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

You should read the following management's discussion in conjunction with our unaudited consolidated interim condensed financial information as of and for the nine months ended 30 September, 2010. The consolidated interim condensed financial information has been prepared in accordance with International Accounting Standard 34 "Interim financial reporting" ("IAS 34"). This financial information should be read together with the consolidated financial statements for the year ended December 31, 2009, prepared in accordance with International Financial Reporting Standards ("IFRS").

OVERVIEW

We are one of the world's largest oil and gas companies in terms of reserves, production and market capitalization. Our revenues are primarily derived from sales of natural gas, crude oil and other hydrocarbon products to Western and Central Europe, Russia and other former Soviet Union countries.

We divide our operations into the following principal businesses:

- Production of gas – exploration and production of gas;
- Transport – transportation of gas;
- Distribution – sales of gas within Russian Federation and abroad;
- Gas storage – storage of extracted and purchased gas in underground gas storages;
- Production of crude oil and gas condensate – exploration and production of oil and gas condensate, sales of crude oil and gas condensate;
- Refining – processing of oil, gas condensate and other hydrocarbons, and sales of refined products; and
- Electric and heat energy generation and sales.

Other businesses primarily comprise production of other products and sales of several goods, works, services.

Our main business segments are mutually dependent, with a significant portion of the revenues of one segment comprising a part of the costs of another segment. In particular, our Distribution segment purchases natural gas from our Production of gas segment and transportation services from our Transport segment. Our Refining segment purchases gas from our Production of gas segment and crude oil and gas condensate from the Production of crude oil and gas condensate segment. We establish internal transfer prices with reference to the specific funding requirements of the individual subsidiaries within each segment. Accordingly, the results of operations of these segments on a stand-alone basis do not necessarily represent each segment's underlying financial position and results of operations as if it was a stand-alone business. For this reason, we do not analyze any of our main segments separately in the discussion that follows.

RESULTS OF OPERATIONS

(RR million)

	Nine months periods ended September 30, 2010	2009
Sales	2,507,744	2,154,742
Net gain from trading activity	10,316	2,876
Operating expenses	(1,743,321)	(1,568,784)
Operating profit	**774,739**	**588,834**
Purchase of non-controlling interest in OAO Gazprom neft	-	13,865
Finance income	126,967	339,679
Finance expense	(128,402)	(383,245)
Share of net income of associated undertakings and jointly controlled entities	74,153	43,040
Gains on disposal of available-for-sale financial assets	2,481	2,321
Profit before profit tax	**849,938**	**604,494**
Current profit tax expense	(148,389)	(120,112)
Deferred profit tax (expense) benefit	(32,796)	(5,093)
Profit tax expense	(181,185)	(125,205)
Profit for the period	**668,753**	**479,289**
Other comprehensive income		
Gains arising from change in fair value of available-for-sale financial assets, net of tax	13,426	22,831
Share of other comprehensive income of associated undertakings and jointly controlled entities	1,406	4,331
Translation differences	(5,163)	(3,337)
Revaluation of equity interest	-	9,911
Other comprehensive income for the period, net of tax	**9,669**	**33,736**
Total comprehensive income for the period	**678,422**	**513,025**
Profit attributable to:		
owners of OAO Gazprom	653,721	470,874
non-controlling interest	15,032	8,415
	668,753	**479,289**
Total comprehensive income attributable to:		
owners of OAO Gazprom	662,968	509,265
non-controlling interest	15,454	3,760
	678,422	**513,025**

Sales

The following table sets out our volumes and realized prices for the nine months periods ended September 30, 2010 and 2009.

