Annual report | 2004 |

JOINT-STOCK FINANCIAL CORPORATION

SISTEMA

WE ARE WINNING—
INVESTORS ARE WINNING

Contents

Contents

In the present Annual Report, except where the context implies a different interpretation, the terms Sistema, the Group, the Company, Corporation, 'we', 'us', 'our' and similar terms apply to the consolidated business of Sistema and its subsidiaries.

Certain phrases in the present Annual Report may be related to forecasts and projections concerning forthcoming events, based on assumptions and estimates of the executive management of Sistema. Such words as 'expected', 'considered', 'estimated', 'intended', 'will be', 'may be' and other similar terms reflect these forecasts and projections. These statements reflect a true position of the company. Considering possible risks and unforeseeable circumstances, including changes in the overall economic situation, changes in the currency and stock markets, and so forth, we wish to warn you that actual results may differ from those indicated in the statements and forecasts.

In the information in the sections 'Structure of the Shareholding Capital', 'Board of Directors', 'Executive Management', 'Asset Structure' and 'Organizational Structure' is cited as of July 1, 2005.

ABOUT THE COMPANY

SISTEMA: WE BRING UP LEADERS

Sistema Joint-Stock Financial Corporation:

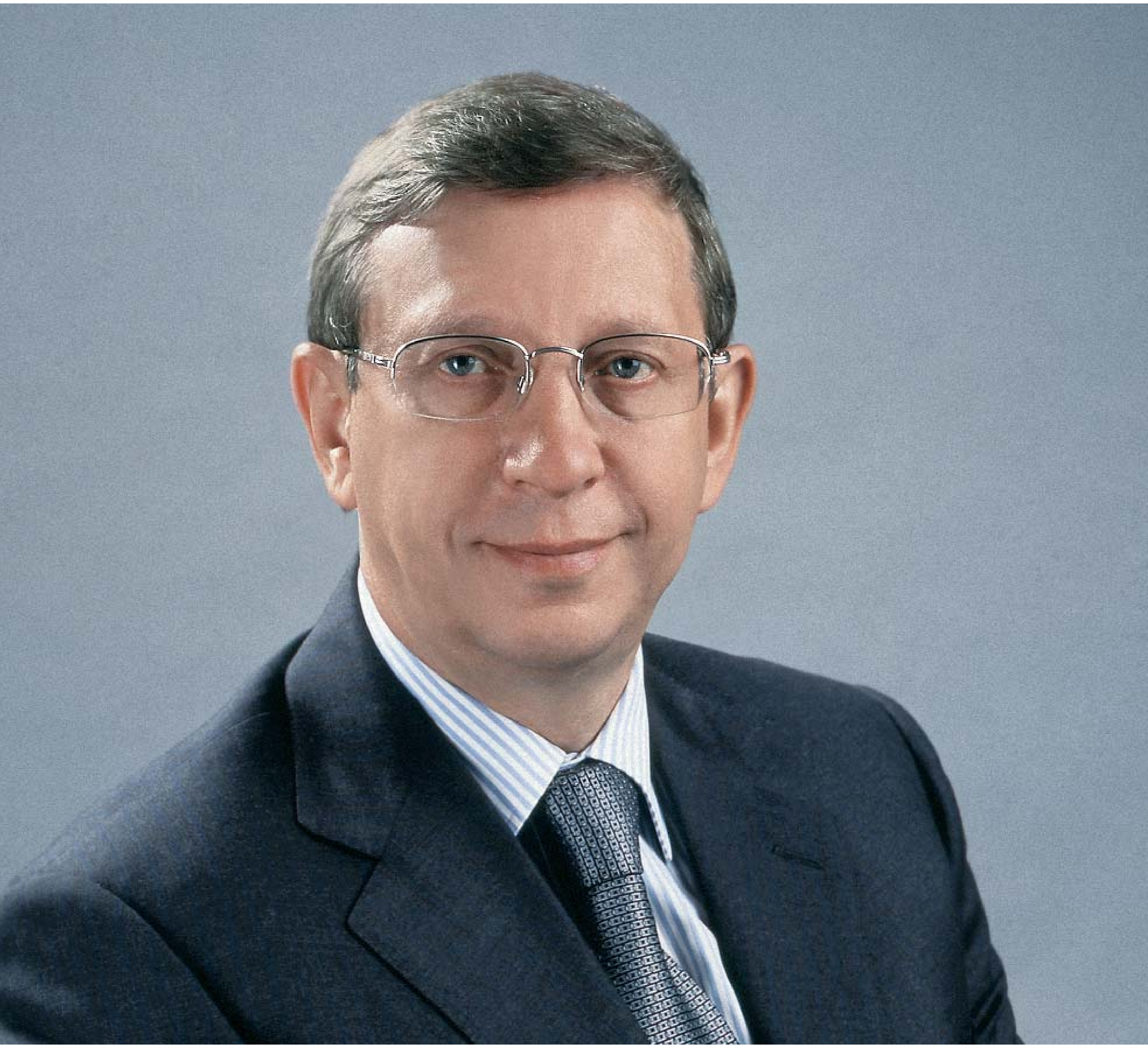
- the largest publicly held diversified company in Russia and the CIS oriented to the market of high-technology services with more than 40 million consumers;
- in February 2005, following an initial public offering, placed global depository receipts (GDRs) on the London Stock Exchange;
- maintaining steady growth of its assets and profitability, aimed at achieving leading positions in diverse, fast-growth sectors of the economy;
- expanding strategic partnership with leading international companies while independently entering overseas markets;
- continuing its mission of developing high technology in Russia, seeing this as its social responsibility;
- constantly evaluating opportunities to enter new market segments;
- possessing a modern corporate governance structure and implementing a long-term social policy

Sistema's Strategic Areas of Activity:

telecommunications;
insurance;
high technology;
finance;
real estate;
retail;
mass media.

Sistema in 2004:
(US dollars, millions)

Sales +51,9%	5711
Operating Profit +50,5%	1665
Net Profit +6,2%	411
Summary Assets +29%	8780
Number of Employees:	70000



President, Sistema
Vladimir **Yevtushenkov**

THE PRESIDENT'S MESSAGE

For Sistema, the year 2004 represented a period of maximum concentration of all of the company's intellectual and organizational resources during the run-up to the biggest event in its history, the initial public offering of shares on the London Stock Exchange. Once again we confirmed our reputation as leaders and pioneers. The IPO undertaken by Sistema was the largest ever undertaken by a Russian company and permitted the corporation to begin the process of further integration into the global business community.

This achievement, significant for the entire Russian economy, required considerable work. The primary factor setting Sistema apart from other participants in the market, which operate primary in raw material sectors, is the concentration of a large part of our assets in the area of high technology production and services. It is in this sphere that Sistema tightly focuses all of its potential and energy. The corporation views the high technology sector as the primary driver of the development of the Russian economy and, over the long-term perspective, the basis for the well-being of the country.

In 2004 Sistema consolidated its leadership in key, strategically important sectors. Telecommunications, first of all, dominated the financial indicators of the corporation. But we also made substantial advances in increasing the diversification of our business. The high technology segment showed strong growth. The share of Concern Scientific Center of the total sales of the corporation increased by more than four times in comparison with 2003 and reached 8.5%. The Real Estate business area demonstrated an impressive rate of growth, increasing sales by the end of the year by more than two times. The Insurance segment of the ROSNO corporation and its affiliates showed 60% growth in insurance premiums, outpacing the overall market. We believe that the share of non-telecommunications assets in the corporation's business portfolio will continue to grow steadily.

As a whole the consolidated sales of the corporation increased by 52% to $5.71 billion in 2004. The operating profit grew to $1.66 billion and the figure for net profit reached $411 million, a 6% increase compared to 2003.

In 2004, thanks to successful merger and acquisition deals, asset restructuring and the completion of business plans by operating companies, we were able to scale new business heights. Entry to the London Stock Exchange allowed Sistema to gain access to unprecedented investment capital. The funds raised by the IPO, $1.3 billion, expand our business horizons and give us the ability to implement a more flexible development strategy, both in the investment plan for existing companies as well as plans for possible acquisitions of new assets. The long-term plans of Sistema envision the eventual placement of a range of large subsidiary structures on the international capital markets.

But the IPO of the corporation has already passed into history. We must now think about moving forward. The world is constantly changing, particularly the business world. In order to keep pace and to move ahead we must make quantum leaps forward.

We would like to acknowledge all of our shareholders, managers, partners and employees for their support and their understanding of our common goals. I am entirely convinced that it is the quality of people that separates a successful company from an unsuccessful one. Sistema, occupying a leading position in the high-technology business, has enormous potential and all of the necessary components to become a company on the global level and maintain our position in conditions of global competition. Of course this cannot be accomplished in a single year. But we have established a good pace and are confident of success.

Vladimir **Yevtushenkov**
President, Sistema

Chairman of the Board of Directors, Sistema
Yevgeny **Novitsky**

THE CHAIRMAN OF THE BOARD OF DIRECTORS MESSAGE

A high degree of integration into the global economy is an indispensable condition for the successful development of a modern, large business. For our corporation this is an axiom. From the moment of its founding, Sistema has striven to meet the requirements of the global marketplace.

The basic principles that are the foundation of our activity — efficient management, wide diversification, the high profitability of all of our businesses and transparent management — have allowed the corporation to become one of the most successful financial industrial groups in Russia.

The year 2004 will go down in the history of Sistema as a moment when we reached yet another frontier. It was the last year of our work as a private company. The placement of shares of Sistema on the London Stock Exchange at the beginning of 2004 positioned the corporation in a new orbit, confirming the interest of investors in the market where Sistema is the acknowledged leader.

Our new status as a public entity required adherence to still higher standards of doing business. Having become a player in the world league, Sistema took upon itself a range of serious obligations. Investors expect us to play according to the tightly established rules of the world financial markets. And we are working to justify the trust of our partners.

We are fully aware that being active on a global scale is impossible without the highest level of corporate governance and the maximum transparency of our business. In 2004 Sistema worked very actively in this direction and made significant efforts to ensure our partners and contractors gained a full understanding of our business. We adopted a Code of Corporate Governance, formed a Corporate Governance Committee on the Board of Director level, appointed a corporate secretary and developed a Code of Ethics for the corporation. These steps allow us to earn the trust of the business community in the global arena and increase our attractiveness to investors.

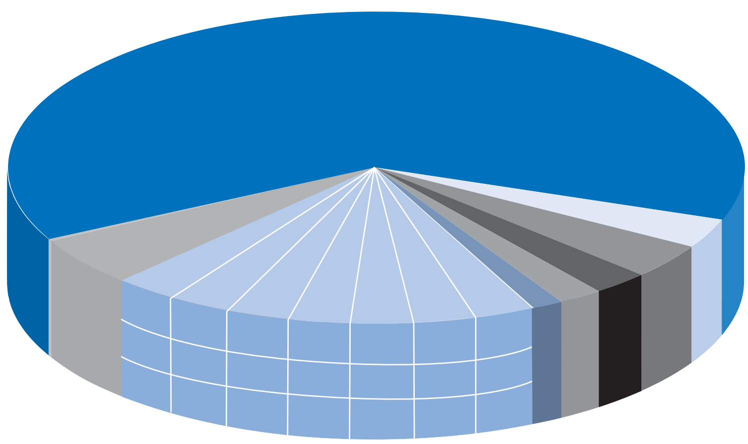
One of the most important principles that Sistema always strives to follow in full measure is the responsible development of business in the interests of society. We see real values, which form the national wealth of the country, in intellectual leadership. The very nature of the corporation's activities is a part of its exercise of social responsibility. Our investments in high technology are dictated by the steadfast belief that it is the economy of ideas and innovation that are most effective and have the greatest potential for Russia, rather than an economy based on the exploitation of raw material resources.

We are investing in the development of an intellectually driven society where our services will be most called upon. The corporation is working actively with the leading scientific institutions of the country — providing scholarships for the best students, taking part in teaching activities and the creation of joint programs that support young people's creativity. In these efforts we see our role in increasing Russia's competitiveness in the global marketplace.

In 2004 the corporation undertook a range of important initiatives to support culture. We worked towards the realization of a wide-ranging program of cooperation with the Russian State Museum of St. Petersburg, the largest depository of Russian art in the world. Providing the possibility for as many Russians as possible to take part in national cultural traditions and preserve them for future generations is our social investment in the future.

Yevgeny **Novitsky**
Chairman of the Board
of Directors, Sistema

Structure of Shareholding Capital



- Vladimir Yevtushenkov - 63,13%
- Yevgeny Novitsky - 3,2%
- Alexander Leiviman - 3,58%
- Alexander Gorbatovsky - 2,43%
- Alexander Goncharuk - 2%
- Dmitry Zubov - 1,39%
- Nikolai Mikhailov - 0,07%
- GDR holders - 18,95%
- Other Shareholders - 5,26%

* Shareholders owning two or more percent of the shares of Sistema

ASSET STRUCTURE

TELECOMMUNICATIONS

SISTEMA TELECOM
Wireless
GSM Standard 900/1800
MTS and subsidiary companies
Standard CDMA 2000
Sky Link
Fixed Line
Incumbent Operators:
MGTS
CLEC operators under Comstar-UTS Brand-Name
Comstar
MTU-Inform
Telmos
Internet and Data transfer
MTU-Intel
Golden Line
Telematics
MTS P
Trunking
Center-Telco
AMT
Traffic Transit
MTT
Infrastructure
Metro Telecom

ELECTRONICS

Concern Scientific Center (CSC)
Information Communications Systems
STROM Telecom Group of companies
Iskratel (Novosibirsk)
Telsa Tech (Prague)
BS Telecom 2 (Sarajevo)
Mediatel
Programming Services
Kvazar Micro Group of companies
Microelectronics
NIIME and Mikron
Kvant
VZPP-Mikron
Consumer and Industrial Electronics
Sitronics
Elax
Elion
NIITM
Kontsel

INSURANCE

All insurance products
ROSNO
Obligatory medical insurance
SK Rosno-MS
Reinsurance
PK ROSNO-Center
Medical services
American Hospital Group

REAL ESTATE

Sistema-Hals
Construction and Real Estate Management
City-Hals
Hals Management
MosDachTrest
Sistema-Hals North-West
Organizator
Project Management
Kuntsevo-Invest
Landshaft
Sistema-Temp
Beijing-Invest
Hotel-Korona Intourist

RETAIL

DETSKY MIR GROUP OF COMPANIES
Retail Trade
Detsky Mir Center
Bauland
Retail Trade, Retail Property Management
Detsky Mir
Detsky Mir-Orel
Dom Igrushki
Warehousing
DM Baza
Wholesale Trade
Noekoeln

ASSET STRUCTURE

FINANCE

MBRD
East-West United Bank

TOURISM AND FOREIGN ASSETS

SISTEMA-INTERNATIONAL INVESTMENT GROUP

Travel Services
Intourist and subsidiary companies
Ten Viagi (Italy)
Intourist-Japan (Japan)
Intourist-Warsaw (Poland)
Intourist Corporation (Canada)
Fram Resource (Sweden)
Hotel Services
Intourist Hotel Group

RADIO ENGINEERING

RTI-Systemy Concern
Radio Engineering
RTI
NIIDAR Research and Production Complex
RTI-Radio
Instrument Building
STZ (Saransk)
Radio Tesla Sistema
Info-telecommunications Systems
Vimpel-S
OKTA-SISTEMS (Belarus)

MASS MEDIA

SISTEMA MASS MEDIA
Printed and Electronic Media
Literaturnaya Gazeta
METRO Newspaper
Rossiya Public Newspaper
Rosbalt Information Agency
Concern Radio Center
Kosmos-TV
Advertising
Maxima Communications Group
TV-Project
Metroreklama Group
Press Distribution
Nasha Pressa Group of companies
Multimedia services
Sistema Multimedia
Motion picture production
Thema Productions

OTHER COMPANY PROJECTS

Helicopter Manufacturing
Kamov Holding
Pharmaceuticals
Medicine Technologies Holding Company (MTH)
Innovative Venture Project Management
Sistema Venture
Sports Facilities Management
Olympic System
Medical Services
Medsi Holding
Cargo Vehicles Assembly
VTS-Zelenograd
Securities Operations, Real Estate Investments
Ecu-Gest and subsidiary companies
Managing Company
Sistema Investments
Leasing
Invest-Svyaz-Holding
Pension Fund
Sistema Non-State Pension Fund
Charitable Activities
Sistema Charity Fund

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KEY PRINCIPLES THAT SISTEMA FOLLOWS IN MANAGING ITS COMPANIES ARE TRANSPARENCY AND INFORMATION DISCLOSURE STANDARDS TO ENSURE THE CONFIDENCE OF PARTNERS AND INVESTORS, AS THIS IS CRITICAL TO SUCCESS

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ING, report “Sistema. Number One!”,
January 7, 2005

BOARD OF DIRECTORS

President, Sistema
Vladimir Yevtushenkov

Chairman of the Board of Directors, Sistema
Yevgeny Novitsky

Deputy Chairman of the Board of Directors, Sistema
Dmitry Zubov

Deputy Chairman of the Board of Directors, Sistema
Vyacheslav Kopiev

General Director, Concern Scientific Center
Alexander Goncharuk

Member of the Board of Directors, Sistema, Independent Director
Alexander Gorbatovsky

Senior Vice-President, Sistema, Head of Property Affairs
Sergei Drozdov

General Director, Sistema Telecom
Vladimir Lagutin

General Director, Sistema Mass Media
Alexander Leiviman

Member of the Board of Directors, Sistema, Independent Director
Nikolai Mikhailov

Member of the Board of Directors, Sistema, Independent Director
Ron Sommer

EXECUTIVE MANAGEMENT

from the left

First Vice-President, Sistema,
Head of Strategy and Development
Levan Vasadze

Senior Vice-President, Sistema,
Head of Finance and Investments
Alexey Buyanov

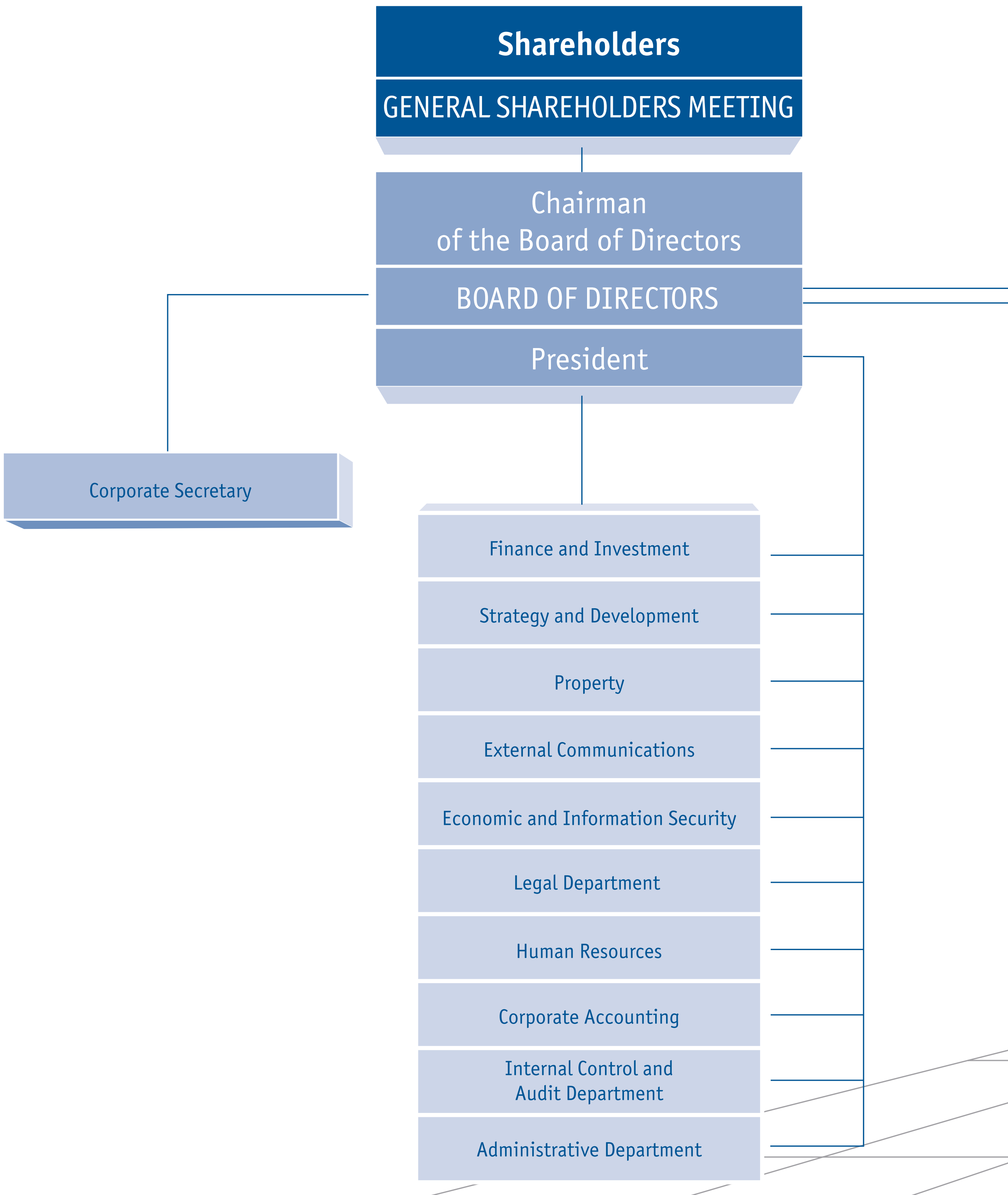
Senior Vice-President, Sistema, Head of
Property Affairs
Sergei Drozdov

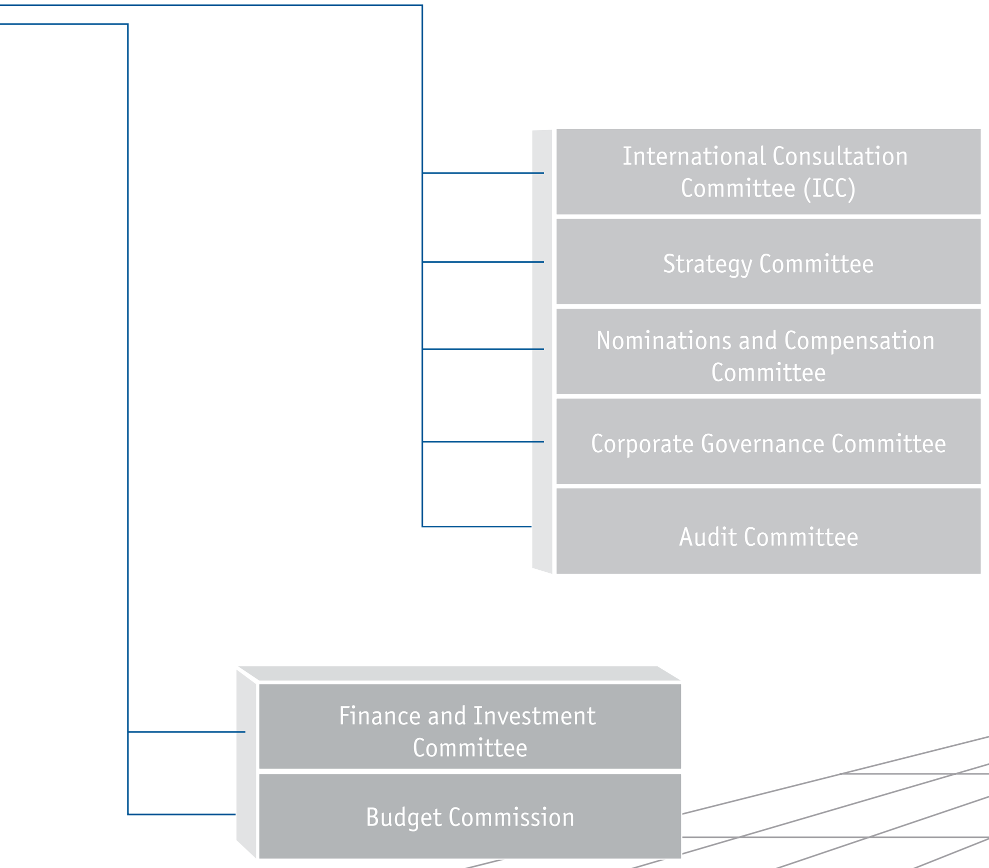
Vice-President, Sistema,
Head of External Relations
Sergey Cheremin

Vice-President, Sistema, Head of Economic and
Information Security
Ruslan Almakaev

Chief Accountant, Sistema
Vasily Platoshin

ORGANIZATIONAL STRUCTURE




International Consultation Committee (ICC)
Strategy Committee
Nominations and Compensation Committee
Corporate Governance Committee
Audit Committee
Finance and Investment Committee
Budget Commission

DEVELOPMENT STRATEGY

The strategy of Sistema is directed at the development of market leading companies. The corporation is oriented towards efficient investment, the diversification of its business portfolio, partnerships with strategic investors, the retention of a high level of management resources and a considered approach to investment.

Sistema intends to realize its strategy by cultivating the internal potential of its key business areas and acquiring assets that complement these businesses, as well as carefully selected investments in new areas of activity.

Sistema's size, experience of successful cooperation with international strategic investors, effective management and a diversified structure of assets provide its companies with considerable resources for achieving their strategic goals.

Strategic Goals

Diversification

The largest component of Sistema's business is telecommunications. The goal is to maintain the intensive growth of non-telecommunications assets and to increase their relative weight in the overall business profile of the corporation.

Monetary flows

The main goal of the corporation following the IPO is to increase the share of regular contributions from business areas to the total volume of revenues.

Stability

Sistema makes use of its access to capital markets for financing the development of its businesses. The goal is to maintain the high level of financial stability of the corporation and to observe limits on maximum debt levels.

Leadership

Strengthening the leading position of the telecommunications and insurance businesses of the corporation is a priority for Sistema. We have also set the goal of becoming leaders in the remaining business areas such as high technology, retail, real estate and finance.

Management

A strategic goal of Sistema is to sustain the high quality of the management resources of the corporation as a whole and in each business in particular. We have formed a solid team of managers who have shown their ability to create and develop efficient, working businesses and who have experience of successful work in different industries and a record of cooperation with state entities.

In order to achieve these strategic goals, the corporation has developed a Criteria Base for each business area. The goal of each Criteria Base is to strengthen each business and ensure the diversification of the business profile of Sistema as a whole. It includes a selection of ten basic and several specific industrial criteria that the businesses should meet over both the short and medium term.

Financial Strategy

The financial strategy of Sistema is based on the following principles:

Financial transparency

Sistema has prepared consolidated, audited reporting according to US GAAP standards since 1997. The corporation has disclosed its reporting to the investment community since 2003. From 2006 Sistema plans to convert the reporting of all business areas to US GAAP in order to increase transparency and improve financial controls.

Optimal use of capital markets

Sistema is the largest holding company in the consumer services sector in Russia and has unique experience of successful investment in the country. This provides us with far more extensive means for access to global capital markets than many of our competitors. The widespread geography of international investors allows us to optimize the structure of financing sources for the corporation in order to lower the cost of investment and increase its overall efficiency. For the period from 2002 to 2004 the share of public instruments in the overall debt of Sistema increased to 60%.

Control over consolidated borrowing

Active work in the capital markets requires our constant attention to the structure and management of our debt obligations. Having increased borrowing, Sistema works carefully to support the financial stability of the corporation. The Committee for Finance and Investment and the Budget Commission control the level of debt both on the corporate level and at each individual business. We have developed a system of strict controls on the size of debt obligations.

Universal approach to budgeting

Sistema is a large holding structure and uses a 'bottom-up' approach to corporate budgeting. Each business area compiles a yearly budget that goes to the Budget Commission for approval. The budgets of the separate businesses of Sistema are brought together in the consolidated budget and it is approved at the corporate level. We carefully track the results at each of the business areas and their adherence to the strategic goals set before them. Beginning in 2005, the corporation is moving to the development of yearly and five-year financial economic plans according to US GAAP standards to raise the efficiency of financial planning and control to a qualitatively new level.

Priority of financing strategic businesses

During the creation of an investment plan, Sistema gives priority to projects in strategic business areas that preserve their efficient development and that are in accordance with the requirements of the Criteria Base.

Investment strategy

The investment strategy of Sistema is based on the following principles:

Concentration of investment resources in strategic business areas

Projects that ensure the intensive growth of key businesses have undisputed investment priority.

In relation to other areas of activity, self-financing and the attraction of outside financing and strategic investors are encouraged.

Development of perspective business areas

Sistema develops only the most perspective business areas with the goal of promoting them to the level of strategic businesses or merging them into such areas. Businesses that have achieved the peak of their development that demonstrates sub-optimal efficiency as well as representing industries that have lost growth potential, may be sold.

Search for new development possibilities

Sistema constantly evaluates the possibility of entering new market segments that demonstrate a high growth rate and correspond to the strategic goals and investment criteria of the corporation. Sistema reviews possibilities for creating new major business areas and actively participates in high technology venture projects.

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SISTEMA PROVIDES EXPOSURE TO RUSSIA'S RAPIDLY-GROWING SERVICE SECTORS **WITHOUT DIRECT COMMODITY SECTOR RISK**

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Morgan Stanley, report “Sistema. Leadership in Russia’s High Growth Service Sectors”, January 10, 2005

General Director, Sistema Telecom
Vladimir **Lagutin**

The telecommunication sector demonstrated record growth in its client base in 2004. The number of subscribers grew two times over the year, exceeding 40 million. Such a base of consumers of telecommunication services is unique in Russia today.

TELECOMMUNICATIONS

Marketplace

Today telecommunications is one of the most dynamic sectors of the Russian economy. The market continues to demonstrate significant growth potential and considerable attractiveness as an investment. According to data from the Russian Ministry of Information Technologies and Communications, the volume of the Russian telecommunication market grew by 45% to $18.4 billion in 2004 and the average yearly growth rate of the sector over the last five years was 35%. Sistema views business in this sector as fundamental for the successful development of the whole corporation. At the conclusion of 2004, the telecommunication business of Sistema accounted for a quarter of the overall Russian market.

Business

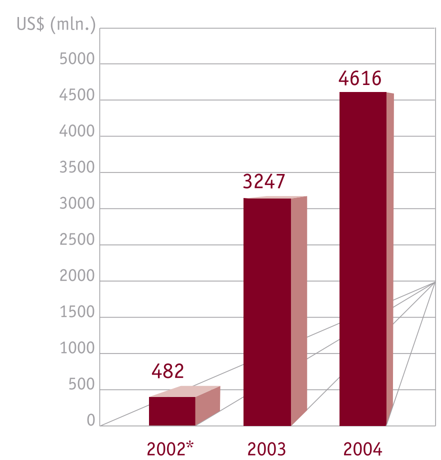
Sistema owns assets of leading operators in the telecommunication industry and is the largest non-governmental player in the market. Sistema Telecom manages the corporation's assets in this segment. In all there are more than 50 telecommunications operators working in the main segments of the market - fixed and mobile telephony, Internet, data transfer, transit traffic and so forth. Sistema Telecom undertakes operating and strategic management of companies, including Mobile TeleSystems (MTS), Moscow City Telephone Network (MGTS), Comstar United Telesystems and others. These all provide a wide range of high-technology services to more than 40 million subscribers in Russia and the countries of the CIS.

Results

In 2004 the consolidation of alternative operators Comstar, MTU-Inform and Telmos into Comstar United Telesystems was essentially completed. Sistema succeeded in creating a large, highly efficient alternative fixed-line operator that is the leader in its segment of the telecommunications market. Sistema Telecom successfully completed the task of technological and financial consolidation of the companies and the creation of a unified system of business processes over a short period of time.

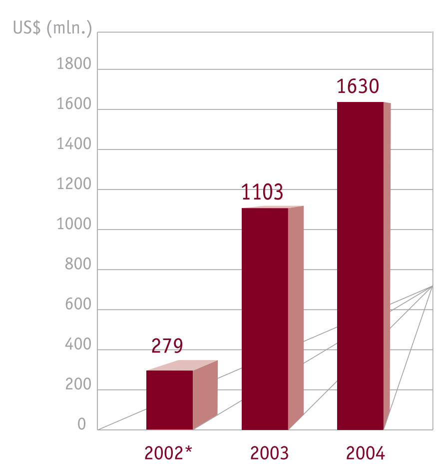
A range of strategic investments was made in the group of companies during the year. Sistema acquired 30% of Interregional Transit Telecom (MTT), an operator of a national scale transit network. With this transaction, the corporation

Revenues



* Not including revenues from MTS

Operating profit

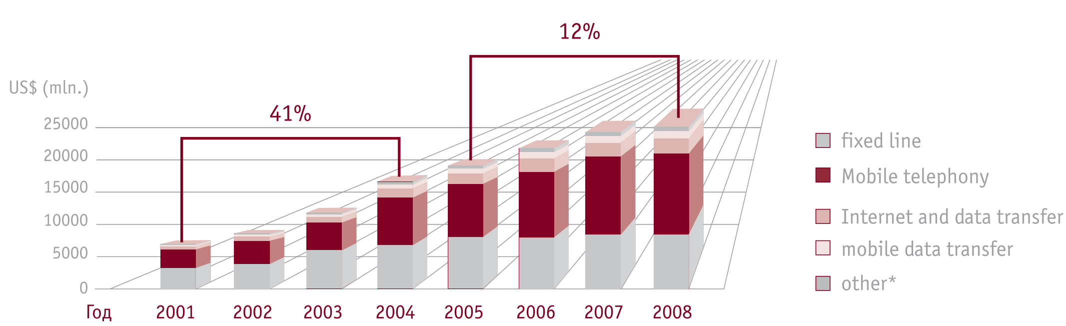


* including operating profit from MTS

increased its share in MTT to 45%. In July 2004 Mobile TeleSystems undertook a major acquisition, buying 74% of the largest Uzbek wireless operator Uzdunrobita. With this move, MTS strengthened its position as the leading operator of mobile telephony in the CIS. MTS also continued to move into the Russian regions during 2004. The company undertook a range of strategic acquisitions of regional mobile operators and created potential for further expansion in the regions.

Consolidated sales in the telecommunication segment grew by 42% to $4.62 billion in 2004. The level of sales growth outpaced the overall rate of the telecommunications market for the fifth year in a row. The rapid development of the telecommunication segment required substantial capital investment, which was undertaken chiefly

Growth rate of the telecommunications industry



* Includes pay TV, video on demand and other content services
Source: Sistema Telecom, Pyramid Research, AT Kearney, Renaissance Capital, ACM Consulting

through the Company's own funds. Capital expenditures grew by 42% over the year and the attraction of outside sources of financing increased the debt load of Sistema Telecom by 33%. Investors positively viewed the development rate of the telecommunication sector and as a result the capitalization of the main assets of the group increased by 59% over the year.

In the beginning of 2005 Sistema increased its share in MTT to 50%, purchasing an additional 5% of the operator's shares. In May, as a result of the de-monopolization of the Russian long-distance market, MTT received the first license for the provision of intercity and international telephone services. The company plans to launch intercity telephone services for a wide range of subscribers in the second half of 2005. In addition, in March Sistema increased its presence in the shareholding capital of the Moscow alternative fixed-line operator Telmos to 100%, having purchased the remaining 20% of its shares.

Outlook

The primary strategic goal of Sistema Telecom is to strengthen its leading positions in all segments of the telecommunication market. Its decision will be enabled by the creation of a national cellular operator on the base of MTS as well as the further expansion of the company's activities in the CIS and in attractive overseas markets. A priority for Sistema Telecom is the regional expansion of the fixed-line operators and their entry into the markets of a number of countries in the CIS, Eastern Europe and Asia. To preserve and build upon these achievements, Sistema Telecom is working actively to grow its potential technologies and services while closely following trends in the market and constantly searching for new opportunities.

General Director, Concern Scientific Center
Alexander **Goncharuk**

Concern
Scientific Center
showed unprecedented
growth in turnover
for a Russian
high technology
company in 2004.
Revenues increased
five times to
$489.4 million
on the back of organic
growth and acquisitions.

High Technology

Marketplace

Sistema is a strategic investor in the high technology industry, owning assets in a range of leading enterprises in this sphere and undertaking long-term investment in its development. Sistema believes in the potential development of this segment. Its inherent high intellectual potential and innovations are a primary competitive advantage in the global marketplace in the 21st century. The corporation views electronics and high technology as a key area of diversification in its business.

Business

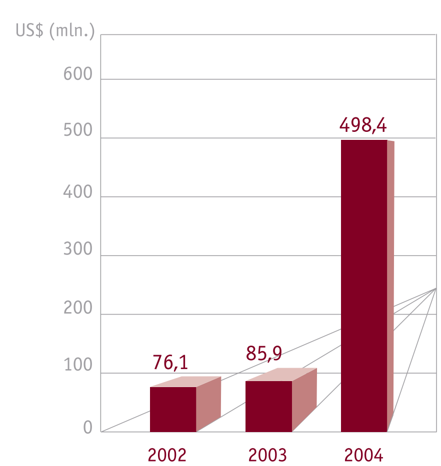
Concern Scientific Center (CSC) manages the assets of Sistema in high technology industries. Created in May 1997 with the goal of consolidating the resources of the company for the execution of large-scale projects in the electronic industry, CSC is one of the largest holdings to bring together leading high-technology enterprises in Russia as well as in Ukraine and the Czech Republic. CSC enterprises specialize in five major areas: info-communications systems (the production of telecommunication equipment and program support), information technology (integration systems, implementation of ERP systems, production of computer equipment), micro-electronic components (development and production of semi-conductors), industrial platforms (production of electronic technology), and complex security systems (development, production and implementation of security systems). CSC is made up of enterprises such as STROM Telecom, Kvazar Micro, NIIME and Mikron, Videophone MV and Sitronics.

Results

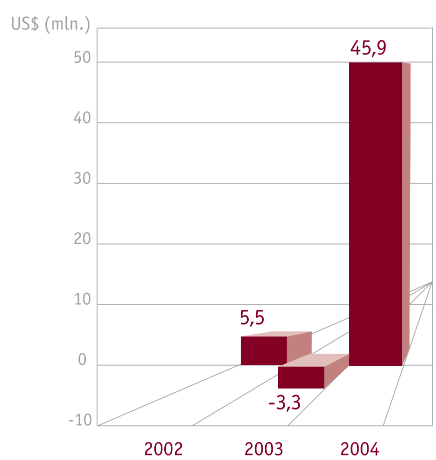
In 2004 CSC entered a new segment of the high-technology business, purchasing 51% of Kvazar-Micro of Ukraine. The company specializes in the provision of system integration services, management consulting, programming services development and the production of computer equipment. Kvazar-Micro operates in 12 countries and occupies one of the top positions in the Central and Eastern European market.

Last year in Zelenograd, production of modern telecommunication equipment began under the brand STROM Telecom. The new production

Revenues



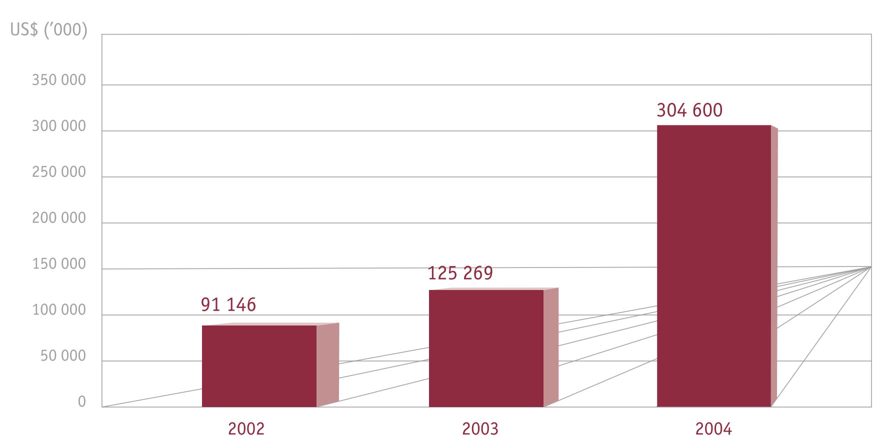
Operating profit



capacity enabled the timely fulfillment of CSC's portfolio of orders. These increased by more than two times in the info-communications system segment in 2004.

During 2004 CSC continued to expand and strengthen its market position in household electronics. The brand Sitronics achieved a 9.8% market share in domestic televisions, significantly increasing the level of brand awareness among consumers. In Moscow, recognition of the trade-mark reached approximately 30%. To a significant degree the growth in the market share of CSC was enabled by the expansion of the brand's product line to 140 named items. In 2004 a distribution network was created including more than 85 dealers.

Asset growth rate



The company Videophone MV became part of CSC in 2004. This company provided a base for a fifth business area for CSC - Complex Security Systems. During the year the company increased its presence in the Moscow security services market by two times and now occupies a third of this market.

CSC's sales increased by more than five times during 2004, reaching $498.4, compared with $85.9 million in 2003. Over the same period the share of CSC in the aggregated revenues of Sistema grew to 8.5%. Organic growth as well as acquisitions drove growth in the segment. The revenues of STROM telecom grew by 154.2% to $101.8 million and the consolidation of Kvazar-Micro increased the revenues of the segment by $293.5 million.

Outlook

The corporation views CSC's strategic goal as the creation of a diversified holding and continued leadership in the area of high technology in Russia and Eastern Europe. Sistema sees the achievement of this goal in the creation of high-technology production and the continuation of intensive growth and the organic development of the Concern's businesses. In 2005 the corporation plans to substantially increase the turnover in the high-technology business area. In the future, Sistema plans to place the shares of the Concern on one of the international stock exchanges.

General Director, ROSNO
Leonid **Melamed**

ROSNO is the most recognized insurance brand in Russia.
In 2004 the company won the nationwide competition ‘National Brand’.
When questioned, more than 32% named ROSNO as the insurance company they considered the best.

INSURANCE

Marketplace

Insurance is one of the most rapidly developing sectors of the Russian economy. According to data from the Russian Federal Service for Insurance Oversight, the volume of the insurance market grew by 70% to $17 billion during the period 2001-2004. Today the insurance industry occupies 2.8% of Russia's gross domestic product and has enormous potential. The high rate of growth of the domestic economy is stimulating demand for insurance products from companies and organizations. Also noteworthy is the steady growth of interest from individual clients in the services of insurance companies.

The insurance market is constantly under consolidation. This is being driven to a great degree by changes in the legal foundation of the market and the strengthening of the control of state bodies for insurance oversight over the activity of insurance companies. Due to the failure to meet minimal charter capital requirements 200 companies lost the right to work in the market in 2004. At the same time the combined charter capital of the 20 largest players doubled over the year. Not only the amount of capital but the growth in capitalization of a company serves as a guarantee of efficient growth in the insurance market. Sistema rapidly reacts to the dynamic of the market with the carefully planned diversification of its business in the insurance segment and the increase in its financial potential.

Business

ROSNO represents the business of the corporation in the insurance sphere and is one of the largest insurance companies in Russia. Its regional network is made up of 100 affiliates that are brought together by 10 territorial directorates and 186 agencies operating throughout the Russian Federation. Today more than seven million people and more than 50,000 enterprises and organizations use ROSNO insurance products. Over the last five years the company has consistently been in the top five of the largest Russian insurers.

ROSNO has licenses to provide 95 types of obligatory and voluntary insurance. ROSNO's strategy envisions the further strengthening of its leading position and an increase in the company's share of the insurance market through providing clients with high-quality insurance products. Playing a major role in this vision is the presence of one of the leaders of the world insurance market Allianz AG among ROSNO's shareholders (47.2%).

ROSNO has quality mandatory reinsurance protection of its risks. Partners of the company in reinsurance include Allianz, Hannover Re, SCOR, Munich Re, Swiss Re and the largest Russian reinsurance companies. ROSNO also works with the broking agents of Lloyd's corporation.

