JSFC SISTEMA

ANNUAL REPORT

2008

JOINT-STOCK FINANCIAL CORPORATION
SISTEMA

To whom it may concern

April 30, 2009

Responsibility Statement

To the best of my knowledge (a) the financial statements, prepared in accordance with the US GAAP, give a true and fair view of the assets, liabilities, financial position and profit or loss of Sistema JSFC and the undertakings included in the consolidation taken as a whole; and (b) the management report includes a fair review of the development and performance of the business and the financial position of Sistema JSFC and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Yours sincerely,

Alexei Buyanov
Head of Financial functional division
Senior Vice President

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PART 1 SISTEMA OVERVIEW

1. About Sistema

Sistema is the largest public diversified corporation in Russia and the CIS, which manages fast growing companies operating in the telecommunications, consumer services sectors and technology industries and has over 100 million customers. Sistema develops and manages market-leading businesses in selected industries, including telecommunications, IT, aerospace technologies, banking, real estate, retail, media, tourism, healthcare and others. Sistema's subsidiaries operate in various countries of Central and Eastern Europe as well as India.

Founded in 1993, the company reported revenues of US$ 16.7 billion in 2008 and total assets of US$ 29.2 billion as at December 31, 2008. Following Sistema's IPO in February 2005, 19% of Sistema's shares are now traded under the symbol "SSA" on the London Stock Exchange, under the symbol "AFKS" on the Russian Trading System (RTS), under the symbol "AFKC" on the Moscow Interbank Currency Exchange (MICEX), and under the symbol "SIST" on the Moscow Stock Exchange (MSE).

In July 2008 Sistema adopted a matrix model and formed three new operating units in addition to functional divisions. These units will be responsible for the management of Sistema's subsidiaries.

The operating unit "Telecommunications Assets", previously the Telecommunications Assets Development unit, will be responsible for the development and implementation of Sistema's telecommunications strategy, as well as management of telecommunications and media assets, including MTS, Comstar-UTS, Sistema Mass Media, and other companies in Russia, as well as Sistema Shyam TeleServices Ltd., Sistema's telco subsidiary in India.

The operating unit "Consumer Assets" will focus on the development of companies in the consumer sector, including Detsky Mir, Intourist, MEDSI and MBRD, as well as Sistema-Hals.

The operating unit "High Technologies and Industry" will be engaged in Sistema's high-tech and venture projects, as well as private-public partnerships. This unit, will also oversee Sitronics, RTI Systems and Binnopharm.

Since March 2009, Sistema has been the controlling shareholder of a number of oil production companies in Bashkortostan, Russia.

The Corporation focuses on the development of advanced technologies and innovative services which is in line with our strategy to create additional shareholder value, to maximize the returns from our portfolio investments, to make a significant contribution to the development and diversification of the economy and improvement in the quality of life for people in Russia and the other markets in which it operates.

BUSINESS UNIT 'TECECOMMUNICATION ASSETS'

Telecommunications		
	MTS	*The largest mobile-phone operator in Russia and the CIS in terms of subscriber numbers, sales and market capitalization.*
	Comstar UTS	*A national fixed-line provider of integrated telecommunication solutions in Russia and the CIS.*
	Sky Link	*A leader in the Russian 3G telecommunications market, providing high-speed mobile Internet access and voice communications.*
	Sistema Shyam TeleServices	*A joint venture company, between Shyam Group of India & Sistema Corporation of Russia.*
Media Content	**Sistema Mass Media**	*One of the largest Russian companies in the market for the development and distribution of content for pay-TV networks and other media platforms and resources.*

BUSINESS UNIT 'CONSUMER ASSETS'

Real Estate	**Sistema-Hals**	*One of the key players in the Russian market for construction and real estate.*
Financial Services	**MBRD**	*One of Russia's largest universal banks and operates a leading national retail banking network.*
Travel	**Intourist**	*Russia's leading universal operator in the travel market, providing services for Russian tourists and international visitors to Russia.*
Retail	**Detsky Mir**	*The leading retailer of children's goods in Russia and one of the country's best-known and trusted retail brands.*
Healthcare	**Medsi**	*Russia's first national chain of private medical clinics which provide medical treatment, preventative care, dental, fitness and other health-enhancing services in Moscow and regions*

BUSINESS UNIT 'TECHNOLOGY AND INDUSTRY'

High Technology	**Sitronics**	*The largest high-technology company in Eastern Europe, with business interests in telecom solutions, information technology, system integration and consulting, and microelectronics.*
Radar and Aerospace	**Concern "RTI Systems"**	*One of Russia's largest defense-industrial holdings and incorporates leading Russian*

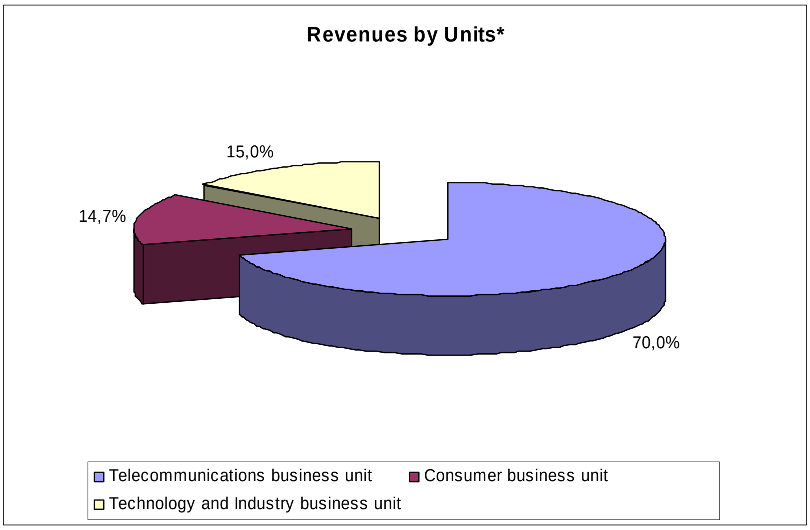
		companies with enormous scientific and production potential and experience in high-technology projects.
Pharmaceuticals	**Binnopharm**	*One of Russia's leading vertically integrated pharmaceutical and biotechnology holding.*