(RR million unless indicated otherwise)	Nine months periods ended September 30, 2010	2009
Sales of gas		
Europe and other countries		
Gross sales [1]	953,358	1,031,750
Excise tax	-	(290)
Customs duties	(180,478)	(206,458)
Net sales	772,880	825,002
Volumes in billion cubic meters (bcm)	107.8	103.4
Gross average price, U.S.$ per mcm[2] (including excise tax and customs duties) [3]	292.4	307.2
Gross average price, RR per mcm[2] (including excise tax and customs duties)	8,847.0	9,977.9
FSU (Former Soviet Union)		
Gross sales (net of value added tax (VAT))	323,315	253,389
Customs duties	(33,245)	(27,631)
Net sales	290,070	225,758
Volumes in bcm	46.9	36.3
Gross average price, U.S.$ per mcm [2] (including customs duties, net of VAT) [3]	228.0	214.8
Gross average price, RR per mcm [2] (including customs duties, net of VAT)	6,897.5	6,976.2
Russian Federation		
Gross sales (net of VAT)	437,410	325,964
Net sales	437,410	325,964
Volumes in bcm	191.4	183.7
Gross average price, RR per mcm [2] (net of VAT)	2,284.7	1,774.7
Total sales of gas		
Gross sales (net of VAT)	1,714,083	1,611,103
Excise tax	-	(290)
Customs duties	(213,723)	(234,089)
Net sales	1,500,360	1,376,724
Volumes in bcm	346.1	323.4
Net sales of refined products (net of excise tax, VAT and customs duties)	504,711	402,361
Net sales of electric and heat energy (net of VAT)	206,610	136,989
Net sales of crude oil and gas condensate (net of excise tax, VAT and customs duties)	141,366	122,336
Gas transportation net sales (net of VAT)	67,195	41,563
Other revenues (net of VAT)	87,502	74,769
Total sales (net of excise tax, VAT and customs duties)	**2,507,744**	**2,154,742**

Notes:

[1] VAT is not charged on sales to Europe and other countries.

[2] One mcm is equivalent to 35,316 cubic feet.

[3] Calculated on the basis of average rate.

Total sales (net of excise tax, VAT and customs duties) increased by RR 353,002 million, or 16%, to RR 2,507,744 million in the nine months period ended September 30, 2010 compared to the same period of the prior year.

Net sales of gas accounted for 60% and 64% of total net sales in the nine months periods ended September 30, 2010 and 2009, respectively.

Net sales of gas increased from RR 1,376,724 million in the nine months period ended September 30, 2009 to RR 1,500,360 million in the nine months period ended September 30, 2010 or by 9%.

Net sales of gas to Europe and other countries decreased in the nine months period ended September 30, 2010 compared to the nine months period ended September 30, 2009, by RR 52,122 million, or 6%, to

RR 772,880 million. The overall decrease in net sales of gas to Europe and other countries was primarily driven by the decrease in average prices. The gross average RR price (including excise tax and customs duties) decreased by 11% in the nine months period ended September 30, 2010, compared to the nine months period ended September 30, 2009. At the same time volume of gas sold in the nine months period ended September 30, 2010 increased by 4% compared to the same period of the prior year.

Net sales of gas to FSU countries increased in the nine months period ended September 30, 2010 compared to the nine months period ended September 30, 2009, by RR 64,312 million, or 28%, to RR 290,070 million. This increase was mainly due to increase in volumes of gas sold to FSU countries by 29% in the nine months period ended September 30, 2010 compared to the nine months period ended September 30, 2009. At the same time the gross average RR price (including customs duties, net of VAT) decreased by 1% in the nine months period ended September 30, 2010 compared to the same period of the prior year.

Net sales of gas in the domestic market increased in the nine months period ended September 30, 2010 compared to the same period of the prior year, by RR 111,446 million, or 34%, to RR 437,410 million. This increase was mainly due to the increase in the gross average price for domestic gas sales by 29% in the nine months period ended September 30, 2010 compared to the same period of the prior year due to increase in tariffs which are set by the Federal Tariffs Service (FTS), and increase in the volumes of gas sold by 4% in the nine months period ended September 30, 2010 compared to the same period of the prior year.

Net sales of refined products (net of excise tax, VAT and customs duties) increased by RR 102,350 million, or 25%, to RR 504,711 million in the nine months period ended September 30, 2010 in comparison with the same period of the prior year. The increase mainly resulted from the increase in volumes sold and increase of prices for refined products of Gazprom neft Group, as well as the acquisitions of subsidiaries in 2009 by Gazprom neft Group. In the nine months periods ended September 30, 2010 and 2009 Gazprom neft Group's sales comprised 84% and 81% of the total amount of our net sales of refined products, respectively.

Net sales of electric and heat energy (net of VAT) increased by RR 69,621 million, or 51%, to RR 206,610 million in the nine months period ended September 30, 2010 compared to the same period of the prior year. This increase was mainly due to consolidation of TGC-1 starting from 31 December 2009 after control over that entity was obtained that resulted in an increase of RR 36,275 million and increase of sales of electric and heat energy related to activity of Mosenergo, WGC-2 and WGC-6 by RR 34,083 million, or 25%.