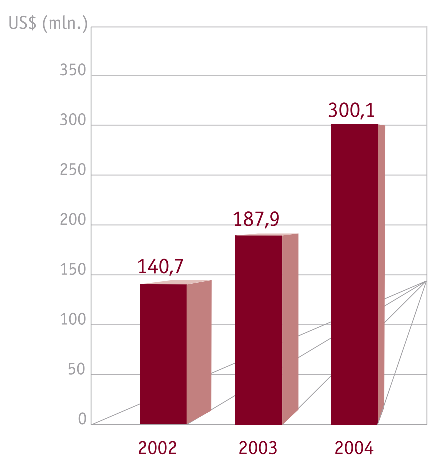
Results

ROSNO's main financial indicators reflect the rate of development of the company and its stable financial situation. The company has demonstrated growth as measured by practically any parameter. In 2004, ROSNO concluded 1.45 million insurance contracts. The company's client base grew by 19%. The overall sales of the insurance segment of Sistema for the year grew by 60%

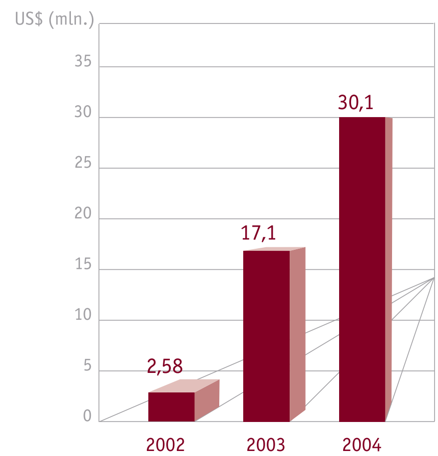
to $300.2 million. The main reason for the increase in revenues of the company was the growth of insurance premiums in the main areas of activity of ROSNO, such as voluntary medical insurance, property insurance and auto insurance. In 2004, operating profit in this segment increased by 76% to $30.2 million. Operating margins grew from 9.1% to 10%. A substantial role in the increase in profit was played by a strict policy of cost controls.

Shareholders see investment in ROSNO as promising and profitable. Therefore a decision was taken on the capitalization of profit as well as introduction of additional funds into the charter capital of the company, which was increased in 2004 by almost 2.5 times. The company's own funds grew by 43% by comparison with 2003.

Revenues



Operating profit



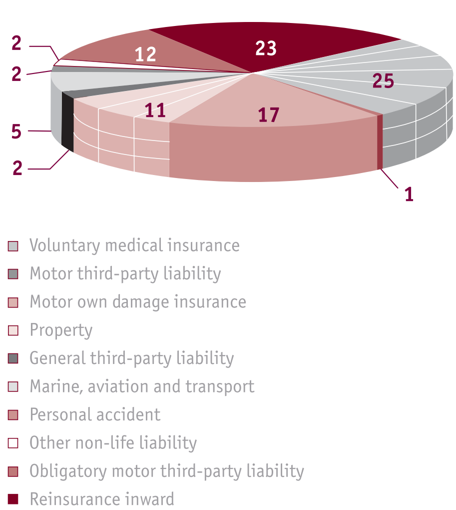
Growth in ROSNO's key indicators was achieved by the development of new sales channels while strengthening traditional ones. In addition, with the support of shareholders, a priority project for the development of the company was launched: the introduction to the market of two specialized subsidiary companies, Allianz ROSNO Asset Management and Allianz ROSNO Life. The new companies bring together the international experience in the insurance field of German company Allianz AG and ROSNO's knowledge of the specifics of the Russian market.

Outlook

ROSNO's primary efforts in 2005 will be concentrated on strengthening the position of the company in the non-life retail insurance market and on the development of sales in the small and mid-size enterprise segment.

Particular attention will be focused on the support of key lines of business - the preservation of its leading position in the market for voluntary medial insurance and the achievement of leading positions in targeted segments of the CASCO (voluntary auto insurance) market and increasing the share of OSAGO (compulsory auto insurance) in the portfolio of the company (primarily through profitable segments) and the preservation of the traditionally high share of property insurance.

ROSNO insurance premiums



Life insurance is seen as one of the key areas of activity for the company. In 2005, ROSNO's subsidiary company Allianz ROSNO Life plans to become one of the top three companies in 'New Business Premiums' (premiums by contract concluded over the course of the year).

ROSNO sees as one of its major goals the continual improvement of the quality of client services both in Moscow and in the regions. With this goal in mind, the creation of a single call center is planned for 2005, enabling the development of the service aspects of ROSNO's business. The company is implementing a program for improving the quality of service at each stage of interaction with clients. This program is oriented towards regular measurement and increasing client satisfaction.

One of the most important areas of activity for ROSNO in 2005 will be the development of its retail network. Through the opening of new sales offices as well as the recruiting of qualified specialists, the company plans to increase its share of the market in priority Russian regions. Within the framework of regional expansion, ROSNO is also looking at the markets of the near abroad. The company's plans include entry active expansion in the Ukrainian market.

General Director, Sistema-Hals
Felix **Yevtushenkov**

There are more
than 60 companies
in the portfolio
of Sistema Hals.
The total floor-space
of the projects
exceeds 2.5 million
square meters.

REAL ESTATE

Marketplace

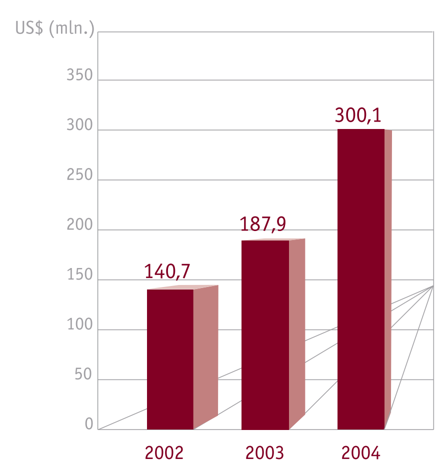
The market for real estate in Russia continues its intense rate of development. Today the market has acquired the essential characteristics of developed Western markets. The transparency of the Russian real estate market has reached the level where existing and potential participants see it on the same level as the main European markets. The investment attractiveness of the Moscow market, where Sistema focuses its primary efforts, is today sufficiently high so as to allow it to compete with the markets of London and Paris. The expansion of business and steady consumer demand ensure high demand for office and retail space. In 2004 the share of empty space in these sectors reached a level of practically nil in the most attractive segments of the market.

The stable microeconomic situation and the increase in Russia's credit rating to investment grade have stimulated the entry into the market of new investors, including Russian pension funds and international credit institutions. In addition, 2004 was marked by the active development of the sector of joint investment in real estate. Thirty real estate share investment funds, with a volume of investment of $30 million each, were formed over the course of the year. The rapid flow of investment into the real estate sector and the strengthening of competition led a slight decrease in the level of profitability, which, nonetheless, remained sufficiently high by comparison with the rates of capitalization of the European market.

Business

Sistema is actively developing the area of commercial real estate. In the business portfolio of the corporation this area of activity was one of the first and still retains its significance. Sistema-Hals is the management company for the real estate business area of Sistema, one of the leading developers in the real estate market. Sistema-Hals manages the activity of more than 50 companies, the specialization of which allows an integrated approach to the implementation of stages of a project - from the formulation of an idea and development of the project, to the construction and subsequent exploitation of the facility. Successful experience in the construction of high-quality office property and elite

Revenues



housing, large shopping centers and transportation infrastructure facilities provides a main competitive advantage for Sistema-Hals.

Results

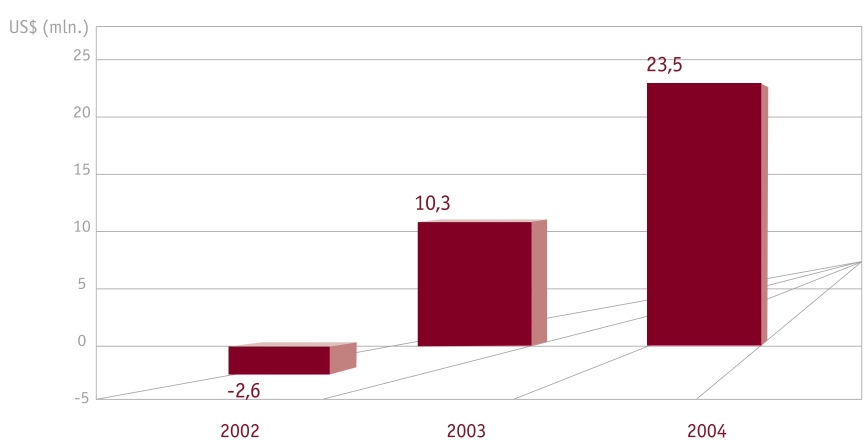
In 2004, Sistema-Hals significantly expanded its presence in promising segments of the real-estate market: shopping and entertainment complexes and low-rise construction. In particular, the portfolio of projects of the company was filled with such projects as the cottage village ForrestVille, the village Aurora and other residential facilities located in picturesque areas of Moscow and Moscow Region. Continuing its expansion in Russia's regions, Sistema-Hals began construction of large shopping and entertainment complexes in Kazan and Krasnoyarsk.

In 2004 the revenues of the companies, operating in the real estate sphere under the management of Sistema-Hals, increased more than two times to $90.4 million. Growth was driven by the successful completion of a range of projects, as well as by high revenues from leasing of property. OIBDA of the company for the year 2004 grew by 2.4 times to $24.5 million versus $10.3 million in 2003.

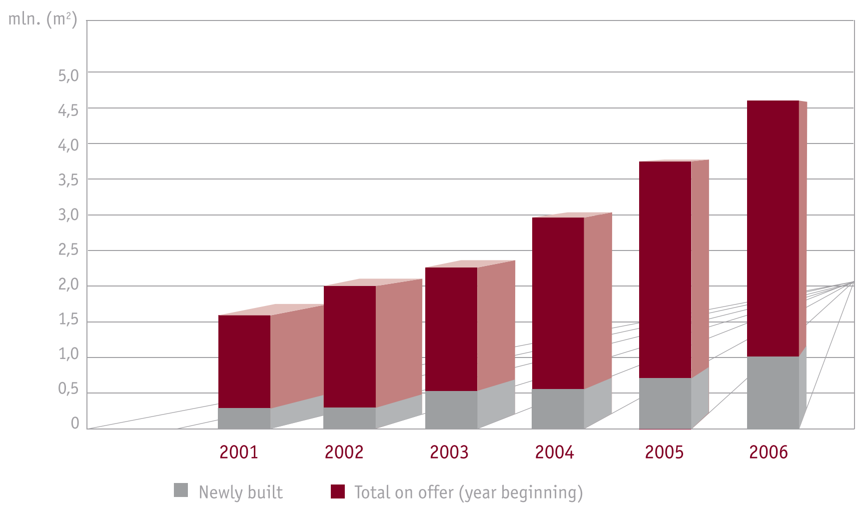
Outlook

Taking into account the current dynamic of the real-estate market and its potential for growth, the corporation gives great significance to the development of Sistema-Hals. The company's strategy

Operating profit



Revenues



Source: Colliers International

is seen as the further strengthening of competitive advantages, expansion and diversification of its portfolio of orders and entry into new market segments. One of these promising areas is the development of large infrastructure projects. The strengthening of a leading position in the Moscow real-estate market and regional expansion are seen as strategic goals for Sistema-Hals.

General Director, Detsky Mir-Center
Sergei **Kushakov**

In 2004 the Detsky Mir (Children's World) group of companies began the large-scale construction of a retail network. Today it is the largest network of stores for children's products in Russia with locations in Moscow, St. Petersburg and other Russian cities.

RETAIL

Marketplace

Children's products represent one of the most promising areas of retail trade. The overall capacity of the market for children's products is estimated at $6 billion and its yearly growth is no less than 15%. Growing consumer demand and new retail-space technologies are the main drivers of the market. Despite impressive capacity, the market for children's products is still in the formative stage. There are a large number of trading companies present and this creates conditions for the consolidation of the market around the strongest players. According to its own estimates, the share of Sistema of the market for children's products is around 1.5% and continues to grow at a pace outstripping the rest of the market.

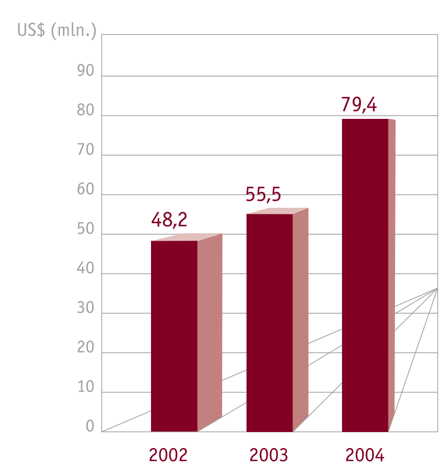
Business

The assets of Sistema in the retail segment are managed by the Detsky Mir (Children's World) - group of companies occupying the leading position in Russia in the area of children's products. The trademark Detsky Mir is one of the most recognozable Russian brands in the market for children's products and has a more than 50-year history. Detsky Mir has 17 stores in Moscow, St. Petersburg and a number of other cities, and operates the largest department store for children in Europe located on Lubyanka Square in Moscow with an overall floor space of around 55,000 square meters.

Results

In 2004 the Detsky Mir group of companies concluded the implementation of the first stage of a development program launched two years earlier. As part of this program a management team was formed and the necessary infrastructure was created for the beginning of a wide-scale regional expansion. All Detsky Mir stores were converted to a single format of organization and trading space configuration and an electronic inventory management system was introduced. Centralized purchasing and a proprietary distribution center allowed the company to achieve significant cost savings and offer customers high quality children's goods at competitive prices.

Revenues



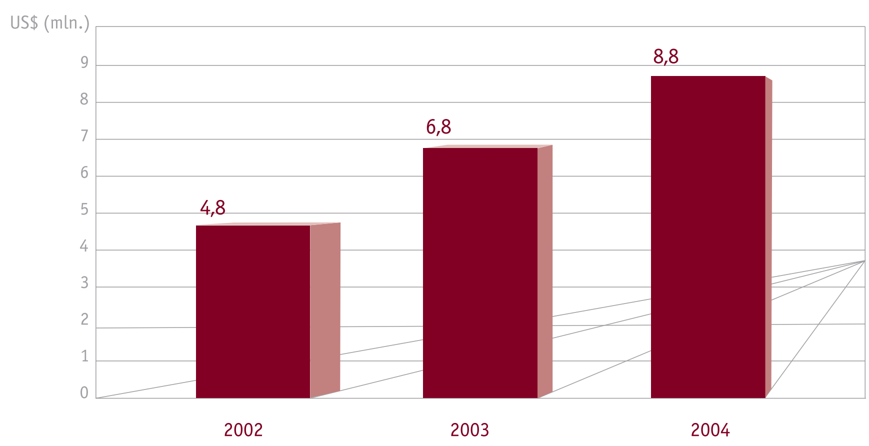
In 2004 the Detsky Mir group of companies significantly increased its retail network. Four new stores opened in Moscow and two more in St Petersburg. In 2005 the retail network continues to expand. In April the company opened its first store in the city of Yaroslavl and in May it opened a new store in the Ladya shopping and entertainment center in the Moscow neighborhood of Mitino. Detsky Mir stores began serving customers in Novoperedelkino and the Babushkinsky neighborhood of Moscow. By the end of 2005, Detsky Mir plans to open no fewer than 15 stores in Moscow and other Russian regions.

Turnover in the Retail business area increased by 42.9% to $79.3 million in 2004, compared to $55.5 million in 2003. The increase in revenues was due primarily to new retail outlets and an increase in space in shopping centers. The active expansion of the retail network of the Detsky Mir companies led to a decline in OIBDA margin from 17% in 2003 to 12.9% in 2004.

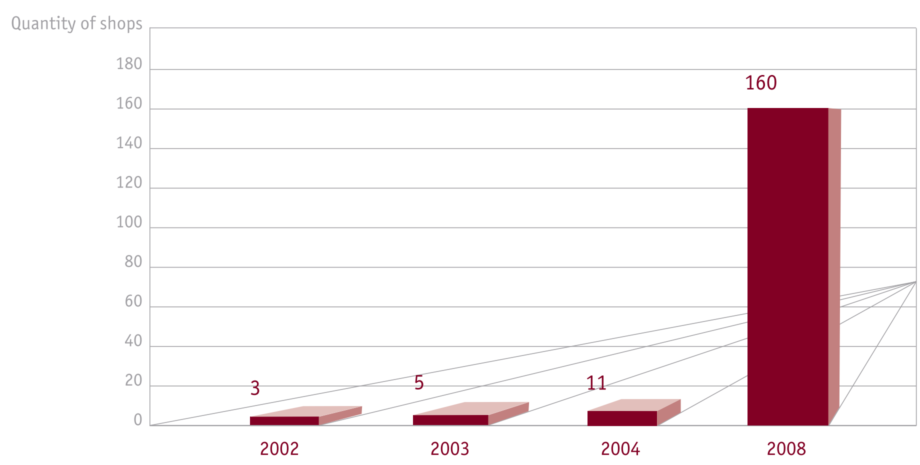
Outlook

The strategy for the Retail business area of Sistema is directed at the strengthening of the leading position of the Detsky Mir group of companies in the market for children's goods, the further development of the retail network throughout Russia as well as the increase of the share of the group of companies in the market for children's goods. By the end of 2008, the group of companies plans to substantially expand its retail network, having increased the number of stores operating under the Detsky Mir trademark

Operating profit



Growth rate of the retail network



by more than ten times to 160 stores. Only 25 of these will be located in Moscow and the remaining stores will be located in the most promising Russian regions. Over the coming four years, Sistema plans to significantly increase the revenues in the Retail business area.

General Director, Sistema Mass Media
Alexander **Leiviman**

In 2004 the company Sistema Mass Media prepared the launch of a unique consumer product, the first interactive television service in Russia. ‘Stream’ brings together the latest cable television system, package of channels and producers of television and internet content.

MASS MEDIA

Marketplace

In 2004 the Russian media market maintained its rapid rate of development. Growth in the market stayed above 30%. As in 2003, the television industry developed at break-neck speed. But the cable television segment demonstrated the most impressive rate of growth - for the year the market increased by almost 1.5 times to $260 million. This was linked primarily to the expansion of consumer demand for the services of pay television operators and the completion of the consolidation of market players around large media groups.

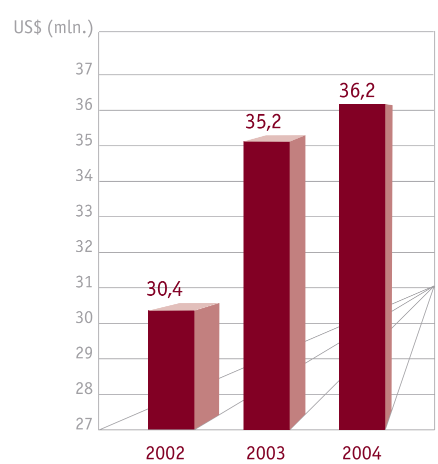
Business

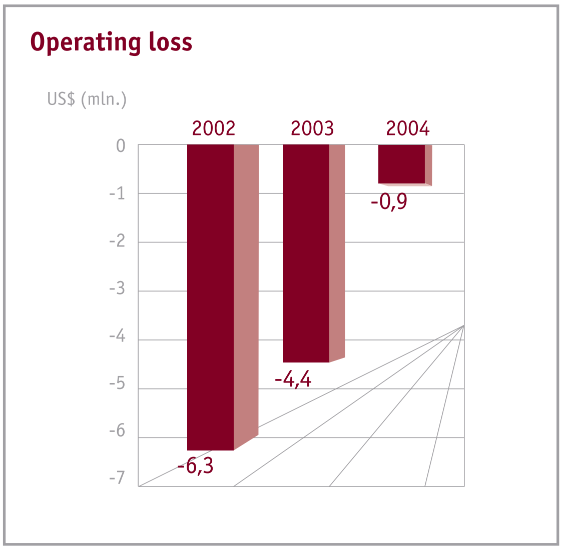
Sistema Mass Media manages the assets of Sistema in the media sphere. The company is one of the largest in the market and is developing business in four areas: advertising (the Maxima agency is one of the five largest advertising agencies in Russia), circulation of periodical publications (the group of companies Our Press is the largest retail operator in Moscow Region), print and electronic mass media (the radio station Govorit Moskva (Moscow Speaking), the information agency Rosbalt, Metro, Rossiya (Russia) and Literaturnaya Gazeta (Literary Gazette) newspapers, as well as pay television and interactive multimedia services (Sistema Multimedia, Cosmos TV). Among the company's print media, Literaturnaya Gazeta is one of the oldest publications in Russia and is distributed in more than 30 Russian regions.

Results

In 2004, Sistema Mass Media continued to implement its strategy directed at the mastery of the market for new media services, based on the latest breakthroughs in the sphere of information and telecommunications technologies. The Sistema Multimedia company was created, which today is actively developing new areas in the activity of the holding - the provision of pay television services and interactive media services. In May 2005 the company launched the Stream interactive television project in Moscow, bringing together the latest system of cable television, a package of television channels and a range of television and Internet content providers.

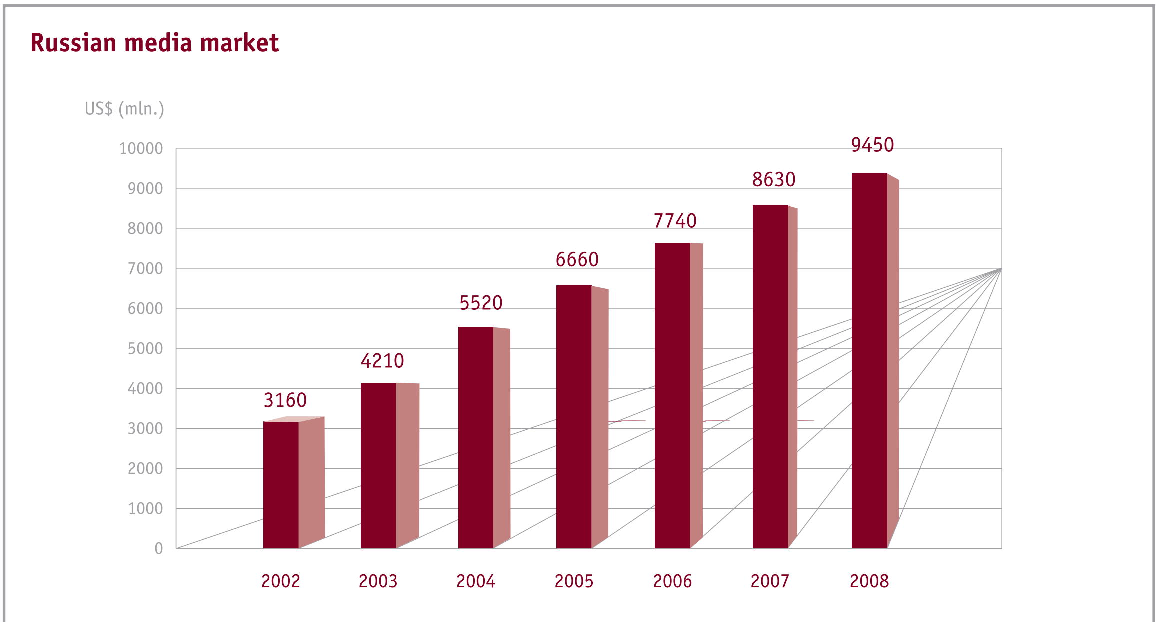
Revenues





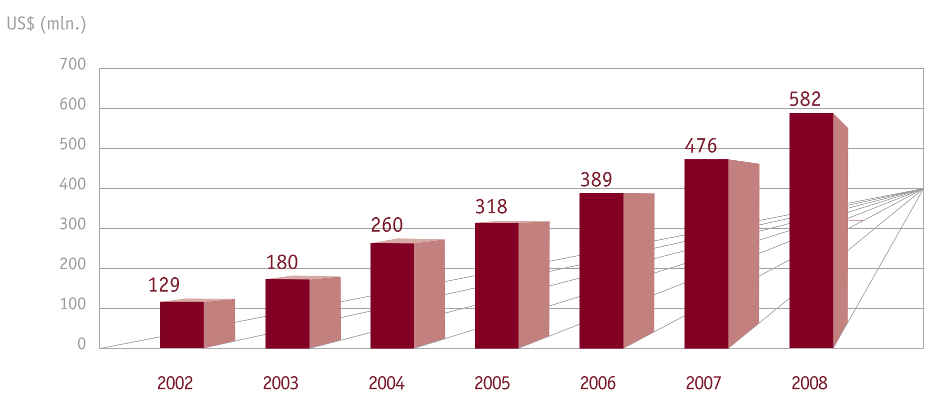
In 2004, within the framework of the development of the interactive television project, Sistema Mass Media developed its own television channels and in the beginning of 2005 began their distribution in Russia, the CIS and overseas.

For the year, the revenues of Sistema Mass Media increased 2.8% to $36.2 million, compared to $35.3 million in 2003. The growth in the financial indicators of the group of companies was driven primarily by an increase in revenues from traditional areas of activity, including production and distribution of print products as well as the advertising business.



Source: Video International, Cosmos TV, SMM

Pay television market



Outlook

The strategy of Sistema Mass Media is to conquer and strengthen the leading positions of its group companies in all areas of the market. Particular attention will be paid to the advancement of services for high-speed access to the Internet and pay television. The subscriber base for broadband Internet services is planned to reach 300,000 by the end of 2005. The holding also aims to achieve significant synergies from cooperation in implementing a multimedia project with Moscow City Telephone Network, Comstar United Telesystems and MTU-Intel. The development of pay television on the infrastructure base of the three companies will allow Sistema Mass Media to sign-up several tens of thousands of subscribers in Moscow. The implementation of this goal will also enable the integration of Cosmos TV into the project, where the holding plans to increase its presence.

Sistema Mass Media also plans expansion into regional markets for cable broadcasting and the creation of a national pay television operator as part of the holding.

Chairman of the Board of directors, MBRD
Sergey **Cheremin**

MBRD began the active development of its retail banking business in 2004. The volume of consumer deposits grew 74.5% and the volume of international VISA and MasterCard cards issued grew by more than 2.7 times.

FINANCE

Marketplace

Russia's microeconomic situation exercises substantial influence on the banking business. In 2004 the situation was beneficial and provided a stimulus for the development of the banking sector. The rate of growth in the banking sector in 2004 was comparable with the dynamic of the development of the Russian economy as a whole. In addition, the legal framework for banking activity was improved. The practical implementation of new currency legislation began and the law 'On Credit Histories' was passed and came into effect from June 1, 2005. The most important event in the banking sector was the creation of a system of insured deposits for private persons.

Continuing economic growth led to an increase in demand for banking services. Interest among consumers in organized savings grew by 10.2%. The sum of deposits attracted by banks from the population grew by more than 8% for the year. The implementation of a series of measures aimed at increasing the stability and trust in the banking system had a positive effect on the growth of deposits. The increase in real incomes of the population led to heightened interest in consumer credit, as a result of which this segment enjoyed growth at the level of 50% for the third year in a row.

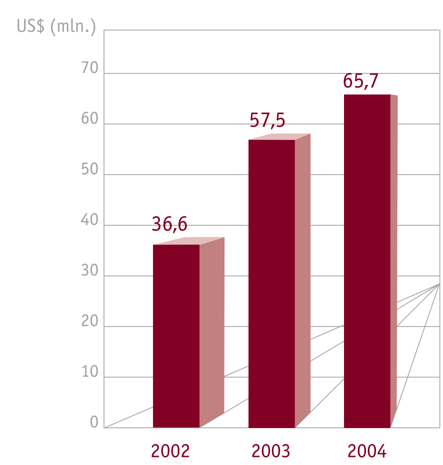
Business

The main asset of Sistema in the financial sector is AKB Moscow Bank of Reconstruction and Development (MBRD), a large universal commercial bank founded in 1993. Along with Sistema, its shareholders include Intourist and Moscow City Telephone Network. MBRD is developing three strategic business areas - corporate, investment and retail. Possessing a diversified client base, the bank offers a wide range of banking services as well as fulfilling a treasury function for the companies of Sistema.

Results

MBRD continued dynamic development in 2004 directed at the creation of an efficient, high-technology financial structure. The implementation of a program for the development of the retail business, developed jointly with the company Deloitte & Touche CIS, is a main priority in the strategy of the bank. In 2004 MBRD opened affiliates in

Revenues

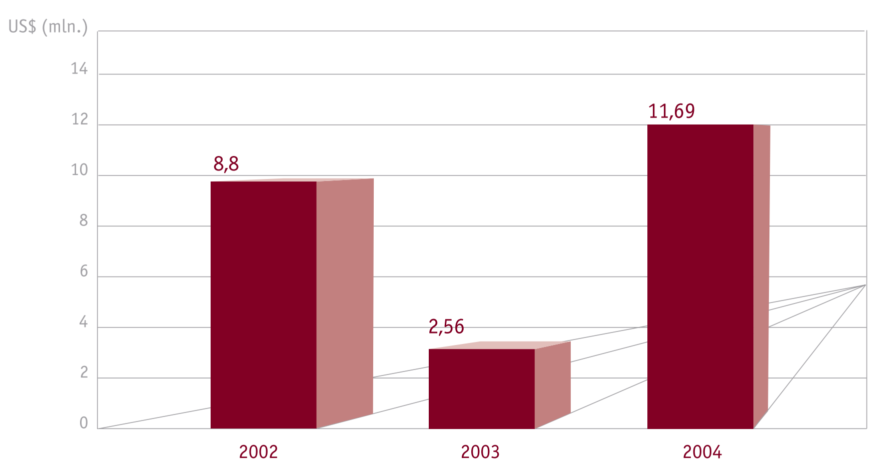


Krasnodar and Yekaterinburg. The sales network in Moscow was increased by two times, with the bank opening 11 additional offices bringing the total number in the capital to 22. MBRD's network of automatic bank machines increased by 2.2 times and at the end of the year consisted of 123 units. Technology was introduced for accepting payments in self-service banking devices for Mobile TeleSystems. A system is being developed for the acceptance of payments for other companies including those that are part of Sistema.

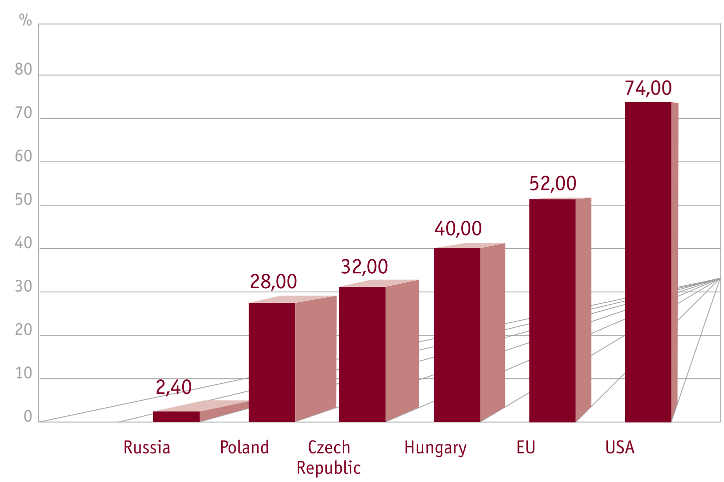
The most important element of the retail business strategy is the development of products and technology on the foundation of plastic banking cards. In 2004, MBRD and Mobile TeleSystems implemented the first co-branding project for subscribers of the operator and clients of the bank, combining the opportunity for the free receipt of credit cards and additional bonus minutes for use on the mobile network. During the year MBRD significantly increased the output of VISA and MasterCard cards. The volume of output was 34.3 thousand units, 2.7 times greater than in 2003. The payment systems have noted the efficient activity of the bank in the market for plastic cards. In the near future VISA International plans to raise the status of MBRD to principle member of the payment system, which will allow the bank to receive additional revenue from its card program.

In 2004 the system was expanded for distance service and interaction with clients of the bank. The Center for Telephone Service was brought into operation as well as the SMS BankInfo service that allows bankcard holders to get real-time information about card transactions. Work on the introduction of the Internet Banking and Mobile Banking services was carried out in 2004. The launch of these services is planned for 2005.

Operating profi



Consumer credit in Russia and other countries (GDP,%)



MBRD's revenues increased by 14% to $65.7 million in 2004. Operating profits for the bank grew four times to $11.7 million. Primarily revenues drove profit growth from interest on banking activity for the service of corporate clients and individuals.

Outlook

The priority development goals of the bank for 2005 are the further implementation of the retail project as well as the development of the corporate business, both through attracting new clients and the development of mutually beneficial cooperation with the bank's existing clients. In 2005, MBRD plans to strengthen its position among the top 30 universal banks and become one of the top 20 leading banks by volume of credit for individual clients.

OTHER PROJECTS

Sistema is investing in promising segments of the Russian economy and creating a foundation for the efficient growth of the corporation in the future. In 2004 Sistema took an active part in the development of several promising projects, primarily in the areas of services, high technology and innovation.

Tourism

President, Intourist
Alexander **Arutyunov**

Sistema owns leading Russian enterprises that have great scientific potential and unique experience in implementing high technology projects in the field of radio technology. Concern Radio Technical and Information Systems (RTI) manages the assets of the corporation in this segment, and the production activity of RTI covers three areas of activity having great potential for synergies - radio construction, info-telecommunications and apparatus construction. RTI is one of the world leaders in the field of radio location technology and management systems for airspace movement. The strategy of the company envisions the vertical integration of the entire production chain from scientific development to the creation of a finished product, industry diversification and expansion into foreign markets.

Radio Technology

General Director, RTI-Systemy Concern
Sergei **Boyev**

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Helicopter Building

General Director, Kamov Holding
Valery **Lukin**

Kamov Holding is a helicopter building holding created by the corporation in 2003. It includes the world leader in the field of design and production of civil and military helicopters, Kamov. Operating for over fifty years in the helicopter technology segment, the enterprise has created an extensive research base and built up unique experience and leading edge technology for the creation of rotary-wing aircraft earning world recognition under the trademark 'Ka'. The holding oversees the production of helicopters, organizes the advancement of production and sales systems, maintains technical service of helicopter technology and finances design development.

Medicine and Pharmaceuticals

General Director, MTH
Yevgeny **Kurgin**

Medical Technological Holding (MTH) specializes in the production of medicines and modern medical equipment. The holding brings together a range of companies that carry out scientific research activity, design and construction of pharmaceutical production, launch and distribution of medicines and medical supplies. The company concentrates its efforts in separate niches of the Russian market for pharmaceuticals and medical technology. MTH has strong positions in the production of biotechnological vaccines (hepatitis B), centrally acting analgesics and ampoule forms of finished medicines.

Sport

General Director, Olympic System
Marina **Strelchenko**

In 1997, Sistema and the Russian Olympic Committee founded the sport holding Olympic Sistema. The company specializes in the creation and management of sporting structures. The equipping of sporting facilities with required equipment is another main area of activity for Olympic Sistema. Today the holding manages the largest fitness center in Europe, Olympic Star, and the Wellness Club health and fitness complex. In addition, Olympic Sistema provides support to national sporting federations participating in the program of modernizing obsolete sporting equipment in Moscow schools. Sistema views the sporting industry as a promising business requiring the latest approaches in management and efficient investment.

Venture Capital

President, Sistema Venture
Dmitry **Rototaev**

Sistema is one of the few business entities in Russia to take part in venture capital business and consulting in the area of intellectual property. Through its subsidiary company, Sistema Venture, the corporation manages innovative projects in high-technology areas. The company operates on the principle of a fund of direct investment - acquiring, restructuring, capitalizing and selling small companies, trying not only to increase profit but also to identify promising areas of growth for the national high-technology industry.

«

SISTEMA PROVIDES ACCESS TO SECTORS THAT MIGHT NOT OTHERWISE BE ACCESSIBLE VIA EXISTING MARKET INSTRUMENTS OR ONLY THROUGH A LIMITED NUMBER OF THOSE INSTRUMENTS

Troika Dialog, report “Sistema: Beyond Natural Resources”, January 10, 2005

»

SOCIAL RESPONSIBILITY

Social responsibility is a key principle in the activity of Sistema. We see the development of business in harmony with the outside world and in the interests of all of society as a strategic priority and an important factor for success. The corporation aims to meet the expectations of a developing society requiring a responsible attitude in all aspects of our activity and the observance of high standards in all areas touching upon our business.

Sistema sees its main social role as helping Russia to develop a full-fledged market for high-technology products and services. We are convinced that a high-technology sector of services is the strategic competitive advantage that will permit the country to develop efficiently in the conditions of a global marketplace and strengthen its position in the international arena. Following from this conviction, the corporation conducts its business primarily in service sectors of the economy. We invest in innovative projects and infrastructure, cutting-edge technology, science, education and culture and in the intellectual development of the personnel of the corporation and society as a whole.

The corporation strives to be a successful, responsible and steadily developing company. We are distinctly aware that the achievement of this goal is impossible in isolation from society, without the intersection of corporate interests with societal expectations. In our understanding, social responsibility includes the unconditional priority of social, ethical and legal norms. In its practices, the corporation aims to follow these principles and not to retreat from them for the sake of achieving commercial results.

Sistema was one of the first Russian companies to sign the Global Compact of the United Nations, which confirmed its adherence to worldwide standards of corporate social responsibility (CSR). In 2003 the corporation became a member of the World Business Council for Sustainable Development (WBCSD). Like other participants in the WBCSD, we aim to ensure a high level of transparency and responsibility in our business and to act in accordance with the expectations of society and the long-term interests of the country.

Sistema demonstrates its efforts to reach the highest standards of social responsibility, creating and developing the necessary procedures and structures. In the beginning of 2005, the company adopted the Code of Ethics regulating the ethical norms of corporate relationships and which is binding on all employees. The corporation's International Consultation Committee (ICC) is made up of leading representatives of the business and scientific world and has already been in place for two years. The corporation takes recommendations of the ICC into account when taking key decisions, in particular those aspects connected to the observation of CSR standards. The support and expertise of the ICC in this sphere enables the company to take full account of the socially significant aspects of its activity and the responsibility of the corporation in relation to all interested parties.

Generally accepted standards of social responsibility are at the foundation of the human resources policy of Sistema and its participation in many different social and humanitarian projects. The corporation makes a conscious social investment aimed at the creation of a new quality of life.

Human Resources

Sistema's employees are its most important resource. Their professionalism and interest in achieving results are the foundation for the development of the corporation. The corporate policy of Sistema is aimed at the matching the professional qualities with the work requirements of employees, the creation of favorable conditions for work and just compensation. Providing great possibilities for professional development and intensive career growth, we give our tens of thousands of employees a belief in tomorrow.

An all-round program for the development of personnel has been developed and is in place at Sistema. It calls for creation of conditions, which enable a harmonious combination of the interests of the corporation and employees. The program includes a system for training and increasing qualifications, medical insurance, private pension contributions, incentive based payment plans, corporate communications and events.

Sistema conducts yearly performance reviews with employees. The goal of these discussions is to increase the motivation of personnel, to uncover existing problems and seek their timely resolution. The reviews also allow the definition of potential for the professional development of employees and the identification of prospects for career growth.

As a result of the review, personnel are compensated, receive recommendations for improving their efficiency and the quality of their duties and plans of study for raising qualifications. A personnel reserve has been created in the corporation in case of expansion or rotation and this is regularly renewed with employees who have been the most successful in their performance reviews. The best employees are singled out with honorary gold and silver symbols of Sistema.

The system of raising the qualification and retraining of employees is considered not only a human resources requirement but both a strategic and tactical goal. The professional competency of personnel is a particular focus of attention. Sistema's president personally approves the plan for educational work with personnel. Accordingly, a monthly seminar on a financial, economic or legal theme is held for employees of the central office of the corporation and its subsidiary companies. The top managers at Sistema improve their qualifications in the course of yearly organized outside learning sessions.

Corporate educational institutions play a significant role in the growth of the professional level of personnel. In the Teaching and Methodology Center of Sistema, and the teaching centers of

MGTS, MTS, ROSNO, NIIME and Mikron factory, Kvazar-Micro, Mediatel and STROM Telecom, annually educate and increase the qualifications of more than 14,000 people. The corporation supports the efforts of its employees to become more professionally qualified, providing them with the possibility of receiving secondary higher education, studying in MBA programs and taking part in seminars and educational courses in outside learning institutions. In addition there are opportunities for further education in doctrinal and graduate programs and education and work experience with overseas partners.

The system of personnel selection at Sistema allows it to satisfy its human resources requirements. A databank of candidates to fill vacancies and of specialists possessing MBA degrees has been created. Each candidate passes through a thorough qualifications check. An interview is conducted with each prospective employee and a series of conversations and testing with the help of expert systems. Sistema has worked since 2003 with the Club of Graduates at the British Council. It also conducts targeted preparation of young specialists in the leading Moscow learning institutions for its companies.

Social Investment

Education and Innovation

Programs in the sphere of education and innovation are the most important component of Sistema's social responsibility. In the support of science and education, the corporation sees a goal of national importance and sees it as the main priority of its social activity. The social investment of Sistema in this area is an example of the organic combination of corporate and social interests. The corporation participates in long-term innovative and technological projects whose realization is only possible in an educated and rapidly developing society. Supporting science, education and culture, Sistema invests in the development of its own business, ensuring professional employees in the future and highly educated consumers of high-technology services.

A program of grants has existed since 1998 within the framework of the corporate system of preparation of a personnel reserve - graduate and undergraduate students at leading Russian institutes of higher learning receive these grants from Sistema. In 2004, these grants were 1,500 rubles per month. Providing grants at the time of education, the corporation also takes upon itself the responsibility for the organization of internships and work training grants. 126 students have participated in the grant program from the Lomonosov Moscow State University, MGIMO, the Financial Academy of the Government of the Russian Academy, MFTI, Bauman Moscow State Technology University, the High School of Economics, the Moscow Technical University of Communications and Informatics, the Moscow State Institute of Electronic Technology (Zelenograd), the Academy of Budget and Treasury of the Ministry of Finance of the Russian Federation, Moscow

Pedagogical State University, Moscow State Open University, RGGU and Plekhanov REA.

The cooperation of the corporation with institutes of higher learning is not limited to the support of talented students and young scientists. Managers and specialists from Sistema companies teach in selected institutions. In 2004 within the framework of the celebration of the 250th anniversary of the Lomonosov Moscow State University, the corporation supported special scientific and educational programs.

The revival of the collapsed state system of preliminary specialized technical education, which is a foundation for the education of highly professional engineers and talented scientists, is an object of particular attention for the corporation. In this system there were scientific and technical study groups and creative laboratories where gifted young people could develop their abilities and gained a chance of entering selected state institutes. Sistema, together with the Bauman Moscow State Technical University and other technical institutes, is developing a large-scale program for the intellectual development of young people - 'Step into the Future'. The main goal of the program will be the support of the intellectual creativity of youth, the organization of cooperation of researchers and scientists of different generations, the effective attraction of young people to the sphere of engineering art, and the creation of special conditions for the education of professionally oriented and scientifically minded young people. The realization of this program carries significant investment in the improvement of the intellectual level of society and the development of innovative processes in Russia.

In 2004, Sistema and the Russian Federal Nuclear Center All-Russian Scientific Institute of Experimental Physics moved forward on a project to create the Sistema-Sarov technology park. Within the framework of the project the necessary conditions will be created for the fruitful activity of young scientists who in the future will make up the elite of scientific and technical thought of Russia. In addition, a decision was made to create, over the next few years, a corporate technology park on the base of Concern RTI Sistema. The formation of these compact and highly efficient 'points of growth' in the high technology sector will be an important step in the development of a Russian environment of innovation.

Culture and Art

Sistema is a socially responsible company that considers its duty to preserve its reputation as a worthy member of society and to do all it can to invest in the cultural and humanitarian development of society. The corporation strives to ensure that Russia occupies its deserved place in world society as an educated and highly moral nation, aware of and valuing its culture and national traditions.