PETROCHEMICALS

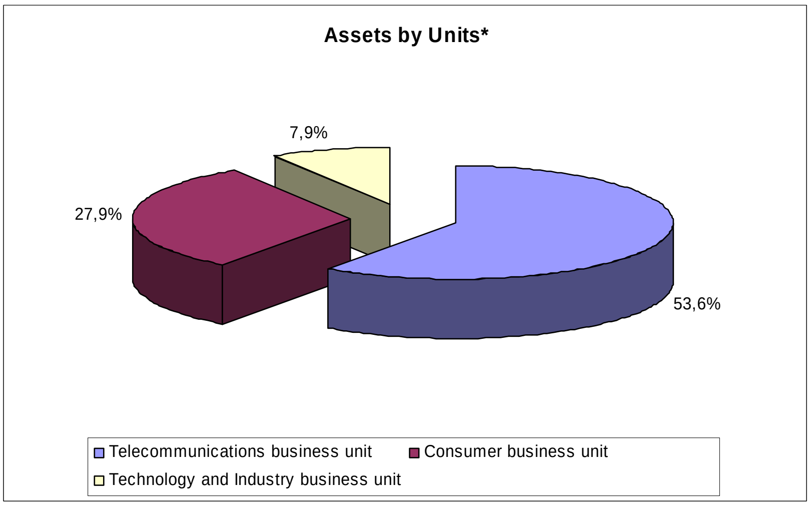
Bashkir Oil & Energy Group	*One of Russia's Top-10 oil producers and Top-5 oil refiners with the fourth largest reserves among Russian oil companies.*

2. Financial Highlights

	Revenues, ($ million)	OIBDA*, ($ million)	OIBDA margin	Net Income, ($ million)	Assets, ($ million)	Shareholders' Equity ($ million)	EPS ($)
2008	16, 670.8	5,489.6	32.9%	62.0	29,158.8	5,557.9	0.67
2007	13,701.0	5,050.4	36.9%	1,571.9	28,396.7	6,658.8	16.88
2006	10,266.6	3,977.1	38.7	813.0	20,191.2	4,505.1	8.50



*Before interunits eliminations and without Corporate & Other segment



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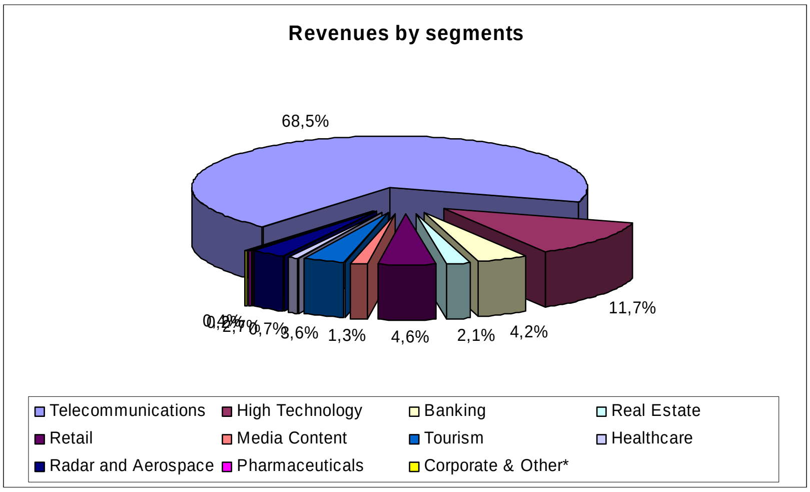
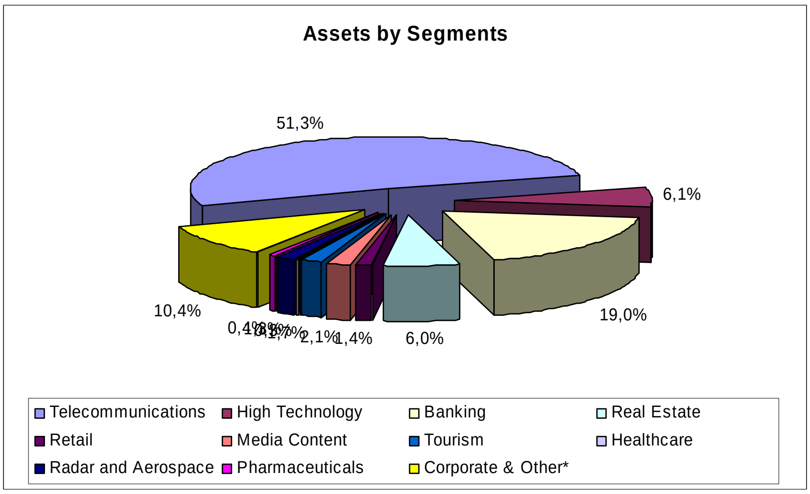


*The Corporate & Other segment comprises the companies that control and manage the Group's interests in its subsidiaries.



3. Strategy

Sistema's mission reflects the shareholders' aspiration to develop a large-scaled, competitive, diversified business in Russia and CIS and selected emerging markets with high potential for long term equity value growth.

In accordance with the mission, Sistema sets up the following strategic aims over the next three to five years:

- The Total Shareholder Return of Sistema should surpass the weighted average cost of capital for Sistema and index performance for comparable companies,
- The company should remain financially stable,
- Sistema should strengthen its leading positions on key markets and ensure stable cash flow from its businesses.

Along with these priorities, Sistema intends to continuously develop its main businesses, focus on optimizing its current assets portfolio, increase the share of the non-public companies in its portfolio and realize possible synergies between its businesses.