Net sales of crude oil and gas condensate (net of excise tax, VAT and customs duties) increased by RR 19,030 million, or 16%, to RR 141,366 million in the nine months period ended September 30, 2010 compared to RR 122,336 million in the nine months period ended September 30, 2009. The increase was mainly caused by the increase of oil and gas condensate price in the nine months period ended September 30, 2010 compared to the same period of the prior year. Also the increase resulted from the increase of the volume of gas condensate sold in the nine months period ended September 30, 2010 compared to the same period of the prior year. Sales of crude oil included in net sales of crude oil and gas condensate (net of excise tax, VAT and customs duties), amounted to RR 121,675 million and RR 113,506 million in the nine months periods ended September 30, 2010 and 2009, respectively.

Gas transportation net sales (net of VAT) increased by RR 25,632 million, or 62%, to RR 67,195 million in the nine months period ended September 30, 2010 from RR 41,563 million in the nine months period ended September 30, 2009. The increase was mainly caused by increase in gas volumes transported for independent gas suppliers in the nine months period ended September 30, 2010 compared to the same period of the prior year.

Other revenues increased by RR 12,733 million, or 17%, to RR 87,502 million in the nine months period ended September 30, 2010 compared to RR 74,769 million in the nine months period ended September 30, 2009.

Operating expenses

Operating expenses increased by 11% in the nine months period ended September 30, 2010 to RR 1,743,321 million from RR 1,568,784 million in the nine months period ended September 30, 2009. Operating expenses as a percentage of sales decreased from 73% in the nine months period ended September 30, 2009 to 70% in the nine months period ended September 30, 2010. The table below presents a breakdown of operating expenses in each period:

(RR million)	Nine months periods ended 30 September, 2010	2009
Purchased gas and oil	444,269	487,439
Staff costs	216,931	184,201
Taxes other than on income	208,556	171,881
Transit of gas, oil and refined products	208,508	167,617
Depreciation	175,832	155,749
Repairs and maintenance	104,798	93,724
Materials	60,586	58,612
Cost of goods for resale, including refined products	51,891	43,234
Electricity and heating expenses	44,404	31,182
Rental expenses	18,347	12,969
Research and development expenses	17,589	15,744
Social expenses	16,726	14,309
Transportation services	12,973	5,610
Insurance expenses	11,105	11,243
Charge for impairment provisions	9,742	15,376
Exchange rate differences on operating items	6,961	(34,401)
Other	134,103	134,295
Total operating expenses	**1,743,321**	**1,568,784**

Purchased gas and oil

Cost of purchased gas and oil decreased by 9% to RR 444,269 million in the nine months period ended September 30, 2010 from RR 487,439 million in the nine months period ended September 30, 2009. The decrease in cost of purchased gas primarily relates to the decrease of volumes and price of gas purchased from Central Asian suppliers. The cost of purchased oil included in the cost of purchased gas and oil increased by RR 42,157 million, or 38%, and amounted to RR 153,575 million in the nine months period ended September 30, 2010 in comparison with RR 111,418 million in the nine months period ended September 30, 2009 due to increase in oil prices and increase in volumes of purchased oil.

Staff costs

Staff costs increased by 18% to RR 216,931 million in the nine months period ended September 30, 2010 from RR 184,201 million in the nine months period ended September 30, 2009. The increase mainly resulted from the salary indexation. The increase also reflects the consolidation of TGC-1 starting from 31 December 2009 after control over that entity was obtained and acquisitions of new subsidiaries by Gazprom neft Group in 2009.

Taxes other than on income

Taxes other than on income consist of:

(RR million)	Nine months periods ended September 30, 2010	2009
Natural resources production tax	123,100	98,719
Property tax	32,296	26,215
Other taxes	53,160	46,947
Taxes other than on income	**208,556**	**171,881**

The natural resources production tax increased by 25% to RR 123,100 million in the nine months period ended September 30, 2010 from RR 98,719 million in the nine months period ended September 30, 2009. The increase mainly resulted from increase of natural resources production tax base due to increase in average world oil prices as well as from the increase of gas production.

Transit of gas, oil and refined products

Transit of gas, oil and refined products increased by 24% to RR 208,508 million in the nine months period ended September 30, 2010 from RR 167,617 million in the nine months period ended September 30, 2009. This growth mainly relates to increased costs of gas transportation through Ukraine.

Depreciation

Depreciation increased by 13% or RR 20,083 million to RR 175,832 million in the nine months period ended September 30, 2010 from RR 155,749 million in the nine months period ended September 30, 2009. The increase primary relates to the growth in the fixed asset base.

Repairs and maintenance

Cost of repairs and maintenance increased by 12% to RR 104,798 million in nine months period ended September 30, 2010 from RR 93,724 million in the nine months period ended September 30, 2009. This increase was caused by the increase of volume of repair services rendered by third parties to the Group in the nine months ended September 30, 2010.