Sistema's programs in the cultural realm are directed toward the support of museums, the rebirth and development of musical culture and the revival of cultural monuments. The corporation supports leading Russian museums, among which are the Pushkin State Museum of Fine Arts, the Tretyakov State Gallery and the Museum of V.A. Tropinin and Moscow Artists of His Time and others.

In 2004, Sistema implemented the largest project in the field of culture, the ten-year program of cooperation with the Russian State Museum of St Petersburg. First, at the faculty of Art at the Lomonosov Moscow State University an Informational and Education Center 'The Virtual World of the Russian Museum' was opened, a network of which has already been created in more than 10 large regional centers. Thanks to this program and the possibilities of modern computer technology, thousands of Russians can take part in virtual tours around the halls of the Russian Museum and become engrossed in the world of national fine arts. With this goal the Corporation began the creation of an electronic media package with virtual tours of the leading Russian museums and cultural lectures for free distribution in Russian schools. In the near future, the corporation plans to open a virtual affiliate of the Russian Museum in London that will be the beginning of an ambitious program of popularizing Russian culture abroad.

Sistema also places great emphasis on projects in the realm of musical culture. Over the last several years the corporation has supported the Mariinsky Theater. Long partnerships and multi-faceted programs tie Sistema to the Nikolai Petrov International Charitable Fund, the Irina Arkhipova Fund, the Meyerhold Charitable Fund and the Moscow cinema festival MoFest. The Earlymusic traditional festival and concerts of baroque music, the prestigious ballet competition for the prize Benois de la Danse and other cultural events receive Sistema's support.

Social support

Sistema targets assistance to underprivileged members of society, first of all orphans, who require particular support. The corporation pays particular attention to its relationship with Orphanage 39 in Pushkino and the Pansion Family Education Support for Orphans. The corporation has taken upon itself the full financial maintenance of the children and also finances the development of the infrastructure of children's homes.

The corporation is a general partner of the international prize 'Philanthrope', an award for outstanding achievements in the area of culture and art directed toward people with physical disabilities. The prize was founded in 1997 by the All-Russian Society of Invalids and the Philanthrope Fund, which have embarked on a multi-year program in the field of artistic rehabilitation of people with restricted abilities. Over the last four years citizens of 25 countries have taken part in the competition.

« WE BELIEVE THAT OPERATIONAL CHARACTERISTICS OF SISTEMA'S BUSINESS - STRONG GROWTH COUPLED WITH HIGH EFFICIENCY - ARE UNIQUE IN THE RUSSIAN MARKET FOR A LARGE HOLDING COMPANY AND THIS IS ONE OF SISTEMA'S MAIN ATTRACTIONS AS A SOLID INVESTMENT WITH ATTRACTIVE UPSIDE POTENTIAL »

Dresdner Kleinwort Wasserstein, report "Russian telecoms", September 2005

CORPORATE GOVERNANCE

The dynamically developing business of Sistema gives rise to ever-greater requirements for the quality of corporate governance and level of transparency. The trust of investors and partners of the corporation is viewed as one of the most important factors for increasing the efficiency of business, a guarantee for successful work in the financial market and the expansion of cooperation with international partners. At Sistema, a tight system of corporate governance is in place that is in full accordance with generally accepted global standards and legislative requirements.

The general shareholders meeting is the highest management body of Sistema. Its activity is regulated by the Charter of Shareholders Meetings, which defines the order of its convocation, the registration of participants, the make-up of bodies at the meeting and the order of its conduct. The document creates transparent procedures and the proper conditions for the participants in the work of the meeting.

During periods between shareholders meetings, the Board of Directors undertakes the strategic management of the corporation. Its remit includes: the definition of the development strategy of Sistema and its subsidiary and dependent companies; control over the activity of executive bodies; the resolution of key financial and economic issues; the maintenance of the rights and the observance of the interests of shareholders, investors and partners of the corporation. Committees created within the Board of Directors undertake preliminary review of the most important issues. Today committees work successfully on Strategy, Nominations and Compensation and Corporate Governance. Committees on Audit and Communications with Investors have been created and have begun their work.

An International Consultation Committee (ICC) has been in place since 2003. It is made up of independent experts and well-known leaders from the business and scientific communities. The corporation consults this board when taking decisions on strategically important issues in order to enhance the effectiveness of the decisions taken and to introduce best practices of corporate governance into business practices. Sistema was one of the first Russian companies to appoint independent directors. Today there are three independent directors on the Board of Directors who facilitate decision-making and ensure that it corresponds to the interests of all shareholders and partners of the corporation.

The president, who is an individual executive body of the corporation, undertakes the operational management of the activity of Sistema. The president is appointed and relieved of his duties by the Board of Directors and is subordinate to its activities. The Department for Audit and Internal Control conducts the financial and economic activity of Sistema and ensures the observance of legislation and internal normative documents.

In 2004, Sistema confirmed the Corporate Governance Code, voluntarily taking upon itself additional requirements in the area of corporate relations exceeding the requirements defined by existing legislation. The Code requires the observance of the rights of shareholders and investors and ensures transparency and access to information about the corporation. Rigorous control on the fulfillment of the requirements of the Code and legislation in the realm of corporate governance falls into the area of responsibility of the corporate secretary.

The beginning of 2005 was marked by the adoption of the Code of Ethics, which regulates the ethical norms of the corporate relations of Sistema. In the Code the corporation reflects its adherence to the full account of its socially significant aspects of its activity and observance of commonly accepted norms of business ethics.

Sistema attributes great importance to the disclosure of information. The corporation regularly publishes information about its activities, sends out news about the most important facts and events at subsidiary companies and develops communications with the investment community, mass media and all other interested audiences. Sistema uses various channels for the provision of information. The basic form of information disclosure is its publication on the corporate website. Information about the history and development strategy of the corporation, management bodies and the asset structure of the holding is available on the website in a concise and structured form. Financial results and business news about Sistema and subsidiary structures are regularly published.

Press conferences for foreign and Russian mass media, teleconferences for investors and analysts and presentations for investors in the largest global financial centers are important forms of information disclosure. The Investor Relations department oversees Sistema's communications with the investment community.

Since 1998 Sistema has prepared consolidated financial reporting according to international standards (US GAAP) and regularly discloses this reporting to the investment community. In 2003 the practice of half yearly reporting was introduced and beginning in the second half of 2005 the corporation plans to report on its financial activity on a quarterly basis.

The ongoing improvement of corporate governance is one of the strategic goals Sistema sets for itself. The conditions of today's global economy require the corporation to take information transparency very seriously and to undertake ongoing work with the investment community. Sistema endeavors to create a structure for corporate governance and information disclosure that ensures its efficiency and investment attractiveness while creating an atmosphere of trust, openness and cooperation between the corporation, its shareholders, managers, investors and other interested parties.

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CONSOLIDATED FINANCIAL STATEMENTS

JSFC SISTEMA AND SUBSIDIARIES

INDEPENDENT AUDITORS' REPORT

Years Ended December 31, 2004 and 2003

JSFC SISTEMA AND SUBSIDIARIES

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Deloitte.

INDEPENDENT AUDITORS' REPORT

TO THE SHAREHOLDERS OF JSFC SISTEMA:

We have audited the accompanying consolidated balance sheets of JSFC Sistema and subsidiaries (the "Group") as of December 31, 2004 and 2003, and the related consolidated statements of operations and comprehensive income, changes in shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as of December 31, 2004 and 2003, and the consolidated results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the consolidated financial statements, effective January 1, 2004, the Group adopted Financial Accounting Standards Board Interpretation "Consolidation of Variable Interest Entities" ("FIN 46R"). The adoption of FIN 46R resulted in recognition of a loss of $35.5 million, which was classified as a cumulative effect of a change in accounting principle for the year ended December 31, 2004.

Deloitte & Touche

May 23, 2005

JSFC SISTEMA AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2004 AND 2003

(Amounts in thousands of U.S. dollars, except share amounts)

	Notes		2004		2003
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	5	$	503,747	$	283,165
Short-term investments	6		207,293		278,850
Loans to customers and banks, net	7		379,310		364,982
Insurance-related receivables	8		130,278		96,309
Accounts receivable, net	9		327,921		182,251
Other receivables and prepaid expenses, net	10		583,074		567,125
Inventories	11		276,832		166,203
Deferred tax assets, current portion	24		73,592		53,964
Total current assets			2,482,047		1,992,849
Property, plant and equipment, net	12		4,435,215		3,368,121
Advance payments for non-current assets			181,281		52,969
Long-term receivables			4,513		1,223
Long-term investments	13		45,911		41,393
Investments in affiliated companies	14		206,520		150,936
Goodwill	2		174,341		71,998
Licenses, net	15		750,933		669,988
Other intangible assets, net	16		467,160		446,381
Debt issuance costs, net	2		27,267		17,251
Deferred tax assets	24		3,482		5,575
TOTAL ASSETS		$	8,778,670	$	6,818,684

	Notes		2004		2003
LIABILITIES AND SHAREHOLDERS' EQUITY					
CURRENT LIABILITIES:					
Accounts payable		$	361,016	$	234,871
Bank deposits and notes issued	17		326,861		173,748
Insurance-related liabilities	18		344,460		207,440
Taxes payable			117,888		117,142
Deferred tax liabilities, current portion	24		22,071		508
Accrued expenses, subscriber prepayments and other current liabilities	19		737,394		607,083
Short-term notes payable	20		221,103		349,083
Current portion of long-term debt	22		340,938		844,106
Total current liabilities			2,471,731		2,533,981
LONG-TERM LIABILITIES:					
Capital lease obligations	21		3,412		4,943
Long-term debt	22		2,494,522		1,475,921
Subscriber prepayments, net of current portion	23		156,233		103,059
Deferred tax liabilities	24		218,620		230,986
Postretirement benefit obligation	25		16,226		8,590
Total long-term liabilities			2,889,013		1,823,499
Deferred revenue	26		130,913		115,363
TOTAL LIABILITIES			5,491,657		4,472,843
Minority interests in equity of subsidiaries			1,851,027		1,356,557
Commitments and contingencies	30		-		-
SHAREHOLDERS' EQUITY:					
Share capital (68,325,000 shares authorized, 8,100,000 shares issued and outstanding with par value of 90 RUR and 0.1 RUR as of December 31, 2004 and 2003, respectively)	27		25,090		171
Additional paid-in capital	3,4		198,882		189,934
Retained earnings			1,164,404		783,258
Accumulated other comprehensive income			47,610		15,921
TOTAL SHAREHOLDERS' EQUITY			1,435,986		989,284
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		$	8,778,670	$	6,818,684
See notes to consolidated financial statements.					

JSFC SISTEMA AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

(Amounts in thousands of U.S. dollars, except share and per share amounts)

	Notes		2004		2003
Sales		$	5,392,827	$	3,543,154
Revenues from financial services			318,459		216,761
TOTAL REVENUES			5,711,286		3,759,915
Cost of sales, exclusive of depreciation and amortization shown separately below			(2,020,124)		(1,256,494)
Financial services related costs, exclusive of depreciation and amortization shown separately below			(201,631)		(131,533)
TOTAL COST OF SALES			(2,221,755)		(1,388,027)
Selling, general and administrative expenses			(1,009,716)		(689,057)
Depreciation and amortization			(799,885)		(520,976)
Goodwill impairment			-		(19,251)
Other operating expenses, net			(44,529)		(37,326)
Equity in net income of investees			27,121		465
Gain on disposal of interests in subsidiaries			2,184		-
OPERATING INCOME			1,664,706		1,105,743
Interest income			18,061		19,341
Interest expense, net of amounts capitalized			(213,943)		(198,346)
Currency exchange and translation gain/(loss)			12,620		(3,015)
Income from continuing operations before income tax, minority interests and cumulative effect of a change in accounting principle			1,481,444		923,723
Income tax expense	24		(445,731)		(290,933)
Income from continuing operations before minority interests and cumulative effect of a change in accounting principle		$	1,035,713	$	632,790
Minority interests		$	(589,014)	$	(402,120)
Income from continuing operations before cumulative effect of a change in accounting principle			446,699		230,670
Gain from discontinued operations (net of income tax effect of $3,248)			-		12,810
Gain on disposal of discontinued operations (net of income tax effect of nil)			-		143,567
Cumulative effect of a change in accounting principle (net of income tax effect of nil)	2		(35,472)		-

	Notes		2004		2003
NET INCOME		$	411,227	$	387,047
Other comprehensive income/(loss):					
Unrealized gain on securities available for sale, net of income tax effect of nil			1,967		5,582
Change in fair value of interest rate swaps, net of taxes			(257)		-
Translation adjustment, net of minority interest of $28,582 and $24,426, respectively, and income tax effect of nil	2		29,979		35,321
Income tax effect of changes in the functional currency, net of minority interest of $17,184			-		(22,449)
Comprehensive income					
Weighted average number of common shares outstanding			8,100,000		8,100,000
Earnings (loss) per share, basic and diluted:					
Income from continuing operations before cumulative effect of a change in accounting principle		$	55.1	$	28.5
Gain from discontinued operations			-		19.3
Cumulative effect of a change in accounting principle			(4.3)		-
Net income			50.8		47.8
See notes to consolidated financial statements.					

JSFC SISTEMA AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003
(Amounts in thousands of U.S. dollars)

	Notes		2004		2003
OPERATING ACTIVITIES:					
Net income		$	411,227	$	387,047
Adjustments to reconcile net income to net cash provided by operations:					
Gain from discontinued operations			-		(12,810)
Depreciation and amortization			799,885		520,976
Goodwill impairment			-		19,251
Loss on disposal of property, plant and equipment			1,551		15,048
Long-term investments impairment			3,070		-
Gain on disposal of discontinued operations			-		(143,567)
Loss on disposal of interests in subsidiaries			1,862		-
Cumulative effect of a change in accounting principle			35,472		-
Minority interests			589,014		402,120
Equity in net income of investees			(27,121)		(465)
Deferred income tax benefit			(58,903)		(42,601)
Provision for doubtful accounts receivable			29,809		9,972
Allowance for loan losses			13,810		9,902
Inventory obsolescence charge			5,868		(797)
Changes in operating assets and liabilities, net of effects from purchase of businesses:					
Trading securities			27,142		(38,988)
Loans to banks			(25,661)		(121,444)
Insurance-related receivables			31,111		(19,715)
Accounts receivable			(101,567)		(47,005)
Other receivables and prepaid expenses			(3,929)		(101,632)
Inventories			(112,269)		(54,406)
Accounts payable			54,110		(1,600)
Insurance-related liabilities			51,985		43,877

	Notes		2004		2003
Taxes payable			(1,997)		24,694
Accrued expenses, subscriber prepayments and other liabilities			171,966		136,567
Postretirement benefit obligation			7,636		1,978
Net cash provided by operations			1,904,071		986,402
INVESTING ACTIVITIES:					
Purchase of property, plant and equipment			(1,498,098)		(1,024,870)
Purchase of intangible assets			(164,577)		(134,424)
Purchase of businesses, net of cash acquired			(338,906)		(1,005,451)
Proceeds from disposal of subsidiaries, net of cash disposed			649		71,417
Purchase of long-term investments			(76,217)		(88,281)
Proceeds from sale of long-term investments			-		6,538
Purchase of short-term investments			(142,696)		(102,165)
Proceeds from sale of short-term investments			187,500		312
Proceeds from sale of property, plant and equipment			7,807		4,384
Net increase in loans to customers			(39,898)		(92,696)
Net cash used in investing activities			(2,064,436)		(2,365,236)

JSFC SISTEMA AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003
(Amounts in thousands of U.S. dollars)

	Notes		2004		2003
FINANCING ACTIVITIES:					
(Principal payments on)/proceeds from short-term borrowings, net			(263,981)		120,772
Net increase/(decrease) in deposits from customers			150,876		(15,294)
Net increase in bank promissory notes issued			12,838		56,449
Proceeds from grants			3,285		7,390
Proceeds from capital transactions of subsidiaries			9,445		-
Proceeds from long-term borrowings, net of debt issuance costs			1,458,082		2,182,802
Principal payments on long-term borrowings			(868,347)		(758,784)
Principal payments on capital lease obligations			(7,924)		(25,534)
Payments to shareholders of subsidiaries			(108,165)		(63,069)
Dividends paid			(5,162)		-
Net cash provided by financing activities		$	380,947	$	1,504,732
INCREASE IN CASH AND CASH EQUIVALENTS		$	220,582	$	125,898
CASH AND CASH EQUIVALENTS, beginning of the year			283,165		157,267
CASH AND CASH EQUIVALENTS, end of the year		$	503,747	$	283,165

	Notes		2004		2003
CASH PAID DURING THE YEAR FOR:					
Interest, net of amounts capitalized		$	(265,779)	$	(146,863)
Income taxes			(487,447)		(335,636)
NON-CASH INVESTING AND FINANCING ACTIVITIES:					
Property, plant and equipment contributed free of charge		$	13,597	$	18,793
Equipment acquired through vendor financing			20,714		17,093
Equipment acquired under capital leases			6,393		17,709
In addition, non-cash investing activities during the years ended December 31, 2004 and 2003 included acquisitions and dispositions of subsidiaries and affiliates, as described in Notes 3 and 4.					
See notes to consolidated financial statements.					

JSFC SISTEMA AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

(Amounts in thousands of U.S. dollars)

		Share capital		Additional capital		Retained earnings		Accumulated other comprehensive income/ (loss)		Total
Balances at January 1, 2003	$	171	$	200,931	$	396,211	$	(2,533)	$	594,780
Capital transactions of subsidiaries		-		(10,997)		-		-		(10,997)
Unrealized gain on securities available for sale, net of income tax of nil		-		-		-		5,582		5,582
Translation adjustment, net of minority interest of $24,426 and income tax of nil (Note 2)		-		-		-		35,321		35,321
Income tax effect of changes in the functional currency, net of minority interest of $17,184		-		-		-		(22,449)		(22,449)
Net income		-		-		387,047		-		387,047
Balances at January 1, 2004	$	171	$	189,934	$	783,258	$	15,921	$	989,284
Capital transactions of subsidiaries, net of minority interest of $2,628 and income tax of nil (Note 4)		-		8,948		-		-		8,948

	Share capital	Additional capital	Retained earnings	Accumulated other comprehensive income/ (loss)	Total
Unrealized gain on securities available for sale, net of income tax of nil	-	-	-	1,967	1,967
Change in fair value of interest rate swaps, net of taxes	-	-	-	(257)	(257)
Translation adjustment, net of minority interest of $28,582 and income tax of nil (Note 2)	-	-	-	29,979	29,979
Dividends declared (Note 27)	-	-	(5,162)	-	(5,162)
Increase of par value of shares (Note 27)	24,919	-	(24,919)	-	-
Net income	-	-	411,227	-	411,227
Balances at December 31, 2004	$ 25,090	$ 198,882	$ 1,164,404	$ 47,610	$ 1,435,986

See notes to consolidated financial statements.

JSFC SISTEMA AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2004 AND 2003

(Amounts in thousands of U.S. dollars, except share and per share amounts or if otherwise stated)

1. DESCRIPTION OF BUSINESS

The financial statements of JSFC Sistema and subsidiaries (the "Group") reflect the consolidation of separate financial statements of operating entities related by means of direct or indirect ownership of their voting stock by the Group's holding company, JSFC Sistema. Most of the consolidated entities and the parent company are incorporated in the Russian Federation ("RF").

The controlling shareholder of JSFC Sistema is Vladimir P. Evtushenkov. Minority holdings are owned by certain top executives and former top executives of the Group.

The principal activities of the significant entities of the Group are as follows:

Operating Entities	Short Name	Principal activity
JSFC Sistema	JSFC Sistema	Investing and financing activities
Telecommunications Segment:		
MTS and subsidiaries	MTS	
MGTS and subsidiaries	MGTS	
Comstar and subsidiary	Comstar	
MTU-Inform	MTU-Inform	
"Telmos"	Telmos	
MTU-Intel and subsidiary	MTU-Intel	Wireless and fixed line telecommunication services, data transmission and internet services
Technology Segment:		
CSC and subsidiaries	CSC	Production and marketing of integrated circuits, wafers, electronic devices and consumer electronics, research and development

Operating Entities	Short Name	Principal activity
Kvazar-Micro and subsidiaries	Kvazar-Micro	IT and systems integration, computer hardware and software distribution
Insurance Segment:		
Rosno and subsidiaries	Rosno	Medical, property, casualty, life and personal insurance and reinsurance, administration of state medical insurance programs
Banking Segment:		
Moscow Bank for Reconstruction and Development and subsidiaries	MBRD	Banking activities, securities transactions and foreign currency transactions
Other businesses:		
Detsky Mir and subsidiaries	Detsky Mir	Retail trading in Moscow and other Russian cities, rent of premises
Detsky Mir-Center and subsidiaries	DM-Center	
VAO Intourist and subsidiaries	Intourist	Sale of tour packages in the RF and abroad
Sistema-Hals and subsidiaries	Sistema-Hals	Development and marketing of real estate projects in Moscow
Sistema Mass Media and subsidiaries	Sistema Mass Media	Production and distribution of periodicals, publishing activities, broadcasting, advertising
Concern RTI Systems and subsidiaries	Concern RTI	Manufacturing of radiotechnical equipment, research and development
ECU GEST Holding S.A. and subsidiaries	ECU GEST	Investing in real estate projects, financing activities

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying consolidated financial statements have been prepared in conformity with the accounting principles generally accepted in the United States of America ("U.S. GAAP"). The Group's Russian entities maintain accounting records in Russian Rubles in accordance with the requirements of Russian accounting and tax legislation. The accompanying financial statements differ from the financial statements prepared for statutory purposes in Russia in that they reflect certain adjustments, appropriate to present the financial position, results of operations and cash flows in accordance with U.S. GAAP, which are not recorded in the accounting books of the Group's entities.

Principles of Consolidation

The consolidated financial statements include the accounts of JSFC Sistema, as well as entities, where JSFC Sistema has operating and financial control through direct or indirect ownership of a majority voting interest. The consolidated financial statements also include accounts of variable interest entities where the Group is a primary beneficiary. All significant intercompany transactions, balances and unrealized gains (losses) on transactions have been eliminated.

The beneficial ownership interest of JSFC Sistema and proportion of voting power of the Group in the significant subsidiaries as of December 31, 2004 and 2003 are as follows:

Operating entities	Ownership interest		Proportion of voting power	
	2003	2004	2003	2004
MTS	51%(1)	51%(1)	51%	51%
Ukrainian Mobile Communications ("UMC"), subsidiary of MTS	51%(1)	51%(1)	100%	100%
Telecom XXI, subsidiary of MTS	51%(1)	51%(1)	100%	100%
Kuban-GSM, subsidiary of MTS	51%(1)	51%(1)	100%	100%
Telecom-900, subsidiary of MTS	51%(1)	51%(1)	100%	100%
SCS-900, subsidiary of MTS	50%(1)	45%(1)	100%	89%
FECS-900, subsidiary of MTS	51%(1)	30%(1)	100%	60%
Uraltel, subsidiary of MTS	51%(1)	51%(1)	100%	100%
Recom, subsidiary of MTS	27%(1)	27%(1)	54%	54%
BM-Telecom, subsidiary of MTS	51%(1)	51%(1)	100%	100%
TAIF Telcom, subsidiary of MTS	51%(1)	27%(1)	100%	53%
Dontelecom, subsidiary of MTS	51%(1)	51%(1)	100%	100%

Operating entities	Ownership interest		Proportion of voting power	
	2003	2004	2003	2004
Sibchallenge, subsidiary of MTS	51%[1]	51%[1]	100%	100%
Tomsk Cellular Communications, subsidiary of MTS	51%[1]	51%[1]	100%	100%
Primtelefon, subsidiary of MTS	51%[1]	Affiliate	100%	Affiliate
Uzdunrobita, subsidiary of MTS	37%[1]	-	74%	-
Gorizont RT, subsidiary of MTS	39%	-	76%	-
Telesot-Alania, subsidiary of MTS	27%	-	53%	-
MGTS	56%	56%	56%	56%
Comstar	77%[1]	77%[1]	100%	100%
MTU-Inform	76%[1]	76%[1]	99%	99%
Telmos	62%[1]	62%[1]	80%	80%
MTU-Intel	87%[1]	87%[1]	100%	100%
Golden Line, subsidiary of MTU-Intel	87%[1]	87%[1]	100%	100%
Personal Communications (“P-Com”)	Affiliate	63%[1]	Affiliate	83%
Rosno	49%[1]	47%	51%	51%
MBRD	82%[1]	59%[1]	86%	86%
Intourist	91%	91%	91%	91%
DM-Center	100%	100%	100%	100%
Detsky Mir	75%[1]	71%	75%	75%
CSC	78%	83%	78%	83%
NIIME and Micron (“Micron”), subsidiary of CSC	60%[1]	58%[1]	76%	71%
STROM telecom, subsidiary of CSC	52%[1]	81%[1]	67%	100%
Kvazar-Micro	50%[1]	-	51%	-
Sistema-Hals	100%[1]	99%[1]	100%	100%
Nasha Pressa	100%[1]	100%[1]	100%	100%
Concern RTI	100%	100%	100%	100%
ECU GEST	99%	99%	99%	99%

[1] - Including indirect ownership.

Accounts of newly-acquired subsidiaries have been consolidated in the Group's financial statements from the beginning of the year, when control was acquired, with pre-acquisition earnings of an interest purchased during the year included in minority interest in the consolidated statement of operations.

Consolidation of Variable Interest Entities

In December 2003, Financial Accounting Standards Board ("FASB") issued a revision to Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51" ("FIN 46R" or the "Interpretation"). FIN 46R clarifies the application of Accounting Research Bulletin ("ARB") No. 51, "Consolidated Financial Statements", to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. FIN 46R requires the consolidation of these entities, known as variable interest entities ("VIEs"), by the primary beneficiary of the entity. The primary beneficiary is the entity, if any, that will absorb a majority of the entity's expected losses, receive a majority of the entity's expected residual returns, or both. Among other changes, the revisions of FIN 46R (a) clarified some requirements of the original FIN 46, which had been issued in January 2003, (b) eased some implementation problems, and (c) added new scope exceptions. FIN 46R deferred the effective date of the Interpretation for public companies, to the end of the first reporting period ending after March 15, 2004, except that all public companies must at minimum apply the provisions of the Interpretation to entities that were previously considered "special-purpose entities" under the FASB literature prior to the issuance of FIN 46R by the end of the first reporting period ending after December 15, 2003.

Following the adoption of FIN 46R, the Group reevaluated the relationships with its related parties: Promtorgcenter, Notris, Laminea, Finescort-M, Kuntsevo-Invest, Putney Assets and Mosdachtrest. Kuntsevo-Invest and Mosdachtrest are engaged in construction activities of the Group. Promtorgcenter, Notris, Laminea, Finescort–M and Putney Assets possess shareholdings in and provide financing through intercompany loans to other entities of the Group. Mosdachtrest was accounted for under the equity method for the periods prior to January 1, 2004. The Group determined that these entities were variable interest entities and that it was their primary beneficiary. Accordingly, the Group has consolidated these companies effective January 1, 2004. All intercompany balances have been eliminated in consolidation and the results of these VIEs have been included in the Group's consolidated statement of operations and statement of cash flows for the year ended December 31, 2004. In accordance with the provisions of FIN 46R, the Group recorded a charge for the cumulative effect of this accounting change of $35.5 million, net of income tax of nil, in the year ended December 31, 2004. This charge reflects the cumulative impact to the Group's results of operations had these VIEs been consolidated since their inception.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses of the reporting period. Actual results could differ from those estimates.

Examples of significant estimates include the allowance for doubtful accounts, the recoverability of intangible assets and other long-lived assets, and valuation allowances on deferred tax assets.

Concentration of Business Risk

The Group's principal business activities are within the RF. Laws and regulations affecting businesses operating in the RF are subject to rapid changes, which could impact the Group's assets and operations.

Foreign Currency Translation

The Group follows a translation policy in accordance with Statement on Financial Accounting Standards ("FAS") No. 52, "Foreign Currency Translation". Due to a highly inflationary economy in the RF until the year 2003, the U.S. dollar (the Group's reporting currency) has been designated as the Group's functional currency. Accordingly, all foreign currency amounts were translated into U.S. dollars ("USD") using the remeasurement method.

Starting from January 1, 2003, the Russian economy ceased to be considered highly inflationary for accounting purposes. Management has determined that for the fiscal year beginning January 1, 2003 the functional currency of MGTS, Rosno, Kuban-GSM, CSC, Detsky Mir, DM-Center, Sistema Mass Media and Concern RTI is the Russian Ruble ("RUR"). Accordingly, the reporting currency amounts for these subsidiaries were translated into their functional currency at the exchange rate current at January 1, 2003. These amounts became the new accounting basis for the non-monetary assets and liabilities. The functional currency of UMC is the Ukrainian Hryvnia ("UAH") and the functional currency of STROM telecom is the Czech Krona. Management believes that USD is still the appropriate functional currency for the other subsidiaries of the Group due to the pervasive use of the U.S. dollar in their operations.

The Group has selected the USD as its reporting currency and translates financial statements of subsidiaries with functional currencies other than USD. Assets and liabilities are translated at the exchange rates current at the balance sheet date, while income and expense items are translated at average rates of exchange prevailing during the period. The resulting translation adjustments in the amounts of $30.0 million and $35.3 million, net of minority interest of $28.6 million and $24.4 million, were recorded as a separate component of other comprehensive income for the years ended December 31, 2004 and 2003, respectively.

The Ruble is not a fully convertible currency outside of the territory of the Russian Federation. The translation of RUR denominated assets and liabilities into USD for the purpose of these financial statements does not indicate that the Group could or will in the future convert the reported values of the assets and liabilities in USD.

Revenue Recognition

The Telecommunications Segment of the Group earns revenues from the provision of wireless telecommunication services, local telephone and data transmission services and usage of its local exchange networks and facilities. Segment revenues consist of (i) usage charges, (ii) monthly subscription fees, (iii) service activation and connection fees, (iv) revenues from use of prepaid phone cards, (v) charges for value-added telecommunication services, (vi) roaming fees charged to other operators for guest roamers utilizing the Group's network and (vii) equipment sales. The Group records revenues over the periods they are earned as follows:

- Revenues derived from wireless and local telephone usage and data transmission are recognized as the services are provided.
- Monthly telephone and network service fees are recognized in the month during which the telephone services are provided to customers.
- Upfront fees received for installation and activation of wireless, wireline and data transmission services ("connection fees") are deferred and recognized over the expected subscriber relationship period. Prior to December 31, 2003, MTS estimated that the average expected term of the subscriber relationship ranged from 39 to 47 months. Commencing January 1, 2004, MTS calculates an average expected term of the subscriber relationship for each region and amortizes regional connection fees accordingly. Average expected subscriber life is ranging from 20 to 76 months. The effect of this change in estimate in the year ended December 31, 2004 was an increase in net income of approximately $4.3 million, or $0.5 per share. The customer relationship period for residential wireline voice phone subscribers is 15 years. For all other categories of subscribers the customer relationship period is estimated at 3 to 5 years.
- The Group recognizes revenues from the prepaid phone cards in the period when customer uses time under the phone card. Unused time on sold cards is not recognized as revenues until the related services have been provided to the customer or the prepaid phone card has expired. Revenues under prepaid service tariff plans, whereby a customer may purchase a package that allows a connection to the Group's wireless network and a predetermined allotment of wireless phone calls and/or other services offered by the Group, are allocated between connection fees and service fees based on their relative fair values.
- Revenues derived from value-added telecommunication services are recognized in the period when the services are provided to customers.
- The Group charges roaming per-minute fees to other wireless operators for their subscribers utilizing the Group's networks. Revenues derived from roaming services are recognized as the services are provided.
- The Group sells handsets and accessories to customers who are entering into contracts for service and as separate distinct transactions. The Group recognizes revenues from the handsets and accessories when title passes to the customer. Estimated returns are recorded as a direct reduction of sales at the time the related sales are recorded. In Ukraine, the Group also from time to time sells handsets at prices below cost. The Group recognizes these subsidies in cost of equipment when sale is recorded.

Local telephone services, provided by MGTS, totaling approximately 5% and 6% of the consolidated revenues for the years ended December 31, 2004 and 2003, respectively, are regulated tariff services, and changes in rate structure are subject to the Federal Tariff's Service approval.

MGTS is required to grant discounts ranging from 20% to 100% on installation and monthly fees to certain categories of residential subscribers, such as pensioners, military veterans and disabled individuals, and is entitled to reimbursement from the federal budget for these discounts. Due to the lack of certainty of reimbursement, MGTS accounts for such revenues upon collection.

STROM telecom's arrangements with its customers typically include multiple elements, such as equipment and software development, installation services and post-contract customer support. In accordance with Statement of Position ("SOP") No. 97-2, "Software Revenue Recognition", the aggregate arrangement fee is allocated to each of the undelivered elements in an amount equal to its fair value with the residual of the arrangement fee allocated to the delivered elements. Fair values are based upon vendor-specific objective evidence. Fees allocated to each element of an arrangement are recognized as revenue when the following criteria have been met: (i) a written contract for the delivery of an element has been executed, (ii) the Group has delivered the product to the customer, (iii) the fee receivable is fixed or determinable, and (iv) collectibility of the resulting receivable is deemed probable. If evidence of fair value of the undelivered elements of the arrangement does not exist, all revenue from the arrangement is deferred until such time evidence of fair value does exist, or until all elements of the arrangement are delivered. Fees allocated to post-contract customer support are recognized as revenue ratably over the support period. Fees allocated to other services are recognized as revenue as services are performed.

Premiums on written non-life insurance of the Insurance Segment are recognized on a pro-rata basis over the term of the related policy coverage, normally not exceeding 1 year. The unearned premium provision represents that portion of premiums written relating to the unexpired term of the policy. Premiums from traditional life and annuity policies with life contingencies are recognized as revenue when due from the policyholder.

Interest income of the Banking Segment is recognized on accrual basis. Loans are placed on non accrual status when interest or principal is delinquent for a period in excess of 90 days, except when all amounts due are fully secured by cash or marketable securities and collection proceedings are in process. Interest income is not recognized where recovery is doubtful. Loans are written off against allowance for loan losses in case of uncollectibility of loans and advances, including through repossession of collateral.

Revenues on construction contracts are recognized under the completed-contract method.

The other Group's entities recognize revenues when products are shipped or when services are rendered to customers.

In arrangements where the Group acts as an agent, including travel agency arrangements and arrangements to administer construction projects, only the net agency fee is recognized as revenue.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, amounts on deposit in banks, cash invested temporarily in various instruments with maturities of three months or less at time of purchase and minimum reserve deposits with the Central Bank of the Russian Federation. Short-term interbank loans originated by MBRD with original maturities of three months or less are included in loans to customers and banks.

Financial Instruments

The Group's financial instruments include cash, short-term and long-term investments, receivables, payables and debt. Except as described below, the estimated fair value of such financial instruments as of December 31, 2004 approximated their carrying value as reflected in the consolidated balance sheet. The fair value of the Group's publicly traded long-term notes as of December 31, 2004 ranged from 100.9% to 106.0% of the principal amount. As of December 31, 2004, fair value of other fixed rate debt, including capital lease obligations and variable rate debt approximated carrying value.

From time to time, in its acquisitions the Group uses derivative instruments, consisting of put and call options on all or part of the minority stakes of acquired companies, to defer payment of the purchase price and provide optimal acquisition structuring. In addition, in December 2004, the Group entered into two variable-to-fixed interest rate swap agreements to manage its exposure to changes in fair value of future cash flows of its variable-rate long term debt, which is caused by interest rate fluctuations. The Group does not use derivatives for trading purposes.

The Group accounts for derivative instruments in accordance with FAS No. 133 "Accounting for Derivative Instruments and Hedging Activities" and FAS No. 149 "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". All derivatives, including some embedded derivatives, are measured at fair value and recognized as either assets or liabilities on balance sheets. The Group's interest rate swap agreements are designated as a cash flow hedge and the hedging relationship qualifies for hedge accounting. The effective portion of the change in fair value of interest rate swap agreements is, accordingly, recorded in other comprehensive income and reclassified to interest expense when the hedged debt affects the interest expense. Changes in fair value of other derivative instruments are recognized in net income as those instruments were not designated as hedges.

At the inception of the hedge and on a quarterly basis, the Group performs an analysis to assess whether changes in cash flows of its interest rate swap agreements are deemed highly effective in offsetting changes in cash flows of the hedged debt. If at any time the correlation assessment will indicate that the interest rate swap agreements are no longer effective as a hedge, the Group will discontinue hedge accounting and all subsequent changes in fair value will be recorded in net income.

MBRD also enters into sale and purchase back agreements ("repos") and purchase and sale back agreements ("reverse repos") in the normal course of its business. A repo is an agreement to transfer a financial asset to another party in exchange for cash or other consideration and a concurrent obligation to reacquire the financial assets at a future date for an amount equal to the cash or other consideration exchanged plus interest. Assets sold under repos are retained in the financial statements and a consideration received is recorded in liabilities as collateralized deposit received. A reverse repo is an agreement to purchase assets and resell them at a future date with accrued interest received. Assets purchased under reverse repos are recorded in the financial statements as cash received on deposit which is collateralized by securities or other assets. During the years ended December 31, 2004 and 2003, the Group did not enter into material repo or reverse repo agreements.

Accounts Receivable

Accounts receivable are stated at their net realizable value after deducting an allowance for doubtful accounts. Such provisions reflect either specific cases of delinquencies or defaults or estimates based on evidence of collectibility.

Loans to Customers and Banks

Loans to customers and banks arise out of operations of the Banking Segment. The determination of the allowance for losses in respect of loans provided by MBRD is based on an analysis of the loan portfolio and reflects the amount, which, in the judgment of management of the Group, is adequate to provide for losses inherent in the loan portfolio. A specific provision is made as a result of a detailed appraisal of risk assets. In addition, a general provision is carried to cover risks, which although not specifically identified, are present in any portfolio of banking assets.

Management's evaluation of the allowance is based on MBRD's past loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral and current economic conditions. It should be understood that estimates of loan losses involve an exercise of judgment. While it is possible that in particular periods MBRD may sustain losses, which are substantial relative to the allowance for loan losses, it is the judgment of management that the allowance for loan losses is adequate to absorb losses inherent in the loan portfolio.

Insurance-related Receivables

Insurance-related receivables include receivables arising from insurance operations and advances to health care providers under voluntary and obligatory medical insurance programs. Receivables arising from insurance operations consist of outstanding direct premiums due from policyholders, outstanding assumed premiums due from ceding companies and receivables due from claims ceded.

Policy Acquisition Costs

Policy acquisition costs represent costs of the acquisition or renewal of insurance policies by Rosno. They are deferred as an asset and are amortized over the period for which costs are expected to be recoverable out of associated revenues. Deferred acquisition costs are included in other receivables and prepaid expenses, net of the unexpired risk provision, that is recognized when unearned premiums are insufficient to meet claims and expenses, which may be incurred after the end of the financial year.

Subscriber Acquisition Costs

Subscriber acquisition costs represent the direct costs paid for each new subscriber. The Group expenses these costs as incurred.

Inventories

Inventories are stated at the lower of cost or market. The cost of MGTS's inventories (including mostly spare parts) is computed on an average cost basis. Cost of goods for resale held by retail businesses of the Group is determined using the retail method. Other subsidiaries of the Group account for their inventories using the first-in-first-out ("FIFO") cost method.

Cost of raw materials includes cost of purchase, customs duties, transportation and handling costs. Work-in-progress and finished goods are stated at production cost which includes direct production expenses and manufacturing overheads. Project costs include the accumulated costs of projects contracted with third parties, net of related progress billings. The entities of the Group periodically assess their inventories for obsolete or slow moving stock.

Value-Added Taxes

Value-added taxes ("VAT") related to sales are payable to the tax authorities on an accrual basis based upon invoices issued to the customer. VAT incurred for purchases may be reclaimed, subject to certain restrictions, against VAT related to sales. VAT related to purchase transactions that are not reclaimable as of the balance sheet dates are recorded in other receivables and prepaid expenses.

Property, Plant and Equipment

For subsidiaries acquired by the Group through business combinations accounted for by the purchase method, property, plant and equipment ("PP&E") were assigned their fair values at the acquisition date. If fair values of the identifiable net assets of the acquired entities exceeded acquisition cost, the fair values of non-current assets held by the acquired entities at the acquisition date, including PP&E, were reduced by such excess. All subsequent additions to PP&E have been recorded at cost.

Cost includes major expenditures for improvements and replacements, which extend useful lives of the assets or increase their revenue generating capacity. Repairs and maintenance are charged to the statement of operations as incurred.

Capital leases are recorded at the lower of the fair market value of the asset or the present value of future minimum lease payments.

Depreciation is computed under the straight-line method utilizing estimated useful lives of the assets as follows:

Buildings	20-50 years
Leasehold improvements	Lesser of the estimated useful life or the term of the lease
Switches and transmission devices	17-31 years
Network and base station equipment	5-12 years
Other plant, machinery and equipment	3-15 years

Items of property, plant and equipment that are retired or otherwise disposed of are eliminated from the consolidated balance sheet along with the corresponding accumulated depreciation. Any gain or loss resulting from such retirement or disposal is included in the determination of consolidated net income.

Construction-in-progress and equipment for installation are not depreciated until an asset is placed into service.

Maintenance and repair costs are expensed as incurred, while upgrades and improvements are capitalized.

As a result of recent financial statement restatements by numerous U.S. public companies and publication of a letter by the Chief Accountant of the SEC regarding the interpretation of longstanding lease accounting principles, MTS has corrected its accounting practices for the leasehold improvements in the fourth quarter of 2004. The primary effect of this accounting correction was to accelerate to earlier periods depreciation expenses with respect to certain components of previously capitalized leasehold improvements.

These corrections resulted in a cumulative, net charge to net income of $17.7 million in the fourth quarter of 2004, of which $10.9 million relates to the years 1998 through 2003. The net cumulative charge is comprised of a $44.5 million increase in depreciation expense related primarily to depreciation of capitalized leasehold improvements for base stations; a decrease of $1.4 million in the equity net income from the MTS-Belarus also related to depreciation of capitalized leasehold improvements expenses for base stations positions; increase of $11.0 million related to additional deferred tax benefit due to the change in accounting base for property, plant and equipment; and decrease in minority interest of $17.2 million.

All components of the net charge are non-cash and do not impact historical or future cash flows or the timing of payments under the related leases.

Asset Retirement Obligations

In accordance with FAS No. 143, "Accounting for Asset Retirement Obligations", the Group calculates an asset retirement obligation and an associated asset retirement cost when the Group have a legal obligation in connection with the retirement of tangible long-lived assets. The Group's obligations under FAS No. 143 arise from certain of its leases and relate primarily to the cost of removing equipment from such lease sites. As of December 31, 2004 the estimated assets retirement obligations were not significant to the Group's consolidated financial position and results of operations.

License Costs

Costs of licenses for providing telecommunications services are capitalized as a result of (a) purchase price allocated to licenses acquired in business combinations (Note 3) and (b) licenses purchased directly from government organizations, which require license payments.

Current operating licenses of the Group do not provide for automatic renewal upon expiration. As the Group and the telecommunications industry do not have sufficient experience with the renewal of licenses, license costs are being amortized, subject to periodic review for impairment, on the straight-line basis over the initial term of the license without consideration of possible future renewals commencing from the date such license area becomes commercially operational.