The company intends to achieve these strategic purposes by developing and managing its businesses actively, focusing on effective investments, and maintaining a reasonable financing. Operational growth is being planned by organic accretion as well as through acquisitions and strategic partnerships.

In order to achieve these goals, especially while the current economy is uncertain, Sistema has defined three-level approach to optimize its businesses:

1. Improving business efficiency at all levels, including strengthening financial discipline, introducing new KPIs for our subsidiaries, increasing revenues and reducing operating costs;
2. Optimising investment policy, including focusing on more profitable investment projects; reviewing capital-intensive projects, investing subject to availability of capital, reducing the Group's CAPEX by 30% in 4Q 2008.
3. Searching for partners in investment projects with long term investment return.

The management will be able to make timely and effective decisions about businesses that do not meet the above criteria.

Fulfilment of this three-step approach will enable the company to achieve all strategic purposes.

4. Key events of 2008

January

Sistema increased its stake in Shyam Telelink Ltd. from 10% to 51%. At the same time, Shyam Telelink Ltd was awarded unified telecommunication licenses for the provision of fixed-line and cellular services in 21 Indian circles. Sistema guaranteed US$ 520 million of the total US$ 630 million to be paid for obtaining the licenses.

Sistema completed the acquisition of 50.5% additional shares in Dalcombank for a cash consideration of approximately US$ 107.5 million. Sistema now holds a 98.7% stake in Dalcombank.

February

Sistema completed integration of its Healthcare Services division's assets into the «Medsi Companies Group» Holding, 100% owned by Sistema. Sistema transferred to Medsi Group its 20% stake in MedExpress, 100% of American Hospital Group and 53.3% of the Medsi clinic. Sistema is also investing RUB 900 million (US$ 36 million) to increase the capital of the holding.

MBRD securitised part of its car loan portfolio. This deal will provide the Bank with funding in the amount of RUB 1.5 billion. The Issuer may increase the borrowing up to US$ 200 million in the next 12 months. Bayerische Hypo- und Vereinsbank AG, a member of the UniCredit Group, was the sole Arranger and Lead Manager for the Bank in this deal.

RTI Systems completed the sale of 100% in CJSC Sahles to CJSC Saturn, a subsidiary of OPK Oboronprom, for a total cash consideration of US$ 190 million. CJSC Sahles owns a 71.63% stake in OJSC Perm Motors Plant, as well as controlling stakes in other entities which constitute the Perm Motors Group ("PMG"). PMG comprises 18 companies specializing in military and civil aviation engine construction.

March

Sistema successfully placed its RUB 6 billion (approximately US$ 251.6 million) corporate Bond issue. The annual interest rate for the first and second coupon payments has been set at 9.45%. The Bonds mature in five years and coupon payments will be made on a semi-annual basis.

The Board of Directors of Comstar UTS approved the introduction of a long-term incentive program for the Company’s management team. The program is set to run from April 1, 2008 with a two year vesting period.

Sitronics acquired a 36% stake in Kvazar-Micro from Melrose Holding Company for US$ 116.9 million. As a result of the transaction, Sitronics owns 87% of Kvazar-Micro and Melrose Holding Company owns a 3.07% stake in Sitronics.

April

Sistema repaid its US$ 350 million Eurobond issue. The Eurobond issue was repaid upon its maturity in full using the Company's cash flows and previously obtained debt financing.

Sistema Board of Directors recommended an annual dividend of RUB 2,512.5 million, (approximately US$ 106.4 million), for the year ended December 31, 2007 to holders of Sistema shares. The dividend, which amounts to a payment of RUB 0.25 per share (approximately US$ 0.21 per Global Depositary Receipt), is more than five times higher than the dividend paid for the same period of 2006.

Shyam Telelink Ltd. received radio frequencies for building mobile networks in eleven Indian circles. Together with radio frequencies already obtained in Rajasthan, Shyam Telelink will be able to start building a full scale CDMA network in 12 Indian circles, which will cover over half of the territory of India with a target population of approximately 650 million people.

May

Sistema's Board of Directors appointment Leonid Melamed as President and Chief Executive Officer of Sistema with immediate effect. Mr Melamed, the former CEO and President of MTS, replaced Alexander Goncharuk, who will continue to serve as First Deputy Chairman of Sistema's Board of Directors.

Sistema signed a Memorandum of Understanding with DAS Holding LLC, an international investment holding company with headquarters in Abu Dhabi. The main goal of the Memorandum is to develop the cooperation in various sectors of the economy, such as investments into real estate and construction projects, banking, medicine, tourism and the hotel business in Russia, the CIS and United Arab Emirates.

Sistema signed an agreement on cooperation with CPMIEC, the Chinese National Precision Machinery Import & Export Corporation. The agreement aims to develop cooperation on the Russian and Chinese markets, and also in third countries in the sphere of hightechnology and developers' services.

Sistema signed an amendment to the call option agreement, which gave it the right to accelerate the purchase of an additional 21% stake in Shyam Telelink. In accordance with this amendment, Sistema has exercised a call option and acquired the additional 21% stake in Shyam Telelink, increasing its stake from 51% to 72%.

MTS' Board of Directors appointed Mr. Mikhail Shamolin as the President and CEO of MTS. Mr. Shamolin has previously served as the Head of MTS Russia.

Comstar signed a strategic agreement with FON Wireless Ltd., a developer of a shared wireless internet access network based on Wi-Fi technology. Under the terms of the agreement, Comstar and FON will develop a Wi-Fi internet access network.

June

Sistema signed US$ 613.3 million syndicated multi-tranche loan facility with ABN AMRO.

Comstar completed the acquisition of 100% of the share capital of Interlink Group for a total cash consideration of RUB 200 million (approximately US$ 8.5 million). The Group comprises Intersvyaz Service, the alternative fixed-line telecommunications operator, and Inter-TV Media, the cable TV operator, which operate under the unified brand "Interlink" in Ryazan and the Ryazan region.

