**104**	**22,634**	**641**
Changes attributable to:						
Revisions of previous estimates	1,043	30	321	9	1,364	39
Production	(1,008)	(29)	-	-	(1,008)	(29)
Reserves at 31 December 2006	**18,984**	**538**	**4,006**	**113**	**22,990**	**651**
Changes attributable to:						
Revisions of previous estimates	(3,668)	(105)	4,109	117	441	12
Extension of license	7,521	213	(7,521)	(213)	-	-
Extension and discoveries	446	13	-	-	446	13
Additions	96	3	91	2	187	5
Production	(997)	(28)	-	-	(997)	(28)
Reserves at 31 December 2007	**22,382**	**634**	**685**	**19**	**23,067**	**653**
Net proved developed reserves (included above)						
At 31 December 2005	10,513	298	2,925	83	13,438	381
At 31 December 2006	14,911	422	3,134	89	18,045	511
At 31 December 2007	19,290	546	106	3	19,396	549

UNAUDITED SUPPLEMENTAL OIL AND GAS DISCLOSURES (CONTINUED)

Net proved reserves of crude oil, gas condensate and natural gas liquids are presented below.

	Net proved reserves of crude oil, gas condensate and natural gas liquids recoverable up to license expiry dates		Net proved reserves of crude oil, gas condensate and natural gas liquids recoverable past license expiry dates		Total net proved reserves of crude oil, gas condensate and natural gas liquids	
	Millions of barrels	*Millions of metric tons*	*Millions of barrels*	*Millions of metric tons*	*Millions of barrels*	*Millions of metric tons*
Reserves at 31 December 2005	**325**	**39**	**56**	**7**	**381**	**46**
Changes attributable to:						
Revisions of previous estimates	30	4	14	2	44	6
Production	(18)	(2)	-	-	(18)	(2)
Reserves at 31 December 2006	**337**	**41**	**70**	**9**	**407**	**50**
Changes attributable to:						
Revisions of previous estimates	(35)	(5)	35	5	-	-
Extension of license	97	13	(97)	(13)	-	-
Extension and discoveries	11	1	-	-	11	1
Additions	6	1	1	-	7	1
Production	(19)	(3)	-	-	(19)	(3)
Reserves at 31 December 2007	**397**	**48**	**9**	**1**	**406**	**49**
Net proved developed reserves (included above)						
At 31 December 2005	123	15	10	1	133	16
At 31 December 2006	199	24	11	1	210	25
At 31 December 2007	259	31	4	1	263	32

OAO NOVATEK was incorporated as a joint stock company in accordance with the Russian law and is domiciled in the Russian Federation. The Group's registered office is:

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