Goodwill and Other Intangible Assets

Goodwill represents the excess of the cost of business acquired over the fair value of identifiable net assets at the date of acquisition. Goodwill is reviewed annually for impairment or whenever it is determined that the impairment indicators exist. The Group determines whether an impairment has occurred by assigning goodwill to the reporting unit identified in accordance with FAS No. 142 "Goodwill and Other Intangible Assets", and comparing the carrying amount of the reporting unit to the fair value of the reporting unit. If a goodwill impairment has occurred, the Group recognizes a loss for the difference between the carrying amount and the implied fair value of goodwill. No material impairment of goodwill was identified in the year ended December 31, 2004.

The carrying amount of goodwill attributable to each reportable operating segment with goodwill balances and changes therein, are as follows:

(000's)		Telecommunications		Insurance		Corporate and Other		Total
Balance as of January 1, 2003	$	19,347	$	-	$	635	$	19,982
Purchase price allocation		71,267		-		-		71,267
Impairment charge		(19,251)		-		-		(19,251)
Balance as of December 31, 2003		71,363		-		635		71,998
Purchase price allocation		101,002		1,341		-		102,343
Balance as of December 31, 2004	$	172,365	$	1,341	$	635	$	174,341

Other intangible assets represent acquired customer bases, trademarks, roaming contracts with other telecommunications operators, telephone numbering capacity, rights to use premises and various purchased software costs. Trademarks and telephone numbering capacity with unlimited contractual life are not amortized, but are reviewed, at least annually, for impairment in accordance with the provisions of FAS No. 142.

Acquired customer bases are amortized over the estimated average subscriber life from 20 to 76 months. Deferred telephone numbering capacity costs with limited contractual life and the rights to use premises are being amortized over their contractual lives, which vary from five to twenty years. Software costs and other intangible assets are being amortized over three to ten years. All finite-life intangible assets are being amortized using the straight-line method.

Investments

The Group's share in net assets and net income of certain entities, where the Group holds 20 to 50% of voting shares and has the ability to exercise significant influence over their operating and financial policies ("affiliates") is included in the consolidated net assets and operating results using the equity method of accounting. Due to the Group's day-to-day involvement in the affiliates' business activities, the Group's share of their income is recorded within the operating income.

Investments in corporate shares where the Group owns more than 20% of voting shares, but does not have the ability or intent to control or exercise significant influence over operating and financial policies, including investments in NIIDAR, a Research and Development Institute of Long-Distance Radio Communications, operating under governmentally imposed restrictions, as well as investments in corporate shares where the Group owns less than 20% of share capital, are accounted for at cost of acquisition. Management periodically assesses realizability of the carrying values of such investments and records impairment charges, if required.

Trading securities held by the Group are stated at market value. Unrealized holding gains and losses for trading securities are included in earnings.

The Group also purchases promissory notes for investing purposes. These notes are carried at cost and the discount against the nominal value is accrued over the period to maturity. A provision is made, based on management assessment, for notes that are considered uncollectible.

Debt Issuance Costs

Debt issuance costs are amortized using the effective interest method over the terms of the related loans. Debt issuance costs amounted to $27.3 million and $17.3 million, net of accumulated amortization of $11.7 million and $5.8 million as of December 31, 2004 and 2003, respectively.

Impairment of Long-lived Assets

The Group periodically evaluates the recoverability of the carrying amount of its long-lived assets in accordance with FAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, the Group compares undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, the Group records impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets. For the year ended December 31, 2004, no significant impairments have been identified.

Bank Deposits and Notes Issued

Bank deposits and notes issued arise out of operations of the Banking Segment and include deposits from banks and customers and promissory notes issued.

Insurance-related Liabilities

Insurance-related liabilities arise out of the operations of the Insurance Segment and include the unearned premium provision, loss provision for outstanding claims, undisbursed funds of the Moscow Government Fund for Obligatory Medical Insurance (“MGFOMS”), accumulated under an obligatory medical insurance program, prepaid insurance and reinsurance premiums and liabilities under deposit type insurance contracts (policies in force under which the Group does not assume insurance risk).

Rosno provides for losses on outstanding claims on an individual case basis for the estimated cost of claims notified but not settled as at the balance sheet date. Provision is also made for the ultimate cost of claims, including claims incurred but not reported, or not fully reported. This provision is actuarially determined by line of business, and includes assumptions based on prior years claims experience. The loss provision for life insurance is actuarially determined based upon mortality, morbidity and interest rate assumptions applied to all life insurance policies in force as at year-end.

Unexpired risk provision is recognized when unearned premiums are insufficient to meet claims and expenses, which may be incurred after the end of the financial year. The Group does not consider anticipated investment income in making determination whether a premium deficiency exist.

MGFOMS carries out an obligatory medical insurance program to provide RF citizens with free of charge medical services via certain appointed insurers, including Rosno. Rosno has contracted with MGFOMS to administer a portion of this plan. Rosno receives advances from MGFOMS and makes payments to medical centers in respect of services provided by them to policyholders. Any funds received from MGFOMS by Rosno, which are not paid out for medical services, are retained and recorded as a liability. These funds may be spent by the Group only on the provision of the medical facilities and care, as presently defined under the program.

Deferred Revenue

Telecommunication equipment and transmission devices, installed at the newly constructed properties in Moscow, have been historically transferred to MGTS free of charge. These assets are capitalized by the Group at their market value at the date of transfer. Simultaneously deferred revenue is recorded in the same amount, which is amortized as a reduction of the depreciation charge in the consolidated statement of operations over the contributed assets’ life.

Deferred grant revenue represents funds contributed to the Group, which usage is restricted. Deferred grants are released to income when the conditions of the grant are substantially met.

Income Taxes

Income taxes have been computed in accordance with RF laws. Income tax rate in the RF equals 24%. In July 2004, amendments to Russian income tax legislation were enacted to increase, effective January 1, 2005, the income tax rate on dividends paid within Russia to 9% (previously 6%). The foreign subsidiaries of the Group are paying income taxes in their jurisdictions. Income tax rate in the Ukraine and in the Czech Republic equals 25% and 26%, respectively.

Deferred income taxes are accounted for under the liability method and reflect the tax effect of all significant temporary differences between the tax bases of assets and liabilities and their reported amounts in the accompanying consolidated financial statements. A valuation allowance is provided for deferred tax assets if it is more likely than not that these items will either expire before the Group will be able to realize the benefit, or the future deductibility is uncertain.

Stock-Based Compensation

The Group accounts for stock options issued to employees, non employee directors and consultants of MTS following the requirements of FAS No. 123, "Accounting for Stock-Based Compensation" and FAS No. 148 "Accounting for Stock Based Compensation - Transition and Disclosure, an amendment to FASB Statement No. 123." Under the requirements of these statements, the Group elected to use the intrinsic method to value options on the measurement date as a method for accounting for compensation to employees and non-employee directors. Compensation to consultants is measured based on the fair value of options on the measurement date as determined using a binomial option-pricing model.

During the years ended December 31, 2004, 2003 and 2002, MTS made several grants pursuant to its stock option plan to its employees and directors. These options generally vest over a two year period from the date of the grant, contingent on continued employment of the grantee with MTS.

A summary of the status of MTS' option plan for the years ended December 31, 2004 and 2003 is presented below:

	MTS shares		Weighted average exercise price
Outstanding at January 1, 2003	4,648,421	$	1.42
Granted	1,952,632		2.43
Exercised	(37,557)		1.31
Exchanged for cash award	(1,746,310)		1.31
Forfeited	(19,776)		1.31
Outstanding at December 31, 2003	4,797,410		1.87
Granted	1,665,256		5.95
Exercised	(2,726,966)		1.49
Forfeited	(204,730)		1.92
Outstanding at December 31, 2004	3,530,970	$	4.09

As of December 31, 2004, MTS had the following stock options outstanding:

Number of MTS' shares		Exercise prices	Remaining weighted average life (years)
1,868,214	$	2.43	0.54
1,662,756		5.95	1.54
3,530,970			

None of the options outstanding as of December 31, 2004 and 2003 were exercisable.

According to the terms of the option plan, the exercise price of the options equals the average market share price during the hundred day period preceding the grant date. The difference in the exercise price of the option and the market price at the date of the grant is shown as unearned compensation in the consolidated statements of changes in shareholders' equity and is amortized to expense over the vesting period of 2 years. This amount historically had been insignificant to the consolidated financial statements.

MTS' option plan does not routinely allow a grantee to receive cash in lieu of shares, however due to the lack of liquidity for MTS' stock in the Russian market, 1,746,310 options were cancelled by MTS in 2003 and exchanged for a cash award of $2.9 million.

The fair value of options granted by MTS during the years ended December 31, 2004 and 2003 were estimated using the binomial option pricing model using the following assumptions:

	2004	2003
Risk free rate	4.5%	5.2%
Expected dividend yield	3%	3%
Expected volatility	48.8%	40.0%
Expected life (years)	2	2
Fair value of options (per share)	$ 2.36	$ 1.02

If the Group had elected to recognize compensation costs based on the fair values of options at the date of the grant, net income and earnings per share amounts for the years ended December 31, 2004 and 2003 would have been as follows:

	2004	2003
Net income as reported	$ 411,227	$ 387,047
Pro forma effect of the application of fair value method of accounting for stock options	(545)	(371)
Pro forma net income	410,682	386,676
Earnings per share, basic and diluted		
As reported	$ 50.8	$ 47.8
Pro forma	$ 50.7	$ 47.7

Retirement and Post-Retirement Benefits

Subsidiaries of the Group contribute to the local state pension fund and social fund, on behalf of all their employees.

In Russia, all social contributions, including contributions to the pension fund, are substituted with a unified social tax ("UST") calculated by the application of a regressive rate from 35.6% to 2% of the annual gross remuneration of each employee. UST is allocated to three social funds, including the pension fund, where the rate of contributions to the pension fund vary from 28% to 2% depending on the annual gross salary of each employee. The contributions are expensed as incurred.

In Ukraine, the subsidiaries of the Group are required to contribute a specified percentage of each employee payroll up to a fixed limit to pension fund, unemployment fund and social security fund. The contributions are expensed as incurred.

During the years ended December 31, 2004 and 2003, the Group managed a defined contribution plan to provide eligible employees with additional income upon retirement. The Group's contributions to the plan totaled $0.8 million and $1.7 million for the years ended December 31, 2004 and 2003, respectively.

In addition, MGTS has historically offered its employees certain benefits upon and after retirement. The cost of such benefits is recognized during an employee's years of active service (Note 25).

The Group accounts for pension plans following the requirements of FAS No. 87 "Employers' Accounting for Pensions."

In December 2003, FASB issued a revision to FAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits, an amendment of FASB Statements No. 87, 88, and 106" ("FAS No. 132R"). FAS No. 132R revised employers' disclosure about pension plans and other postretirement benefit plans. It requires additional disclosures about the plan assets, benefit obligations, cash flows and net periodic benefit cost of defined benefit plans and other defined postretirement plans. It does not change the measurement or recognition of those plans required by previous Financial Accounting Board Standards. Following the adoption of FAS No. 132R, the Group included the required disclosures in its consolidated financial statements as of December 31, 2004 (Note 25).

Borrowing Costs

Borrowing costs were recognized as an expense in the period in which they were incurred. Borrowing costs for assets that require a period of time to get them ready for their intended use are capitalized and amortized over the related assets' estimated useful lives. The capitalized borrowing costs for the years ended December 31, 2004 and 2003 amounted to $34.0 million and $1.2 million, respectively.

Advertising Costs

Advertising costs are expensed as incurred. Advertising costs for the years ended December 31, 2004 and 2003 were $168.5 million and $120.0 million, respectively, and were reflected as a component of selling, general and administrative expenses in the accompanying consolidated statements of operations.

Earnings per Share

Basic earnings per share ("EPS") have been determined using the weighted average number of shares outstanding during the years ended December 31, 2004 and 2003. Diluted EPS reflect the potential dilution of MTS' stock options, granted to employees.

Distributions to Shareholders

Distributable retained earnings of the Group are based on amounts extracted from statutory accounts of individual entities and may significantly differ from amounts calculated on the basis of U.S. GAAP.

New Accounting Pronouncements

In November 2003, the Emerging Issues Task Force ("EITF") reached a final consensus on Issue No. 03-10, "Application of EITF Issue No. 02-16, 'Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor', by Resellers to Sales Incentives Offered to Consumers by Manufacturers." The consensus was reached that consideration received by a reseller from the vendor in exchange for vendor sales incentives tendered by consumers should not be reported as a reduction of the cost of the reseller's purchases from the vendor but instead should be shown as revenue. EITF Issue No. 03-10 is effective for reporting periods beginning after November 25, 2003. The adoption of Issue No. 03-10 did not have a material impact on the Group's results of operations or financial position.

In March 2004, the EITF reached a consensus on Issue No. 03-6, "Participating Securities and the Two-Class Method under FASB Statement No. 128, Earnings per Share". This Issue defines participating security and clarifies some practical issues related to including participating securities in the calculation of EPS. EITF Issue No. 03-6 is effective for reporting periods beginning after March 31, 2004. The adoption of Issue No. 03-6 did not have a material impact on the Group's financial position or results of operations.

In July 2004, the EITF issued EITF No. 02-14, "Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock." A consensus was reached regarding an investor that has the ability to exercise significant influence over the operating and financial policies of the investee. This type of investor should apply the equity method of accounting only when it has an investment(s) in common stock and/or an investment that is in-substance common stock. The Task Force also reached a consensus on the definition of in-substance common stock and related guidance. EITF No. 02-14 is effective for reporting periods beginning after September 15, 2004. The Group does not anticipate that the adoption of EITF Issue No. 02-14 will have a material impact on its financial position or results of operations.

In September 2004, the U.S. Securities and Exchange Commission ("SEC") staff issued the EITF Topic D-108, "Use of the Residual Method to Value Acquired Assets Other Than Goodwill", which requires the companies to use the direct value method to determine the fair value of their intangible assets acquired in business combinations completed after September 29, 2004. The SEC staff also announced that companies that currently apply the residual value approach for valuing intangible assets with indefinite useful lives for purposes of impairment testing, must use the direct value method by no later than the beginning of their first fiscal year after December 15, 2004.

As of December 31, 2004, the Group performed the annual impairment test to measure the fair value of its 900 and 1800 MHz licenses in its national footprint using the residual value approach. Under this new accounting guidance, the Group performed an impairment test to measure the fair value of its 900 and 1800 MHz licenses as of January 1, 2005 using the direct value method. Based on the assessment no impairment charge as of December 31, 2004 is required.

In September 2004, the EITF issued a final consensus on EITF Issue No. 04-1, "Accounting for Preexisting Relationships between the Parties to a Business Combination". In this issue the EITF reached a consensus that a business combination between two parties having a preexisting relationship is a multiple-element transaction with one element being the business combination and the other element being the settlement of the preexisting relationship. This Issue requires certain additional disclosures for business combinations between parties with a preexisting relationship. EITF Issue No. 04-1 is effective for reporting periods beginning after October 13, 2004. The Group does not anticipate that the adoption of EITF Issue No. 04-1 will have a material impact on its financial position or results of operations.

In October 2004, the EITF reached a consensus on EITF Issue No. 04-10, "Determining Whether to Aggregate Operating Segments that Do Not Meet the Quantitative Thresholds". EITF No. 04-10 provided additional guidance on when operating segments that are below the 10% threshold can be aggregated. EITF Issue No. 04-10 states that segments can only be aggregated if they have similar economic characteristics and if they are similar in areas such as production processes, types of customers, distribution channels and the products themselves are similar. The consensus reached by EITF No. 04-10 is effective for fiscal years ending after October 13, 2004. The adoption of Issue No. 04-10 did not have a material impact on the Group's results of operations or financial position.

In November 2004, the Financial Accounting Standards Board ("FASB") issued FAS No. 151, "Inventory Costs", an amendment of ARB No. 43, Chapter 4. FAS No. 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facility. FAS No. 151 is effective prospectively

for inventory costs incurred during fiscal years beginning after June 15, 2005. The Group does not anticipate the adoption of FAS No. 151 to have a material impact on its results of operations or financial position.

In December 2004, the FASB issued FAS No. 123R, "Share-Based Payment" ("FAS No. 123R"), a revision of FAS No. 123, "Accounting for Stock-Based Compensation". FAS No. 123R supersedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" and requires all entities to recognize compensation cost in an amount equal to the fair value of share-based payments granted to employees. That cost will be recognized over the period during which an employee is required to provide service in exchange for an award of equity instruments. FAS No. 123R is effective as of the beginning of the first fiscal year beginning after June 15, 2005, at which time companies can select whether they will apply the standard retroactively by restating their historical financial statements or prospectively for new stock-based compensation arrangements and the unvested portion of existing arrangements. The Group does not anticipate the adoption of FAS No. 123R will have a material impact on its financial position, cash flows and results of operations.

In December 2004, the FASB issued FAS No. 153, "Exchanges of Nonmonetary Assets", an amendment of APB Opinion No. 29, "Accounting for Nonmonetary Transactions". FAS No. 153 eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets set in the APB Opinion No. 29 and replaces it with a general exception for exchanges that do not have commercial substance. FAS No. 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. FAS No. 153 is effective prospectively for nonmonetary exchanges occurring after June 15, 2005. The Group does not anticipate the adoption of FAS No. 153 to have a material impact on its results of operations or financial position.

In March 2005, the FASB issued Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations - an interpretation of FASB Statement No. 143." This Interpretation clarifies that the term "conditional asset retirement obligation" as used in FASB Statement No. 143, "Accounting for Asset Retirement Obligations", refers to a legal obligation to perform an asset retirement activity, in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement. Uncertainty about the timing and (or) method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists to make a reasonable estimate of the fair value of the obligation. Interpretation No. 47 is effective for the Group beginning January 1, 2006. The Group is currently in the process of assessing the impact of Interpretation No. 47 on its consolidated financial position and result of operations.

In March 2005, the SEC released Staff Accounting Bulletin 107, “Share-Based Payments”, or SAB 107. The interpretations in SAB 107 express views of the SEC staff regarding the interaction between FAS No. 123R and certain SEC rules and regulations, and provide the SEC staff’s views regarding the valuation of share-based payment arrangements for public companies. In particular, SAB 107 provides guidance related to share-based payment transactions with nonemployees, the transition from nonpublic to public entity status, valuation methods (including assumptions such as expected volatility and expected term), the accounting for certain redeemable financial instruments issued under share-based payment arrangements, the classification of compensation expense, non-GAAP financial measures, first-time adoption of FAS No. 123R in an interim period, capitalization of compensation cost related to share-based payment arrangements, the accounting for income tax effects of share-based payment arrangements upon adoption of FAS No. 123R, the modification of employee share options prior to adoption of FAS No. 123R.

Reclassifications

Certain other reclassifications of prior years’ amounts have been made to conform to the presentation adopted for the year ended December 31, 2004.

3. ACQUISITIONS

Acquisition of MTS

In March 2003, the Group entered into a call option agreement to acquire 199,332,614 shares of MTS, representing 10% of its outstanding share capital. In connection with the call option, the Group also entered into an agreement with T-Mobile, a shareholder of MTS. Under the shareholders' agreement, T-Mobile undertakes to vote when necessary to ensure (in so far that it is able) that the Group will have a majority of the members of the MTS board of directors. However, certain actions will require T-Mobile's approval, including new issuances of MTS shares, actions which would dilute T-Mobile's shareholding in MTS and acquisitions by MTS with a value between 25% and 50% of the balance sheet value of MTS' total assets, in accordance with Russian accounting standards. Under the agreement, both the Group and T-Mobile have a right of first refusal with respect to sales of MTS shares by the other party to third parties, subject to certain exceptions. The Group and T-Mobile agreed to consult each other with respect to any dividend policy of MTS, with the expectation that annual distributions of not less than the equivalent of 25% of OJSC MTS' net profits (as determined under Russian accounting standards) will be made as dividends, including dividends with respect to MTS' fiscal year 2002.

In April 2003, the Group exercised its option with T-Mobile to purchase an additional 6% of the outstanding common stock of MTS and T-Mobile's 49% interest in Invest-Svyaz-Holding, a subsidiary of the Group holding 8% of the outstanding common stock of MTS, for $370.0 million in cash. Additionally $0.8 million was paid in legal fees. As a result of this transaction, the Group's share in MTS increased to 50.6%.

The acquisition was accounted for using the purchase method. Purchase price allocation was as follows:

		(000's)
Current assets	$	687,587
Non-current assets		1,983,412
License costs		497,738
Acquired customer base		113,979
Goodwill		67,615
Trademarks		41,780
Roaming contracts		35,220
Current liabilities		(588,374)
Non-current liabilities		(874,238)
Deferred taxes		(164,726)
Minority interest		(900,423)
Carrying value of the Group's investment in MTS as of the date of acquisition		(528,810)
Purchase price allocation	**$**	**370,760**

In accordance with FAS No. 141 "Business Combinations," the Group recognized $67.6 million of goodwill primarily relating to workforce-in-place and expectation of MTS, due to its established status on the telecommunications market, being able to prolong its operating licenses beyond their current terms for a consideration lower than their market value.

Acquisition of UMC

In March 2003, MTS acquired 58% of the outstanding voting interest of UMC, a provider of wireless telecommunication services in Ukraine, for the cash consideration of $199.0 million. In connection with the acquisition, MTS also assumed debt of UMC with face value of approximately $65.0 million, with the fair value of approximately $62.0 million. The purchase price allocation was as follows:

(000's)		
Current assets	$	82,293
Non-current assets		272,721
License costs		82,200
Acquired customer base		30,927
Current liabilities		(63,551)
Non-current liabilities		(78,580)
Deferred taxes		(27,425)
Minority interest		(99,581)
Purchase price allocation	**$**	**199,004**

MTS paid $171.5 million of the purchase price in cash and agreed to pay the balance of the purchase price of $27.5 million within one year. The amount payable accrued interest of 9% per annum and was paid in April 2004.

MTS also had an option agreement with Ukrtelecom to purchase its remaining 26% stake in UMC, exercisable from February 5, 2003 to November 5, 2005, with an exercise price of $87.6 million.

In June 2003, MTS exercised this call option. As a result of the transaction, the Group's voting power in UMC has increased from 58% to 84%. The allocation of purchase price increased recorded license cost by $10.2 million, increased customer base cost by $13.9 million, and decreased minority interest by $66.4 million.

In addition, MTS entered into a put and call option agreement for the purchase of remaining 16% stake in UMC. The exercise period of the call option was from May 5, 2003 to November 5, 2004, and the put option was exercisable from August 5, 2003 to November 5, 2004. The call option price was $85.0 million plus interest accrued from November 5, 2002 to the date of the exercise at 11% per annum; the price of the put option was calculated based on reported earnings of UMC prior to the exercise and was subject to a minimum amount of $55.0 million. In July 2003, the Group exercised its rights under the put and call option agreement for a cash consideration of approximately $91.7 million. The allocation of purchase price increased recorded license cost by $52.7 million, increased customer base cost by $8.7 million, and decreased minority interest by $43.8 million.

The UMC license costs are amortized over the remaining contractual terms of the licenses of approximately 9 to 13 years at the date of the acquisition, acquired customer base is amortized over the average remaining subscriber's life of approximately 32 months. Other acquired intangible assets, represented mostly by software, are amortized over their respective useful lives of 3 to 10 years. In accordance with SFAS No. 141 "Business Combinations", the Group recognized $8.0 million of goodwill relating to workforce-in-place.

UMC is one of the two leading operators in Ukraine, operating under nationwide GSM-900/1800 and NMT-450 licenses.

Acquisition of Minority Interest in Kuban-GSM

In September 2003, MTS acquired 100% of Kubtelesot for cash consideration of $107.0 million. Kubtelesot owned 47.3% of Kuban-GSM, and the Group's purchase of this stake increased its voting power in Kuban-GSM to 100%. The acquisition was accounted for using the purchase method of accounting. The allocation of purchase price increased recorded license cost by $57.5 million, increased customer base cost by $8.4 million, and decreased minority interest by $59.0 million.

License costs are amortized over the remaining contractual term of the license of approximately 5 years at the date of the acquisition. Acquired customer base is amortized over the average remaining subscribers' life of approximately 48 months.

Kuban-GSM operates in thirteen major cities throughout the south of the European part of RF, including Sochi, Krasnodar and Novorossiisk.

Acquisition of TAIF-Telcom

In April 2003, the Group acquired 51% of the common shares of TAIF-Telcom, a provider of mobile telecommunication services in the Republic of Tatarstan, RF and in the Volga region of Russia, for cash consideration of $51.0 million and 50% of the preferred shares of TAIF-Telcom for cash consideration of $10.0 million. In May 2003, the Group acquired an additional 2% of the common shares of TAIF-Telcom for cash consideration of $2.3 million. In connection with the acquisitions, the Group also assumed indebtedness of approximately $16.6 million that is collateralized by telecom equipment. As a result of these transactions, the Group acquired 53% voting interest in TAIF- Telcom.

The Group also entered into call and put option agreements with the existing shareholders of TAIF Telcom to acquire the remaining 47% of common shares and 50% of preferred shares of TAIF-Telcom. The exercise period for the call option on common shares was 48 months from the acquisition date and for the put option on common shares was 36 months following an 18 month period after the date of acquisition. The call and put option agreements for the common shares stipulated a minimum purchase price of $49.0 million plus 8% per annum commencing from the acquisition date. The exercise period for the call option on preferred shares was 48 months following a 24 month period after the date of acquisition and for the put option on preferred shares it was a 24 month period after the date of acquisition. The call and put option agreements for the preferred shares stipulated a minimum purchase price of $10.0 million plus 8% per annum commencing from the acquisition date.

The purchase price allocation was as follows:

		(000's)
Current assets	$	3,870
Non-current assets		48,391
License costs		68,407
Current liabilities		(26,099)
Non-current liabilities		(5,550)
Deferred taxes		(16,814)
Minority interest		(8,965)
Purchase price allocation	**$**	**63,240**

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 4 years and customer base is amortized over the average remaining subscribers' life of approximately 38 months.

In September 2004, MTS exercised its option to acquire the remaining 47.3% of common shares and 50% of preferred shares in TAIF Telcom for cash consideration of $63.0 million, increasing its ownership to 100.0%. The Group received title to the acquired shares in October 2004. The purchase price allocation increased recorded license cost by $35.8 million, increased acquired customer base by $4.2 million; goodwill was recorded in the amount of $21.2 million. Goodwill is mainly attributable to economic potential of the market.

Acquisition of Sibchalle

In August 2003, MTS completed the purchase of 100% of Sibchallenge, a cellular operator in the Krasnoyarsk region, for cash consideration of $45.5 million, paid a finder's fee of $2.0 million and assumed net debt of approximately $6.6 million. Sibchallenge provides mobile telecommunication services in the Krasnoyarsk region of Siberia, the Republic of Khakasiya, and in the Taimyr Autonomous region.

The purchase price allocation was as follows:

		(000's)
Current assets	$	4,078
Non-current assets		16,678
License costs		52,625
Current liabilities		(6,405)
Non-current liabilities		(6,628)
Deferred taxes		(12,894)
Purchase price allocation	**$**	**47,454**

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 8 years and customer base is amortized over the average remaining subscribers' life of approximately 36 months.

Acquisition of Tomsk Cellular Communications

In September 2003, MTS purchased 100% of Tomsk Cellular Communications ("TSS") for cash consideration of $47.0 million. TSS holds licenses to provide mobile telecommunication services in the Tomsk region.

The purchase price allocation was as follows:

		(000's)
Current assets	$	3,299
Non-current assets		11,412
License costs		49,282
Current liabilities		(4,543)
Non-current liabilities		(105)
Deferred taxes		(12,345)
Purchase price allocation	**$**	**47,000**

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 8 years and customer base is amortized over the average remaining subscribers' life of approximately 76 months.

Acquisition of Comstar and Kosmos-TV

In September and October 2002, the Group acquired senior discounted notes of Metromedia International Group, a U.S.-based company with interests in telecommunications and mass media businesses in RF, for $34.3 million. The par value of the notes acquired by the Group equaled $56.7 million. In April 2003, the Group disposed of the notes to a third party as an advance for acquisition of 50% of the voting shares of Comstar, an affiliate of the Group, and 50% of the voting shares and debt of $23.3 million (including accrued interest of $4.8 million) of Kosmos-TV, a provider of satellite television services, operating in Moscow.

In December 2003, the Group acquired 50% of voting shares of Comstar, 50% of voting shares of

Kosmos-TV and debt of $23.3 million in exchange for the notes with the fair value of $20.8 million, $7.2 million and $6.3 million, respectively. This transaction increased the Group's voting power in Comstar to 100% and resulted in obtaining control over Comstar operations by the Group.

The purchase price allocation was as follows:

		(000's)
Current assets	$	23,645
Non-current assets		53,165
Current liabilities		(16,983)
Non-current liabilities		(6,540)
Carrying value of the Group's investment in Comstar as of the date of acquisition		(32,495)
Purchase price allocation	**$**	**20,792**

Acquisition of Primtelefon

In August 2003, the Group reached an agreement to acquire, in a series of related transactions, equity interests in five Russian regional mobile phone operators from MCT Corporation for a total of $71.0 million. The Group agreed to purchase a 44% stake in Uraltel and 100% of Vostok Mobile BV, which holds a 50% stake in Primtelefon.

In August 2003, the Group completed the acquisition of Vostok Mobile BV and recorded a 50% stake investment in Primtelefon using the equity method of accounting.

In June 2004, MTS purchased 50.0% of Far Eastern mobile operator Primtelefon ("Primtelefon") for cash consideration of $31.0 million, increasing the Group's voting power in Primtelefon to 100%. Primtelefon holds licenses to provide GSM-900/1800 mobile cellular communications in the Far East region. Primtelefon's subscriber base as at the date of acquisition was approximately 216,000.

The acquisition was accounted for using the purchase method. The purchase price allocation was as follows:

		(000's)
Current assets	$	11,041
Non-current assets		16,809
License costs		21,891
Current liabilities		(7,488)
Non-current liabilities		(5,671)
Deferred taxes		(5,582)
Purchase price allocation	**$**	**31,000**

License costs acquired are amortized over the remaining contractual terms of the licenses of approximately 7 years and customer base is amortized over the average remaining subscribers' life of approximately 41 months.

Acquisition of Uzdunrobita

In July 2004, MTS entered into an agreement to acquire 74.0% of Uzbekistan mobile operator JV Uzdunrobita ("Uzdunrobita") for a cash consideration of $121.2 million, including transaction costs of $0.2 million. The acquisition was completed on August 1, 2004. Uzdunrobita holds licenses to provide GSM-1800 mobile communication services in the whole territory of Uzbekistan, which has a population of approximately 25.2 million. Uzdunrobita's subscriber base as of the date of acquisition was approximately 230,000 people.

MTS also entered into call and put option agreements with the existing shareholders of

Uzdunrobita to acquire the remaining 26.0% of common shares of the company. The exercise period for the call and put option is 48 months from the acquisition date. The call and put option agreements stipulate a minimum purchase price of $37.7 million plus 5% per annum commencing from the acquisition date. Fair value of the option was $3.6 million at December 31, 2004.

The acquisition was accounted for using the purchase method. The purchase price allocation for the acquisition was as follows:

		(000's)
Current assets	$	5,950
Non-current assets		67,293
License costs		40,861
Customer base		958
Trademark		3,622
Goodwill		41,290
Current liabilities		(14,705)
Non-current liabilities		(1,356)
Deferred taxes		(6,384)
Minority interest		(16,308)
Purchase price allocation	**$**	**121,221**

Goodwill is mainly attributable to economic potential of the market assuming low penetration level as of the date of acquisition. License costs are amortized over the remaining contractual terms of the licenses of approximately 12 years and customer base is amortized over the average remaining subscribers' life of approximately 39 months.

Acquisition of Kvazar-Micro Corporation B.V.

In July 2004, the Group purchased 51.0% of Kvazar-Micro Corporation B.V. for a cash consideration of $28.0 million, including a contribution to the share capital of Kvazar-Micro of $18.0 million. Kvazar-Micro business is based in Ukraine and includes distribution of computer hardware and software, IT and systems integration. Through acquisition of Kvazar-Micro, the Group added IT and systems integration business division to its Technology segment.

The acquisition was accounted for using the purchase method. The purchase price allocation was as follows:

		(000's)
Current assets	$	58,933
Non-current assets		3,083
Trademark		3,211
Customer base and distribution agreements		9,796
Current liabilities		(43,485)
Non-current liabilities		(3,538)
Purchase price allocation	**$**	**28,000**

Customer base and distribution agreements acquired are amortized over the remaining contractual terms of approximately 12 months. The purchase price allocation for Kvazar-Micro acquisition has not been yet finalized at the date of these statements.

Acquisition of Sibintertelecom

In November 2004, MTS acquired a 93.53% stake in Sibintertelecom, mobile phone operator in Chita region and Aginsk-Buryatsk District in the Far-East of Russia, for cash consideration of $37.4 million. Sibintertelecom holds license to provide 900 MHz services in Chita region and Aginsk-Buryatsk District in the Far-East of Russia. Sibintertelecom is the sole mobile service provider in two regions with a total population of 1.23 million. The company's customer base as at the date of acquisition was approximately 100,000 subscribers.

The acquisition was accounted for using the purchase method of accounting. The purchase price allocation was as follows:

		(000's)
TCurrent assets	$	5,939
Non-current assets		6,966
License costs		29,555
Customer base		1,488
Trademark		465
Goodwill		10,376
Current liabilities		(9,523)
Deferred taxes		(7,668)
Minority interest		(190)
Purchase price	**$**	**37,408**

Goodwill is mainly attributable to economic potential of the market assuming low regional penetration level as of the date of acquisition. License costs are amortized over the remaining contractual terms of the licenses of approximately 9 years for Chita region and one year for Aginsk-Buryatsk District and customer base is amortized over the average subscribers' life of approximately 44 months.

Acquisition of Telesot Alania

In December 2004, MTS purchased a 52.5% stake in Telesot Alania, a GSM mobile phone operator in the Republic of North Osetia in the Southern part of Russia, for cash consideration of $6.2 million. Telesot Alania holds license to provide 900/1800 MHz services in the Republic of North Osetia in the Southern part of Russia. Telesot Alania's customer base as at the date of acquisition was approximately 54,000 subscribers.

The acquisition was accounted for using the purchase method of accounting. The purchase price allocation was as follows:

		(000's)
Current assets	$	2,229
Non-current assets		5,085
License costs		3,606
Customer base		90
Current liabilities		(767)
Deferred taxes		(887)
Minority interest		(3,110)
Purchase price	**$**	**6,246**

CLicense costs are amortized over the remaining contractual terms of the licenses of approximately 2 years and customer base is amortized over the average subscriber's life of approximately 2 years.

Acquisition of Gorizont-RT

In December 2004, MTS completed transaction to acquire a 76.0% stake in Gorizont-RT, a GSM mobile phone operator in the Republic of Sakha (Yakutia) in the Far East of Russia, for cash consideration of $53.2 million. Gorizont-RT holds licenses to provide GSM-900/1800 services in the Republic of Sakha (Yakutia). The Gorizont-RT's customer base as at the date of acquisition was approximately 100,000 subscribers.

The acquisition was accounted for using the purchase method. The purchase price allocation was as follows:

		(000's)
Current assets	$	3,820
Non-current asset		17,501
License costs		26,362
Customer base cost		1,050
Trademark		153
Goodwill		20,214
Current liabilities		(4,949)
Non-current liabilities		(529)
Deferred taxes		(6,814)
Minority interest		(3,604)
Purchase price	**$**	**53,204**

Goodwill is mainly attributable to economic potential of the market assuming low regional penetration level as of the date of acquisition. License costs are amortized over the remaining contractual terms of the licenses of approximately 6 months and customer base is amortized over the average subscribers' life of approximately 60 months.

Other Acquisitions

In October 2003, the Group completed the purchase of Vostok Mobile South and thus acquired a 50% stake in Volgograd Mobile and Astrakhan Mobile and an 80% stake in Mar Mobile GSM. Also, in a separate transaction the Group completed the acquisition of the remaining 20% stake in Mar Mobile GSM from existing shareholders unrelated to MCT Corporation, thus consolidating a 100% ownership in the company.

During the year ended December 31, 2003, the Group increased its ownership interests in MBRD from 52% to 59%, in DM-Center from 53% to 100% and in Bolshaya Ordynka from 0% to 70% by acquiring their shares from related parties for an aggregate cash consideration of less than $0.1 million.

The aggregate effect of such transactions on the Group's equity amounted to a net decrease of $2.7 million, which was charged to additional paid-in capital.

In March 2004, the Group acquired 11% stake in SCS-900 for cash consideration of $8.5 million, increasing the Group's voting power in SCS-900 to 99.5%. The acquisition was accounted for using the purchase method of accounting. The allocation of purchase price increased recorded license cost by $2.6 million. In April 2004, the Group acquired 40% stake in FECS-900 for cash consideration of $8.3 million, increasing the Group's voting power in FECS-900 to 100%. The acquisition was accounted for using the purchase method of accounting. The allocation of purchase price increased recorded license cost by $4.1 million. License costs are amortized over the remaining contractual terms of the respective license, ranging from 6 to 10 years at the date of the first acquisition.

In April 2004, the Group acquired additional 7.5% stake in MSS, a mobile operator in the Omsk region, for $2.2 million in cash. This acquisition increased the Group's voting power in MSS to 91%. The acquisition was accounted for using the purchase method of accounting. The allocation of purchase price increased recorded license cost by $1.1 million.

In April and May of 2004, the Group acquired the remaining stakes in the following subsidiaries:

- 35% of MTS-NN (a service provider in Nizhny Novgorod) for $0.5 million, and
- 49% of Novitel (handsets dealer in Moscow) for $1.3 million.

Both acquisitions increased the Group's voting power in the respective companies to 100%. The acquisitions were accounted for using the purchase method of accounting. The allocation of purchase price increased recorded goodwill by $1.8 million.

In August 2004, the Group acquired the remaining stakes in Astrakhan Mobile and Volgograd Mobile, increasing the Group's voting power in these subsidiaries to 100%. The acquisition price was $1.1 million and $2.9 million, respectively. Astrakhan Mobile holds a AMPS/DAMPS-800 and GSM-1800 licenses covering Astrakhan region (population of approximately 1.0 million) and Volgograd Mobile holds a AMPS/DAMPS-800 and GSM-1800 licenses covering Volgograd region (population of approximately 2.7 million). As of July 31, 2004, the two companies provided AMPS/DAMPS services to around 10 thousand subscribers. As the result of the allocation of purchase price for the first and second stakes in both companies, the Group recorded license cost of $16.5 million.

In August 2004, the Group acquired the remaining 49% stake in UDN-900 for $6.4 million in cash. This acquisition increased the Group's voting power in UDN-900 to 100%. The allocation of purchase price increased recorded license cost by $0.3 million. UDN-900 provides GSM-900 services under the MTS brand in Udmurtia Republic (population of 1.6 million). UDN's subscriber base as of July 31, 2004 was 219,760.

In September 2004, the Group acquired 29.8% stake in Mezhregionalny Transit Telecom ("MTT"), operator of a nation-wide transit network providing telecommunications services and network interconnection for mobile and fixed network operators throughout Russia, for cash consideration of $39.8 million, increasing its ownership interest in MTT to 44.8%. In October 2004, the Group purchased an additional 0.2% stake in MTT for cash consideration of $0.1 million. As a result, by December 31, 2004, the Group's ownership interest in MTT increased to 45.0%.

During the year ended December 31, 2004, Rosno repurchased 3.4% of its outstanding shares from a director of the Group for cash consideration of $5.6 million. The transaction resulted in a reduction of additional paid-in capital of the Group by $1.3 million, net of minority interest of $2.6 million. Later in the same period the Group acquired from Rosno 1.75% of its shares for $2.8 million in cash. The remaining treasury shares were sold by Rosno to an affiliate of Allianz AG. In December 2004, Rosno issued 10.9 million new shares, 5.6 million of which were purchased by the Group for a cash payment of $9.8 million. The rest of the newly issued shares were sold to Allianz AG. As a consequence of these transactions, the Group's ownership interest in Rosno reached 49.0%.

In October 2004, Rosno acquired from RAO UES 100% stake in Leader. The value of consideration equaled $3.0 million. Leader is an insurance company, selling primarily property insurance to energy companies. During 2002-2004, the Group assumed reinsurance from Leader and performed operational management of this company.

In October 2004, Rosno acquired 100% stake in Deutsche Investment Trust for cash consideration of $2.4 million. The allocation of purchase price increased goodwill by $1.3 million.

During the first nine months 2004, the Group acquired 5% share in East-West United Bank for cash consideration of $1.7 million. In November 2004, the Group acquired from Vneshtorgbank 14% stake in East West United Bank, increasing its ownership to 49%. The value of consideration equaled $5.3 million. East West United Bank is a bank incorporated in Luxembourg.

Pro forma results of operations (unaudited)

The following unaudited pro forma financial data for the years ended December 31, 2004 and 2003 give effect to the acquisitions of Primtelefon, SCS-900, FECS-900, Kvazar-Micro, Uzdunrobita, Sibintertelecom, Telesot Alania, Gorizont-RT and acquisitions made during the year ended December 31, 2003, including MTS, UMC, Kuban-GSM, TAIF Telcom, Sibchallenge, TSS and Comstar, as if they had occurred as of January 1, 2003:

		2004		2003
Net revenues	$	5,711,286	$	4,085,607
Income from continuing operations before cumulative effect of a change in accounting principle		453,025		215,905
Net income		417,553		372,282
Earnings per share, basic and diluted:	$	**51.5**	$	**46.0**

The pro forma information is based on various assumptions and estimates. The pro forma information is not necessarily indicative of the operating results that would have occurred if the Group's acquisitions had been consummated at the beginning of the respective period, nor is it necessarily indicative of future operating results. The pro forma information does not give effect to any potential revenue enhancements or cost synergies or other operating efficiencies that could result from the acquisitions.

4. DISPOSITIONS AND CAPITAL TRANSACTIONS OF SUBSIDIARIES

In July 2004, the Group sold 33.0% of common shares of its subsidiary STROM telecom to a third party for a cash consideration of $2.0 million. The transaction resulted in recognition of loss from disposal of $1.2 million.

In August 2004, the Group sold 83.5% of common shares of its subsidiary P-Com to Sky Link, the Group's affiliate, for promissory notes of $16.0 million. The transaction resulted in recognition of loss from disposal of $1.9 million. Revenues of P-Com were excluded from the Group's consolidated revenues effective January 1, 2004, and the Group's share in P-Com's earnings for the year ended December 31, 2004 was recorded using the equity method of accounting.

In October 2004, the Group disposed of its 24% shareholding in MCC to Sky Link, the Group's affiliate, for cash consideration of $0.7 million.

In August 2004, the Group sold its interest in Sofora, a subsidiary operating in media business, to a third party for cash consideration of $1.1 million. The transaction resulted in recognition of gain from disposal of $1.3 million. Sofora's assets and operations were not material for the Group.

During the year ended December 31, 2004, the Group sold its interests in Petrovskoye Podvorye and Ordynka to related parties. These transactions resulted in an increase of additional paid-in capital by approximately $10.3 million, net of minority interests of $2.6 million.

5. CASH AND CASH EQUIVALENTS

Cash equivalents amounting to $113.6 million and $56.1 million as of December 31, 2004 and 2003, respectively, are comprised primarily of term deposits with banks and bank promissory notes with original maturities less than 90 days. Within this amount, $3.8 million and $44.3 million, respectively, represent the Group's deposits with East-West United Bank, an affiliate of the Group. As of December 31, 2004, the Group had $5.6 million in current accounts with East-West United Bank.

Also included in cash as of December 31, 2004 and 2003 are $10.9 million and $45.7 million, respectively, which represent the MBRD's minimum reserve deposit, required by the Central Bank of Russian Federation.