Comstar commenced the merger of Comstar-Direct, a leading provider of broadband internet access services in Moscow. Comstar currently owns 51.8% of Comstar-Direct, with the remaining 48.2% owned by Sistema Mass Media.

Sistema increased its stake in Shyam Telelink from 72% to 73.71%. Sistema also received radio frequencies under CDMA 800 MHz in four additional Indian circles.

July

Sistema adopted a matrix model and formed three new operating units: Telecommunications Assets, headed by Vitaly Savelyev, First Vice President of Sistema; Consumer Assets, led by Felix Evtushenkov, Vice President of Sistema; High Technologies and Industry, headed by Sergey Boyev, Vice President of Sistema, in addition to functional divisions. These units will be responsible for the management of Sistema's subsidiaries.

Mikhail Shamolin, President and Chief Executive Officer of MTS, joined the Board of the GSM Association (GMSA), the global trade association for the mobile industry.

The Board of Directors of Shyam Telelink appointed Mr. Vsevolod Rozanov as President and CEO of the Company.

Comstar UTS has acquired 100% stake in LLC "Strategy", the owner of CJSC Ural Telephone Company, a leading alternative telecommunications operator in Ekaterinburg and the Sverdlovsk region, for a total cash consideration of RUB 1.0 billion (approximately US$ 43.4 million).

Sistema Hals announced the results of an independent valuation of its project portfolio carried out by Cushman & Wakefield Stiles & Riabokobylko (C&WS&R). As at July 1, 2008 Sistema Hals stake in properties and projects was valued at US$ 3.8 billion

Sistema Hals has completed the first phase of construction of the RWS – St Petersburg Film Studio. The new studio will be managed by Russian World Studios, one of the leading Russian film and video production companies.

The Board of Directors of Sistema Hals has approved two 5-year bond issues for a total of RUB 5 billion (approximately US$ 200 million). Raiffeisenbank and Renaissance Capital are acting as Arrangers of the issues.

Detsky Mir has signed a 5-year syndicated loan agreement with EBRD for US$ 50 million. The loan proceeds will finance the expansion of the retail network in 2008.

Detsky Mir has signed a US$ 20 million trade finance agreement with Deutsche Bank Russia.

August

Shyam Telelink received radio frequencies in the CDMA 800 MHz range in three additional Indian circles with a population of over 62 million people.

Comstar UTS has received the access codes for provision of inter-city and international long distance telephony services from the Russian Ministry of Information Technologies and Communications.

Access Telecommunications Coöperatief U.A. has initiated the process of exercising its put option to sell 46,232,000 Comstar UTS shares to MGTS Finance S.A. The Option Interest represents 11.06% of the total number of issued and outstanding Comstar UTS shares. The transaction is expected to be completed, by means of the transfer of rights and payment, within 60 business days from August 25, 2008.

September

Comstar UTS commenced the integration of the regional operators of STREAM-TV Group, which is owned by Sistema Mass Media and providing cable TV and broadband internet access services in 40 Russian cities with a combined population of over 15 million people.

Shyam Telelink launched a CDMA 800 MHz mobile network under the brand name «Rainbow» in the state of Rajasthan. This marks the beginning of the expansion of Shyam Telelink's pan-Indian mobile network.

October

MTS and Vodafone signed a strategic, non-equity partnership to provide customers with high quality communications services and to collaborate jointly on future technological developments.

MTS placed a RUB 10 billion bond with maturity in 2013 and a RUB 10
billion bond with maturity in 2015. The coupons are to be paid semi-annually.

Sistema Mass Media launched the movie and TV production at Russian World Studios (RWS) in St Petersburg.

November

Comstar UTS completed the transfer of rights in relation to exercising the put option held by Access Telecommunications Coöperatief U.A. Comstar subsidiary MGTS Finance S.A. thereby acquired 46,232,000 Comstar UTS shares at US$ 10.03 per share for a total cash consideration of US$ 463.6 million.

Comstar UTS exercised its share options allocated under its 2006-2008 incentive programme. The programme was discontinued in April 2008 due to the launch of a new long-term incentive programme. Comstar UTS paid US$ 1.8 million for the repurchase of the shares from the programme participants.

Shyam Telelink connected the one hundred thousandth subscriber to its CDMA 800 MHz mobile network in the state of Rajasthan since its launch on September 30, 2008.

In November 2008, Sistema Invest, a subsidiary of Sistema, signed agreements with the majority shareholders of Bashkir Oil and Energy Group to act as a management company in respect of companies which own a majority stake in the Group.

December

Sistema Hals received a RUB 7 billion credit facility from Bank VTB repayable in 2 years.

Sistema Hals obtained changes to the terms of its credit agreements with Bank VTB. Under the new terms, the five-year credit facilities for the amounts of US$ 500 million and US$ 200 million granted by Bank VTB in 2007 were converted into rubles at the rate of the Russian Central Bank as of December 2, 2008.

Sitronics signed a US$ 230 million credit facility agreement with Vnesheconombank. The new funds will be used to refinance loan facilities of US$ 125 million and US$ 75 million, which mature in November 2008 and March 2009, respectively. As at December 18, 2008 the loan facility of US$ 125 million was fully paid off.

EVENTS AFTER THE REPORTING PERIOD

January 2009

Shyam Telelink was renamed Sistema Shyam TeleServices Ltd., following the decision made at the EGM of Shareholders of Shyam.

MTS secured a credit facility worth 300 million euros. The credit facility was negotiated with Gazprombank and expires in 2.5 years. Funds from the credit will be used for general corporate needs.