Materials

Cost of materials increased by 3% to RR 60,586 million in the nine months period ended September 30, 2010 from RR 58,612 million in the nine months period ended September 30, 2009. The increase mainly resulted from the increase of expenses of fuel in the segment “Electric and heat energy generation and sales”.

Cost of goods for resale, including refined products

Cost of goods for resale, including refined products increased by 20% to RR 51,891 million in the nine months period ended September 30, 2010 from RR 43,234 million in the nine months period ended September 30, 2009. The increase in cost of goods for resale mainly results from operations of WGC-2 and WGC-6 (purchase and sale of electricity).

Electricity and heating expenses

Electricity and heating expenses increased by 42% to RR 44,404 million in the nine months period ended September 30, 2010 from RR 31,182 million in the nine months period ended September 30, 2009. The increase mainly resulted from the increase of electricity consumption and increase of tariffs.

Exchange rate differences on operating items

Exchange rate differences on operating items in the nine months period ended September 30, 2010 amounted to a net loss of RR 6,961 million in comparison with exchange rate differences on operating items in the amount of a net gain of RR 34,401 million in the same period of the prior year. The change was primarily driven by appreciation of RUR against EUR by 5% in the nine months ended 30 September 2010 that was partly offset by depreciation of RUR against USD by 1% comparing to depreciation of RUR against USD and EUR by 2% and 6% respectively, in the same period of the prior year.

Other operating expenses

Other operating expenses decreased by 5% to RR 127,107 million in the nine months period ended September 30, 2010 from RR 134,295 million in the nine months period ended September 30, 2009. Other operating expenses include refining services, heat energy transmission expenses, bank charges, security services, legal and consulting services, charity and financial aid, and advertising.

Operating profit

As a result of the factors discussed above, our operating profit increased by RR 185,905 million, or 32%, to RR 774,739 million in the nine months period ended September 30, 2010 from RR 588,834 million in the same period of the prior year. Our operating profit margin increased from 27% in the nine months period ended September 30, 2009 to 31% in the nine months period ended September 30, 2010.

Finance income (expense)

(RR million)	Nine months periods ended September 30, 2010	2009
Exchange gains	111,774	312,367
Exchange losses	(97,612)	(326,258)
Net exchange gain (loss)	14,162	(13,891)
Interest income	15,188	27,230
Interest expense	(30,790)	(56,987)
Gains on extinguishment of restructured liabilities	5	82
Net finance expense	**(1,435)**	**(43,566)**

Exchange gains decreased by RR 200,593 million to RR 111,774 million in the nine months period ended September 30, 2010, compared to RR 312,367 million in the nine months period ended September 30, 2009. Exchange losses decreased by RR 228,646 million to RR 97,612 million in the nine months period ended September 30, 2010 from RR 326,258 million in the nine months period ended September 30, 2009. The decrease in exchange gains and exchange losses resulted from lower fluctuation of USD and EUR exchange rates against RR in the nine months ended September 30, 2010 in comparison with the same period of the prior year.

Interest income decreased by 44% to RR 15,188 million in the nine months period ended September 30, 2010 from RR 27,230 million in the nine months period ended September 30, 2009, mainly due to deconsolidation of ZAO Gazenergoprombank in the second quarter 2010.

Interest expense decreased by 46% to RR 30,790 million in the nine months period ended September 30, 2010 from RR 56,987 million in the nine months period ended September 30, 2009, mainly due to decrease of average borrowings balance during nine months period ended September 30, 2010, in comparison with the same period of the prior year.

Share of net income of associated undertakings and jointly controlled entities

Share of net income of associated undertakings and jointly controlled entities increased by RR 31,113 million, or 72%, to RR 74,153 million in the nine months ended September 30, 2010 compared to RR 43,040 million in the same period of the prior year. The increase of the Group's share of net income of associated undertakings and jointly controlled entities in the nine months ended September 30, 2010 relates mainly to increase of net income of Sakhalin Energy Investment Company Ltd. due to the start of liquefied natural gas production in March 2009 and increase of net income of Gazprombank Group due to petrochemical business in the nine months period ended September 30, 2010 compared to the same period of the prior year.

Profit tax

Total profit tax expense increased by RR 55,980 million, or 45%, to RR 181,185 million in the nine months period ended September 30, 2010 compared to RR 125,205 million in the nine months period ended September 30, 2009. The effective profit tax rate was 21.3% and 20.7% in the nine months periods ended September 30, 2010 and 2009, respectively.