6. SHORT-TERM INVESTMENTS

Short-term investments as of December 31, 2004 and 2003 consisted of the following:

	(000's)			
		2004		2003
Trading securities:				
RF Eurobonds		-	$	54,394
Corporate bonds	$	36,669		19,696
Municipal bonds		12,622		4,012
Corporate shares		11,541		2,250
Other trading securities		9,141		10,998
		69,973		91,350
Other short-term investments:				
Credit linked notes		-		38,170
Promissory notes and deposit certificates from third parties		35,546		95,881
Promissory notes from related parties		13,028		20,946
Bank deposits with original maturities exceeding 90 days		80,743		24,040
Other short-term investments		8,003		8,463
		137,320		187,500
Total	**$**	**207,293**	**$**	**278,850**

Corporate bonds denominated in RUR represent bonds issued by major Russian companies with maturity dates from 2004 to 2009 and coupon rates of 7-20% per annum.

Corporate shares are liquid publicly traded shares of Russian companies. They are reflected at period-end market value based on last traded prices obtained from Moscow Interbank Currency Exchange ("MICEX").

The weighted average interest rate on promissory notes from third parties as of December 31, 2004 and 2003, was 8% and 8%, respectively, while promissory notes from related parties are mostly interest-free. Deposit certificates bear an interest rate of 5% as compared to 7% in 2003. Most of the notes and certificates mature within 1 year from the latest balance sheet date.

The effective interest rates on bank deposits with original maturities exceeding 90 days as of December 31, 2004 were 4% for RUR-denominated deposits and 7% on deposits in USD. Included in bank deposits as of December 31, 2004, are deposits with East-West United Bank of $53.0 million bearing interest of 2%.

7. LOANS TO CUSTOMERS AND BANKS, NET

Loans to customers and banks, net of an allowance for loan losses, as of December 31, 2004 and 2003 consisted of the following:

		(000's)		
		2004		2003
Loans to customers	$	227,668	$	231,918
Loans to banks		173,179		147,518
		400,847		379,436
Less allowance for loan losses		(21,537)		(14,454)
Tota	**$**	**379,310**	**$**	**364,982**

8. INSURANCE-RELATED RECEIVABLES

Insurance-related receivables as of December 31, 2004 and 2003 consisted of the following:

		(000's)		
		2004		2003
Receivables from insurance operations	$	104,834	$	71,066
Advances to health care providers		25,444		25,243
Total	**$**	**130,278**	**$**	**96,309**

9. ACCOUNTS RECEIVABLE, NET

Accounts receivable, net of provision for doubtful accounts, as of December 31, 2004 and 2003 consisted of the following:

Included in trade receivables as of December 31, 2004 and 2003 are receivables for services provided and goods shipped to the Group's affiliates and other related parties in the amounts of $42.2 million and $4.3 million, respectively. Management anticipates no losses in respect of receivables from related parties.

		(000's)		
		2004		2003
Trade receivables	$	370,988	$	211,333
Less: provision for doubtful accounts		(43,067)		(29,082)
Total	**$**	**327,921**	**$**	**182,251**

10. OTHER RECEIVABLES AND PREPAID EXPENSES, NET

Other receivables and prepaid expenses, net of provision for doubtful accounts, as of December 31, 2004 and 2003 consisted of the following:

		(000's)		
		2004		2003
Recoverable VAT	$	345,999	$	278,441
Receivables for sale of oil assets		-		153,500
Advances to suppliers		111,505		58,266
Prepaid expenses		22,582		15,897
Deferred policy acquisition costs		26,203		9,410
Other taxes prepaid		22,746		11,728
Receivables for sale of Micron shares		5,052		4,759
Receivables for sale of STROM telecom shares		1,606		-
Other		51,445		39,406
Less: provision for doubtful accounts		(4,064)		(4,282)
Total	**$**	**583,074**	**$**	**567,125**

Policy acquisition costs' amortization charge for the years ended December 31, 2004 and 2003 was $42.7 million and $22.5 million, respectively.

11. INVENTORIES

Inventories as of December 31, 2004 and 2003 consisted of the following:

		2004		2003
Raw materials and spare parts	$	97,427	$	51,216
Work-in-progress		34,888		15,643
Finished goods and goods for resale		89,123		62,693
Project costs - construction, net of progress billings		55,394		36,651
Total	**$**	**276,832**	**$**	**166,203**

12. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment, net of accumulated depreciation, as of December 31, 2004 and 2003 consisted of the following:

		2004		2003
Land	$	37,944	$	3,894
Buildings and leasehold improvements		547,629		439,838
Switches, transmission devices, network and base station equipment		3,284,977		2,223,603
Other plant, machinery and equipment		431,030		412,519
Construction in-progress and equipment for installation		1,080,900		764,178
		5,382,480		3,844,032
Less: accumulated depreciation		(947,265)		(475,911)
Total	**$**	**4,435,215**	**$**	**3,368,121**

Depreciation expense for the years ended December 31, 2004 and 2003 amounted to $509.5 million and $335.3 million, respectively.

13. LONG-TERM INVESTMENTS

Long-term investments as of December 31, 2004 and 2003 consisted of the following:

		2004		2003
Loans, promissory notes and deposits with related parties	$	20,309	$	14,279
Loans, promissory notes and deposits with third parties		8,513		6,836
Mutual investment funds		9,942		9,616
Other		7,147		10,662
Total	$	**45,911**	$	**41,393**

Loans and promissory notes from related parties are mostly RUR denominated and interest-free. Majority of such loans and promissory notes mature in 2006.

14. INVESTMENTS IN AFFILIATED COMPANIES

Investments in affiliated companies as of December 31, 2004 and 2003 consisted of the following:

		2004			2003		
		Voting power, %		Carrying value	Voting power, %		Carrying value
Primtelefon	Consolidated				50%	$	31,174
Astrakhan Mobile and Volgograd Mobile	Consolidated				50%		5,806
Mosdachtrest	Consolidated				44%		4,024
MTT (Note 3)		45%	$	49,205	15%		30
MTS Belarus		49%		27,699	49%		5,884
Sky Link (Note 4)		50%		16,011	50%		-
East-West United Bank		49%		16,518	30%		8,382
ZETA Telecom		49%		6,699	49%		7,390
Cosmos TV		50%		4,100	50%		7,239
MCC (Note 4)		-		-	24%		4,862
Loans to MTS Belarus		-		51,894	-		51,481
Loans to Sky Link		-		19,316	-		-
Acquired debt of Cosmos TV		-		1,000	-		6,333
Loans to Astrakhan Mobile and Volgograd Mobile		-		-	-		6,850
Other investments and loans to investees		Various		14,078	Various		11,481
Total			$	**206,520**		$	**150,936**

Investments in affiliates include $51.9 million in loans to MTS Belarus bearing interest at 3% to 11% per annum. Based on projected cash flows of MTS Belarus, the Group has concluded that no impairment of the Group's investments in MTS Belarus is required as of December 31, 2004.

15. LICENSES, NET

Licenses, net of accumulated amortization, as of December 31, 2004 and 2003 consisted of the following:

		(000's)		
		2004		2003
Operating licenses	$	1,007,369	$	773,073
Less: accumulated amortization		(256,436)		(103,085)
Total	**$**	**750,933**	**$**	**669,988**

Amortization expense for licenses for the years ended December 31, 2004 and 2003 amounted to $160.5 million and $103.1 million, respectively. The estimated amortization expense for each of the five succeeding years and thereafter is as follows:

		(000's)
2005	$	187,733
2006		140,799
2007		105,601
2008		79,200
2009		59,398
Following periods		178,202
Total	**$**	**750,933**

Actual amortization expense to be reported in future periods could differ from these estimates as a result of new licenses acquisitions, changes in useful lives and other relevant factors.

16. OTHER INTANGIBLE ASSETS, NET

Intangible assets, other than goodwill and licenses, net of accumulated amortization, as of December 31, 2004 and 2003 consisted of the following:

		2004						2003				
		Gross carrying value		Accumulated amortization		Net carrying value		Gross carrying value		Accumulated amortization		Net carrying value
Amortized intangible assets:												
Acquired customer base	$	152,060	$	(78,491)	$	73,569	$	137,747	$	(28,877)	$	108,870
Numbering capacity with finite contractual life, rights to use premises, software and other		474,377		(148,398)		325,979		319,498		(53,007)		266,491
		626,437		(226,889)		399,548		457,245		(81,884)		375,361
Unamortized intangible assets:												
Numbering capacity with indefinite contractual life		22,237		-		22,237		28,855		-		28,855
Trademarks		45,375		-		45,375		42,165		-		42,165
Total intangible assets	$	694,049	$	(226,889)	$	467,160	$	528,265	$	(81,884)	$	446,381

Amortization expense recorded on other intangible assets for the years ended December 31, 2004 and 2003 amounted to $129.9 million and $82.6 million, respectively. The estimated amortization expense for each of the five succeeding years and thereafter is as follows:

		(000's)
2005	$	161,795
2006		104,099
2007		59,642
2008		42,942
2009		8,142
Following periods		22,928
Total	**$**	**399,548**

Actual amortization expense to be reported in future periods could differ from these estimates as a result of new intangible assets acquisitions, changes in useful lives and other relevant factors.

17. BANK DEPOSITS AND NOTES ISSUED

Bank deposits and notes issued as of December 31, 2004 and 2003 consisted of the following:

	(000's)			
		2004		2003
Deposits repayable on demand	$	133,008	$	57,981
Term deposits		132,694		67,446
Promissory notes issued		61,159		48,321
Total	**$**	**326,861**	**$**	**173,748**

Bank deposits and notes issued as of December 31, 2004 and 2003 include deposits from and promissory notes issued to related parties for $8.4 million and $30.2 million, respectively.

18. INSURANCE-RELATED LIABILITIES

Insurance-related liabilities as of December 31, 2004 and 2003 consisted of the following:

	(000's)			
		2004		2003
Unearned premium provision, net of reinsurance	$	164,589	$	88,244
Loss provision, net of reinsurance		76,641		50,070
Undisbursed MGFOMS funds		45,719		38,140
Other insurance-related liabilities		57,511		30,986
Total	**$**	**344,460**	**$**	**207,440**

Usage of MGFOMS funds, in the amount of $45.7 million, accumulated and undisbursed by Rosno as of December 31, 2004, is limited to payments for medical facilities and care provided to RF citizens by medical centers under MGFOMS's obligatory medical insurance program.

19. ACCRUED EXPENSES, SUBSCRIBER PREPAYMENTS AND OTHER CURRENT LIABILITIES

Accrued expenses, subscriber prepayments and other current liabilities as of December 31, 2004 and 2003 consisted of the following:

		(000's)		
		2004		2003
Subscriber prepayments, current portion (Note 23)	$	391,880	$	255,988
Payables for purchase of oil assets		-		96,530
Payroll and other accrued expenses		112,878		39,836
Accrued interest on loans		63,809		50,726
Customers' advances		59,146		38,586
Payables for purchase of UMC shares		-		27,500
Current portion of capital lease obligations (Note 21)		4,926		11,387
Dividends payable		6,237		10,841
Tax and legal contingencies		23,633		27,179
Other		74,885		48,510
Total	**$**	**737,394**	**$**	**607,083**

Short-term notes payable as of December 31, 2004 and 2003 consisted of the following:

20. SHORT-TERM NOTES PAYABLE

Short-term notes payable as of December 31, 2004 and 2003 consisted of the following:

	Currency	Annual interest rate (Actual at December 31, 2004)		(000's)		
				2004		2003
Credit Suisse First Boston	USD	LIBOR+2.2% (4.8%)	$	140,000		35,000
Commerzbank Eurasia	USD	LIBOR+5.0% (7.4%)		20,000	$	10,000
Sberbank	RUR	10.0%-15.0%		10,248		3,828
Vneshtorgbank	EUR	11%		7,501		-
West LB	USD	LIBOR+6.8% (9.4%)		5,000		-
Credit Linked Notes	USD	-		-		100,000
Trust Bank	USD	-		-		25,000
Deutsche Bank	USD	-		-		15,280
AVAL Bank	UAH	-		-		10,890
Loans and promissory notes payable to related parties	Various	Various		21,422		134,574
Other	Various	Various		16,932		14,511
Total			$	**221,103**	$	**349,083**

Credit Suisse First Boston - In October 2004, MTS entered into a short-term loan facility with Credit Suisse First Boston for a total amount of $140.0 million. Amounts outstanding under the loan agreement bear interest of LIBOR+2.2% (4.8% as of December 31, 2004). The short-term loan facility matures in April of 2005. As of December 31, 2004, the balance outstanding under the loan was $140.0 million. The loan is subject to certain restrictive covenants including, but not limited to, certain financial ratios. As of December 31, 2004, the MTS is in compliance with all existing covenants.

Commerzbank Eurasia - In November 2003, Sistema-Hals entered into a loan agreement with Commerzbank Eurasia for the amount of $20.0 million. The loan bears interest at LIBOR+5% (7.4% as of December 31, 2004) and is due in March 2005. The loan is guaranteed by JSFC Sistema.

Sberbank - The Group has entered into several short-term loans with Sberbank. The outstanding balance under the loans as of December 31, 2004 was $10.2 million. The loans bear interest of 10%-15%. The Sberbank loans are secured by pledge of PP&E with the carrying value of approximately $8.2 million as of December 31, 2004.

Vneshtorgbank - In December 2004, Kamov-Holding entered into a loan agreement with

Vneshtorgbank for the amount of EUR 5.5 million. The loan bears interest at 11% and is due in June 2005.

West LB - In December 2004, Sistema-Hals entered into a loan agreement with West LB for the amount of $5.0 million. The loan bears interest of LIBOR + 6.8% per annum (approx. 9.4% as of December 31, 2004) and matures in 2005.

21. CAPITAL LEASE OBLIGATIONS

Capital lease obligations as of December 31, 2004 and 2003 consisted of the following:

		(000's)		
		2004		2003
Capital lease obligations	$	8,338	$	16,330
Less: current portion of capital lease obligations (Note 19)		(4,926)		(11,387)
Total	**$**	**3,412**	**$**	**4,943**

During 2001-2004, the Group entered into several lease agreements for telecommunications equipment and vehicles. Most of the agreements expire in 2005-2006 and assume transfer of ownership for leased assets to the Group at the end of the lease term.

The net book value of leased assets comprised $20.3 million and $23.2 million as of December 31, 2004 and 2003, respectively. Interest expense, recorded within income from continuing operations, was $1.9 million and $4.2 million for the years ended December 31, 2004 and 2003, respectively. Future minimum payments under the lease agreements are disclosed in Note 30.

22. LONG-TERM DEBT

Long-term debt as of December 31, 2004 and 2003 consisted of the following:

	Currency	Annual interest rate (Actual at December 31, 2004)		(000's)		
				2004		2003
Sistema Finance Notes	USD	10.3%	$	348,808	$	348,561
Sistema Capital Notes	USD	8.9%		350,000		-
MTS Finance Notes due 2010	USD	8.4%		400,000		400,000
MTS Finance Notes due 2008	USD	9.8%		400,000		400,000
MGTS Bonds	RUR	10%-12.3%		90,094		52,643
MTS Finance Notes due 2004	USD	-		-		299,640
Floating Rate Notes due 2004	USD	-		-		298,196
Sistema Finance Investments Bonds	RUR	-		-		40,747
Micron Bonds	RUR	15.0%		6,293		7,541
TAIF Telcom Bonds	RUR	-		-		4,074
Total Corporate Bonds				**1,595,195**		**1,851,402**
Syndicated Loan	USD	LIBOR+2.5% (5.3%)		600,000		-
EBRD	USD	LIBOR+3.1% (5.9%)		150,000		-
HSBC Bank plc and ING-BHF-Bank	USD	LIBOR+0.4% (3.2%)		77,003		-
Hermes Credit Facility	EUR	EURIBOR+0.7% (2.9%)		63,851		55,550
ING-Bank (Eurasia)	USD	LIBOR+2.3%-4.2% (4.8%-6.7%)		46,667		60,000
Vendor Financing	Various	Various		33,181		25,033
Commerzbank (Eurasia)	USD	LIBOR+1.4%-3.5% (4.0%-6.1%)		27,213		19,958
Raiffeisenbank	USD	LIBOR+5.0%-7.0% (7.6%-9.6%)		19,684		33,036
HSBC	USD	LIBOR+2.8% (5.2%)		17,500		25,000
Ericsson Project Finance	USD	LIBOR+4.0% (6.6%)		14,850		23,400
Sberbank	RUR	11.0%-20.3%		17,299		34,732
Vneshtorgbank	USD, EUR	LIBOR+4.9% (7.3%), EURIBOR+5.6% (7.8%), 13%		16,981		17,297
Citibank	USD	LIBOR+1.6% (4.2%)		15,144		18,616
Nordea Bank Sweden	USD	LIBOR+0.4% (3.0%)		6,500		-
WestLB	EUR	EURIBOR+2% (4.2%)		4,000		-
Dresdner Bank	USD	-		-		15,400

	Currency	Annual interest rate (Actual at December 31, 2004)		(000's)		
				2004		2003
Deutsche Telecom	USD	-		-		57,981
International Moscow Bank	RUR	-		-		10,864
TDC Mobile International	USD	-		-		6,838
Loans from related parties	Various	Various		86,432		31,898
Other	Various	Various		43,960		33,022
				2,835,460		2,320,027
Less amounts maturing within one year				(340,938)		(844,106)
Total			$	**2,494,522**	$	**1,475,921**

Corporate Bonds

In January 2004, Sistema Capital, a wholly-owned subsidiary of the Group domiciled in Luxembourg, issued $350.0 million of 8.875% notes, due in January 2011. The notes are fully and unconditionally guaranteed by JSFC Sistema. Interest payments on the notes are due semi-annually in January and July of each year, commencing July 2004. On or prior to January 2007, the Group may redeem up to 35% of the notes with the net proceeds of offerings of JSFC Sistema's common equity at 108.9% of the principal amount. The notes are listed on the London Stock Exchange. In January 2007, the holders of the notes may require Sistema Capital to redeem their notes at 100% of the principal amount thereof, together with accrued interest. In addition, these notes provide the holders with a right to require Sistema Capital to redeem all of the notes outstanding at 101% of the principal amount of the notes plus accrued interest upon any change in control.

In April 2003, Sistema Finance, a wholly-owned subsidiary of the Group, issued $350.0 million 10.25% notes, due in April 2008, at 99.52% of par. These notes are secured by 193,473,900 shares of common stock of MTS. The notes are listed on the Luxembourg Stock Exchange. JSFC Sistema is a guarantor of the notes. Interest on the notes is payable semi-annually in arrears. On or prior to April 14, 2006, the Group may redeem up to 35% of the notes with the net proceeds of offerings of JSFC Sistema's common equity at 110.25% of par. These notes are subject to certain restrictive covenants including, but not limited to, limitations on the incurrence of additional indebtedness, restrictions on mergers or consolidations, limitations on liens and dispositions of assets and limitations on transactions with affiliates. In addition, these notes provide the holders with a right to require Sistema Finance to redeem all of the notes outstanding at 101% of the principal amount of the notes plus accrued interest upon any change in control.

In October 2003, MTS Finance ("MTS Finance"), a wholly-owned subsidiary of the Group, issued

$400.0 million notes bearing interest at 8.375% at par. The cash proceeds, net of issuance costs of approximately $4.6 million, amounted to $395.4 million. These notes are fully and unconditionally guaranteed by MTS and will mature in October 2010. MTS Finance is required to make interest payments on the notes semi-annually in arrears in April and October of each year, commencing April 2004. The notes are listed on the Luxembourg Stock Exchange.

In January 2003, MTS Finance issued $400.0 million 9.75% notes at par. These notes are fully and unconditionally guaranteed by MTS and mature in January 2008. MTS Finance is required to make interest payments on the notes semi-annually in arrears in January and July, commencing July 2003. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes were $400.0 million and related debt issuance costs of $3.9 million were capitalized.

In August 2003, MTS Finance issued $300.0 million notes bearing interest at a rate of 3 months LIBOR+4% at the price of 99%. These notes were fully and unconditionally guaranteed by MTS and matured in August 2004. MTS Finance was required to make interest payments on the notes quarterly, commencing November 2003. The notes were listed on the Luxembourg Stock Exchange. Proceeds received from the notes, net of underwriting discount, were $297.0 million and related debt issuance costs of $1.8 million were capitalized. In May 2004, the Group redeemed all outstanding floating rate notes, mentioned above, in the principal amount plus accrued interest thereon to the date of redemption.

In December 2001, MTS Finance issued $250.0 million 10.95% (effective interest rate of 11.25%) notes at the price of 99.254%. Proceeds received from the notes, net of underwriting discount, were $248.1 million. Related debt issuance costs in the amount of $3.9 million were capitalized. In March 2002, MTS Finance issued additional $50.0 million 10.95% (effective interest rate of 10.25%) notes at a price of 101.616%. Proceeds received from these notes, including the offering premium, were $50.8 million. Related debt issuance costs in the amount of $0.6 million were capitalized. All the notes were fully and unconditionally guaranteed by MTS and were fully repaid in December 2004.

Subject to certain exceptions and qualifications, the indentures governing the MTS' notes contain covenants limiting MTS' ability to incur debt; create liens; lease properties sold or transferred by MTS; enter into loan transactions with affiliates; merge or consolidate with another person or convey its properties and assets to another person; and sell or transfer any of its GSM licenses for Moscow, St. Petersburg, Krasnodar and Ukraine license areas.

In addition, if MTS experiences certain types of mergers, consolidations or other changes in control, noteholders will have the right to require MTS to redeem the notes at 101% of their principal amount, plus accrued interest. MTS is also required to take all commercially reasonable steps necessary to maintain a rating of the notes from Moody's or Standard & Poor's. The notes also have cross default provisions with publicly traded debt issued by the JSFC Sistema. If MTS fails to meet these covenants, after certain notice and cure periods, the noteholders can accelerate debt to be immediately due and payable. The Group believes that MTS is in compliance with all restrictive provisions as of December 31, 2004.

In November 2002, Sistema Finance Investments, a wholly-owned subsidiary of the Group, issued RUR denominated bonds with face value of 1,200.0 million RUR (equivalent of $43.2 million as of December 31, 2004). The bonds were traded on MICEX and carried a coupon rate of 17.75% during the first year of trading and of 15% during the second year. The notes were fully repaid in November 2004.

In July 2004, Sistema Finance Investments issued RUR denominated bonds with face value of 2,000.0 million RUR (equivalent of $72.1 million as of December 31, 2004). The bonds carried a coupon rate of 11%. As of December 31, 2004, the Group had repurchased 100% of the second issue of Sistema Finance Investments bonds.

In February 2003, MGTS issued 2-year RUR denominated bonds in the amount of 1,000 million RUR (equivalent of $36.0 million as of December 31, 2004). The bonds carry coupon of 12.3% during the first year of trading and 17.0% during the second year. In February 2005, MGTS fully repaid the bonds.

In April 2004, MGTS issued 5-year RUR-denominated bonds in the amount of RUR 1,500 million (equivalent of $54.1 million as of December 31, 2004). The bonds carry a coupon of 10% per annum. MGTS made an unconditional offer to repurchase the bonds at par value in April 2006.

In July 2003, Micron issued RUR denominated bonds with face value of RUR 300.0 million (equivalent of $10.8 million as of December 31, 2004) due in January 2005. Interest is payable semi annually. The interest rate was set at 15% per annum, and two-thirds of the interest payments were covered by the municipal government. The Group fully repaid the bonds in January 2005.

Syndicated Loan

In July 2004, MTS entered into a $500.0 million syndicated loan agreement with international financial institutions: ING Bank N.V., ABN AMRO Bank N.V., HSBC Bank PLC, Raiffeisen Zentralbank Oesterreich AG, Bank Austria Creditanstalt AG, Commerzbank AG and others. The credit facility bears interest LIBOR+2.5% per annum (5.3% as of December 31, 2004) and matures in 3 years. The proceeds were used by MTS for corporate purposes, including refinancing of its existing indebtedness. In September 2004, MTS extended total amount available under the syndicated loan facility for an additional $100.0 million to total amount of $600.0 million. Commitment fee for the syndicated loan facility amounted to $0.5 million. Debt issuance costs of $10.2 million related to the syndicated loan facility have been capitalized. As of December 31, 2004, $600.0 million was outstanding under this credit facility. The loan facility is subject to certain restrictive covenants including, but not limited to, certain financial ratios of MTS. As of December 31, 2004, MTS is in compliance with all existing covenants.

EBRD

In December 2004, MTS entered into a credit line with the European Bank for Reconstruction and Development ("EBRD") limited to $150.0 million. The facility bears interest at LIBOR+3.1% (5.9% as of December 31, 2004). Commitment fee of 0.5% per annum should be paid in accordance with the credit agreement. The final maturity of this agreement is in December 2011. As of December 31, 2004, the balance outstanding under the loan was $150.0 million. The loan is subject to restrictive covenants including, but not limited to, certain financial ratios of MTS. As of December 31, 2004, the MTS is in compliance with all existing covenants.

HSBC Bank and ING BHF Bank

In October 2004, MTS entered into two credit facility agreements with HSBC Bank and ING BHF Bank for the total amount of $122.3 million. The funds were used to purchase telecommunication equipment and software from Siemens AG and Alcatel SEL AG for the technical upgrade and expansion of network. Euler Hermes Kreditversicherung AG, the German credit export agency, is providing export credit cover in respect to both facilities. The facilities bear interest at LIBOR+0.4% (3.2% as of December 31, 2004). A commitment fee of 0.2% per annum and an agreement fee of 0.25% should be paid in accordance with the loan agreement. The principal and interest amounts are to be repaid in seventeen equal semi-annual installments, starting July 2005 for the first agreement and September 2005 for the second one. As of December 31, 2004, the outstanding balance under these agreements was $77.0 million. The final maturity of these agreements is in July and September 2013. The loan facility is subject to certain restrictive covenants applying to MTS. As of December 31, 2004, MTS is in compliance with all existing covenants.

Hermes Credit Facility

In December 2003, UMC entered into Hermes Credit Facility with ING BHF Bank and Commerzbank to finance the acquisition of GSM equipment from Siemens AG. The aggregate amount available under this credit facility is EUR 47.4 million (equivalent of $64.5 million as of December 31, 2004). In 2004, the agreement was amended to increase the amount available under the facility by EUR 9.2 million (equivalent of $12.5 million as of December 31, 2004). The loan is fully and unconditionally guaranteed by MTS and bears interest at EURIBOR+0.7% (2.9% as of December 31, 2004). The amount outstanding is redeemable in 10 equal semi-annual installments, commencing July 2004. The balance outstanding as of December 31, 2004 was $63.9 million.

ING Bank (Eurasia)

In September 2003, UMC entered into a $60.0 million syndicated credit facility with ING Bank (Eurasia), Standard Bank and Commerzbank AG with an interest rate of LIBOR+2.3%-4.2% (4.8%-6.7% as of December 31, 2004). The loan is fully and unconditionally guaranteed by MTS. The proceeds were used by UMC to refinance its existing indebtedness. The loan is payable in 8 equal quarterly installments starting from September 2004. As of December 31, 2004, the balance outstanding under this credit facility was $46.7 million.

Vendor Financing

Foreign suppliers of telecommunications equipment provide non-collateralized commercial credit (vendor financing) to the Group denominated in various currencies on short-term and long-term bases, mostly interest free.

Commerzbank (Eurasia)

InvestSvyazHolding, a subsidiary of the Group, entered into a number of credit facilities with Commerzbank (Eurasia) for a total amount of $27.2 million. The facilities bear interest of LIBOR+1.4%-3.5% per annum (4.0%-6.1% as of December 31, 2004). As of December 31, 2004, approximately $27.2 million was outstanding under these facilities. The facilities are fully and unconditionally guaranteed by MTS.

Raiffeisenbank

In September 2002, MGTS entered into a credit line with Raiffeisenbank limited to $15.0 million. The equipment with fair value of $23.9 million was pledged under this credit line as of December 31, 2004. In addition, MGTS is required to maintain monthly gross cash flows with the bank of not less than $1.5 million. The credit line bears interest of LIBOR+5% (7.6% as of December 31, 2004) and matures in 2007. As of December 31, 2004, approximately $3.8 million was outstanding under this credit line.

In November 2002, JSFC Sistema entered into a credit line with Raiffeisenbank (Austria) limited to $20.0 million. The building with fair value of $16.8 million was pledged under this credit line as of December 31, 2004. In addition, the Group is required to maintain monthly gross cash flows with the bank of not less than $1.5 million. The loan bears interest of LIBOR+7% per annum (9.6% as of December 31, 2004) and matures in 2007. As of December 31, 2004, approximately $15.9 million was outstanding under this credit line.

HSBC

In October 2003, TAIF Telcom entered into a $25.0 million credit facility with HSBC Bank LLC, which is fully and unconditionally guaranteed by MTS. The facility bears interest at LIBOR+2.8% (5.2% as of December 31, 2004) and is redeemable in ten equal quarterly installments commencing June 2004. The funds were used to purchase telecommunication equipment and for general corporate purposes. As of December 31, 2004, the outstanding balance of the facility was $17.5 million.

Sberbank

In September 2004, MGTS received a loan from Sberbank of $12.6 million. The loan bears interest of 11% and matures in March 2007. Equipment with fair value of $29.0 million was pledged to collateralize the outstanding balance under the loan as of December 30, 2004. The total balance outstanding under several other loans the Group received from Sberbank was $4.7 million as of December 31, 2004.

Vneshtorgbank

The loans provided by Vneshtorgbank are collateralized by pledge of equipment with fair value of $9.5 million and by a pledge of 4% of MGTS common shares. The weighted average interest rate on the loans outstanding as of December 31, 2004 was 8.2% per annum. The loans mature in 2005-2010.

Citibank

In July 2003, MGTS received a loan from Citibank for purchase of equipment in the amount of $7.1 million. In addition, in May and August 2004, MGTS received loans from Citibank for purchase of equipment and software in the total amount of $8.0 million. All loans bear interest of LIBOR+1.6% (4.2% as of December 31, 2004). The loans are collateralized by pledged equipment with fair value of $9.5 million and by deposit in Citibank of $1.0 million and guaranteed by Export Guarantee and Insurance Corporation, Czech Republic. As of December 31, 2004, approximately $15.1 million was outstanding under these loans. Based on the restrictive covenants of the agreements, the Debt to Equity ratio and Debt Service to Earnings Before Interest and Taxes ("EBIT") ratio of MGTS should not exceed 3:1. MGTS is not allowed to obtain borrowings individually $30.0 million (apart from the Sberbank loan, Raiffeisenbank loan and the issues of MGTS bonds) or alienate more than 10% of its assets without the written approval of Citibank and its aggregate debt may not exceed $250.0 million.

Ericsson Project Finance

In December 1996, Rosico entered into a credit agreement with Ericsson Project Finance AB, which provided for a credit facility with an aggregate principal amount of $60.0 million. The loan bears interest of LIBOR+4% per annum (6.6% as of December 31, 2004). The loan is collateralized by a pledge of 16.8% of MGTS voting shares held by the Group. In February 2003, Ericsson Project Finance AB assigned all of its rights and obligations under the loan to Salomon Brothers Holding Company, Inc. As of December 31, 2004, the loan balance was $14.9 million.

Nordea Bank Sweden

In September 2003, Primtelefon entered into a long-term loan facility with Nordea Bank Sweden for the total amount of $9.8 million. Amounts outstanding under the loan agreement bear interest at LIBOR+0.4% (3.0% as of December 31, 2004) and mature in October 2006. The loan is fully and unconditionally guaranteed by MTS. As of December 31, 2004, the amount outstanding under the loan was $6.5 million.

WestLB

In July 2002, MTS-P, a subsidiary of MTS, entered into a credit facility agreement with West LB International S.A. Amounts outstanding under this agreement bear interest of EURIBOR+2.0% (4.2% as of December 31, 2004) per annum for the first two years for each advance and EURIBOR+4.0% (6.2% as of December 31, 2004) per annum for the remaining interest periods for each advance until maturity. The final maturity of this agreement is in December 2006. The loan is fully and unconditionally guaranteed by MTS. As of December 31, 2004, the amount outstanding under the loan agreement was $4.0 million.

Dresdner Bank

In October 2002, MSS, a subsidiary of MTS, entered into a credit agreement with Dresdner Bank to borrow up to $10.0 million. Borrowings under this agreement bear interest of LIBOR+3.2%-3.4% (5.8%-6.0% as of December 31, 2004) per annum. The loan was fully and unconditionally guaranteed by MTS. In October 2004 the loan was fully repaid.

Deutsche Telekom и TDC Mobile International

The credit facilities with Deutsche Telecom AG and TDC Mobile International A/C bear interest at LIBOR+5.0%-7.0% (7.6%-9.6% as of December 31, 2004) and were redeemable in five quarterly installments commencing April 2003. The debt was fully repaid in April 2004.

The schedule of repayments of long-term debt over the five-year period beginning on December 31, 2004 is as follows:

		(000's)
Year ended December 31,		
2005	$	340,938
2006		432,315
2007		333,029
2008		799,834
2009		97,943
Following periods		831,401
Total	**$**	**2,835,460**

In December 2004, MTS entered into two variable-to-fixed interest rate swap agreements with ABN AMRO Bank N.V and with HSBC Bank PLC to hedge MTS' exposure to variability of future cash flows caused by the change in LIBOR related to the syndicated loan. MTS agreed with ABN AMRO to pay a fixed rate of 3.27% and receive a variable interest of LIBOR on $100.0 million for the period from October 7, 2004 up to July 27, 2007. MTS agreed with HSBC Bank PLC to pay a fixed rate of 3.25% and receive a variable interest of LIBOR on $150.0 million for the period from October 7, 2004 up to July 27, 2007. These instruments qualify as cash flow hedges under the requirements of SFAS No. 133 as amended by SFAS No. 149. As of December 31, 2004, the Group recorded a liability of $0.6 million in relation to these contracts in the accompanying balance sheet and a loss of $0.5 million, net of tax of $0.1 million as other comprehensive income in the accompanying consolidated statement of changes in shareholders equity in relation to the change in fair value of these agreements. In 2004 there were no amounts reclassified from other comprehensive income to income due to hedge ineffectiveness.

23. SUBSCRIBER PREPAYMENTS

Subscriber prepayments as of December 31, 2004 and 2003 consisted of the following:

		(000's)		
		2004		2003
Current portion (Note 19)				
Connection fees	$	83,021	$	60,609
Advances and customers' deposits		308,859		195,379
		391,880		255,988
Non-current portion				
Connection fees		156,233		103,059
Total	**$**	**548,113**	**$**	**359,047**

24. INCOME TAX

The Group's provision for income taxes is as follows for the years ended December 31, 2004 and 2003:

	(000's) December 31, 2004	(000's) December 31, 2003
Current provision	$ 504,634	$ 333,534
Deferred benefit	(58,903)	(42,601)
Total income tax expense	445,731	290,933

The provision for income taxes is different from that which would be obtained by applying the statutory income tax rate (24% in 2004 and 2003) to net income from continuing operations before income tax, minority interests and cumulative effect of a change in accounting principle. The items causing this difference are as follows:

	(000's) December 31, 2004	(000's) December 31, 2003
Income tax provision computed on income from continuing operations before taxes at statutory rate	$ 355,546	$ 221,694
Adjustments due to:		
Change in valuation allowance	234	91
Non-deductible items	50,951	42,366
Non-taxable items	(7,584)	-
Taxable losses not carried forward	32,007	7,566
Currency exchange and translation differences	21,496	18,083
Effect of rates different from standard	(6,919)	1,133
Income tax expense	**$ 445,731**	**$ 290,933**

The tax effects of temporary differences that give rise to the deferred tax assets and liabilities are presented below:

	(000's) December 31, 2004	(000's) December 31, 2003
Deferred tax assets		
Subscriber and customer prepayments	$ 76,364	$ 40,014
Property, plant and equipment	60,963	21,191
Deferred revenues	24,581	19,070
Allowance for doubtful accounts	14,559	20,338
Accrued expenses	27,293	3,434
Tax losses carried forward	8,930	8,795
Other	16,101	3,362
Total	**228,791**	**116,204**
Less: valuation allowance	(8,908)	(9,142)
Total deferred tax assets	**$ 219,883**	**$ 107,062**
Deferred tax liabilities		
Intangible assets	(224,522)	(191,249)
Property, plant and equipment	(111,930)	(71,357)
Undistributed earnings of affiliates	(25,220)	(4,462)
Other	(21,828)	(11,949)
Total deferred tax liabilities	**$ (383,500)**	**$ (279,017)**
Net deferred tax assets, current	$ 73,592	$ 53,964
Net deferred tax assets, long-term	$ 3,482	$ 5,575
Net deferred tax liabilities, current	$ (22,071)	$ (508)
Net deferred tax liabilities, long-term	$ (218,620)	$ (230,986)

Deferred tax assets relating to tax losses carried forward in amount of $8.9 million as of December 31, 2004 expire in 2008 and are attributable to MSS and Rosico, subsidiaries of MTS.

25. POSTRETIREMENT BENEFITS

MGTS has historically provided certain benefits to employees upon their retirement and afterwards. Currently such benefits include bonus payments of a fixed amount to retiring employees with at least five years of service (RUR 12,300 or RUR 24,600 ($443 or $887 at the exchange rate current as of December 31, 2004), depending on actual years of service); lifetime payments of a fixed amount to employees retiring with at least fifteen years of service (RUR 4000 per year, per employee, or approximately $144 at the exchange rate as of for the year ended December 31, 2004); and discounted telephone service to employees retiring with at least thirty years of service. An employee is withdrawn from the benefit plan if his/her employment with MGTS is discontinued prior to retirement.

The assumed discount rate used in determining net periodic cost is 8% per annum. The future benefit payments to retirees under the defined benefit plan are expected as follows:

		(000's)
Year ended December 31,		
2005	$	2,958
2006		1,075
2007		1,023
2008		977
2009		936
2010 - 2014		3,422
Thereafter		1,122
Total	**$**	**11,513**

MGTS's defined benefit plan is unfunded. For the years ended December 31, 2004 and 2003 the net periodic benefit costs recognized and the contributions paid by MGTS under the plan were not material.

26. DEFERRED REVENUE

Deferred revenue is comprised of property, plant and equipment contributions and grants received by the Group and as of December 31, 2004 and 2003 was as follows:

		(000's)		
		2004		2003
Deferred revenue at the beginning of the year	$	115,363	$	89,894
Contributions received during the year		21,530		26,183
Currency translation effect		1,044		9,705
		137,937		125,782
Deferred revenue amortized		(7,024)		(10,419)
Deferred revenue at the end of the year	**$**	**130,913**	**$**	**115,363**

In 2000 the Group was awarded a grant for construction of a manufacturing facility for production of medicines (vaccines and infusion dissolvents) in the Moscow region. The grant facility of $20.1 million was received in full during 2001 and 2000. The grant is repayable to the grantor (state organization) during the period to 2010. These contributions are accounted for as deferred revenues.

27. SHARE CAPITAL

At January 1, 2004, JSFC Sistema had 68,325,000 voting common shares authorized and 8,100,000 shares issued and outstanding with a par value of 0.1 RUR.

In June 2004, JSFC Sistema declared dividends for the year ended December 31, 2003, amounting to $5.2 million.

In July 2004, JSFC Sistema increased the par value of its shares to 90.0 RUR. As a result of this transaction, the share capital of the Group increased and retained earnings decreased by $24.9 million.

28. SEGMENT INFORMATION

SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", established standards for reporting information about operating segments in financial statements. Operating segments are defined as components of an enterprise engaging in business activities about which separate financial information is available that is evaluated regularly by the chief operating decision maker or group in deciding how to allocate resources and in assessing performance.

The Group's operating segments are: Telecommunications, Technology, Insurance, Banking and Other. The Group's management evaluates performance of the segments based on both operating income and net income before minority interests and cumulative effect of a change in accounting principle.

Intercompany eliminations presented below consist primarily of the following items: intercompany sales transactions, elimination of gross margin in inventory and other intercompany transactions conducted under the normal course of operations.

An analysis and reconciliation of the Group's business segment information to the respective information in the consolidated financial statements for the years ended December 31, 2004 and 2003 is as follows:

For the year ended December 31, 2004						
	Telecommu-nications	Techno-logy	Insurance	Banking	Corporate and Other	Total
Net sales to external customers (a)	4,615,846	396,912	275,510	42,950	380,068	5,711,286
Intersegment sales	856	101,515	24,684	22,788	5,191	155,034
Income/(loss) from equity affiliates	27,324	-	191	1,097	(1,491)	27,121
Interest income	30,202	197	-	-	4,977	35,376
Interest expense	(134,816)	(6,876)	-	-	(91,467)	(233,159)
Net interest revenue (b)	-	-	-	11,713	-	11,713
Depreciation and amortization	(783,668)	(3,484)	(3,378)	(1,119)	(8,236)	(799,885)
Operating income/(loss)	1,630,305	45,918	30,168	11,691	(32,600)	1,685,482
Income tax expense	(405,772)	(10,594)	(8,646)	(1,338)	(19,381)	(445,731)
Investments in affiliated companies	165,724	-	-	16,519	24,277	206,520
Segment assets	6,926,288	284,330	420,964	519,756	643,789	8,795,127
Cash and cash equivalents	227,414	32,636	127,590	84,404	31,703	503,747
Indebtedness (c)	(2,138,661)	(27,481)	(522)	(7,316)	(890,921)	(3,064,901)
Capital expenditures	1,538,321	11,882	14,079	3,032	59,672	1,626,986

(a) - Interest income and expenses of the Insurance and Banking segments are presented as revenues from financial services in the Group's consolidated financial statements.

(b) - The Banking segment derives a majority of its revenue from interest. In addition, management primarily relies on net interest revenue, not the gross revenue and expense amounts, in managing that segment. Therefore, only the net amount is disclosed.

(c) - Represents the sum of short-term and long-term debt and capital lease obligations

For the year ended December 31, 2003						
	Telecommu-nications	Techno-logy	Insurance	Banking	Corporate and Other	Total
Net sales to external customers (a)	3,246,813	57,609	169,569	47,192	238,732	3,759,915
Intersegment sales	755	28,333	18,360	10,321	10,926	68,695
Income/(loss) from equity affiliates	439	-	(509)	490	45	465
Interest income	22,834	-	-	-	6,634	29,468
Interest expense	(161,911)	(2,772)	-	-	(41,719)	(206,402)
Net interest revenue (b)	-	-	-	2,697	-	2,697
Depreciation and amortization	(506,644)	(2,862)	(3,115)	(620)	(7,735)	(520,976)
Goodwill impairment	(19,251)	-	-	-	-	(19,251)
Operating income/(loss)	1,103,282	(3,348)	17,111	2,567	(16,131)	1,103,481
Income tax expense	(293,983)	1,571	(3,858)	(3,116)	8,453	(290,933)
Investments in affiliated companies	56,298	666	-	3,875	21,665	82,504
Segment assets	5,204,668	103,568	265,727	595,516	651,718	6,821,197
Cash and cash equivalents	82,548	1,562	48,154	94,652	56,249	283,165
Indebtedness (c)	(1,845,847)	(33,768)	(3,235)	-	(802,590)	(2,685,440)
Capital expenditures	1,152,216	9,209	7,310	2,994	41,160	1,212,889

(a) - Interest income and expenses of the Insurance and Banking segments are presented as revenues from financial services in the Group's consolidated financial statements.

(b) - The Banking segment derives a majority of its revenue from interest. In addition, management primarily relies on net interest revenue, not the gross revenue and expense amounts, in managing that segment. Therefore, only the net amount is disclosed.