Comstar UTS launched a wireless broadband network in Moscow, which is based on standard 802.16e WiMAX technology. The full commercial launch of the wireless network using the 2.5-2.7 GHz frequency range and based on Nortel technological solutions is expected to be implemented in the second quarter of 2009.

March 2009

Sistema signed an agreement with CJSC Synterra Group to sell its 43.4% stake (50% of voting shares) in MTT. In addition, Synterra Group will assume MTT's intercompany debt obligations to Sistema. The deal is expected to be reached for a total cash consideration of approximately US$ 54 million.

Sistema signed an agreement with Agidel-Invest LLC, Ural-Invest LLC, Inzer-Invest LLC and Yuryuzan-Invest LLC to acquire their stakes in Bashkir Oil and Energy Group companies, including ANK Bashneft JSC, Ufaneftechim JSC, Novoil JSC, Ufaorgsintez JSC, Ufimskiy NPZ JSC and Bashkirnefteprodukt JSC. The deal is expected to be concluded for a total cash consideration of US$ 2.5 billion.

5. Financial Review

The following section presents a brief overview of the company's financial results for 2008, according to US GAAP. The operational and financial performance of each business is discussed in Part II of this annual report.

(US$ millions, except per share amounts)	**FY 2008**	**FY 2007**	**Year on Year Change**
Revenues	**16,670.8**	13,410.7	24.3%
OIBDA	**5,489.6**	4,942.1	11.1%
Operating income	**3,173.3**	3,194.9	(0.7%)
Net income / (loss)	**62.0**	1,571.9	(96.1%)
Basic and diluted (loss)/income per share (US cents)	**0.7**	16.9	(96.0%)

Key Figures

- Consolidated revenues up 24.3% year on year to US$16.7 billion
- OIBDA up 11.1% year on year to US$5.5 billion with OIBDA margin of 32.9%
- Operating income was stable year on year and amounted to US$3.2 billion with operating margin of 19.0%
- Net income of US$62.0 million
- Total assets up 2.7% year on year to US$29.2 billion

Sistema's consolidated revenues grew by 24.3% year-on-year to US$16.67 billion in 2008, compared to US$13.41 billion in 2007. The Group's revenue performance for the full year reflected healthy results across each business unit despite major challenges posed in the second half of the year by the impact of the global financial crisis.

Sistema's businesses outside of the Telecommunications business unit accounted for 27.6% of Group consolidated revenue in 2008, compared to 28.2% in 2007. Organic growth for the Group in 2008, excluding businesses acquired or divested since the end of 2007, was 23.1% year-on-year and amounted to US$3.1 billion.

Selling, general and administrative expenses increased by 45.1% year on year to US$3.44 billion for the full year 2008, reflecting in part general cost inflation, including increased transportation tariffs, higher advertising rates and energy costs. These costs fell 7.8% in the fourth quarter, however, as a result of the appreciation of the US dollar.

Group OIBDA increased by 11.1% year on year in 2008 to US$5.49 billion, compared to US$4.94 billion in 2007. Group OIBDA margin was lower at 32.9% during 2008, compared to 36.9% in 2007.

Depreciation and amortization expenses were up 32.6% year-on-year in 2008, following growth in the depreciable assets of the Group.

Group operating income decreased slightly, by 0.7% to US$3.17 billion in 2008, compared to US$3.20 billion in 2007. Operating margin stood at 19.0% in 2008, compared to 23.8% in 2007. Group interest expenses amounted to US$554.9 million during the year, compared to US$409.8 million during the previous period.

The effective tax rate was 43.1% in 2008, compared to 29.4% in 2007. The increase in the Group's effective tax rate was due to non-deductible losses from the impairment of long-term assets as well as goodwill and losses incurred by Sistema Hals.

The Group reported net income of US$62.0 million during 2008, compared to net income of US$ 1.57 billion in 2007.

Net cash provided by operations increased by 40.5% year-on-year in 2008 to US$ US$3.83 billion. This increase was driven by a change in working capital.

Net cash used in investing activities amounted to US$5.88 billion in 2008. This amount included US$4.27 billion of capital expenditure, compared to US$3.11 billion in the previous period.

The Group spent US$1.94 billion in 2008 on the acquisition of businesses, including US$1.06 billion on the purchase of MTS treasury shares, US$110.1 million for the acquisition of a 6.79% stake in Comstar UTS, US$460.7 million for the purchase of 73.7% in SSTL, US$107.5 million for the purchase of a 49.0% stake in Kvazar Micro, US$44.6 million for the purchase of a 25.0% stake in Detsky Mir, US$51.1 million for the purchase of a 18.0% stake in Sahles and other acquisitions.

Net cash used in financing activities amounted to US$3.27 billion in 2008, compared to US$3.38 billion in 2007. The Group's cash balances stood at US$1.99 billion as of December 31, 2008, compared to US$1.06 billion as of December 31, 2007. The Group's net debt (short-term and long-term debt minus cash and cash equivalents) amounted to US$8.67 billion as of December 31, 2008, compared to US$7.29 billion as of December 31, 2007.

Business Unit 'Telecommunications Assets'

(US$ millions)	**FY 2008**	**FY 2007**	**Year on Year Change**
Revenues	**12,081.5**	9,748.5	23.9%
OIBDA	**5,723.4**	4,892.9	17.0%
Operating income	**3,564.9**	3,260.6	9.3%
Net (loss)[1] / income	**869.5**	1,179.5	(26.3%)

The Telecommunications business unit comprises MTS, Comstar UTS, Sistema Shyam TeleServices Ltd., Sky Link and Sistema Mass Media.

Revenues in the business unit increased by 23.9% in 2008 to US$12.08 billion, compared to US$9.75 billion in 2007. This strong revenue performance was primarily due to the robust performance of MTS. The Telecommunications business unit accounted for 72.4% of the

[1] Here and further net (loss)/ income for the segments are presented after minority interest.