Profit for the period attributable to owners of OAO Gazprom

As a result of the factors discussed above, our profit for the period attributable to owners of OAO Gazprom increased by RR 182,847 million, or 39%, from RR 470,874 million in the nine months period ended September 30, 2009 to RR 653,721 million in the nine months period ended September 30, 2010.

Profit for the period attributable to non-controlling interest

Profit for the period attributable to non-controlling interest increased by RR 6,617 million, or 79%, to RR 15,032 million in the nine months period ended September 30, 2010 compared to RR 8,415 million in the nine months period ended September 30, 2009.

LIQUIDITY AND CAPITAL RESOURCES

The following table summarizes our statement of cash flows for the nine months periods ended September 30, 2010 and 2009:

	Nine months periods ended September 30,	
(RR million)	**2010**	**2009**
Net cash provided by operating activities	1,018,359	587,048
Net cash used for investing activities	(748,776)	(808,400)
Net cash (used for) provided by financing activities	(199,856)	161,067

Net cash provided by operating activities

Net cash provided by operating activities amounted to RR 1,018,359 million in the nine months period ended September 30, 2010 compared to RR 587,048 million in the nine months period ended September 30, 2009. The increase was primarily due to growth of our operating profit in the nine months period ended September 30, 2010 in comparison with the same period of the prior year, which was supplemented by positive dynamics of changes in working capital.

Net cash used for investing activities

Net cash used for investing activities decreased by RR 59,624 million, or 7%, to RR 748,776 million in the nine months period ended September 30, 2010 compared to RR 808,400 million in the nine months period ended September 30, 2009. This change relates mainly to the purchase of non-controlling interest in OAO Gazprom neft in 2009 for RR 138,527 million and receipt of proceeds from redemption of preference shares in Sakhalin Energy Investment Company Ltd. in the nine months period ended September 30, 2010. These effects were partly offset by the increase in cash and cash equivalents used for capital expenditures and decrease in cash and cash equivalents in the amount of RR 32,504 million due to deconsolidation of banking subsidiaries in the current period.

Net cash (used for) provided by financing activities

Net cash used for financing activities amounted to RR 199,856 million in the nine months period ended September 30, 2010 compared to net cash provided by financing activities in the amount of RR 161,067 million in the nine months period ended September 30, 2009. This change was due to decrease in proceeds from long-term and short-term borrowings in the nine months period ended September 30, 2010 compared to the same period of the prior year.

CAPITAL EXPENDITURES

Total capital expenditures (excluding the effect of acquisitions of subsidiaries) by segment for the nine months periods ended September 30, 2010 and 2009 in nominal RR terms, amounted to the following:

	Nine months periods ended September 30,	
	2010	**2009**
(RR million)		
Transport	249,669	200,291
Production of gas	173,614	177,136
Production of crude oil and gas condensate	62,173	54,350
Refining	51,641	43,417
Electric and heat energy generation and sales	33,587	17,183
Distribution	25,089	17,113
Gas storage	8,352	7,616
All other segments	16,426	13,435
Total	**620,551**	**530,541**

Total capital expenditures (excluding the effect of acquisitions of subsidiaries) increased by RR 90,010 million, or 17%, from RR 530,541 million in the nine months period ended September 30, 2009 to RR 620,551 million in the nine months period ended September 30, 2010. The increase of our capital expenditures in the Transport segment was primarily due to increased capital expenditure on the construction of major transportation projects, including Pipeline Sakhalin-Khabarovsk-Vladivostok, Pipeline Bovanenkovo-Uhta, and Nord Stream. The increase of our capital expenditures in the Production of crude oil and gas condensate segment was primarily due to increased capital expenditure of OAO Gazprom neft. The increase of our capital expenditures in the Electric and heat energy generation and sales segment was primarily due to consolidation of TGC-1 starting from 31 December 2009 after control over that entity was obtained.

DEBT OBLIGATIONS

Net debt balance (defined as the sum of short-term borrowings, current portion of long-term borrowings, short-term promissory notes payable, long-term borrowings, long-term promissory notes payable and restructured tax liabilities, net of cash and cash equivalents and balances of cash and cash equivalents restricted as to withdrawal under the terms of certain borrowings and other contractual obligations) decreased by RR 400,527 million, or 29%, from RR 1,372,307 million as of December 31, 2009 to RR 971,780 million as of September 30, 2010. This decrease resulted from decrease of short-term and long-term borrowings, which was primarily caused by the effect of early redemption of long-term borrowings, deconsolidation of banking subsidiaries of the Group as of 30 September 2010 and the increase in cash and cash equivalents.