(c) - Represents the sum of short-term and long-term debt and capital lease obligations

The reconciliation of segment operating income to the consolidated income from continuing operations before income tax, minority interests and cumulative effect of a change in accounting principle and reconciliation of segment assets to the consolidated segment assets are as follows:

		(000's)		
		2004		2003
Total segment operating income	$	1,685,482	$	1,103,481
Inter-segment eliminations		(20,776)		2,262
Interest income		18,061		19,341
Interest expense		(213,943)		(198,346)
Currency exchange and translation gain		12,620		(3,015)
Consolidated income from continuing operations before income tax, minority interests and cumulative effect of a change in accounting principle:	$	1,481,444	$	923,723
Total segment assets	$	8,795,127	$	6,821,197
Inter-segment eliminations		(16,457)		(2,513)
Consolidated assets	$	8,778,670	$	6,818,684

For the years ended December 31, 2004 and 2003 the Group's revenues derived from Ukraine were $1,115.3 million and $307.7 million. Long-lived assets of the Group's entities domiciled in Ukraine were $849.4 million and $648.8 million as of December 31, 2004 and 2003, respectively.

For the years ended December 31, 2004 and 2003, the Group did not have revenues from transactions with a single external customer amounting to 10% or more of the Group's consolidated revenues.

29. RELATED PARTY TRANSACTIONS

The Group provides services to and purchases services from affiliates and companies related by means of common control. During the years ended December 31, 2004 and 2003, the Group entered into transactions with related parties as follows:

		(000's)		
		2004		2003
Sale of computer spare parts and other equipment	$	(131,820)		-
Insurance premium received		64	$	(4,659)
Telecommunication services provided		(10,497)		-
Revenues from financial services		(2,052)		(11,730)
Consulting services provided		(1,799)		(10,768)
Claims paid		-		9,201
Interest expense		4,998		1,457
Finance services related costs		1,510		-
Purchase of goods for resale		2,612		-
Telecommunication services purchased		15,751		-
Other		**2,238**		**16,831**

Related party balances as of December 31, 2004 and 2003 are disclosed in the corresponding notes to the financial statements.

30. COMMITMENTS AND CONTINGENCIES

Operating Leases

The Group leases land, buildings and office space mainly from municipal organizations through contracts, which expire in various years through 2049.

Future minimum rental payments under capital and operating leases in effect as of December 31, 2004, are as follows:

		(000's		
		Capital leases		Operating leases
Year ended December 31,				
2005	$	5,289	$	54,074
2006		2,228		26,625
2007		746		22,597
2008		171		18,626
2009		169		14,812
Following periods		451		59,037
Less: amount representing interest		(716)		-
Total	**$**	**8,338**	**$**	**195,771**

Capital Commitments

As of December 31, 2004, MTS had executed non-binding purchase agreements in the amount of approximately $164.7 million to subsequently acquire property, plant and equipment.

In December 2003, MGTS announced its long-term investment program for the period from 2004 till 2012 providing for extensive capital expenditures including expansion and full digitalization of the Moscow telephone network. The program was approved by the resolution of the Moscow City Government in December 2003. Capital expenditures under the investment program are currently estimated to be approximately $1.6 billion during the years 2004-2012 and include reconstruction of 350 local telephone stations and installation of 4.3 million of new phone numbers. The Group expects to finance approximately 50% of the capital expenditures under the investment program.

In July 2003, Sistema-Hals entered into an agreement with Siemens Real Estate to develop an office building in Moscow, which will become Siemens AG headquarters in Russia. Under this agreement Sistema-Hals is responsible for obtaining all necessary permits, planning and overall control of the construction process. The building is expected to be completed in late 2005. The cost of the project is estimated at approximately Euro 85.8 million (equivalent of $117.0 million as of December 31, 2004).

During 2004, Organizator, a subsidiary of Sistema-Hals, signed an agreement with Government of Moscow to administrate construction of a tunnel in the City of Moscow. Under the agreements signed by Organizator in relation to this project it is responsible for obtaining all permits, planning and oversight of design and construction work. The construction is financed by the City of Moscow and expected to be completed in 2007. The cost of the project is estimated at RUR 53,528.4 million ($1,929.6 million as of December 31, 2004).

Additionally, Sistema-Hals entered into construction agreements with various third party subcontractors for a total amount of $34.6 million.

Operating Licenses

Since the commencement of MTS' operations in 1994, a number of telecommunication licenses for the Russian Federation were issued to MTS and its now consolidated subsidiaries. These license agreements stipulate that certain fixed "contributions" be made to a fund for the development of telecommunication networks in the Russian Federation. Most of MTS' current licenses provide for the payment of such fees, which in the aggregate could total approximately $103.0 million, as at December 31, 2004. According to the terms of licenses, such contributions are to be made during the license period upon the decision and as defined by the Board of Directors of the Association of GSM-900 Operators (the "Association"). The Association is a nongovernmental, not-for-profit association, and their Board of Directors comprises representatives of the major cellular communications companies, including MTS.

The Association has not adopted any procedures enforcing such payments and no such procedures have been established by Russian legislation. To date, MTS has not made any such payments pursuant to any of the current operating licenses issued to MTS and its consolidated subsidiaries. Further, the management of MTS believes that MTS will not be required to make any such payments in the future. In relation to these uncertainties, MTS has not recorded a contingent liability in the accompanying consolidated financial statements.

Each of the Group's telecommunication licenses, except the licenses covering the Moscow license area, contains a requirement for service to be commenced and for subscriber number and territorial coverage targets to be achieved by a specified date. The Group has met these targets or received extensions to these dates in those regional license areas in which the Group has not commenced operations. The management believes that the Group is in compliance with all material terms of its licenses.

The Group's telecommunication licenses do not provide for automatic renewal. The Group has limited experience with the renewal of its existing licenses. However, management believes that the licenses required for the Group's operations will be renewed upon expiration.

Issued Guarantees

As of December 31, 2004, MTS has issued guarantees for MTS-Belarus, an equity investee, for the total amount of $25.0 million. Under these guarantees the Group could be potentially liable for a maximum amount of $25.0 million in case of the borrower's default under the obligations. The guarantees expire by April 2007.

In December 2002, MTU-Inform and Alfabank signed a guarantee agreement. According to the agreement MTU-Inform guaranteed a loan of $4.0 million provided to Golden Line by Alfabank. The loan matures in November, 2005. In addition, MTU-Inform pledged equipment with a fair value of $4.7 million.

In July 2004, MTU-Inform issued guarantees to MBRD on behalf of Sky Link for the total amount of $21.1 million.

Additionally, MBRD guaranteed loans for several companies, including related parties, which totalled $7.4 million as of December 31, 2004.

These guarantees would require payment by the Group only in the event of default on payment by the respective debtor. Under these guarantees the Group could be potentially liable for a maximum amount of $57.5 million in case of the borrower's default under the obligations. As of December 31, 2004, no event of default has occurred under any of the guarantees issued by the Group.

Legal Proceedings

In the ordinary course of business, the Group may be party to various legal and tax proceedings, and be subject to claims. In the opinion of management, the Group's liability, if any, in all pending litigation, other legal proceeding or other matters, will not have a material effect upon the financial condition, results of operations or liquidity of the Group.

In June 2004, the General Prosecutor of Ukraine filed a claim against MTS and others in the Kiev Commercial Court seeking to unwind the sale by Ukrtelecom of its 51% stake in UMC to MTS. The complaint also seeks an order that would prohibit MTS from alienating 51% of its stake in UMC until the claim is resolved. In August 2004, the Kiev Commercial Court rejected a claim of General Prosecutor of Ukraine against MTS. No appellation was filed to the Court by the office of General Prosecutor of Ukraine within an established period. As of the date of these statements an office of General Prosecutor of Ukraine filed a request to the Constitutional Court of Ukraine to clear out terms of the State Privatization Plan for 2000-2002 and respond whether Ukrtelecom had a right to sell 51% stake in UMC. The Group believes that it acquired a stake in UMC in full compliance with Ukrainian law and, if required, intends to vigorously defend its acquisition of UMC.

Minimum Capital Requirements

The Law on insurance in Russia sets minimum share capital requirements for insurance organizations, depending on the type of insurance premiums they are writing. The minimum capital requirement for insurance organizations conducting reinsurance operations is set at 120.0 million RUR (equivalent of $4.3 million as of December 31, 2004). As of December 31, 2004, Rosno's statutory share capital amounted to 1,069.0 million RUR (equivalent of $38.5 million as of December 31, 2004).

The Central Bank of Russia sets minimum share capital requirements for banks. Effective December 1, 2003, the minimum capital requirement is set at Euro 5.0 million for each newly-founded bank. As of December 31, 2004, MBRD's share capital amounted to 400.0 million RUR (equivalent of $14.4 million as of December 31, 2004). In November 2004, shareholders of MBRD approved an additional issue of 130,000 shares of common stock in a closed subscription. The shares of the new issue will be acquired by the existing shareholders for a price of RUR 4,600 per share (equivalent of $166 as of December 31, 2004).

Contingencies

The Russian economy, while deemed to be of market status from 2002, continues to display certain traits consistent with that of an emerging market. These characteristics have in the past included higher than normal inflation, insufficient liquidity of the capital markets, and the existence of currency controls which cause the national currency to be illiquid outside of Russia. The continued success and stability of the Russian economy will be subject to the government's continued actions with regard to legal, and economic reforms.

On January 1, 2004, a new Law on Telecommunications came into effect in Russia. The law sets the legal basis for the telecommunications business in Russia and defines the status that state bodies have in the telecommunications sector.

According to the new Law on Telecommunications, and effective as of January 1, 2005, all MGTS' subscribers will be required to pay the full price for residential service, and those entitled to discounts are to receive reimbursement from the government rather than discounts from MGTS.

The Law on Telecommunications introduces a Universal Service Fund ("USF") which will result in higher costs for all operators, including the Group. Under the Law on Telecommunications, all telecom operators must contribute to the USF. The USF is designed to fund socially important but economically unviable projects. In April 2005, Russian government approved several provisions clarifying how the USF will be collected and administered. Starting July 1, 2005 the amount of the universal service charge will be 1.2% of the total revenues received from the usage of public telecommunication network less connection fees and revenues received from interconnection services provided to other operators.

The Russian government has also issued several implementing acts under the Law on Telecommunications, such as Resolution No. 87, dated February 18, 2005, approving the list of the types of licensed telecommunication activities, and Resolution No. 68, dated February 11, 2005, regarding the rules applicable to the state registration of telecommunication infrastructure such as real property. However, it is presently not yet clear how these regulations would be implemented. Thus, the uncertainty related to the Law on Telecommunications continues.

In recent years, the Russian government has initiated revisions of the Russian tax system. Effective January 1, 1999, the first part of the Tax Code was enacted. Effective January 1, 2001, the second part of the Tax Code was enacted and effective January 1, 2002 new regulations, relating to federal income tax were enacted. The new tax system is generally intended to reduce the number of taxes, the overall tax burden on businesses, and to simplify the tax laws.

Russia currently has a number of laws related to various taxes imposed by both federal and regional governmental authorities. Applicable taxes include value added tax ("VAT"), corporate income tax (income tax), and payroll (social) taxes, together with others. The government's policy on implementation of these regulations is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established. Tax declarations, together with other legal compliance areas (for example, customs and currency control matters), are subject to review and investigation by a number of authorities, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia that is more significant than typically found in countries with more developed tax systems.

Generally, tax declarations remain open and subject to inspection for a period of three years following the tax year. As of December 31, 2004, tax declarations of the Group for the preceding three fiscal years were open to further review.

Management believes that it has adequately provided for tax liabilities in the accompanying consolidated financial statements; however, the risk remains that relevant authorities could take a different position with regard to interpretive issues.

Importation of Goods

The Group utilizes third parties to import goods into the CIS countries. This results in significant savings of customs duties and related taxes for certain subsidiaries of the Group. There is a risk that the third parties' import transactions may be challenged by regulatory authorities and determined as inappropriate. The impact that this determination may potentially have on the Group's net income and financial position can not be quantified at this stage due to the lack of precedent for such determinations and uncertainty in the calculations of penalties and interest. No contingent liabilities have been recorded in the Group's financial statements in relation to these transactions.

31. SUBSEQUENT EVENTS

Initial Public Offering

On February 11, 2005, JSFC Sistema completed an initial public offering of 1,550,000 common shares, with a nominal value of 90 rubles per share in the form of 77,500,000 global depositary receipts ("GDRs"), with 50 GDRs representing one share. On February 14, 2005, JSFC Sistema's GDRs were admitted to trade on the London Stock Exchange. Proceeds from the offering, net of underwriting discount and other direct costs, were $1,284.6 million.

Simultaneously, certain shareholders of the Group sold 42,663 common shares in the form of 2,133,150 GDRs. In addition, shareholders exercised their option to sell additional 238,900 shares in the form of 11,945,000 GDRs.

Additional Debt Issuance

In January 2005, MTS Finance issued $400.0 million 8.0% unsecured notes at 99.736%. These notes are fully and unconditionally guaranteed by OJSC MTS and mature on January 28, 2012. MTS Finance is required to make interest payments on the notes semi-annually in arrears on January 28 and July 28, commencing on July 28, 2005. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes were $398.9 million.

In February 2005, MBRD entered into a loan facility with Standard Bank London and Standard Bank Moscow, pursuant to which the banks agreed to make available to MBRD a loan facility in the amount of $16.0 million, secured by a pledge of MBRD's rights under its loan to Sky-Link. The loan was guaranteed by MTU-Inform.

In March 2005, MBRD entered into a loan agreement with Dresdner Bank AG for the amount of $150.0 million. The loans bears interest of 8.625% and is due in March 2008. To finance the loan to MBRD, Dresdner Bank AG issued Loan Participation Notes that were admitted to trade on the Luxembourg Stock Exchange. Interest payments on the loan are due semi-annually in March and September of each year, commencing in September 2005. Loan agreement contains certain restrictive covenants including, but not limited to, limitations on mergers, liens and dispositions of assets and transactions with the Group's subsidiaries and affiliates.

Acquisitions

In February 2005, the Group acquired an additional 20% equity stake in Telmos from Rostelecom for a cash consideration of $8.5 million, increasing the Group's voting power in the company to 100%.

In February 2005, the Group acquired an additional 74% stake in MTS-Komi Republic, increasing its voting power in the company to 100%. The value of consideration paid equaled $1.2 million. MTS-Komi Republic provides mobile telecommunication services in the Komi Republic of the Russian Federation.

In February 2005, the Group signed an agreement to acquire a 74.9% stake in Sweet-Com LLC, a holder of 3.5GHz radio frequency allocation for Moscow region, for a cash consideration of $2.0 million. The Company is providing wide-range radio access services for the "last mile" based on the Radio-Ethernet technology.

In February 2005, the Group acquired an additional 5% equity stake in MTT for a cash consideration of $6.4 million, increasing its interest in MTT to 50%.

In February 2005, the Group completed acquisition of 13.33% stake in MBRD. The total consideration amounted to $10.0 million, including cash payment of $2.1 million and promissory notes in the amount of $7.9 million. As a result of this transaction, the Group's voting power in MBRD increased to 98.9%.

In April 2005, the Group acquired an additional 53% stake in Kvant, a personal computers and components manufacturer located in Zelenograd, for a total consideration of $6.0 million, increasing the Group's voting power to 88%. The Group plans to utilize Kvant's facilities to enhance its home appliance and computer assembling activity and integrate it into Technology business segment.

The purchase price allocation for these acquisitions has not been yet finalized at the date of these statements.

Other

In December 2004, MTS announced that it will be changing its current ADS ratio effective January 3, 2005, the first trading day in 2005. The ratio has changed from 1 ADS per 20 ordinary shares to 1 ADS per 5 ordinary shares.

In January 2005, Intourist announced issue of new stock to its existing shareholders. Moscow Government purchased the first tranche of 3,120,516,875 shares in exchange for a 40% stake in Cosmos Hotel, a 1000-room hotel complex situated in Moscow. In April 2005, Sistema paid RUR 1,322.6 million (equivalent of $47.7 million as of December 31, 2004) for the remaining 6,961,052,632 newly-issued shares of Intourist. Upon completion of this transaction, Sistema's ownership interest in Intourist decreased to 71%.

In March 2005, the Russian tax authorities audited OJSC MTS's compliance with tax legislation for the year ended December 31, 2002. Based on the results of this audit, the Russian tax authorities assessed that 372,152 thousand roubles (approximately $13.4 million as at December 31, 2004) of additional taxes, penalties and fines were payable by the Group. The Group has prepared and filed with the Arbitrary Court of Moscow a petition to recognize the tax authorities' resolution as partially invalid. The amount of disputed taxes and fines equals 281,504 thousand roubles (approximately $10.1 million as at December 31, 2004).

In March 2005, MGTS's Board of directors approved issue of RUR-denominated bonds (fifth issue) with the face value of RUR 1,500 million (equivalent of $54.1 million as of December 31, 2004) and final maturity date in 2010.

In April 2004, Sistema and Sabre Capital Worldwide Inc. updated their non-binding "Term Sheet for acquisition by Sabre Group Investors of shares in Moscow Bank for Reconstruction and Development", containing the principal terms of a share purchase agreement between Sistema and Sabre Capital Group's investors, a shareholders agreement between Sistema, MBRD and Sabre Capital Group's investors, and a management agreement between Sistema, MBRD and Sabre Capital. Sabre Capital is a London-based private equity firm, whose principals have expertise in developing retail banking in emerging markets. Principal terms of planned transaction assume that Sabre Capital's investors will own 25% plus one share of the outstanding share capital of MBRD upon the completion of the deal and will take part in governance of MBRD's operations.

In May 2005, MTS's Board of directors recommended to the shareholders to approve cash dividends of RUR 5.75 (equivalent of $0.21 as of the announcement date) per share for the year 2004. The dividends, if approved by the Annual Shareholders Meeting, will amount to $409.5 million.

In May 2005, MGTS's Board of directors recommended to the shareholders to approve cash dividends of RUR 1.82 (equivalent of $0.06 as of the announcement date) per common share and approximately RUR 11.78 (equivalent of $0.42 as of the announcement date) per preferred share for the year 2004. The dividends, if approved by the Annual Shareholders Meeting, will amount to $34.6 million.

In May 2005, JSFC Sistema's Board of directors recommended to the shareholders to approve cash dividends of RUR 26.0 (equivalent of $0.93 as of the announcement date) per share for the year 2004. Payment of the dividend is subject to approval at the Annual Shareholders Meeting, which will be held on June 2005. The dividends, if approved by the Annual Shareholders Meeting, will amount to $9.0 million.

In May 2005, CSC and Giesecke & Devrient GmbH ("G&D") concluded a Shareholders' agreement outlining the terms and conditions for the foundation and operation of a joint-venture ("JV") for production and distribution of smart cards and chips. The principal terms of the agreement stipulate that the JV will be established in the form of a limited liability company, 65% of which will be owned by CSC and 35% by G&D, respectively. The production facility will be located in Zelenograd, Moscow.

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

The following is a discussion of our financial condition and results of operations as of and for the years ended December 31, 2003 and 2004, and of the material factors that we believe are likely to affect our consolidated financial condition. You should read this section together with our audited consolidated financial statements for the years ended December 31, 2003 and 2004, including the notes to those financial statements. In addition, this discussion contains forward looking statements that involve risk and uncertainties. Our actual results may differ materially from those discussed in forward looking statements as a result of various factors. Our reporting currency is the U.S. dollar and our consolidated financial statements have been prepared in accordance with U.S. GAAP.

Overview

We are the largest private sector consumer services group of companies in Russia and the CIS. Our business is developing, managing and realizing the value of market-leading businesses in fast-growing service-based industries. We operate in a select number of service-based industries offering the potential for rapid growth of our businesses. In our consolidated financial statements, we report our results in five segments: Telecommunications; Technology; Insurance; Banking; and Other Businesses (which comprises our real estate, retail, media, travel services and miscellaneous businesses together with our other operations and central corporate functions). Given the scale, scope and market position of our existing operations, we are uniquely positioned to exploit the growth in consumer and corporate purchasing power in the countries in which we operate. Our consolidated revenues reached $5,711.3 million for the year ended December 31, 2004 and $3,759.9 million for the year ended December 31, 2003. Net income from continuing operations before cumulative effect of accounting changes was $446.7 million for the year ended December 31, 2004 as compared to $230.7 million for the year ended December 31, 2003.

Our revenues have increased through organic growth, as well as through acquisitions. Our major acquisitions during the years ended December 31, 2003 and 2004 included cellular operators in the CIS and various regions in Russia (UMC, TAIF Telcom, Sibchanllenge, TSS, Kuban-GSM, Primtelefon, Uzdunrobita), as well as the purchase of 10% share in MTS and of controlling stakes in fixed-line operator Comstar and Ukrainian hardware distributor and system integrator Kvazar-Micro. Revenue growth in existing businesses for the year ended December 31, 2004 was $1,536.5 million, or 41%. The consolidation of Kvazar-Micro, Primtelefon, Uzdunrobita and others in the year ended December 31, 2004 contributed a total of $414.9 million to the increase. The Telecommunications segment's share of the Group's revenues continued to decline, from 86% to 81% year on year, as the Group benefited from continued growth across its non-telecom businesses.

We require substantial funds to support our operations, primarily for increasing network capacity and developing networks in our Telecommunications segment. Our cash outlays for capital expenditures in 2004 and 2003 were $2,009.5 million (including $338.9 million paid for purchase of businesses) and $2,190.3 million (including $1,005.5 million paid for purchase of businesses), respectively. We have financed our cash requirements through our operating cash flows and borrowings. Net cash provided by operating activities in 2004 and 2003 was $1,904.1 million, and $986.4 million, respectively. Since 2002, we have raised over $2.5 billion through several U.S. dollar denominated and rouble-denominated notes offerings in both international and Russian capital markets. We, together with our subsidiaries, have also attracted a number of bank loans to finance our operations. As of December 31, 2004, we had indebtedness of $3,064.9 million, including capital lease obligations, and our interest expense for the year ended December 31, 2004 was $213.9 million, net of amounts capitalized.

We strive to capitalize on our competitive advantages to build market-leading businesses in select sectors which exploit the growth in consumer and corporate purchasing power in the Russian and CIS markets. We employ a disciplined approach to our investment decisions with the aim of maximizing returns for our shareholders. Our internal performance benchmarks require that our businesses achieve certain operational, revenue and profitability targets, which also reflect the nature of these individual businesses. Progress against these targets is monitored and used to develop annual budgets, long-term business plans and capital allocation strategies. Companies that fail to achieve their objectives in a specified time frame generally cease to be beneficiaries of direct investments from Sistema and, should they continue to fall short of our objectives, may be sold. Similarly, we may dispose of businesses in industries that have largely fulfilled their growth potential. As of December 31, 2004, all our business segments were in line with their respective targets.

We have finite financial and managerial resources and, therefore, we concentrate our resources on select sectors in which we believe we can capitalize on our competitive advantages to build market-leading businesses. We exploit our close understanding of the markets in which we operate, as well as our established corporate and government relationships to source attractive investment opportunities in a variety of industries at an early stage. In doing so, we capitalize on our management team, which brings substantial experience of growing businesses across a broad range of sectors in Russia and the CIS. Our business development strategy is focused on achieving growth both through organic development of our businesses and through acquisitions. We provide capital, management, administrative and other resources to accelerate the business plans of our companies through business line extension, geographic expansion, participation in industry consolidation and cross-selling with our other businesses. We constantly evaluate potential entry into new high-growth sectors that may meet our investment requirements. We also evaluate selective international expansion opportunities in cases where we can capitalize on our competitive strengths. Where appropriate, we will accelerate the development of our businesses by capitalizing on our ability to access the international capital markets.

We have management control of our key businesses and operate as an active investor. We contribute significant management and other resources to accelerating the development of our businesses, particularly in the early stages of their life-cycles. For example, the rapid growth of our telecommunications businesses is largely a function of our ability to attract and retain skilled management. Continuing to attract and retain top quality managers to develop our businesses will remain one of our key priorities in the future.

Strategic partners have also played an important role in the development of certain of our businesses. Our strategic partnerships with Deutsche Telekom (MTS) and Allianz (ROSNO) have accelerated the growth of our wireless communications and insurance businesses, respectively. We have also recently concluded a long-term partnership agreement with Siemens to assist in the development of our technology business. We will evaluate the potential to enter into further strategic partnerships in certain of our other businesses wherever a strategic partner can add significant value to that business through their brand strength, intellectual property contribution, operational expertise or international presence.

As the largest private sector consumer services company in Russia and the CIS, we believe our businesses present certain cross-selling opportunities, as well as the potential to benefit from economies of scale in their purchasing and selling activity. We also endeavor to capitalize on our vertical integration capabilities and exploit synergy opportunities, for example, by taking advantage of our combined customer base of over 45 million customers in Russia and the CIS.

The following table illustrates our ownership interests in our principal consolidated subsidiaries and equity holdings as of December 31, 2004.

Segment	Company	Beneficial ownership, %(1)	Voting interest, %(2)
Telecommunications	MTS	51	51
	MGTS	46	56
	Comstar UTS(3)		
	MTU-Inform	76	99
	Comstar	77	100
	Telmos	62	80
	MTU-Intel	87	100
	Golden Line	87	100
	Sky-Link	42	50
	MTT	36	45
	Sistema Telecom	100	100
Technology	CSC	78	78
	Kvazar-Micro	50	51
	Mikron	60	76
	STROM telecom	52	67
	Sitronics	78	100
Insurance	ROSNO	49	51
Banking	MBRD	82	86
	East-West United Bank	49	49
Other Businesses			
Real Estate	Sistema-Hals	100	100
	Landshaft	100	100
Retail	Detsky Mir	75	75
	Detsky Mir Center	100	100
Mass Media	Sistema Mass Media	90	90
Travel Services	Intourist	91	91
International Operations	ECU GEST	99	99
Radio and Space Technology	RTI Systems	100%	100
Pharmaceuticals and Biotechnology	Medical Technological Holding Company	74	74

(1) "Beneficial ownership" represents the percentage of ownership interests of the relevant entity that are beneficially owned by Sistema, directly or indirectly, based on Sistema's proportionate ownership of the relevant entity through its consolidated subsidiaries. Our ownership interests in the subsidiaries presented above are calculated based on shares owned by us as well as shares owned by certain companies affiliated but not owned by us, which we are required to consolidate under U.S. GAAP (FIN 46R). Excluding the ownership interests of these affiliated companies, our beneficial ownership interests in certain subsidiaries listed above would have been lower by the following amounts: CSC (2.0%), Mikron (1.5%), STROM telecom (1.4%), Sitronics (2.0%), ROSNO (1.6%), MBRD (15.1%), Detsky Mir (4.5%), Sistema-Hals (1.1%) and Landshaft (1.1%).

(2) "Voting interest" represents the percentage of ownership interests of the relevant entity that Sistema or any of its consolidated subsidiaries has the power to vote.

(3) The entities comprising the businesses of Comstar UTS are currently being restructured and combined into a single legal entity. After the completion of the restructuring, we expect that Sistema will own at least 51% of Comstar UTS directly with an additional stake owned indirectly through MGTS. References herein to "Comstar" are to our alternative fixed line subsidiary Comstar only.

Macroeconomic Factors Affecting Our Results of Operations

Most of our operations are based in Russia. As a result, Russian macroeconomic trends and country-specific risks significantly influence our performance. In recent years, Russia has been able to overcome the consequences of the 1998 financial crisis. Below is a summary of several key macroeconomic factors that may have a substantial impact on our business:

Year ended December 31,		
	2003	2004
GDP growth	7.3%	7.1%
Consumer price index	12.0%	11.7%
Unemployment rate	8.9%	8.2%
Nominal exchange rate (rubles per U.S. dollar)[1]	30.6	28.7
Real ruble appreciation against U.S. dollar[2]	**20.9%**	**18.6%**

Sources: Central Bank of Russia, Goskomstat, EIU, Russian Ministry of Economic Development.

(1) The average of the exchange rates on the last business day of each full month during the relevant period.

(2) Real ruble appreciation against U.S. dollar is a consumer price index adjusted for nominal exchange rate changes over the same period.

GDP growth rates in Russia remain relatively high compared to North America and Europe. The Russian economy has not been significantly affected by the current global economic slowdown due to the high proportion of oil and oil products in its export revenues and the high oil prices on the international markets. Real incomes have increased significantly since the financial crisis in August 1998. The higher disposable income of the Russian population has stimulated demand for the services provided by our main businesses, such as telecommunications, insurance, banking and retail. The continuation of growth in Russian GDP and real and disposable income in Russia is subject to the influences of various political groups whose interests may not be aligned with those of the current government and to the ability of the government to continue to progress economic and regulatory reforms currently underway.

Acquisitions and Divestitures

During the periods under review, we have completed a number of acquisitions and divestitures, several of which have had a significant impact on our results of operations and financial condition. We consolidate revenues and expenses of newly acquired entities from the beginning of the year in which we obtain a controlling interest. Earnings attributable to these entities for the portion of the year prior to the date upon which we obtained a controlling interest are included in minority interests.

Due to the number of significant transactions completed during the periods under review, period-to-period comparisons of our results of operations need to be considered in the light of the impact of such transactions.

Below is a list of our major acquisitions during two last fiscal years.

Company	Principal activity	Date of acquisition	Stake acquired	Acquiring entity	Purchase price[1]
					(in millions)
Year ended December 31, 2003					
MTS	Mobile operator in Russia and Ukraine	April 2003	10.0%	Sistema	$ 370.0
UMC	Mobile operator in Ukraine	March 2003	57.7%	MTS	199.0
UMC	Mobile operator in Ukraine	June 2003	26.0%	MTS	87.6
UMC	Mobile operator in Ukraine	July 2003	16.3%	MTS	91.7
TAIF Telcom	Mobile operator in the Tatarstan Republic and Volga region	April 2003	51.0%	MTS	61.0
TAIF Telcom	Mobile operator in the Tatarstan Republic and Volga region	May 2003	1.7%	MTS	2.3
Sibchallenge	Mobile operator in the Krasnoyarsk region	August 2003	100.0%	MTS	45.5
TSS	Mobile operator in Eastern Siberia	September 2003	100.0%	MTS	47.0
Kuban-GSM	Mobile operator in Krasnodar region	September 2003	47.3%	MTS	107.0
Comstar	Fixed line operator in Moscow	December 2003	50.0%	ECU GEST	20.8
					$1,031.9
Year ended December 31, 2004					
SCS-900	Mobile operator in Siberian region	March 2004	11.0%	MTS	$ 8.5
FECS-900	Mobile operator in Far East region	April 2004	40.0%	MTS	8.3
Primtelefon	Mobile operator in Far East region	June 2004	50.0%	MTS	31.0
Kvazar-Micro	Distributor of computer components and system integrator in Ukraine	July 2004	51.0%	ECU GEST	28.0
Uzdunrobita	Mobile operator in Uzbekistan	August 2004	74.0%	MTS	121.2
UDN-900	Mobile operator in Udmurtia Republic	August 2004	49.0%	MTS	6.4
TAIF Telcom	Mobile operator in the Tatarstan Republic and Volga region	September 2004	47.3%	MTS	63.0
MTT	Nationwide transit network operator	September 2004	29.8%	ECU GEST, Hurdsfield	39.8
MTT	Nationwide transit network operator	October 2004	0.2%	Sistema	0.1
Sibintertelecom	Mobile operator in Far East region	November 2004	93.53%	MTS	37.4
Telesot Alania	Mobile operator in the Republic of North Osetia (south of Russia)	December 2004	52.5%	MTS	6.2
Gorizont-RT	Mobile operator in the Republic of Sakha (Yakutia)	December 2004	76.0%	MTS	53.2
					$403.1

[1] acquisition-related costs.

Recent Acquisitions

In February 2005, we acquired an additional 20% equity stake in Telmos from Rostelecom for a cash consideration of $8.5 million, which increased our voting power in Telmos to 100%.

In February 2005, MTS purchased an additional 74% stake in MTS-Komi Republic, a provider of mobile telecommunication services in the Komi Republic, increasing our voting power in the company to 100%. The value of consideration paid equaled $1.2 million.

In February 2005, we signed an agreement to acquire a 74.9% stake in Sweet-Com LLC, a holder of 3.5GHz radio frequency allocation for Moscow region, for a cash consideration of $2.0 million. Sweet-Com LLC provides wide-range radio access services for the "last mile" based on the Radio-Ethernet technology.

In February 2005, we acquired an additional 5% equity stake in MTT for a cash consideration of $6.4 million, increasing our voting share in MTT to 50%. In May 2005, MTT was issued one of the first long-distance telephony licenses in the process of liberalization of the long-distance market, which we expect to provide a significant effect on the growth of MTT business.

In February 2005, we completed the acquisition of 13.3% stake in MBRD. The total consideration amounted to $10.0 million, including cash payment of $2.1 million and promissory notes in the amount of $7.9 million. As a result of this transaction, our voting share in MBRD increased to 98.9%.

In April 2005, we acquired an additional 53% stake in Kvant, a personal computers and components manufacturer located in Zelenograd, for a total consideration of $6.0 million, increasing our voting power in Kvant to 88%. We plan to utilize Kvant's facilities to enhance our home-appliance and computer assembling activity as a part of the Technology business segment.

Consolidation of MTS

In April 2003, we exercised our rights under a call option agreement with T-Mobile to acquire from T-Mobile 199,322,614 shares of common stock of MTS, amounting to an additional 10% of MTS' outstanding common stock, for the total consideration of $370.0 million. As a consequence, since April 2003 we have had a controlling interest of 50.6% of MTS' shares, and we have consolidated the results of operations of MTS in our financial statements for the year commencing January 1, 2003 and subsequent periods.

For the year ended December 31, 2004 and the year ended December 31, 2003, MTS accounted for approximately $3,918.2 million and $2,638.2 million, or 68.6% and 70.2% of our net revenues. MTS share in our revenues continues to decrease as we benefit from the growth of our non-telecom businesses and acquisitions in non-telecom segments.

Other Acquisitions

Below is a discussion of our other acquisitions during the fiscal years ended December 31, 2003 and December 31, 2004.

In October 2003, MTS completed the purchase of Vostok Mobile South and thus acquired a 50% stake in Volgograd Mobile and Astrakhan Mobile and an 80% stake in Mar Mobile GSM. Also, in a separate transaction, MTS completed the acquisition of the remaining 20% stake in Mar Mobile GSM from existing shareholders unrelated to MCT Corporation, thus consolidating a 100% ownership in the company. In August 2004, MTS acquired the remaining stakes in Astrakhan Mobile and Volgograd Mobile, increasing our voting power in these subsidiaries to 100%. The acquisition price equaled to $1.1 million and $2.9 million, respectively. Astrakhan Mobile holds a AMPS/DAMPS-800 and GSM-1800 licenses covering Astrakhan region (population of approximately 1.0 million) and Volgograd Mobile holds a AMPS/DAMPS-800 and GSM-1800 licenses covering Volgograd region (population of approximately 2.7 million). As of July 31, 2004, the two companies provided AMPS/DAMPS services to around 10 thousand subscribers. As a result of the allocation of the purchase price for these transactions, we increased license cost for $16.5 million

During the year ended December 31, 2003, we increased our ownership interest in MBRD from 52% to 59%, in DM-Center from 53% to 100% and in Bolshaya Ordynka from 0% to 70% by acquiring their shares from related parties for an aggregate cash consideration of less than $0.1 million. The aggregate effect of such transactions on the Group's equity amounted to a net decrease of $2.7 million, which was charged to additional paid-in capital.

In April 2004, MTS acquired additional 7.5% stake in MSS, a mobile operator in the Omsk region, for $2.2 million in cash. This acquisition increased our voting power in MSS to 91%. The acquisition was accounted for using the purchase method of accounting, whereas the allocation of purchase price increased recorded license cost by $1.1 million.

In April and May 2004, MTS acquired the remaining stakes in the following subsidiaries: 35% of MTS-NN, a telecommunications service provider in Nizhny Novgorod, for $0.5 million, and 49% of Novitel, a handsets dealer in Moscow, for $1.3 million. Both acquisitions increased the Group's voting power in the respective companies to 100%. The transactions were accounted for using the purchase method of accounting, with an increase of recorded goodwill by $1.8 million as a result of the purchase price allocation.

During the year ended December 31, 2004, ROSNO repurchased 3.4% of its outstanding shares from a director of the Group for cash consideration of $5.6 million. The transaction resulted in a reduction of additional paid-in capital by $1.3 million, net of minority interest of $2.6 million. Later in the same period we acquired from ROSNO 1.75% of its shares for $2.8 million in cash. The remaining treasury shares were sold by ROSNO to a subsidiary of Allianz AG. In December 2004, ROSNO issued 10.9 million new shares, 5.6 million of which were purchased by the Group for a cash payment of $9.8 million. The rest of the newly issued shares were sold to Allianz AG. As a consequence of these transactions, the Group's ownership interest in ROSNO reached 49.0%.

In October 2004, ROSNO acquired from RAO UES 100% stake in Leader. The value of consideration equaled $3.0 million. Leader is an insurance company, selling primarily property insurance to energy companies. During 2002-2004, the Group assumed reinsurance from Leader and performed operational management of this company.

In October 2004, ROSNO acquired 100% stake in Deutsche Investment Trust for cash consideration of $2.4 million. The allocation of purchase price increased goodwill by $1.3 million.

In June 2004, we acquired 5% share in East-West United Bank for cash consideration of $1.7 million. In November 2004, we acquired from Vneshtorgbank an additional 14% stake in East-West United Bank, increasing our ownership to 49%. The value of consideration equaled $5.3 million. East West United Bank is a bank incorporated in Luxembourg.

In addition, during the periods under review we acquired controlling and non-controlling stakes in several small regional companies. Moreover, we increased our shareholdings in several subsidiaries by acquiring stakes from minority shareholders and related parties.

Divestitures

During 2003, we continued to dispose of our interests in our oil business. The gain on the disposal of our oil business was classified as gain on disposal of discontinued operations in our consolidated statements of operations for the year ended December 31, 2003 and amounted to $143.6 million.

In December 2002 and February 2003, we sold 100% of our voting shares in FPK Kedr-M, a network of 30 gasoline stations located in Moscow, to a third party for the total consideration of $45.0 million.

During 2003, we acquired 33.0% of common shares of Belkamneft, 100.0% of Consortium-12, 100.0% of Baikal Oil and 24.0% of Sistema-Neft, the holding company for our oil business line, for total cash consideration of $186.8 million. In December 2003, we sold our interests in these companies to a third party for total cash consideration of $292.5 million and a promissory note with a fair value of $15.9 million collected in 2004.

In July 2004, we sold 33.0% of the common shares of our subsidiary STROM telecom to a third party for cash consideration of $2.0 million. The transaction resulted in recognition of a loss on disposal of $1.2 million.

In August 2004, we sold 83.5% of the common shares of our subsidiary P-Com to Sky-Link, our affiliate, for promissory notes in the amount of $16.0 million. The transaction resulted in recognition of a loss on disposal of $1.9 million. The revenues of P-Com were excluded from our consolidated revenues from January 1, 2004, and our share in earnings of P-Com for the year ended December 31, 2004 was accounted for under equity method of accounting.

In October 2004, we disposed of our 24% shareholding in MCC to Sky-Link for cash consideration of $0.7 million.

During 2003 and 2004, we sold our interests in Mikron-Energo, a manufacturer of electronic devices, Sofora, a subsidiary operating in the media business, and in certain other subsidiaries. The proceeds from these sales and the results of operations of these subsidiaries were not material.

Consolidated Financial Results Overview

The following table sets forth a summary of our financial results for the years ended December 31, 2004 and 2003. This financial information should be read in conjunction with our consolidated financial statements.

	Years ended December 31,			
	2003	% of revenue	2004	% of revenue
	(Amounts in thousands, except percentages)			
Revenues	$ 3,759,915	100.0%	$ 5,711,286	100.0%
Costs of sales, exclusive of depreciation and amortization shown separately below	(1,388,027)	(36.9)	(2,221,755)	(38.9)
Selling, general and administrative expenses	(689,057)	(18.3)	(1,009,716)	(17.7)
Depreciation and amortization	(520,976)	(13.9)	(799,885)	(14.0)
Goodwill impairment	(19,251)	(0.5)	-	0.0
Net other operating expenses	(37,326)	(1.0)	(44,529)	(0.8)
Income from equity investees	465	0.0	27,121	0.5
Net gain on disposal of subsidiaries	-	0.0	2,184	0.0
Operating income [(1)]	$ 1,105,743	29.4%	$ 1,664,706	29.1%
Interest income	19,341	0.5	18,061	0.3
Interest expense	(198,346)	(5.3)	(213,943)	(3.7)
Income tax	(290,933)	(7.7)	(445,731)	(7.8)
Foreign exchange (loss)/gain	(3,015)	(0.1)	12,620	0.2
Income from continuing operations before minority interests and cumulative effect of accounting changes	$ 632,790	16.8%	$ 1,035,713	18.1%
Minority interests	(402,120)	(10.7)	(589,014)	(10.3)
Gain from discontinued operations	156,377	4.2	-	0.0
Cumulative effect of a change in accounting principle	-	0.0	(35,472)	(0.6)
Net income	$ 387,047	10.3%	$ 411,227	7.2%
OIBDA [(2)]	$1,626,719	43.3%	$2,464,591	43.2%

[(1)] Operating income is calculated as revenues less operating costs, plus income from equity investees and net gain on sale of subsidiaries. Operating costs include costs of sales, selling, general and administrative expenses and depreciation and amortization, as well as other operating expenses (net of other operating income).

[(2)] OIBDA represents operating income before depreciation and amortization. OIBDA is not a measure of financial performance under U.S. GAAP. You should not consider it an alternative to net income as a measure of operating performance or to cash flows from operating activities as a measure of liquidity. Our calculation of OIBDA may be different from the calculation used by other companies and therefore comparability may be limited. We believe that OIBDA provides useful information to investors because it is an indicator of the strength and performance of our ongoing business operations, including our ability to fund discretionary spending such as capital expenditures, acquisitions of subsidiaries and other investments and our ability to incur and services debt. While depreciation and amortization are considered operating costs under U.S. GAAP, these expenses primarily represent non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods.

The following tables set forth a summary of revenues and operating income by reporting segment for the years ended December 31, 2003 and 2004. In our comparison of period-to-period results of operations, in order to analyze changes, developments and trends in revenues by reference to individual segment revenues, we present our revenues on an aggregated basis, which is revenues after elimination of intra-segment (between entities in the same segment) transactions, but before inter-segment (between entities in different segments) eliminations. Amounts attributable to individual companies, where appropriate, are shown prior to both intra-segment and inter-segment eliminations.

Revenues by segment:

	Years ended December 31,			
	2003	% of revenue	2004	% of revenue
	(Amounts in thousands, except percentages)			
Telecommunications	$ 3,247,568	86.4%	$ 4,616,702	80.8%
Technology	85,942	2.3	498,427	8.7
Insurance	187,929	5.0	300,194	5.3
Banking	57,513	1.5	65,738	1.2
Other Businesses[1]	249,658	6.6	385,259	6.7
Aggregated revenue	$ 3,828,610	101.8%	$ 5,866,320	102.7%
Eliminations[2]	(68,695)	(1.8)%	(155,034)	(2.7)%
Total	$ 3,759,915	100.0%	$ 5,711,286	100.0%

[1] Other Businesses includes our real estate, retail and media businesses together with our other operations and central corporate functions.
[2] Eliminations of inter-segment revenue.

Operating income by segment:

	Years ended December 31,			
	2003	% of operating income	2004	% of operating income
	(Amounts in thousands, except percentages)			
Telecommunications	$ 1,103,282	99.8%	$ 1,630,305	97.9%
Technology	(3,348)	(0.3)	45,918	2.8
Insurance	17,111	1.5	30,168	1.8
Banking	2,567	0.2	11,691	0.7
Other Businesses (1)	(16,131)	(1.5)	(32,600)	(2.0)
Aggregated revenue	$ 1,103,481	99.8%	$ 1,685,482	101.2%
Eliminations (2)	2,262	0.2%	(20,776)	(1.2)%
Total	$ 1,105,743	100.0%	$ 1,664,706	100.0%

[1] Other Businesses includes our real estate, retail and media businesses together with our other operations and central corporate functions.
[2] Eliminations of inter-segment operating income.