Group's consolidated revenues in 2008. MTS continued to be the main contributor and accounted for 84.3% of the unit's revenues in 2008.

The Telecommunications business unit's OIBDA increased 17.0% year–on-year in 2008 to US$5.72 billion, compared to US$4.89 billion in 2007. OIBDA margin stood at 47.4% in 2008, compared to 46.4% during the corresponding period of 2007.

The Telecommunications business unit saw net income decrease 26.3% year-on-year to US$869.5 in 2008. This was primarily the result of non-cash losses due to the translation of US dollar-denominated debt and losses from the impairment of the investment in MTT.

Business Unit 'Consumer assets'

(US$ millions)	**FY 2008**	**FY 2007**	**Year on Year Change**
Revenues	**2,596.5**	1,844.5	40.8%
OIBDA	**(94.7)**	173.1	-
Operating (loss)/ income	**(159.4)**	141.5	-
Net (loss) /income	**(394.4)**	65.2	-

The Consumer business unit comprises: the Real Estate segment (Sistema Hals); the Banking segment (MBRD); the Retail segment (Detsky Mir); the Tourism segment (Intourist) and the Healthcare segment (Medsi).

The Consumer business unit's revenues increased 40.8% year on year in 2008 to US$2.60 billion, compared to US$1.85 billion in 2007.

The Consumer business unit reported an OIBDA loss in 2008 of US$94.7 million due to difficult market conditions, primarily in the Real Estate segment.

The Consumer business unit reported a net loss of US$394.4 million in 2008. This was primarily due to foreign currency exchange losses and an increase in the operating losses of Sistema-Hals.

Business Unit 'Technology & Industry Assts'

(US$ millions)	**FY 2008**	**FY 2007**	**Year on Year Change**
Revenues	**2,532.4**	2,082.8	21.6%
OIBDA	**180.2**	(56.7)	417.7%
Operating income/ (loss)	**96.3**	(120.8)	-
Net loss	**(50.0)**	(164.6)	-

The Technology and Industry business unit comprises the High Technology segment, including Sitronics, the Radars and Aerospace segment and the Pharmaceuticals segment (Binnofarm).

The unit's revenues increased 21.6% to US$2.53 billion in 2008, compared to US$2.08 billion in 2007. The unit contributed 12.5% of the Group's consolidated revenues in 2008. Sitronics accounted for 79% of the unit's revenues in 2008.

The Technology and Industry business unit's OIBDA increased substantially to US$180.2 million in 2008, compared to a loss of US$56.7 million in 2007.

The Technology and Industry business unit reported a significantly reduced net loss of US$50.0 million in 2008, compared to a loss of US$164.6 million in 2007 and this was due to the continued improvement in the High Technology segment's performance.