Year ended December 31, 2004 compared to year ended December 31, 2003

Revenues

Our consolidated revenues increased by 51.9% to $5,711.3 million for the year ended December 31, 2004 from $3,759.9 million for the year ended December 31, 2003.

The growth in our revenues was attributable to the growth in our Telecommunications Segment of $1,369.1 million, in our Technology Segment of $412.5 million, in our Insurance Segment of $112.3 million, in our Banking Segment of $8.2 million and in our Other Businesses Segment of $135.6 million.

Growth in revenues for the year ended December 31, 2004 compared with the year ended December 31, 2003 was primarily due to organic growth, as well as to acquisitions made subsequent to December 31, 2003, including Primtelefon, Kvazar-Micro and Uzdunrobita, the results of which are only reflected in the current period. The consolidation of Primtelefon, Kvazar-Micro and Uzdunrobita contributed $69.4 million, $293.5 million, and $58.0 million, respectively, to the increase in aggregated revenues for the year ended December 31, 2004. P-Com had revenues of $51.3 million in the year ended December 31, 2003, which is not included in aggregated revenues in the year ended December 31, 2004. From our existing businesses, growth in our consolidated revenues for the year ended December 31, 2004 was $1,536.5 million, or 78.7% of the overall growth.

The Telecommunications Segment continued to be the largest revenue contributor for the year ended December 31, 2004, though its share of the aggregated revenues decreased to 80.8% from 86.4% for the year ended December 31, 2003 due to accelerated growth and significant acquisitions in our other segments. In the year ended December 31, 2004, MTS and MGTS were the largest contributors to the growth of the Telecommunications Segment revenue. Revenues of MTS and MGTS grew by $1,280.0 million (inclusive of the effects of the acquisitions of Primtelefon and Uzdunrobita), and $101.2 million, or by 48.5% and 26.6%, respectively, over the year ended December 31, 2003. This increase was primarily due to the significant growth in MTS' subscriber base from 16.7 million as of December 31, 2003 to 34.2 million as of December 31, 2004. The increase in MGTS' revenues was primarily due to increases in subscription fees for residential and government subscribers that took effect in June 2003, August 2003 and October 2004.

The increase in revenues of our Technology Segment was attributable to the organic growth of STROM telecom and Sitronics, as well as to the acquisition of Kvazar-Micro in July 2004. Revenues of STROM telecom and Sitronics for the year ended December 31, 2004 increased by $57.6 million and $27.4 million, or by 154.2% and 816.5%, respectively, compared with the year ended December 31, 2003. Revenues of STROM telecom increased mainly due to sales of new billing systems to MTS and MGTS. Revenues of Sitronics increased as a result of increased production of consumer electronics under the Sitronics umbrella brand. The consolidation of Kvazar-Micro contributed $293.5 million to the increase in revenues of our Technology Segment for the year ended December 31, 2004.

Revenues from our Insurance Segment grew by 60.0% for the year ended December 31, 2004, compared with the year ended December 31, 2003 due to ROSNO's promotion of new insurance products and the expansion of its client base in line with the overall growth of the insurance market in Russia.

Our real estate, tourism and retail businesses were the largest contributors to the organic growth in our Other Businesses Segment, with increases in revenue of $51.3 million, $34.5 million and $23.8 million, respectively, for the year ended December 31, 2004, compared with the same period in 2003. Our real estate business revenues increased as a result of the sale of completed office buildings and residential property in Moscow. The revenues of our tourism business increased primarily due to an increase in the number of tourists, both inbound and outbound, served during the period.

Operating costs

Operating costs include costs of sales, selling, general and administrative expenses and depreciation and amortization, as well as other operating expenses (net of other operating income).

For the year ended December 31, 2004, our cost of sales increased as a percentage of revenues to 38.9% from 36.9% for the year ended December 31, 2003, primarily as a result of the consolidation of the low-margin Kvazar-Micro business, partially offset by a decrease in the cost of sales, as percentage of revenues, in MTS, from 29.6% to 28.8%. This slight decrease in MTS' cost of sales was due to lower interconnection and line rental charges payable to other operators for access to their networks relative to MTS' increasing revenues because, as MTS has expanded its network, more calls are placed and completed solely within its network, thereby avoiding the need to pay such charges to other operators while still fully earning the related revenues from such calls.

Our selling, general and administrative expenses decreased to 17.7% of revenue for the year ended December 31, 2004 from 18.3% of revenue for the year ended December 31, 2003 primarily due to the slower growth of general and administrative expenses of MTS compared with the growth of its revenues for the same period, resulting from economies of scale. Depreciation and amortization increased slightly to 14.0% of revenues for the year ended December 31, 2004 from 13.9% of revenues for the year ended December 31, 2003.

An impairment provision of $19.3 million was recorded for the year ended December 31, 2003 as a result of the impairment of goodwill attributable to P-Com.

Operating income

Operating income is revenues less operating costs, plus income from equity investees and net gain on disposal of subsidiaries.

Our consolidated operating income margin comprised 29.1% of revenues for the year ended December 31, 2004, compared with 29.4% of revenues for the year ended December 31, 2003. MTS continued to be the main contributor to the operating margin with $1,453.7 million, or 87.3% of aggregated operating income, for the year ended December 31, 2004.

Interest

Our consolidated interest expense for the year ended December 31, 2004 increased by 7.9% to $213.9 million from $198.3 million for the year ended December 31, 2003, primarily as a result of an increase in our debt related to MTS' issuance of $300.0 million notes in August 2003 and $400.0 million notes in October 2003, and Sistema Capital's issuance of $350.0 million notes in January 2004, partially offset by the repayment of MTS' Floating Rate Notes in May 2004 for the amount of $300.0 million. In July 2004, MTS entered into a $500.0 million syndicated loan agreement with international financial institutions. In September 2004, MTS extended total amount available under the syndicated loan facility for an additional $100.0 million to total amount of $600.0 million.

Income tax

Our consolidated provision for income taxes for the year ended December 31, 2004 increased by 53.2% to $445.7 million from $290.9 million for the year ended December 31, 2003 following the increase of our pre-tax income. Our effective tax rate for the year ended December 31, 2004 decreased to 30.1%, compared to 31.5% for the year ended December 31, 2003 mainly as a result of the relatively lower amount of non-deductible expenses as a percentage of pre-tax income incurred during the year ended December 31, 2004 as compared with the year ended December 31, 2003.

Net income from continuing operations before minority interest and cumulative effect of accounting changes

Consolidated net income from continuing operations prior to minority interest and cumulative effect of accounting changes increased by 63.7% to $1,035.7 million for the year ended December 31, 2004 from $632.8 million for the year ended December 31, 2004. To arrive at this measure, we add interest income and foreign exchange gain to, and deduct interest expense and income taxes from, operating income. Net income margin from continuing operations prior to minority interests and cumulative effect of accounting changes was 18.1% for the year ended December 31, 2004, compared with 16.8% for the year ended December 31, 2003.

Minority interests

Minority interests in net income of our subsidiaries for the year ended December 31, 2004 increased to $589.0 million from $402.1 million for the year ended December 31, 2003 primarily due to the increase of net income attributable to MTS.

Segment Financial Results Overview

The following analysis concentrates on our five reporting segments: Telecommunications, Technology, Insurance, Banking and Other Businesses. We include the discussion of our real estate, retail, media businesses and other operations as well as corporate functions, under the Other Businesses Segment.

Segment results are presented after elimination of intra-segment transactions, but prior to elimination of transactions between segments.

Telecommunications

We divide our Telecommunications Segment into two divisions: wireless services (MTS and our affiliate Sky-Link) and fixed line communications (MGTS, Comstar UTS and our affiliate MTT).

The following table presents the results of operations for our Telecommunications Segment for the periods under review:

	Year ended December 31,			
	2003	% of revenues	2004	% of revenues
Revenues	$ 3,247,568	100.0%	$ 4,616,702	100.0%
Costs of sales, exclusive of depreciation and amortization shown separately below	(1,059,315)	(32.6)	(1,443,974)	(31.3)
Selling, general and administrative expenses	(539,010)	(16.6)	(763,011)	(16.5)
Depreciation and amortization	(506,644)	(15.6)	(783,668)	(17.0)
Goodwill impairment	19,251)	(0.6)	-	0.0
Net other operating income/(expenses)	(20,505)	(0.6)	(23,068)	(0.5)
Income from equity investees	439	0.0	27,324	0.6
Operating income	$ 1,103,282	34.0%	$ 1,630,305	35.3%
OIBDA[1]	$ 1,609,926	49.6%	$ 2,413,973	52.3%

[1] OIBDA represents operating income before depreciation and amortization. OIBDA is not a measure of financial performance under U.S. GAAP. You should not consider it an alternative to net income as a measure of operating performance or to cash flows from operating activities as a measure of liquidity. Our calculation of OIBDA may be different from the calculation used by other companies and therefore comparability may be limited. We believe that OIBDA provides useful information to investors because it is an indicator of the strength and performance of our ongoing business operations, including our ability to fund discretionary spending such as capital expenditures, acquisitions of subsidiaries and other investments and our ability to incur and services debt. While depreciation and amortization are considered operating costs under U.S. GAAP, these expenses primarily represent non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods.

Year ended December 31, 2004 compared to year ended December 31, 2003

Revenues

Telecommunications Segment revenues increased by 42.2% for the year ended December 31, 2004 to $4,616.7 million compared to $3,247.6 million for the year ended December 31, 2003. MTS and MGTS were the principal contributors to the growth, with an increase in revenues of $1,280.0 million and $101.2 million, respectively.

In August 2004, we sold our 83.5% interest in P-Com to Sky-Link. Revenues of P-Com were excluded from our consolidated revenues from January 1, 2004, and our share in earnings of P-Com for the year ended December 31, 2004 was recorded using the equity method of accounting. P-Com's revenues for the year ended December 31, 2003 were $51.3 million.

Wireless services

Revenues of MTS for the year ended December 31, 2004 were $3,918.2 million, an increase of 48.5% compared to $2,638.2 million for the year ended December 31, 2003. This increase was primarily due to the significant growth in MTS' subscriber base from 16.7 million as of December 31, 2003 to 34.2 million as of December 31, 2004, including 26.5 million in Russia, 7.4 million in Ukraine and 0.3 million in Uzbekistan. A portion of the growth in the subscriber base was due to acquisitions during the year ended December 31, 2004, including Primtelefon and Uzdunrobita with subscriber bases of 0.2 million and 0.3 million, respectively. The growth was also attributable to MTS' sales and marketing efforts and the expansion of its network, as well as improving general economic conditions and income levels in Russia and Ukraine. The increase in revenues from subscriber growth was partially offset by a decrease in tariffs in the Moscow license area and other highly competitive license areas, an increase of mass-market subscribers in MTS' subscriber mix and its continuing expansion into the regions of Russia outside the Moscow license area where tariffs are lower. As a result, average monthly service revenue per subscriber in Russia decreased by 29.4% from $17 per subscriber for the year ended December 31, 2003 to $12 per subscriber for the year ended December 31, 2004.

For the year ended December 31, 2004, MTS' service revenues and connection fees increased by $1,274.4 million, or by 49.8%, to $3,831.5 million from $2,557.1 million for the year ended December 31, 2003 due to growth in the number of its subscribers, as explained above. Revenues from sales of handsets and accessories increased by $5.6 million, or 6.9%, for the year ended December 31, 2004, compared to the year ended December 31, 2003, due to growth of handset sales activity. This growth was partially offset by a decline in the average selling price for handsets.

During the year ended December 31, 2004, Sky-Link acquired our interest in P-Com, as well as a number of Svyazinvest's NMT-450 companies, and started providing services under Sky-Link brand name. As of December 31, 2004, Sky-Link had 213,100 subscribers (including subscribers of MCC and Delta Telecom). Our share in Sky-Link earnings for the year ended December 31, 2004 was insignificant.

Fixed line communications

MGTS' revenues grew by 26.6% in the year ended December 31, 2004 to $481.6 million, compared to $380.4 million for the year ended December 31, 2003. Revenues from monthly subscription fees increased by 19.5% in the year ended December

31, 2004, compared to the same period in 2003, and reached $244.1 million. This increase was primarily due to an increase in monthly subscription fees for residential and government subscribers effective June 2003, August 2003 and October 2004 while the number of active subscribers increased by 1.3%, to 4.2 million. Revenues from local traffic fees, service activation fees and line rentals increased by 38.3% compared to the year ended December 31, 2003, to $144.7 million.

MGTS is not licensed to provide domestic long distance, international long distance or DLD/ILD telecommunications services directly to its subscribers, but must route such traffic through a DLD/ILD licensed operator. As a result, DLD/ILD traffic originated by MGTS subscribers is carried by Rostelecom, which bills MGTS subscribers directly. MGTS has a revenue sharing agreement with Rostelecom pursuant to which Rostelecom pays MGTS a portion of the DLD/ILD revenues generated by MGTS customers. This amount is periodically revised. MGTS' revenues from Rostelecom amounted to $28.8 million for the year ended December 31, 2004, compared to $24.7 million for the year ended December 31, 2003.

Revenues of MTU-Inform did not change in the year ended December 31, 2004 compared to the year ended December 31, 2003 and remained at $101.3 million, as a result of a moderate growth of business offset by a decrease in tariffs on services provided to mobile operators.

Telmos' revenues grew by 26.1%, to $47.3 million, for the year ended December 31, 2004, compared with $37.5 million for the year ended December 31, 2003, primarily due to the negative effect of a temporary disruption in Telmos' services in February through April 2003 due to damage to its equipment caused by a fire. The increased traffic from fixed line operators also contributed to revenue growth. The number of active lines in service grew to 57,175 as of December 31, 2004, from 55,548 as of December 31, 2003.

MTU-Intel's revenues increased for the year ended December 31, 2004 due to growth in the number of active subscribers of ADSL Internet services. In February 2004, MTU-Intel introduced a new residential focused brand, STREAM, and reduced ADSL tariffs by 50%, which increased the number of subscribers as of December 31, 2004 by 525.0% to 112,332, compared to December 31, 2003. As a result, MTU-Intel's revenues grew by 37.5% from $46.1 million for the year ended December 31, 2003 to $63.4 million for the same period in 2004.

Comstar's revenues increased by 22.3% to $81.3 million for the year ended December 31, 2004 from $66.5 for the year ended December 31, 2003 as a result of growth in the number of active subscribers.

Operating income

The operating income margin of the Telecommunications Segment was 35.3% in the year ended December 31, 2004, compared to 34.0% in the year ended December 31, 2003. This growth was primarily attributable to the increase in the operating income margin of MTS.

Wireless services

MTS' operations contributed $1,453.7 million to our operating income from wireless services for the year ended December 31, 2004.

MTS' operating income margin was 37.1% for the year ended December 31, 2004, compared to 36.2% for the year ended December 31, 2003. The increase in MTS' operating income margin is due to lower interconnection and line rental charges payable to other operators for access to their networks relative to increasing revenues. With the expansion of

MTS' network, more calls are placed and completed solely within its network, thereby avoiding the need to pay such charges to other operators while still fully earning the related revenues from such calls. The increase in MTS' operating income margin was also affected by the lower costs of leasing telecommunication lines compared with MTS' increasing revenues as it builds out its own fiber-optic network in its license areas.

P-Com contributed $7.6 million to our operating income for the year ended December 31, 2003.

Fixed line communications

MGTS' operating income margin for the year ended December 31, 2004 was 20.7%, compared to 21.7% for the year ended December 31, 2003, primarily due to an additional property tax payable on its cable network assets as a result of changes in Russian tax legislation effective January 1, 2004. Operating costs increased by $84.1 million, or 28.2%, for the year ended December 31, 2004.

MTU-Inform's operating income margin decreased to 40.5% for the year ended December 31, 2004, compared with 48.3% in the same period in 2003. The lower operating income margin in the year ended December 31, 2004 was attributable primarily to the decreased tariffs charged to mobile operators forced by competition.

Comstar incurred operating loss of $1.8 million for the year ended December 31, 2004 compared to operating income of $4.8 million for the year ended December 31, 2003.

Telmos' operating income increased to $7.6 million for the year ended December 31, 2004, compared to an operating loss of $2.4 million in the same period of 2003 owing to damage to its equipment and temporary disruption of services caused by a fire in 2003. Telmos' operating margin was 16.1% in the year ended December 31, 2004.

The increase in the number of MTU-Intel subscribers was offset by a continued reduction in tariffs in 2004 for corporate and residential subscribers. Operating costs were $63.9 million in the year ended December 31, 2004, or 100.8% of revenues, compared with $46.5 million, or 100.9% of revenues, in the same period in 2003.

Income from equity investees

Income from equity investees accounted for $27.1 million and $0.5 million for the years ended December 31, 2004 and 2003, respectively. The increase in income from equity investees is primarily caused by the increase in the net income of MTS Belarus and MTT, contributing $23.2 and $8.6 million, respectively, for the year ended December 31, 2004, partially offset by losses from other equity investments.

Technology

As of December 31, 2004, our subsidiaries in the Technology Segment operated along four main divisions: telecommunications equipment manufacturing and software (STROM telecom, its subsidiaries and Mediatel), semiconductor design and manufacturing (Mikron, VZPP-Mikron, NIITM and ICM), electronic devices and consumer electronics (Sitronics, Elion and Elaks) and IT and systems integration (Kvazar-Micro). We added the fourth business division, IT and systems integration, in July 2004 through our acquisition of Kvazar-Micro, a company based in Ukraine with a presence throughout Eastern Europe. Kvazar-Micro, STROM telecom and Micron were the largest sources of revenue in the Technology Segment for the year ended December 31, 2004.

The following table presents the operating results of our Technology Segment for the periods under review:

	Year ended December 31,			
	2003	% of revenue	2004	% of revenue
Revenues	$ 85,942	100.0	$ 498,427	100.0
Costs of sales, exclusive of depreciation and amortization shown separately below	(64,162)	(74.7)	(406,621)	(81.6)
Selling, general and administrative expenses	(20,269)	(23.6)	(39,657)	(8.0)
Depreciation and amortization	(2,862)	(3.3)	(3,484)	(0.7)
Net other operating expenses	(1,997)	(2.3)	(2,747)	(0.5)
Operating income	(3,348)	(3.9)	45,918	9.2
OIBDA[1]	(486)	(0.6)	49,402	9.9

[1] OIBDA represents operating income before depreciation and amortization. OIBDA is not a measure of financial performance under U.S. GAAP. You should not consider it an alternative to net income as a measure of operating performance or to cash flows from operating activities as a measure of liquidity. Our calculation of OIBDA may be different from the calculation used by other companies and therefore comparability may be limited. We believe that OIBDA provides useful information to investors because it is an indicator of the strength and performance of our ongoing business operations, including our ability to fund discretionary spending such as capital expenditures, acquisitions of subsidiaries and other investments and our ability to incur and services debt. While depreciation and amortization are considered operating costs under U.S. GAAP, these expenses primarily represent non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods.

Year ended December 31, 2004 compared to year ended December 31, 2003

Revenues

The revenues of our Technology Segment increased by $412.5 million, or by 480.2%, to $498.4 million during the year ended December 31, 2004. The acquisition of a controlling stake and consolidation of Kvazar-Micro revenues effective January 1, 2004 contributed $293.5 million to the increase of our Technology Segment revenues. Exclusive of the effects of the Kvazar-Micro acquisition, segment revenues would have increased by $119.0 million, or 138.5%, for the year ended December 31, 2004. Revenues of the telecommunications equipment manufacturing and software division grew by 201.5% to $112.6 million, or 55.0% of the total segment revenues, net of the effects of the Kvazar-Micro acquisition, in the year ended December 31, 2004, compared to $37.3 million, or 43.5% of the segment revenues in the year ended December 31, 2003. Revenues of the telecommunications equipment manufacturing and software division for the year ended December 31, 2004 include revenues of Mediatel, which was part of Telecommunications Segment in the year ended December 31, 2003. Mediatel contributed $17.6 million to revenues of telecommunications equipment manufacturing and software division for the year ended December 31, 2004. Revenues of the semiconductor design and manufacturing division grew by 16.3% to $47.9 million, or 23.4% of segment revenues, net of the effects of the Kvazar-Micro acquisition and intra-segment sales, in the year ended December 31, 2004 compared to $41.2 million, or 48.0% of the segment revenues in the year ended December 31, 2003. The electronic devices and consumer electronics division demonstrated considerable growth in the year ended December 31, 2004, with revenues increasing to

$43.9 million, or 21.4% of the segment revenues, net of the effects of the Kvazar-Micro acquisition, from $7.4 million, or 8.6% of the segment revenues, for the same period in 2003. The increase of revenues in the electronic devices and consumer electronics division was a result of the increased production of consumer electronics under the Sitronics umbrella brand during the year ended December 31, 2004, following the rise of demand in the market for Sitronics products due to the extensive advertising campaign.

Operating income

Operating income increased to $45.9 million, or 9.2% of segment revenues, for the year ended December 31, 2004 from an operating loss of $3.3 million in the same period of 2003. The consolidation of the low-margin Kvazar-Micro business contributed $1.5 million to the operating income for the year ended December 31, 2004. The increase in operating income was primarily attributable to the sales of telecommunications equipment to our Telecommunication Segment. Net of the effects of the Kvazar-Micro acquisition, cost of sales increased by 93.6%, to $124.3 million, for the year ended December 31, 2004 compared to $64.2 million for the same period in 2003. Selling, general and administrative expenses decreased as a percentage of sales, net of the effects of the Kvazar-Micro acquisition, to 14.8% for the year ended December 31, 2004 from 23.6% for the same period in 2003 mainly due to the increased volume of production and sales and improved cost efficiency.

Insurance

Our Insurance Segment is represented by ROSNO. ROSNO's principal activities are non-life and life insurance, as well as insurance-related services, such as obligatory insurance. ROSNO's corporate clients are primarily in the telecommunications, oil and gas, banking, retail and manufacturing sectors.

The following table presents the results of operations of our Insurance Segment for the periods under review:

	Year ended December 31,			
	2003	% of revenues	2004	% of revenues
Revenues from financial services	$ 187,929	100%	$ 300,194	100
Financial services related costs, exclusive of depreciation and amortization shown separately below	(118,805)	(63.2)	(192,338)	(64.1)
Selling, general and administrative expenses	(48,280)	(25.7)	(76,408)	(25.5)
Depreciation and amortization	(3,115)	(1.7)	(3,378)	(1.1)
Other operating (expenses)/income	(109)	(0.1)	1,907	0.6
(Loss)/gain from equity investees	(509)	(0.3)	191	0.1
Operating income	$ 17,111	9.1	$ 30,168	10.0

Voluntary medical insurance, motor own damage insurance and property insurance historically have been the largest contributors to our gross premiums written, or GPW. However, the share of voluntary medical insurance, a major component of the total GPW, was decreasing throughout the years 2003 and 2004, from 29% in 2003 to 25% in 2004, respectively. Simultaneously, revenues from obligatory motor third party liability policies, the line of business launched by ROSNO in 2003, has considerably developed and reached 12% of total GPW in

The table below provides a breakdown of our Insurance Segment revenues by business line.

2004. Motor own damage insurance also slightly increased from 15% to 17% of total GPW in 2004 as compared to 2003. GPW for non-life insurance products is equal to the total gross premiums to be forth in change in provision in unearned premiums, net of reinsurance, in the table below.

The table below provides a breakdown of our Insurance Segment revenues by business line.

Year ended December 31,		
	2003	2004
	(Amounts in thousands)	
Voluntary medical insurance	62,223	90,704
Motor third-party liability	3,168	1,946
Motor own damage insurance	33,503	62,458
Property	25,462	40,563
General third-party liability	3,201	8,359
Marine, aviation and transport	7,838	19,871
Personal accident	7,044	6,634
Other non-life liability	2,988	7,556
Life insurance	1,710	1,767
Obligatory motor third-party liability	14,993	43,080
Reinsurance inward	56,117	84,622
Total gross premiums written	218,247	367,560
Reinsurance outwards	(46,580)	(40,105)
Change in provision in unearned premiums, net of reinsurance	(8,355)	(49,921)
Net premiums earned	163,312	277,534
Commission income	8,225	4,507
Medical services income	5,278	6,396
Net gains/(loss) on operations with securities	1,867	(1,865)
Interest income	6,143	7,282
Other income	3,104	6,339
Total revenue	$187,929	$300,19

paid over the term of the insurance policies issued by ROSNO during the period, while GPW for life insurance is equal to premiums due under the policies during the period. Premiums for non-life insurance are recorded as revenue primarily on a pro-rata basis over the terms of the related policies whereas life insurance premiums are recognized as revenue when due from the policyholder.

The adjustments necessary to reconcile GPW to revenue derived from the relevant policies are set

Year ended December 31, 2004 compared to year ended December 31, 2003

Revenues

In the year ended December 31, 2004, our Insuance Segment revenues grew by $112.3 million, or 59.8%, compared to the year 2003, as we continued to expand our client base. Voluntary medical insurance, motor own damage and property insurance together accounted for $193.7 million, or 52.7%, of GPW for the year ended December 31, 2004. GPW on obligatory motor third-party liability insurance, which we commenced writing in July 2003, accounted for $43.1 million, or 11.7%, of our GPW for the year 2004.

GPW on property insurance increased to $40.6 million for the year ended December 31, 2004, or by 59.2%, compared to $25.5 million for the year ended December 31, 2003, primarily due to the consolidation in the year ended December 31, 2004 of operations of Leader which we acquired from RAO UES in October 2004.

Overall, GPW increased by 68.4%, to $367.6 million, in the year ended December 31, 2004, in comparison to $218.2 million in the year 2003 following the insurance business expansion.

Operating income

As a result of ROSNO's expansion of its operations, the operating income of our Insurance Segment increased to $30.2 million in the year ended December 31, 2004 from $17.1 million in the year ended December 31, 2003. The operating income margin increased to 10.0% in the year ended December 31, 2004 from 9.1% in the year ended December 31, 2003. General and administrative expenses of the segment increased to $76.4 million in the year ended December 31, 2004 from $48.2 million in the year ended December 31, 2003 primarily due to an increase in payroll costs and advertising and marketing expenses.

Total assets

The total assets of our Insurance Segment increased to $421.0 million as of December 31, 2004 from $265.7 million as of December 31, 2003, or by 58.4%. This increase is primarily attributable to an increase in cash and bank deposits of $79.4 million, in receivables from insurance operations of $33.8 million, and in loans and notes receivable of $32.0 million.

Banking

Our Banking Segment is represented by MBRD, which provides a broad range of services. Historically, MBRD primarily performed treasury functions for companies in or related to our consolidated group. Accordingly, MBRD's revenues are primarily derived from our subsidiaries and related parties. We are currently focusing on developing and expanding MBRD's retail banking business in Moscow and major cities throughout Russia. As of December 31, 2004, MBRD operated in Moscow and in four additional regions.

The following table summarizes MBRD's financial performance for the periods indicated:

Year ended December 31, 2004				
	2003	% of revenues	2004	% of revenues
	(Amounts in thousands, except percentages)			
Revenues from financial services	$ 57,513	100	$ 65,738	100
Including:				
Revenues from consolidated companies	10,321	17.9	22,788	34.7
Revenues from related parties	11,730	20.4	1,971	3.0
Financial services related costs, exclusive of depreciation and amortization shown separately below(1)	(27,635)	(48.1)	(31,075)	(47.3)
Selling, general and administrative expenses	(27,180)	(47.3)	(22,950)	(34.9)
Depreciation and amortization	(620)	(1.1)	(1,119)	(1.7)
Income from equity investees	490	0.9	1,097	1.7
Operating income	$ 2,568	4.5	$ 11,691	17.8

(1) Includes interest expense on deposits.

Year ended December 31, 2004 compared to year ended December 31, 2003

Revenues

For the year ended December 31, 2004, compared with the year ended December 31, 2003, MBRD's revenues increased by 14.3%, to $65.7 million. Interest income grew by $8.6 million in the year ended December 31, 2004 and amounted to $57.2 million. This growth was mainly attributable to interest on loans to customers. As of December 31, 2004, loans to customers, net of allowances for loan losses, increased by 44.0% to $444.3 million, including $238.1 million, or 53.6%, of inter-company loans and $23.5 million, or 5.3%, of loans to our related parties. As of December 31, 2004, the weighted average interest on inter-company loans was 12.0% on U.S. dollar-denominated loans (which totaled $109.5 million) and 11.0% for ruble-denominated loans (which totaled $128.5 million). The weighted average interest rate on U.S. dollar-denominated loans to related parties was 10.0%. Loans to third-party customers, net of allowance for loan losses, increased by $115.1 million to $182.7 million in 2004. The weighted average interest rate on loans to third-party customers was 9.6% for ruble-denominated loans and 7.5% for U.S. dollar-denominated loans as of December 31, 2004.

Operating income

Banking Segment's operating income amounted to $11.7 million in the year ended December 31, 2004, compared to $2.6 million for the same period in 2003, mostly due to an increase in the volume of MBRD's lending operations in 2004.

Selling, general and administrative expenses as a percent of revenues decreased to 34.9% in 2004 from 47.3% in 2003 as a result of a decrease in allowances for loan losses.

Income from equity investees

Income from equity investees of $1.1 million recorded in the operating income of the segment in the year ended December 31, 2004 represents our share of the net income of East-West United Bank. We continued to increase our share in the EWUB during the year 2004 up to 49% as of December 31, 2004.

Total assets

Total assets of the Banking Segment decreased to $519.8 million as of December 31, 2004 from $595.5 million as of December 31, 2003 mainly due to the decrease of loans issued to related parties to $23.5 million as of December 31, 2004 compared to $151.6 million as of December 31, 2003.

Other Businesses

In this segment we include our real estate, retail, media, travel services and miscellaneous businesses, as well as operations of our parent company, Sistema. Thus, costs of our corporate function (other than Sistema Telecom) are included in the operating costs of this segment. These costs amounted to $41.7 million for the year ended December 31, 2004, compared to $21.4 million in 2003.

In our real estate businesses, we are a leading real estate owner, developer and manager predominantly focused on the Moscow market in the segments of Class A and B offices, elite housing, cottages and land development. We have been in the real estate business since the early 1990s, making real estate one of our first businesses. Since 1994, we have successfully completed more than 20 projects totaling over 150,000 sq.m. of space.

We operate our retail business through Detsky Mir, the largest retailer of children's goods in Russia. Detsky Mir is among the most recognized brands in Russia. As of December 31, 2004, we

Year ended December 31,				
	2003	% of revenues	2004	% of revenues
	(Amounts in thousands, except percentages)			
Revenues	$ 249,658	100.0	$ 385,259	100.0
Cost of sales, exclusieve of depreciation and amortization shown separately below	(170,789)	(68.4)	(268,320)	(69.6)
Selling, general and administrative expenses	(75,564)	(30.3)	(127,638)	(33.1)
Depreciation and amortization	(7,735)	(3.1)	(8,236)	(2.1)
Net other operating income/(expenses)	(11,746)	(4.7)	(14,358)	(3.8)
Income/(loss) from equity investees	45	0.0	(1,491)	(0.4)
Net gain/(loss) on disposal of subsidiaries	-	-	2,184	0.5
Operating income/(loss)	$ (16,131)	(6.5)	$ (32,600)	(8.5)

operated nine stores in Moscow, including the flagship Detsky Mir store in central Moscow, and four stores outside of Moscow with a total retail space of 42,868 sq.m. We plan to expand Detsky Mir by opening new stores in Moscow and other Russian cities and to undertake a significant refurbishment of our flagship store.

We operate our media businesses mainly through Sistema Mass Media, a holding company that is active in three main areas: advertising, print distribution and other media, which includes a number of companies that operate in other segments such as publishing, film production and news services. Following a strategic review of our media assets in 2003, we are primarily focused on developing distribution platforms and content for pay-TV and multi-media services initially in Moscow and subsequently in other parts of Russia.

Our travel services business consists of Intourist, a Moscow-based tour operator. Intourist is one of the leading Russian providers of travel and leisure services and operates its business through 40 Russian and five foreign subsidiaries.

Our miscellaneous businesses consist of radio and space technology, pharmaceuticals and biotechnology and international operations.

Year ended December 31, 2004 compared to the year ended December 31, 2003

Revenues

Total operating revenues of the Other Businesses Segment increased to $385.3 million for the year ended December 31, 2004, compared to $249.7 million for the year ended December 31, 2003.

Real estate revenues increased by $51.3 million, to $90.4 million, for the year ended December 31, 2004 over the year ended December 31, 2003. The increase is primarily attributable to the completion and sale of real estate projects during the year ended December 31, 2004, including two residential properties and two office buildings in Moscow.

In our retail business, revenues increased by 42.9%, to $79.3 million, for the year ended December 31, 2004 from $55.5 million for the year ended December 31, 2003. The increase was mostly generated by revenues of our new retail outlets.

Mass media revenues increased to $36.2 million, or by 2.8%, during the year ended December 31, 2004 compared to $35.2 million in the year ended December 31, 2003, primarily due to an increase in print distribution revenues.

The total operating revenues of our travel services business for the year ended December 31, 2004 were $96.6 million compared with $62.1 million for the year ended December 31, 2003, representing growth of 55.6%. During the year ended December 31, 2004, the number of inbound tourists served increased to 164,259 or by 16.0% compared to the year ended December 31, 2003, while the number of outbound tourists increased to 78,348, or by 45.2%, compared to the year ended December 31, 2003.

Operating loss

For the Other Businesses Segment, operating losses increased during the year ended December 31, 2004 to $38.3 million from $16.1 million in the year ended December 31, 2003, mostly due to charity expenses of $17.1 million paid by our corporate office and bonuses of $19.4 million accrued during the year ended December 31, 2004, which was partially offset by improved financial results in our real estate, media and travel services business.

In the real estate business, operating income for 2004 increased to $23.5 million, from $10.3 million for 2003. The increase resulted from the completion and sale of four real estate projects in 2004.

In our retail business, operating income during the year ended December 31, 2004 increased to $8.8 million, compared with $6.8 million in the year ended December 31, 2003, as a result of an increase in the number of retail outlets.

In the media business, we reduced operating losses during 2004 to 2.6% of total revenue, or $0.9 million, from an operating loss of $4.4 million in the year ended December 31, 2003.

In our travel services business, operating income, as a percentage of revenues, increased to 2.9% during the year ended December 31, 2004, compared to an operating loss of 3.1% in the year ended December 31, 2003. The increase was due to our focus on the sale of travel packages, including quality transportation and accommodation which, in turn, resulted in an increase in the gross margin for the tour packages sold.

Telecommunications Operating Data

Our revenues and operating income for the years ended December 31, 2004 and 2003 were influenced by trends in the principal businesses included in our Telecommunications Segment: MTS, MGTS and Comstar UTS. The following discussion contains certain operating data relating to each of the principal businesses in our Telecommunications Segment.

MTS

The following tables show the number of MTS' subscribers and average monthly service revenue per subscriber as of the dates indicated.

In 2003, the subscriber base increased by 151.7% from 6.6 million as of December 31, 2002 to 16.7 million as of December 31, 2003. These trends continued in 2004, with MTS' subscriber base increasing by 104.7%, from 16.7 million as of December 31, 2003 to 34.2 million as of December 31, 2004. A portion of the growth in the subscriber base was due to acquisitions during the year ended December 31, 2004, including Uzdunrobita, Primtelefon, Gorizont RT, Telesot Alania with 0.3, 0.2, 0.1 and 0.1 million subscribers, respectively. MTS' organic growth in revenues amounted to $1,148.1 million, or 43.52% in the year 2004 as compared to the year 2003, while MTS acquisitions in the year 2004 contributed $131.9 million

At December 31,			
	2002	2003	2004
	(Amounts in thousands, except average monthly service revenue per subscriber)		
Subscribers[1]			
Russia	6,644	13,370	26,540
MTS OJSC	3,746	6,529	13,398
Moscow license area	3,082	4,936	7,516
Telecom XXI	854	1,666	2,733
Kuban-GSM	844	1,396	2,543
Russian regions	1,200	3,779	7,866
UMC	n/a	3,350	7,373
Uzbekistan (Uzdunrobita)	n/a	n/a	311
Total	6,644	16,720	34,224
Average monthly service revenue per subscriber			
Russia	$ 23	$ 17	$ 12
Ukraine	n/a	$ 15[2]	$ 13

[1] MTS defines a "subscriber" as an individual or organization whose account shows chargeable activity within 61 days (or 183 days in the case of the "Jeans" and "SIM-SIM" brand tariffs) and whose account does not have a negative balance for more than this period. Prior to October 1, 2004, UMC used a 90-day period for such purposes with respect to its "Jeans" and "SIM-SIM" subscribers.

[2] Calculated based on the months of March through December 2003.

to our revenues for the year ended December 31, 2004.

Average monthly service revenue per subscriber in Russia fell from $23 in 2002 to $17 in 2003, due to the decrease in tariffs in the Moscow license area, an increase of mass-market subscribers in MTS' subscriber mix and its continued expansion into the regions of Russia outside of the Moscow license area where tariffs are lower. This trend continued in 2004. Average monthly service revenue per subscriber in Russia in 2004 decreased to $12. In 2004 more than half of MTS' subscriber growth occurred outside of the Moscow license area. However, as a result of competition and the tariff structure in the Russian regions outside of the Moscow license area, MTS' average revenue per subscriber in the Russian regions remains lower than in the Moscow license area, though costs are generally lower there as well. MTS generally expects to see a continued decline in average monthly service revenue per subscriber due to the introduction of lower tariff plans in connection with its marketing efforts.

UMC has experienced subscriber growth from 3.4 million subscribers at December 31, 2003 to 7.4 million subscribers at December 31, 2004, and we expect this trend to continue, assuming the Ukrainian economy continues to grow. Average monthly service revenue per subscriber decreased in 2004 as a result of an extensive marketing campaign focused on penetration to the mass-market.

MTS' subscriber churn in Russia increased from 33.9% in 2002 to 47.3% in 2003. This trend was reversed in 2004 as a result of MTS marketing initiatives, targeted to raise subscriber loyalty. MTS' subscriber churn for the year ended December 31, 2004 was 27.5%. Although its subscriber churn in Russia decreased for the year ended December 31, 2004, MTS believes that subscriber

	Year ended December 31,		
	2002	2003	2004
Subscriber churn[3]			
Russia	33.9%	47.3%	27.5%
Ukraine[1]	n/a	23.8%	15.8%[2]

[1] Annualized value calculated based on the months of March through December 2003.

[2] In the fourth quarter of 2004, UMC changed its subscriber base calculation method. From October 1, 2004, the subscriber churn period is set at 61 day for UMC subscribers, as opposed to 90-day period prior to October 1, 2004, consistent with the churn period MTS use with respect to its subscribers in Russia. Under the previous churn policy, the 2004 churn rate in 2004 was 23%.

[3] MTS defines churn as the total number of subscribers who cease to be a subscriber (as defined above) during the period (whether involuntarily due to non-payment or voluntarily, at such subscriber's request), expressed as a percentage of the average number of our subscribers during that period.

churn is highly dependent on competition and the number of mass-market subscribers in its overall subscriber mix. Mass-market subscribers generally choose to prepay their mobile phone usage by purchasing pre-paid packages and are more likely to switch providers to take advantage of low-tariff promotions. As a result, competition for these subscribers will likely lead to sustained downward pressure on tariffs. The other reasons for increases in subscriber churn are the absence of service contracts with subscribers in Russia that contain minimal periods of usage and the absence of connection fees, which generally prevent a subscriber's early churn. In order to decrease subscriber churn, in 2004 MTS launched a new marketing campaign that provides a 15% discount for services rendered to certain contract subscribers if they do not terminate their contracts within one year of activation. Churn, as MTS uses it, includes internal churn within its subscriber base, i.e., MTS' subscribers switching between different tariff plans we offer. Internal churn increased following the launch in November 2002 of the "Jeans" tariff plan.

MGTS

MGTS' revenues are dependent on the regulated tariffs approved by the Federal Tariff Service. The following table illustrates MGTS' regulated tariff development in the period from January 1, 2002 to December 31, 2004.

Comstar UTS

Comstar UTS operates in three major segments: corporate and public voice and data services; carrier and operator services; and Internet services. The following table shows the number of Comstar UTS subscribers and active service lines as of the dates indicated.

The number of subscribers for corporate and public voice and data services increased during the years 2003 and 2004. The increase in the total number of subscribers equaled to 11.5% and 5.2% for the years ended December 31, 2003 and 2004, respectively.

The total number of subscribers for our Internet services increased by 29.1% for the year ended December 31, 2003 and decreased by 11.9% for the year ended December 31, 2004. For the year ended December 31, 2004 the number of dial-up subscribers decreased by 150,202, or by 33.1%, while the number of ADSL subscribers increased by 94,358, or by 525.0%.

The total number of active lines for carrier and operator services increased by 3.3% for the year ended December 31, 2004, while was approximately the same for the years ended December 31, 2002 and December 31, 2003.

	At December 31,	
	2003 г.	2004 г.
Corporate and public voice services	206,175	216,970
Comstar	55,896	57,128
Telmos	35,361	36,988
MTU-Inform	114,918	122,854
Corporate data services (Golden Line)	3,375	3,944
Internet services (MTU-Intel)	471,124	415,280
Dial-up subscribers	453,150	302,948
ADSL subscribers	17,974	112,332
Carrier and operator services	303,571	313,574
Comstar	13,993	23,993
Telmos	20,187	20,187
MTU-Inform	269,391	269,394

	Jan 1, 2002	Nov 1, 2002	June 1, 2003	Aug 1, 2003	Oct 1, 2004
Monthly subscription fee					
Residential subscribers(1)	2.7	3.5	4.1	4.6	5.8
Public sector subscribers(2)	3.3	3.9	4.1	4.6	5.8
Corporate subscribers(2)	5.5	5.2	5.4	5.5	6.8
Local call charges					
Public sector subscribers(3)	0.005	0.004	0.005	0.005	0.005
Corporate subscribers(3)	0.013	0.013	0.013	0.013	0.014
Exchange rate (rubles per U.S. dollar)(4)	30.10	31.70	30.71	30.28	29.22

(1) Includes value added tax
(2) Includes 613 "free" minutes per month
(3) Per minute charge for traffic exceeding the monthly "free" minutes.
(4) As of the date the tariff change became effective.

Liquidity and Capital Resources

We use a variety of sources to finance our operations, both external and internal. In addition to net cash provided by operations, our companies use short- and long-term borrowings to fund capital expenditures and strategic investments. Short- and long-term funding sources may change with time, but currently include notes issued in the international and Russian capital markets and credit facilities with international and Russian banks, denominated in both rubles and foreign currencies. In January, April, August, October 2003 and January 2004, we (including MTS) raised approximately $396.0 million, $340.6 million, $297.0 million, $396.0 million and $350.0 million, respectively, through U.S. dollar-denominated bond offerings in the international capital markets. MTS repaid its $300.0 million notes in May 2004 with the proceeds of a short-term bridge loan and operating cash flows. In September 2004, MTS entered into a $600.0 million syndicated loan facility provided by international financial institutions. In December 2004, MTS repaid 10.95% notes due 2004 in principal amount of $300 million from drawings on the syndicated loan facility, which significantly improved our working capital position as the notes were included in short-term liabilities.

Our parent company, Sistema, is a holding company with direct operations mostly limited to certain functions for our group, including budgeting, corporate finance, strategic development and public relations. The ability of Sistema to repay its debts depends primarily upon the receipt of dividends, distributions and other payments from our subsidiaries, proceeds from the sale of subsidiaries and from additional borrowings. In February 2005, Sistema completed its initial public offering on the London Stock Exchange. The amount of proceeds, net of related expenses, equaled to $1,284.6 million. We plan to invest the proceeds from the offering primarily in the purchase of long-term assets.