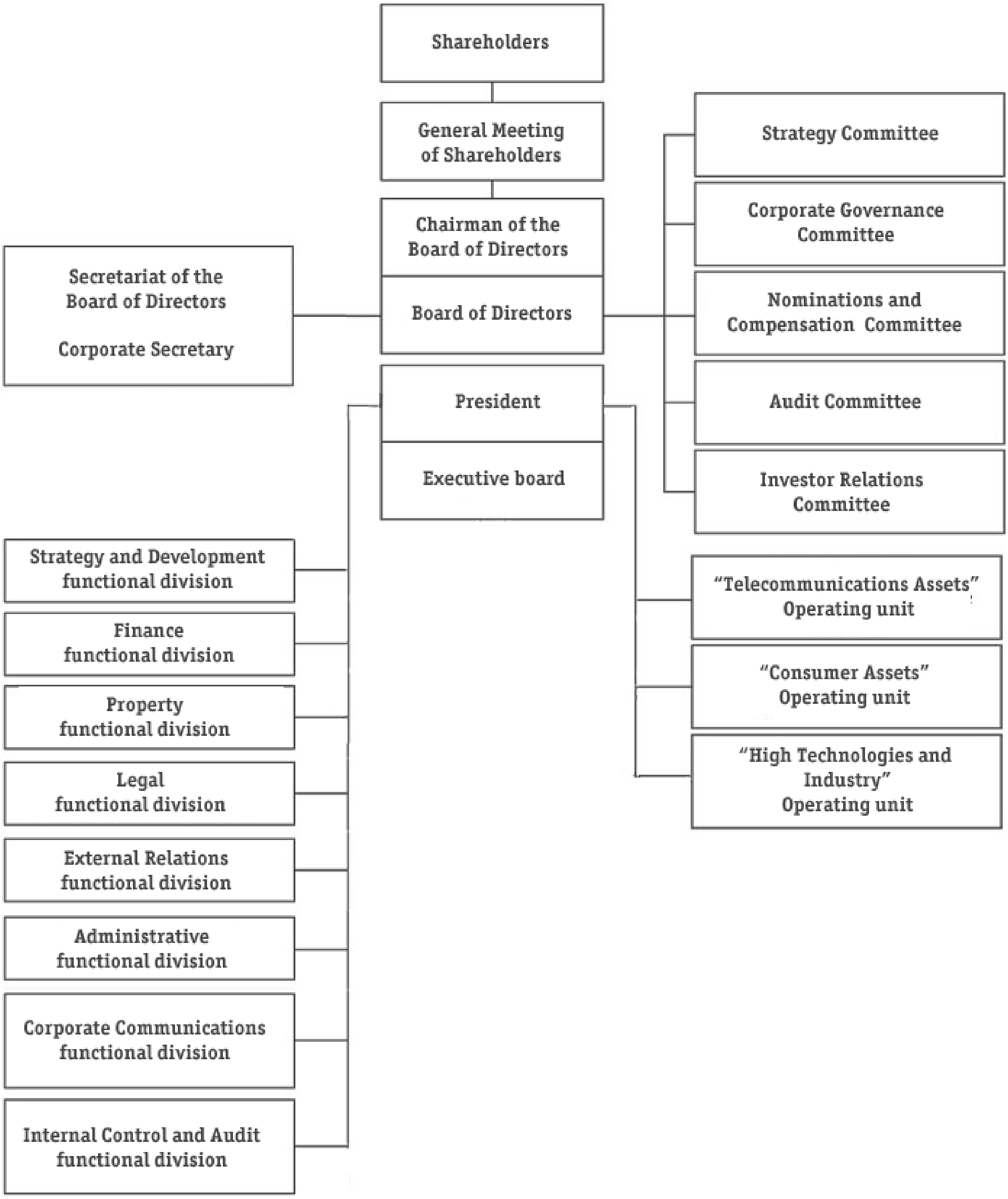
6. Corporate Governance

Sistema was one of the first Russian companies to begin developing a corporate governance system that meets international standards. The Corporation remains internationally respected for its system of transparency today. Its corporate governance system is founded on a set of basic principles: transparency of its procedures for investors and partners; an active and professional Board of Directors; and a systematic and collegial decision-making process. Sistema is guided by these principles in all areas of its business, including strategic and financial management, corporate governance, accounting, audit, risk management, HR policy and social policy.

Sistema's corporate governance principles and procedures are laid out in the Company Charter, as well as in various internal documents. Together, these define the structure and responsibilities of the governing and supervisory bodies. The codes of corporate behavior and of ethics reflect the Corporation's commitment to transparency, social responsibility and the principles of business conduct.

Corporate governance structure

The main governing bodies of Sistema are the General Meeting of shareholders, the Board of Directors, the President and the Executive Board. The Board of Directors and President have committees that help develop policy recommendations for relevant areas of the Corporation's business and organization.



General Meeting of shareholders

The main governing body of Sistema is the General Meeting of shareholders. Its activity is regulated by Russian Company Law, by the Company's charter and by other internal documents. The procedures regarding the General Meeting fully accommodate the shareholders' varying situations and needs. Information and materials for the meeting are distributed to the shareholders in Russian and English 30 days before the meeting, and the materials are also published on company's web site (www.sistema.com). Together with the announcement of the meeting, shareholders receive ballot papers and can cast their votes by letter ballot if they cannot attend in person. Sistema holds all General Meetings in convenient locations close to Corporate headquarters.

In 2008, the Annual General Meeting of shareholders was held on June 28. During the AGM, the following items were considered: the annual report and yearly financials, distribution of company net income and payout of dividends, elections of the Board of Directors, appointment of the auditor and approval of amendments to the internal documents concerning the Board of Directors and Executive Board.

Board of Directors

The Board of Directors is responsible for Sistema's strategy. It devises strategic and financial development plans, regulates investment activity, evaluates the Corporation's risks, approves corporate governance principles and procedures, approves deals and supervises the overall performance and management of the company.

The Board of Directors has 10 members: V. Evtushenkov, A. Goncharuk, A. Gorbatovsky, R. Sommer, D. Zubov, V. Kopev, E. Novitsky, S. Newhouse, R. Skidelsky and S. Cheryomin. Four of the members are Independent Directors. As a rule, the Board of Directors meets a number of times throughout the year.

In 2008, the Board of Directors held 13 meetings, of which 10 were planned meetings and three were held to deal with critical or otherwise outstanding situations.

At each conventional meeting, the Board of Directors considered between three and six main agenda items, such as strategic development, financial strategy and reporting, risk management, internal control and audit, corporate governance and HR matters. Other items for which the Board of Directors is responsible, such as approving deals, issue of securities and approving new internal documents, were included on the agenda as needed. Overall, in 2008, the Board of Directors considered 109 agenda items. Last year, the Board of Directors focused mainly on matters of strategic development, financial reporting and corporate governance.

Committees of the Board of Directors

Within the Board of Directors, there are five committees: Audit, Nominations and Remunerations, Corporate Behavior, Investor Relations and Strategy.

Audit committee

The Audit Committee has three members[*]: A Gorbatovsky (chairman), E Novitsky and S Newhouse. The secretary is L Gorbatova.

The Committee oversees the financial reporting and internal audit at Sistema and its subsidiaries, and coordinates the work of the internal control and audit departments. It also supervises the work of the external auditors, makes recommendations regarding their appointment and remuneration and helps to resolve discrepancies between the external auditors and the company management. In 2008, the committee met seven times.

Nominations and Remunerations Committee

The Nominations and Remunerations Committee has five members[*]: V. Evtushenkov (chairman), A. Goncharuk, D. Zubov, V. Kopiev and R. Skidelsky. The secretary is G. Ermakov.

[*] As of December 31, 2008

The committee determines the company's HR policy, makes recommendations to the Board of Directors concerning top management appointments, and proposes candidates for the Boards of Directors of subsidiaries and other affiliates. It also makes recommendations for the remuneration of the top management. The committee met twice in 2008.

Corporate Behavior Committee

The Corporate Behavior Committee has eight members*: V Kopiev (committee chairman), A Goldin, I Belikov, S Drozdov, G Ermakov, I Petrov, A Semyonov and S Cheryomin. The secretary is E Tulupov.

The committee prepares proposals for improving the corporate governance of Sistema and its subsidiaries and affiliates. It also ensures that the Company complies with current legislation within its charter and internal documents. In addition, the Committee works to prevent and solve corporate and ethical conflicts. In 2008, the committee met eight times.

Investor Relations Committee

The Investor Relations Committee has five members*: R. Sommer (chairman), A. Abugov, A. Buyanov, S. Newhouse and S. Cheryomin. The secretary is I. Potekhina.

The Committee primarily oversees the company's IR policy, presenting its recommendations to the Board of Directors. In 2008, the committee met six times.

Strategy Committee

The Strategy Committee has 11 members*: V. Evtushenkov (chairman), A. Goncharuk (deputy chairman), A. Abugov, A. Buyanov, S. Drozdov, R. Sommer, D. Zubov, V. Kopev, L. Melamed, V. Savelyov and S. Cheryomin. The secretary is A. Abugov.