We expect to repay all long-term debts as they become due from our operating cash flows or through re-financings. See Notes 20, 21 and 22 to our audited consolidated financial statements for a description of our indebtedness.

Working capital

Working capital is defined as current assets less current liabilities. As of the date hereof, we believe our working capital is sufficient for our present requirements. As of December 31, 2004, we had a positive working capital of $10.3 million, compared to a deficit of $541.1 million as of December 31, 2003.

Our working capital turned to positive as we refinanced a portion of our short-term debt with the proceeds from long-term borrowings during the year ended December 31, 2004. Following the receipt of proceeds from our initial public offering in February 2005, our positive working capital significantly increased further.

Credit Ratings

Our credit ratings impact our ability to obtain short- and long-term financing, and the cost of such financing. In determining our credit ratings, the rating agencies consider a number of factors, including our operating cash flows, total debt outstanding, commitments, interest requirements, liquidity needs and availability of liquidity. Other factors considered may include our business strategy, the condition of our industry and our position within the industry. Although we understand that these and other factors are among those considered by the rating agencies, each agency might calculate and weigh each factor differently.

The credit ratings of our parent company and our subsidiaries as of the date of this document were as follows:

Name of issuer	Rating Agency	Date of Rating	Long-term Debt Rating	Outlook / Watch
Sistema	Standard & Poor's	March 24, 2005	BB-	Stable
Sistema	Fitch	February 17, 2005	B+	Stable
Sistema	Moody's	November 19, 2003	B1	Stable
MTS	Moody's	December 10, 2001	Ba3	Stable
MTS	Standard & Poor's	March 24, 2005	BB-	Stable
MGTS	Standard & Poor's	March 24, 2005	BB-	Stable
MBRD	Fitch	February 17, 2005	B	Stable
MBRD	Moody's	December 14, 2004	B1	Stable

None of our existing indebtedness has any triggers related to our credit ratings.

Capital Requirements

We need funding to finance the following:

- capital expenditures, consisting of purchases of property, plant and equipment and intangible assets;
- acquisitions;
- repayment of debt;
- changes in working capital; and
- general corporate activities, including dividends.

We anticipate that capital expenditures, acquisitions and repayment of long-term debt will represent the most significant uses of funds for several years to come.

Our capital expenditures in 2003 and 2004 were $1,212.9 million and $1,627.0 million, respectively. We expect to continue to finance most of our capital expenditure needs through our operating cash flows, and to the extent required, to incur additional indebtedness through borrowings or additional capital raising activities. Historically, a significant portion of our capital expenditures have been related to the installation and build out of our telecommunication networks and expansion into new license areas. Our future expenditures may be higher, in particular if licenses relating to new telecommunication technologies become available and our investment program for expansion and full digitalization of the Moscow public switch telephone network will be implemented. We expect that capital expenditures will remain a large portion of our cash outflows in connection with the continued installation and build out of our networks.

In addition to our capital expenditures, we spent $1,005.5 million, and $338.9 million in 2003 and 2004, respectively, to acquire businesses. We may continue to expand our business through acquisitions. Our cash requirements relating to potential acquisitions can vary significantly based on market opportunities.

We expect to refinance most of our existing debt when it becomes due. In May 2004, MTS retired $300 million in principal amount of our Floating Rate Notes due August 2004 with the proceeds of a $200.0 million short-term bridge loan from Credit Suisse First Boston International and operating cash flows. This $200.0 million bridge loan was repaid from MTS' operating cash flows and drawings on the syndicated loan facility described above. In December 2004, MTS repaid its 10.95% notes due 2004 in principal amount of $300.0 million from further drawings on the syndicated loan facility.

Capital Resources

We plan to finance our capital requirements through operating cash flows and financing activities, as described above. We do not depend on off-balance sheet financing arrangements.

At December 31, 2004, our debt was comprised of the following:

	Currency	Annual interest rate (Actual at December 31, 2004)	December 31 2004
Sistema Finance Notes	USD	10.3%	$348,808
Sistema Capital Notes	USD	8.9%	350,000
MTS Finance Notes due 2010	USD	8.4%	400,000
MTS Finance Notes due 2008	USD	9.8%	400,000
MGTS Bonds	RUR	10%-12.3%	90,094
Micron Bonds	RUR	15.0%	6,293
Total Corporate Bonds			1,595,195
Syndicated Loan	USD	LIBOR+2.5% (5.3%)	600,000
EBRD	USD	LIBOR+3.1% (5.9%)	150,000
Credit Suisse First Boston	USD	LIBOR+2.2% (4.8%)	140,000
HSBC Bank plc and ING-BHF-Bank	USD	LIBOR+0.4% (3.2%)	77,003
Hermes Credit Facility	EUR	EURIBOR+0.7% (2.9%)	63,851
ING-Bank (Eurasia)	USD	LIBOR+2.3%-4.2% (4.8%-6.7%)	46,667
Vendor Financing	Various	Various	33,181
Commerzbank (Eurasia)	USD	LIBOR+1.4%-5.0% (4.0%-7.4%)	47,213
Raiffeisenbank	USD	LIBOR+5.0%-7.0% (7.6%-9.6%)	19,684
HSBC	USD	LIBOR+2.8% (5.2%)	17,500
Ericsson Project Finance	USD	LIBOR+4.0% (6.6%)	14,850
Sberbank	RUR	10.0%-20.3%	27,547
Vneshtorgbank	USD, EUR	LIBOR+4.9% (7.3%), EURIBOR+5.6% (7.8%), 11.0%-13.0%	24,482
Citibank	USD	LIBOR+1.6% (4.2%)	15,144
Nordea Bank Sweden	USD	LIBOR+0.4% (3.0%)	6,500
West LB	USD, EUR	LIBOR+6.8% (9.4%)	
EURIBOR+2% (4.2%)		9,000	
Loans from related parties	Various	Various	107,854
Other	Various	Various	60,892
			3,056,563
Less amounts maturing within one year			(562,041)
Total			$ 2,494,522

The following table presents the aggregate scheduled maturities of debt principal outstanding as of December 31, 2004:

Payments due in the year ended December 31,	(In thousands)
2005	$562,041
2006	432,315
2007	333,029
2008	799,834
2009	97,943
Thereafter	831,401
Total	$ 3,056,563

In addition, we had capital lease obligations in the amount of $8.3 million as of December 31, 2004. The terms of our material debt obligations and capital lease obligations are described in Notes 20, 21 and 22, respectively, to our consolidated financial statements.

Our ability to incur further indebtedness is limited by the covenants in our outstanding notes, including (i) consolidated indebtedness to consolidated EBITDA test (as defined in the indenture relating to the notes), (ii) MTS' debt/cash flow incurrence test. The covenants in our outstanding notes also limit our ability to grant liens on our properties and to enter into mergers, acquisitions, sales and sale-leaseback transactions.

The following table presents a summary of our cash flows and cash outlays for capital expenditures and acquisitions of subsidiaries:

	Year ended December 31,	
	2003	2004
	(Amounts in thousands)	
Cash flows		
Net cash provided by operating activities	$ 986,402	$ 1,904,071
Net cash used in investing activities	(2,365,236)	(2,064,436)
Net cash provided by financing activities	1,504,732	380,947
Net increase in cash	125,898	220,582
Cash outlays for		
Capital expenditures[1]	(1,184,828)	(1,670,599)
Acquisition of subsidiaries, net of cash acquired	(1,005,451)	(338,906)

[1] Includes acquisition of property, plant and equipment, intangible assets and principal payments on capital lease obligations.

During the periods under review, our operating activities generated positive cash flows due to growth through organic growth and acquisitions. During the same periods, our investing activities generated negative cash flows due primarily to increases in capital expenditures in connection with the development of our telecommunications network and the acquisitions of new businesses. We expect for the foreseeable future to continue to use cash in investing activities as we continue to expand our telecommunications network in the Moscow region, into the regions outside of Moscow and into other CIS countries. We also intend to continue to expand our business through acquisitions. We intend to finance our future investments primarily through net cash flows from operations and the incurrence of additional indebtedness. The availability of financing is influenced by many factors, including our profitability, operating cash flows, debt levels, contractual restrictions and market conditions.

Liquidity

As of December 31, 2004 and 2003, we had total cash and cash equivalents of $503.7 million and $283.2 million, respectively. In addition, as of December 31, 2004 and 2003, we had short-term investments of $207.3 million and $278.9 million, respectively, mostly in corporate and municipal bonds and bank deposits.

For details of external financing refer to Notes 20, 21 and 22 to our audited consolidated financial statements. For subsequent events related to our external financing, refer to Note 31 to our audited consolidated financial statements.

Because most of our operating subsidiaries are incorporated in Russia, their ability to pay dividends to us is limited by provisions of Russian law. For example, Russian law requires that, among other things, dividends can only be paid in an amount not exceeding net profits as determined under Russian accounting standards. In addition, dividends may only be paid if the value of the company's net assets is not less than the sum of the company's charter capital, the company's reserve fund and the difference between the liquidation value and the par value of the issued and outstanding preferred stock of the company, if any, as determined under Russian accounting standards. In May 2005, MTS's Board of directors recommended to the shareholders to approve cash dividends of RUR 5.75 (equivalent of $0.21 as of the announcement date) per share for the year 2004, for the total of approximately $402.6 million, which was approved by the Shareholders' meeting on June 21, 2005. This is an almost two-times increase from $218.8 million announced and paid for the year 2003.

In June 2005, the shareholders of JSFC Sistema approved cash dividends of RUR 26.0 (equivalent of $0.91 as of the announcement date) per share for the year ended December 31, 2004, for the total of approximately $8.8 million. Whereas the dividends paid by JSFC Sistema for the year ended December 31, 2003 amounted to $5.2 million.

Competition

We operate in some of the most competitive industries in Russia, including telecommunications, technology, insurance and banking. Our businesses confront aggressive pricing practices, evolving customer demand patterns and changing technologies.

For example, in the Telecommunications Segment, our wireless business is subject to increasing competition from a number of existing and emerging companies, resulting in pricing pressures and lower margins. We compete with at least one other mobile cellular operator in each of our markets. The competition has evolved in recent years to exist primarily between MTS, Vimpelcom and MegaFon, each of which has effective national coverage in Russia. Competition is based largely on local tariff prices and secondarily on network coverage and quality, the level of customer service provided, roaming and international tariffs and the range of services offered.

We compete with a number of alternative fixed line operators servicing Moscow, St. Petersburg and other commercial centers. Intensifying competition in Moscow's alternative carrier market has resulted in increasing pressure on prices and profitability for all operators. Smaller companies with insufficient scale and limited resources are focusing on niche segments of the market while large players act as market consolidators. As a result, the alternative carrier market is presently dominated by two large operators: the companies comprising Comstar UTS and the companies forming the Golden Telecom group.

Market risks

Foreign Currency Risk

The following tables show, for the periods indicated, certain information regarding the exchange rate between the ruble and the U.S. dollar, based on data published by the Central Bank of Russia. These rates may differ from the actual rates used in preparation of our financial statements and other financial information provided herein.

	Rubles per U.S. dollar			
	High	Low	Average[1]	Period End
Year ended December 31,				
2000	28.87	26.90	28.13	28.16
2001	30.30	28.16	29.22	30.14
2002	31.86	30.14	31.39	31.78
2003	31.88	29.25	30.61	29.45
2004	29.45	27.75	28.73	27.75

[1] The average of the exchange rates on the last business day of each full month during the relevant period.

The following tables show, for the periods indicated, certain information regarding the exchange rate between the hryvnia and the U.S. dollar, based on data published by the National Bank of Ukraine. These rates may differ from the actual rates used in preparation of our financial statements and other financial information provided herein.

Our principal exchange rate risk involves changes in the value of the ruble and the euro relative to the U.S. dollar. As a result of inflation in Russia and Ukraine, we link our monetary assets and transactions, when possible, to the U.S. dollar. We have not entered into any significant currency hedging arrangements.

	Hryvnias per U.S. dollar			
	High	Low	Average[1]	Period End
Year ended December 31,				
2000	5.60	5.22	5.44	5.43
2001	5.43	5.27	5.37	5.30
2002	5.33	5.30	5.33	5.33
2003	5.33	5.33	5.33	5.33
2004	5.33	5.31	5.32	5.31

[1] The average of the exchange rates on the last business day of each full month during the relevant period.

A significant part of our capital expenditures and operating and borrowing costs are either denominated in U.S. dollars or tightly linked to the U.S. dollar exchange rate. These mostly include salaries, capital expenditures and borrowings. In order to hedge against a significant portion of this risk, we also denominate tariffs for our unregulated telecommunication services in Russia, which are payable in rubles, in units linked to the U.S. dollar and require accounts to be settled at the official rate of the Russian Central Bank on the date of payment.

If the ruble or the hryvnia decline against the U.S. dollar and tariffs for our telecommunication services cannot be maintained for competitive or other reasons, our operating margins could be adversely affected and we could have difficulty repaying or refinancing our U.S. dollar-denominated indebtedness. Our investment in monetary assets denominated in rubles and hryvnias is also subject to risk of loss in U.S. dollar terms. In particular, we are unable economically to hedge the risks associated with our ruble and hryvnia bank or deposit accounts. Generally, as the value of the ruble or the hryvnia declines, our net ruble and hryvnia monetary asset position results in currency remeasurement losses.

A portion of our capital expenditures and operating and borrowing costs are denominated in euro. These include capital expenditures and certain borrowings. We currently do not hedge against the risk of decline in the U.S. dollar against the euro because settlements denominated in euros are not significant.

Inflation and Exchange Rates

The Russian economy has been characterized by high rates of inflation:

Year	Inflation rate
2000	20.2
2001	18.6
2002	15.1
2003	12.0
2004	11.7

The Ukrainian economy has been characterized by varying rates of inflation:

Year	Inflation rate
2000	25.8
2001	6.1
2002	(0.6)
2003	8.2
2004	12.3

Over the past several years, the rate of increase in the consumer price index in Russia has steadily declined, due to conservative fiscal and monetary policies and the resulting federal budget surpluses. However, inflation remains high in comparison to developed countries.

We link the unregulated tariffs of our telecommunications business to the U.S. dollar. While a majority of our costs are denominated in U.S. dollars or are closely tied to the U.S. dollar, certain of our costs, including salaries and utility costs, are sensitive to rises in the general price level in Russia. During the years ended December 31, 2001 and 2002, the ruble was devaluating against the U.S. dollar. However, the rate of inflation exceeded the rate of devaluation, resulting in real appreciation of the ruble. During the year ended December 31, 2003 and nine months ended September 30, 2004, the ruble appreciated against the U.S. dollar, both in terms of the nominal exchange rate and real appreciation. We would expect increases in ruble-denominated costs, driven by real appreciation of the ruble to put pressure on our margins. While we could seek to raise our prices and tariffs to compensate for such increases in costs, competitive pressures may not permit increases that are sufficient to preserve our operating margins. Accordingly, high rates of inflation in Russia relative to the nominal rate of devaluation could materially adversely affect our results of operations.

Overall, while the sharp decline in the value of the ruble in both nominal and real terms in the immediate aftermath of the 1998 financial crisis supported business growth and helped us to achieve positive results across most of our business lines, the subsequent appreciation of the ruble in real terms and in nominal terms for the year ended December 31, 2003 and the year ended December 31, 2004 has increased our costs in Russia.

Interest Rate Risk

We are exposed to variability in cash flow risk related to our variable interest rate debt and exposed to fair value risk related to our fixed-rate notes. As of December 31, 2004, approximately $1,217.2 million, or 39.7% of our total indebtedness, including capital leases, was variable interest rate debt, while $1,847.7 million, or 60.3% of our total indebtedness, including capital leases, was fixed interest rate debt. In December 2004, we entered into two interest rate swap agreements with respect to $250.0 million of variable-rate indebtedness. We continue to consider other financial instruments available to us on the market to mitigate exposure to variability in the interest rates.

	December 31,								
	Currency	2005	2006	2007	2008	2009	Following periods	Total	Average rate at December 31, 2004 (Amounts in thousands)
Syndicated Loan	USD	140.000	280.000	180.000	–	–	–	600.000	LIBOR+2.5% (5.3%)
EBRD	USD	11.538	23.077	23.077	23.077	23.077	46.154	150.000	LIBOR+3.1% (5.9%)
HSBC Bank plc and ING-BHF-Bank	USD	9.929	9.929	9.929	9.928	9.929	27.359	77.003	LIBOR+0.4% (3.2%)
ING-Bank (Eurasia)	USD	26.667	20.000	–	–	–	–	46.667	LIBOR+2.3%-4.2% (4.8%-6.7%)
Commerzbank (Eurasia)	USD	1.192	592	–	–	–	–	1.784	LIBOR+1.4% (3.8%)
Commerzbank (Eurasia)	USD	16.929	8.500	–	–	–	–	25.429	LIBOR+3.5% (5.9%)
Raiffeisenbank	USD	3.750	–	–	–	–	–	3.750	LIBOR+5.0% (7.6%)
Raiffeisenbank	USD	2.291	2.291	2.501	2.691	2.916	3.244	15.934	LIBOR+7.0% (9.6%)
HSBC	USD	10.000	7.500	–	–	–	–	17.500	LIBOR+2.8% (5.2%)
Ericsson Project Finance	USD	11.700	3.150	–	–	–	–	14.850	LIBOR+4.0% (6.6%)
Vneshtorgbank	USD	872	–	–	–	–	–	872	LIBOR+8.0% (10.4%)
Vneshtorgbank	USD	3.702	1.961	959	–	–	–	6.622	LIBOR+4.9% (7.1%)
Citibank	USD	2.548	4.012	3.450	3.450	1.684	–	15.144	LIBOR+1.6% (4.2%)
Nordea Bank Sweden	USD	3.250	3.250	–	–	–		6.500	LIBOR+0.4% (3.0%)
Credit Suisse First Boston	USD	140.000	–	–	–	–	–	140.000	LIBOR+2.2% (4.8%)
Commerzbank (Eurasia)	USD	20.000	–	–	–	–	–	20.000	LIBOR+5.0% (7.4%)
Total USD variable debt		404.368	364.262	219.916	39.147	37.605	76.757	1,142,055	
Weighted average USD interest rate		5.3%	5.3%	5.3%	5.2%	5.2%	5.1%	5.3%	
Hermes Credit Facility	EUR	14.189	14.189	14.189	14.189	7.095	–	63.852	EURIBOR+0.7% (2.9%)
Vneshtorgbank	EUR	1.454	1.454	1.454	1.454	1.454	–	7.271	EURIBOR+5.6% (7.8%)
West LB International S.A	EUR	–	4.000	–	–	–	–	4.000	EURIBOR+2.0% (4.2%)
Total EUR variable debt		15.643	19.644	15.643	15.643	8.549	–	75.122	
Weighted average EUR interest rate		3.5%	3.5%	3.5%	3.6%	3.7%	0.0%	3.5%	

For indebtedness with variable interest rates, the table below presents principal cash flows and related weighted average interest rates by contractual maturity dates as of December 31, 2004.

Contractual Maturity Dates as of December 31, 2004:

We would experience an additional interest expense of approximately $10.1 million in 2005, $6.1 million in 2006, $3.0 million in 2007, $1.5 million in 2008 and $1.0 million in 2009 on an annual basis as a result of a hypothetical increase in the LIBOR/EURIBOR by 1% over the current rate as of December 31, 2004. The fair value of our publicly traded long-term notes as of December 31, 2004 ranged from 100.9% to 106.0% of the principal amount. At December 31, 2004, the fair value of our other debt approximated its book value. We have not experienced significant changes in the market risks associated with our debt obligations in the table above subsequent to December 31, 2004.

Critical accounting policies

Critical accounting policies are those policies that require the application of management's most challenging, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. Critical accounting policies involve judgments and uncertainties that are sufficiently sensitive to result in materially different results under different assumptions and conditions. We believe that our most critical accounting policies are those described below.

Consolidation of variable interest entities

In December 2003, Financial Accounting Standards Board ("FASB") issued a revision to Interpretation No. 46, "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51" ("FIN 46R" or the "Interpretation"). FIN 46R clarifies the application of Accounting Research Bulletin ("ARB") No. 51, "Consolidated Financial Statements", to certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support. FIN 46R requires the consolidation of these entities, known as variable interest entities ("VIEs"), by the primary beneficiary of the entity. The primary beneficiary is the entity, if any, that will absorb a majority of the entity's expected losses, receive a majority of the entity's expected residual returns, or both. Among other changes, the revisions of FIN 46R (a) clarified some requirements of the original FIN 46, which had been issued in January 2003, (b) eased some implementation problems, and (c) added new scope exceptions. FIN 46R deferred the effective date of the Interpretation for public companies, to the end of the first reporting period ending after March 15, 2004, except that all public companies must at minimum apply the provisions of the Interpretation to entities that were previously considered "special-purpose entities" under the FASB literature prior to the issuance of FIN 46R by the end of the first reporting period ending after December 15, 2003.

Following the adoption of FIN 46R, the Group reevaluated the relationships with its related parties: Promtorgcenter, Notris, Laminea, Finescort-M, Kuntsevo-Invest, Putney Assets and Mosdachtrest. Kuntsevo-Invest and Mosdachtrest are engaged in construction activities of the Group; Promtorgcenter, Notris, Laminea, Finescort-M and Putney Assets possess shareholdings and provide financing through intercompany loans to other entities of the Group. Mosdachtrest was accounted for under equity method for the periods prior to January 1, 2004. The Group determined these entities were variable interest entities and that it was their primary beneficiary. Accordingly, the Group has consolidated these companies effective January 1, 2004. All intercompany balances have been eliminated in consolidation and the results of these VIEs have been included in the Group's consolidated statement of operations and statement of cash flows for the year ended December 31, 2004. In accordance with the provisions of FIN 46R, the Group recorded a charge for the cumulative effect of this accounting change of $35.5 million, net of income tax of nil, in the year ended December 31, 2004. This charge reflects the cumulative impact to the Group's results of operations had these VIEs been consolidated since their inception.

Revenue recognition

Telecommunications

Telecommunications Segment earns revenues from the provision of wireless telecommunication services, local telephone and data transmission services and usage of its local exchange networks and facilities. Revenues are recognized on an accrual basis, when services are actually provided or title to equipment passes to the customer, regardless of when the resulting monetary or financial flow occurs. Segment revenue sources consist of the following: (a) subscription fees, (b) usage fees, (c) value-added service fees, (d) roaming fees charged to other operators for guest roamers utilizing our network, (e) connection fees and (f) sales of handsets and accessories.

We defer initial connection fees paid by subscribers for the first time activation of network service, as well as one time activation fees received for connection to various value-added services. These fees are recognized as revenue over the estimated average subscriber life. The Group periodically reviews its estimates of the expected subscriber relationship period. Effective January 1, 2004, MTS has changed its estimates of average subscriber lives. The effect of this change in estimate in the nine months ended December 30, 2004 was an increase in net income of approximately $4.3 million, or $0.5 per share.

Local telephone services provided by MGTS, totaling approximately 5% and 6% of our consolidated revenues for the year ended December 31, 2004 and the year ended December 31, 2003, respectively, are regulated tariff services, and changes in rate structure are subject to approval by the Federal Tariff Service.

MGTS is required to grant discounts ranging from 20% to 100% on installation and monthly fees to certain categories of residential subscribers, such as pensioners, military veterans and disabled individuals, and is entitled to reimbursement from the federal budget for these discounts. Due to the lack of certainty of reimbursement, MGTS accounts for such revenues upon collection.

Technology

STROM telecom's arrangements with its customers typically include multiple elements, such as equipment and software development, installation services and post-contract customer support. In accordance with the Statement of Position ("SOP") No. 97-2, "Software Revenue Recognition," the aggregate arrangement fee is allocated to each of the undelivered elements in an amount equal to its fair value with the residual of the arrangement fee allocated to the delivered elements. Fair values are based upon vendor-specific objective evidence. Fees allocated to each element of an arrangement are recognized as revenue when the following criteria have been met: a) a written contract for the delivery of an element has been executed, b) the product has been delivered to the customer, c) the fee receivable is fixed or determinable, and d) collectibility of the resulting receivable is deemed probable. If evidence of fair value of the undelivered elements of the arrangement does not exist, all revenue from the arrangement is deferred until such time evidence of fair value does exist, or until all elements of the arrangement are delivered. Fees allocated to post-contract customer support are recognized as revenue ratably over the support period. Fees allocated to other services are recognized as revenue as services are performed.

Insurance

Premiums written on non-life insurance of the Insurance Segment are recognized on a pro-rata basis over the term of the related policy coverage, normally not exceeding 1 year. The unearned premium provision represents that portion of premiums written relating to the unexpired term of the policy. Premiums from traditional life and annuity policies with life contingencies are recognized as revenue when due from the policyholder.

Banking

Interest income of the Banking Segment is recognized on an accrual basis. Loans are placed on non-accrual status when interest or principal is delinquent for a period in excess of 90 days, except when all amounts due are fully secured by cash or marketable securities and collection proceedings are in process. Interest income is not recognized where recovery is doubtful. Loans are written off against allowance for loan losses in the case of uncollectibility of loans and advances, including through repossession of collateral.

Other businesses

Revenues on construction contracts are recognized under the completed-contract method. Our other entities recognize revenues when products are shipped or when services are rendered to customers.

In arrangements where we act as an agent, including travel agency arrangements and arrangements to administer construction projects, only the agency fee is recognized as revenue.

Management estimates

The preparation of our consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the reporting period. Actual results could differ from those estimates. Examples of significant estimates include the provision for doubtful accounts and valuation allowance on deferred tax assets.

License Costs and Other Intangible Assets

We capitalize the cost of licenses acquired in business combinations and directly from the government. As the telecommunications industries in Russia, Ukraine and Uzbekistan do not have sufficient experience with renewal of licenses or extensions of license terms, we amortize each license on a straight-line basis over the term of the license commencing from the date such license becomes commercially operational. We review these licenses and their remaining useful life and, if necessary, revise the useful lives based on our actual utilization. The estimated useful lives of licenses may vary depending on market or regulatory conditions, and any revision to the estimated useful lives may result in a write off or an increase in amortization costs.

Most of our current licenses provide for payments to be made to finance telecommunications infrastructure improvements, which in the aggregate could total approximately $103.0 million, as of December 31, 2004. However, no decisions regulating the terms and conditions of such payments have been formulated by the government authorities. Accordingly, we have made no payments to date pursuant to any of the current licenses, and have not made any accruals for this liability in the financial statements.

Other intangible assets represent acquired customer base, trademarks, roaming contracts with other telecommunications operators, telephone numbering capacity, rights to use premises and various purchased software costs. Trademarks, roaming contracts and telephone numbering capacity with unlimited contractual life are not amortized, but are reviewed, at least annually, for impairment in accordance with the provisions of FAS No. 142, "Goodwill and Other Intangible Assets."

Acquired customer base is amortized over the estimated average subscriber life. Deferred telephone numbering capacity costs with limited contractual life and the rights to use premises are being amortized over their contractual lives, which vary from five to twenty years. Software costs and other intangible assets are amortized over three to five years. All finite-life intangible assets are amortized using the straight-line method.

Useful Lives of Property, Plant and Equipment

We calculate depreciation expense for property, plant and equipment on a straight-line basis over their estimated useful lives. We establish useful lives for each category of property, plant and equipment based on our assessment of the use of the assets and anticipated technology evolution. We review and revise if appropriate the assumptions used in the determination of useful lives of property, plant and equipment at least on an annual basis.

Impairment of Long-Lived Assets

We periodically evaluate the recoverability of the carrying amount of our long-lived assets in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, we compare undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, we record impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets.

Translation Methodology

We follow a translation policy in accordance with Statement on Financial Accounting Standards ("FAS") No. 52, "Foreign Currency Translation." Due to a highly inflationary economy in the Russian Federation in 2002, the U.S. dollar (our reporting currency) has been designated as our functional currency. Accordingly, all foreign currency amounts were translated into U.S. dollars using the remeasurement method.

Starting from January 1, 2003, the Russian economy ceased to be considered highly inflationary for accounting purposes. We determined that for the fiscal year beginning January 1, 2003 the functional currency of MGTS, ROSNO, Kuban-GSM, Mikron, Detsky Mir, Detsky Mir Center, Sistema Mass Media, Media-Center and Concern RTI is the ruble. Accordingly, the reporting currency amounts for these subsidiaries were translated into their functional currency at the exchange rate current at January 1, 2003. These amounts became the new accounting basis for the non-monetary assets and liabilities. The functional currency of UMC is the hryvnia and the functional currency of STROM telecom is the Czech krona. We believe that the U.S. dollar is still the appropriate functional currency for the other subsidiaries of our consolidated group due to the prevalent use of the dollar in their operations.

Pursuant to Emerging Issues Task Force ("EITF") Issue No. 92-8, "Accounting for the Income Tax Effects under FASB Statement No. 109 of a Change in Functional Currency When an Economy Ceases to Be Considered Highly Inflationary," the differences between the new functional currency bases of non-monetary assets and liabilities and their tax basis represent temporary differences, for which deferred taxes must be recognized. Income tax effect of changes in the functional currency amounting to $22.4 million, net of minority interest of $17.2 million, was reported as other comprehensive loss for the year ended December 31, 2003.

We have selected the U.S. dollar as our reporting currency and have translated financial statements of subsidiaries with a different functional currency into U.S. dollars. Assets and liabilities are translated at the exchange rates current at the balance sheet date, while income and expense items are translated at average rates of exchange prevailing during the period. The resulting translation adjustments in the amount of $35.3 million, net of minority interest of $24.4 million, and $30.0 million, net of minority interest of $28.6 million, are recorded as a separate component of other comprehensive income for the year ended December 31, 2003 and the year ended December 31, 2004, respectively.

The ruble is not a fully convertible currency outside of the territory of the Russian Federation. The translation of ruble-denominated assets and liabilities into U.S. dollars for the purpose of these financial statements does not indicate that we could or will in the future convert the reported values of the assets and liabilities in U.S. dollars.

Taxation

We are subject to a variety of taxes levied in the Russian Federation, including income taxes, payroll taxes, VAT, property taxes and other, and our foreign subsidiaries are subject to taxation in their respective jurisdictions.

The taxation system in Russia is subject to frequent changes, varying interpretations and inconsistent enforcement at the federal, regional and local levels. In some instances, new tax regulations have been given retroactive effect, while under the Tax Code only laws benefiting the taxpayer may have retroactive effect. In addition to our substantial tax burden, these conditions complicate our tax planning and related business decisions. For example, tax laws are unclear with respect to the deductibility of certain expenses and at times we have taken a position that may be considered aggressive by tax authorities, but that we consider to be in compliance with current law. Tax declarations, together with other legal compliance areas (for example, customs and currency control matters), are subject to review and investigation by a number of authorities, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia that are more significant than those typically found in countries with more developed tax systems.

Management believes that it has adequately provided for tax liabilities in its financial statements; however, the risk remains that the authorities could take a different position with regard to interpretive issues.

Income taxes

Effective January 1, 2002, the income tax rate in Russia declined to 24% for all companies, income tax on dividends paid within Russia was reduced to 6% (from 15% in 2001 and 2000) and the tax loss carry-forward period was extended to ten years. In July 2004, amendments to the new Tax Code were enacted increasing the rate of income tax on dividends to 9% effective January 1, 2005. The new income tax legislation also adopted a more liberal approach to tax-deductible expenses, permitting deductions so long as expenses are economically proven and justified from the business standpoint. The elimination of investment tax credits offset some of the benefits from the reduction of income tax rates. In periods prior to 2002, we were allowed to offset up to 50% of our taxable income with investment tax credits and other miscellaneous credits.

Value-added tax

During the years ended December 31, 2001, 2002 and 2003 the VAT rate in Russia was 20%. Effective January 1, 2004, it decreased to 18%.

New accounting pronouncements

In November 2003, the Emerging Issues Task Force ("EITF") reached a final consensus on Issue No. 03-10, "Application of EITF Issue No. 02-16, 'Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor', by Resellers to Sales Incentives Offered to Consumers by Manufacturers." The consensus was reached that consideration received by a reseller from the vendor in exchange for vendor sales incentives tendered by consumers should not be reported as a reduction of the cost of the reseller's purchases from the vendor but instead should be shown as revenue. EITF Issue No. 03-10 is effective for reporting periods beginning after November 25, 2003. The adoption of Issue No. 03-10 did not have a material impact on our results of operations or financial position.

In March 2004, the EITF reached a consensus on Issue No. 03-6, "Participating Securities and the Two-Class Method under FASB Statement No. 128, Earnings per Share". This Issue defines participating security and clarifies some practical issues related to including participating securities in the calculation of EPS. EITF Issue No. 03-6 is effective for reporting periods beginning after March 31, 2004. The adoption of Issue No. 03-6 did not have a material impact on our financial position or results of operations.

In July 2004, the EITF issued EITF No. 02-14, "Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock." A consensus was reached regarding an investor that has the ability to exercise significant influence over the operating and financial policies of the investee. This type of investor should apply the equity method of accounting only when it has an investment(s) in common stock and/or an investment that is in-substance common stock. The Task Force also reached a consensus on the definition of in-substance common stock and related guidance. EITF No. 02-14 is effective for reporting periods beginning after September 15, 2004. The adoption of EITF Issue No. 02-14 did not have a material impact on our financial position or results of operations.

In September 2004, the U.S. Securities and Exchange Commission ("SEC") staff issued the EITF Topic D-108, "Use of the Residual Method to Value Acquired Assets Other Than Goodwill", which requires the companies to use the direct value method to determine the fair value of their intangible assets acquired in business combinations completed after September 29, 2004. The SEC staff also announced that companies that currently apply the residual value approach for valuing intangible assets with indefinite useful lives for purposes of impairment testing, must use the direct value method by no later than the beginning of their first fiscal year after December 15, 2004.

As of December 31, 2004, MTS performed the annual impairment test to measure the fair value of its 900 and 1800 MHz licenses in its national footprint using the residual value approach. Under this new accounting guidance, MTS performed an impairment test to measure the fair value of its 900 and 1800 MHz licenses as of January 1, 2005 using the direct value method. Based on the assessment no impairment charge as of December 31, 2004 is required.

In September 2004, the EITF issued a final consensus on EITF Issue No. 04-1, "Accounting for Preexisting Relationships between the Parties to a Business Combination". In this issue the EITF reached a consensus that a business combination between two parties having a preexisting relationship is a multiple-element transaction with one element being the business combination and the other element being the settlement of the preexisting relationship. This Issue requires certain additional disclosures for business combinations between parties with a preexisting relationship. EITF Issue No. 04-1 is effective for reporting periods beginning after October 13, 2004. We do not anticipate that the adoption of EITF Issue No. 04-1 will have a material impact on our financial position or results of operations.

In October 2004, the EITF reached a consensus on EITF Issue No. 04-10, "Determining Whether to Aggregate Operating Segments that Do Not Meet the Quantitative Thresholds". EITF No. 04-10 provided additional guidance on when operating segments that are below the 10% threshold can be aggregated. EITF Issue No. 04-10 states that segments can only be aggregated if they have similar economic characteristics and if they are similar in areas such as production processes, types of customers, distribution channels and the products themselves are similar. The consensus reached by EITF No. 04-10 is effective for fiscal years ending after October 13, 2004. The adoption of Issue No. 04-10 did not have a material impact on our results of operations or financial position.

In November 2004, the Financial Accounting Standards Board ("FASB") issued FAS No. 151, "Inventory Costs", an amendment of ARB No. 43, Chapter 4. FAS No. 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs, and wasted materials (spoilage) should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facility. FAS No. 151 is effective prospectively for inventory costs incurred during fiscal years beginning after June 15, 2005. We do not anticipate the adoption of FAS No. 151 to have a material impact on our results of operations or financial position.

In December 2004, the FASB issued FAS No. 123R, "Share-Based Payment" ("FAS No. 123R"), a revision of FAS No. 123, "Accounting for Stock-Based Compensation". FAS No. 123R supersedes Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees" and requires all entities to recognize compensation cost in an amount equal to the fair value of share-based payments granted to employees. That cost will be recognized over the period during which an employee is required to provide service in exchange for an award of equity instruments. FAS No. 123R is effective as of the beginning of the first fiscal year beginning after June 15, 2005, at which time companies can select whether they will apply the standard retroactively by restating their historical financial statements or prospectively for new stock-based compensation arrangements and the unvested portion of existing arrangements. We do not anticipate the adoption of FAS No. 123R will have a material impact on our financial position, cash flows and results of operations.

In December 2004, the FASB issued FAS No. 153, "Exchanges of Nonmonetary Assets", an amendment of APB Opinion No. 29, "Accounting for Nonmonetary Transactions". FAS No. 153 eliminates the exception from fair value measurement for nonmonetary exchanges of similar productive assets set in the APB Opinion No. 29 and replaces it with a general exception for exchanges that do not have commercial substance. FAS No. 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. FAS No. 153 is effective prospectively for nonmonetary exchanges occurring after June 15, 2005. We do not anticipate the adoption of FAS No. 153 to have a material impact on our results of operations or financial position.

In March 2005, the FASB issued Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations - an interpretation of FASB Statement No. 143." This Interpretation clarifies that the term "conditional asset retirement obligation" as used in FASB Statement No. 143, "Accounting for Asset Retirement Obligations", refers to a legal obligation to perform an asset retirement activity, in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement. Uncertainty about the timing and (or) method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists to make a reasonable estimate of the fair value of the obligation. Interpretation 47 is effective for us beginning January 1, 2006. We are currently in the process of assessing effects of Interpretation 47 on our consolidated financial position and result of operations.

In March 2005, the SEC released Staff Accounting Bulletin 107, "Share-Based Payments", or SAB 107. The interpretations in SAB 107 express views of the SEC staff regarding the interaction between FAS No. 123R and certain SEC rules and regulations, and provide the SEC staff's views regarding the valuation of share-based payment arrangements for public companies. In particular, SAB 107 provides guidance related to share-based payment transactions with nonemployees, the transition from nonpublic to public entity status, valuation methods (including assumptions such as expected volatility and expected term), the accounting for certain redeemable financial instruments issued under share-based payment arrangements, the classification of compensation expense, non-GAAP financial measures, first-time adoption of FAS No. 123R in an interim period, capitalization of compensation cost related to share-based payment arrangements, the accounting for income tax effects of share-based payment arrangements upon adoption of FAS No. 123R, the modification of employee share options prior to adoption of FAS No. 123R.

Off-balance sheet arrangements

Obligations under guarantee contracts

In December 2002, MTU-Inform and Alfabank signed a guarantee agreement. According to the agreement, MTU-Inform guaranteed a loan of $4.0 million provided to Golden Line by Alfabank. The loan matures in November, 2005. In addition, MTU-Inform pledged equipment with a fair value of $4.7 million as security for the loan.

As of December 31, 2004, MTS has issued guarantees on behalf of MTS Belarus, an equity investee, for the total amount of $25.0 million. Under these guarantees, we could potentially be liable for a maximum amount of $25.0 million if MTS Belarus defaults on its obligations. The guarantees expire by April 2007.

Additionally, MBRD guaranteed loans for several companies, including related parties, which totaled $7.4 million as of December 31, 2004.

In July 2004, MTU-Inform issued guarantees to MBRD on behalf of Sky Link for the total amount of $21.1 million.

These guarantees would require payment by us only in the event of default on payment by the respective debtor. Under these guarantees, we could be potentially liable for a maximum amount of $57.5 million in the case of the borrower's default under the obligations. As of December 31, 2004, no event of default has occurred under any of the guarantees issued by us.

Obligations under derivative contracts

In October 2004, MTS exercised its call option in respect of 47.3% of common shares and 50% of preferred shares of TAIF Telcom, increasing our voting power in TAIF Telcom to 100%. The value of consideration equaled $63.0 million. TAIF Telcom provides GSM 900/1800 services under the MTS brand in the Republic of Tatarstan (population 3.8 million), located in the Volga region of Russia.

In connection with MTS' acquisition of 74% of the shares in Uzdunrobita in August 2004, it entered into call and put option agreements with the existing shareholders of the company to acquire the remaining 26% of the shares. The exercise period for the option is 48 months from the acquisition date. The call and put option agreements stipulate a minimum purchase price of $37.7 million plus 5% per annum commencing from the acquisition date. The fair value of the put option was approximately $3.6 million as of December 31, 2004.

Tabular Disclosure of Contractual Obligations

We have various contractual obligations and commercial commitments to make future payments, including debt agreements, lease obligations and certain committed obligations. The following table summarizes our future obligations (including interest) under these contracts due by the periods indicated as of December 31, 2004:

	January 1, 2005-December 31, 2005	January 1, 2006-December 31, 2006	January 1, 2007-December 31, 2007	January 1, 2008-December 31, 2008	January 1, 2009-December 31, 2009	January 1, 2010-Following periods	Total
	(Amounts in thousands)						
Contractual obligations:							
Notes payable	222 593	177 821	177 821	889 065	153 772	1 245 562	2 866 633
Bank loans	617 877	486 653	364 993	215 108	49 318	85 822	1 819 771
Capital lease	5 289	2 228	746	171	169	451	9 054
Operating leases and services agreements	54 074	26 625	22 597	18 626	14 812	59 037	195 771
Committed Investments:							
Purchases of property, plant and equipment	164 700	-	-	-	-	-	164 700
Construction contracts	34 600	-	-	-	-	-	34 600
Total	1 099 133	693 327	566 157	1 122 970	218 071	1 390 872	5 090 530

In December 2003, MGTS announced its long-term investment program for the period from 2004 through 2012. The program was approved by a resolution of the Moscow City Government in December 2003 and provides for total capital expenditures of approximately $1.6 billion, including for the expansion and full digitalization of the Moscow telephone network, the reconstruction of 350 local telephone stations and the installation of 4.3 million new phone numbers. We expect to finance approximately 50% of the capital expenditures under the investment program.

Recent Financing Activities

Initial Public Offering

1On February 11, 2005, we completed an initial public offering of 1,550,000 common shares, with a nominal value of 90 rubles per share in the form of 77,500,000 global depositary receipts ("GDRs"), with 50 GDRs representing one share. On February 14, 2005, our GDRs were admitted to trade on the London Stock Exchange. Proceeds from the offering, net of underwriting discount and other direct costs, were $1,284.6 million.

Simultaneously, certain our shareholders sold 42,663 common shares in the form of 2,133,150 GDRs. In addition, shareholders exercised their option to sell additional 238,900 shares in the form of 11,945,000 GDRs.

Financings

In January 2005, MTS Finance issued $400.0 million 8.0% unsecured notes at 99.736%. These notes are fully and unconditionally guaranteed by OJSC MTS and mature on January 28, 2012. MTS Finance is required to make interest payments on the notes semi-annually in arrears on January 28 and July 28, commencing on July 28, 2005. The notes are listed on the Luxembourg Stock Exchange. Proceeds received from the notes were $398.9 million.

In February 2005, MBRD entered into a loan facility with Standard Bank London and Standard Bank Moscow, pursuant to which the banks agreed to make available to MBRD a loan facility in the amount of $16.0 million, secured by a pledge of MBRD's rights under its loan to Sky-Link. The loan was guaranteed by MTU-Inform.

In March 2005, MBRD entered into a loan agreement with Dresdner Bank AG for the amount of $150.0 million. The loans bears interest of 8.625% and is due in March 2008. To finance the loan to MBRD, Dresdner Bank AG issued Loan Participation Notes that were admitted to trade on the Luxembourg Stock Exchange. Interest payments on the loan are due semi-annually in March and September of each year, commencing in September 2005. Loan agreement contains certain restrictive covenants including, but not limited to, limitations on mergers, liens and dispositions of assets and transactions with the Group's subsidiaries and affiliates.