The Committee looks at strategic development issues across all business lines. It met eight times in 2008.

Executive Board

The Executive Board is responsible for current management. It determines how strategy should be implemented, produces business plans, defines investment procedures, appraises employees and reviews issues to be submitted to the Board of Directors.

The Executive Board has 12 members*: L. Melamed (management chairman and Company President), A. Abugov, R. Almakayev, S. Boyev, A. Buyanov, A. Goldin, S. Drozdov, F. Evtushenkov, D. Muratov, V. Savelyov, I. Potekhina and S. Cheryomin. The Executive Board generally meets once every two weeks.

Development of corporate governance in 2008

In 2008, Sistema implemented various measures to develop its corporate governance system.

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* As of December 31, 2008

In June, economist Robert Skidelsky became the fourth Independent Director. This helped to create a Board of Directors that is more independent, more impartial and more open. In addition, Mr Skidelsky's knowledge will reinforce the overall Board expertise in economics and international economic relations.

Also in June, the Board of Directors approved the company's social responsibility strategy and issued a memorandum to the Sistema group regarding principles and policy in this area. As part of the "Improving the Quality of Life Through Innovation" program, this document forms the basis for the Group's social responsibility policy, and lays the groundwork for a system that will monitor the policy's effectiveness.

Sistema continued its system of rating corporate governance within the group. The results were used to develop the corporate governance systems for its subsidiaries.

In October, the Board of Directors held an extraordinary meeting to discuss ways to manage the company through the financial crisis. Prior to the meeting, we composed an anti-crisis plan and made additions to the regular information provided to the Board. Following the meeting, Sistema took the unusual step of releasing its unaudited current financial indicators to the investment community, aiming to put aside any speculations about the Company's financial condition.

Remuneration

Remuneration of Sistema's Board of Directors is calculated on the basis of the "Provision on Remuneration and Compensation Payable to the Company Board of Directors," adopted in 2006. This document stipulates paying Board members:

- Fixed amounts for attending meetings of the Board of Directors and its committees;
- Fixed amounts to the chairpersons of the Board of Directors and its committees;
- Additional annual remuneration, based on financial results for the year, which are distributed as a fixed sum, half of which is to be paid in shares (US$250,000-350,000);
- Additional remuneration equal to 0.1% of the increase in the company's market capitalization over the course of the year.

Remuneration for the executive management depends on the company's overall results, the achievements of a manager's division(s), and individual results.

In 2008, Sistema's incentive program for managers included the following:

- A monthly salary, set in accordance with company pay grades;
- Additional annual remuneration, if Sistema and the manager choose to continue the employment contract as of December 31 of the current year;
- A bonus for meeting individual targets;
- A bonus for any outstanding achievements, including completing major projects that are essential to the Company that year.

In 2008, Sistema also introduced a stock option program for managers that they are able to exercise within three years. Within the program, they will receive phantom shares in Sistema and its public subsidiaries and/or common shares in the non-traded subsidiaries. Remuneration is not specifically stipulated for participation on the Executive Board.

In 2008, total remuneration paid to the President, Board of Directors and Executive Management equaled RUB 552,455,267.50.

7. Shareholder Capital

Sistema Joint Stock Financial Corporation was registered at the Moscow Registration chamber on July 16, 1993. The Corporation is registered at 17/8/9 Prechistenka Street, Building 1, Moscow, 119034, Russian Federation.

A share issue was announced on November 1, 2007 that split the nominal value of the Company's ordinary shares by 1,000 times. After the share split on November 13, the number of outstanding shares increased to 9,650,000,000 ordinary shares, with a par value of RUR 0.09 per share. Sistema's share capital remained 868,500,000 rubles.

Sistema's shares are listed on the London Stock Exchange in the form of global depositary receipts (GDRs) under the symbol 'SSA'. One GDR represents 20 ordinary shares. Sistema's ordinary shares are traded on the Russian Trading System under the symbol 'AFKS', on the Moscow Interbank Currency Exchange (MICEX) under the ticker 'AFKC', and the Moscow Stock Exchange under the ticker 'SIST'.

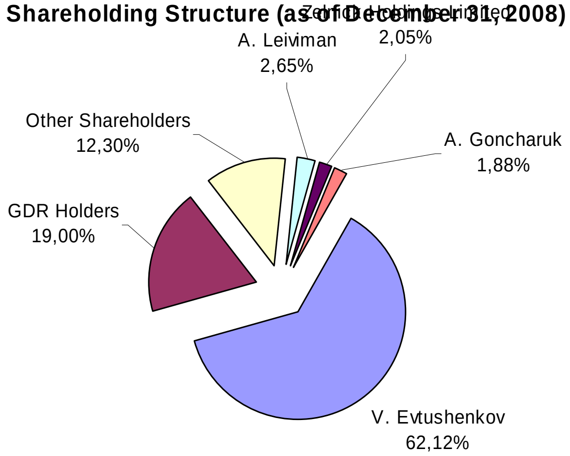
Shareholding Structure

As of December 31, 2008, Sistema had 21 individual shareholders and 12 entities, including 9 nominees. While the identities of its GDR holders are not generally reported to the Corporation, Sistema undertakes regular research to discover the identity of its GDR holders.

Such research allows Sistema to provide as much information as possible to the largest number of shareholders and is aimed at increasing the Corporation's transparency and providing greater liquidity for its shares on Russian and international exchanges.

Between March 2006 and February 2007 Sistema purchased 284,243 of its own shares, equivalent to 2.95% of its outstanding shares, for approximately US$347.3 million. This share buyback was conducted as part of a previously announced plan to establish a share option program for the Corporation's top management.

Shareholding Structure (as of December 31, 2008)

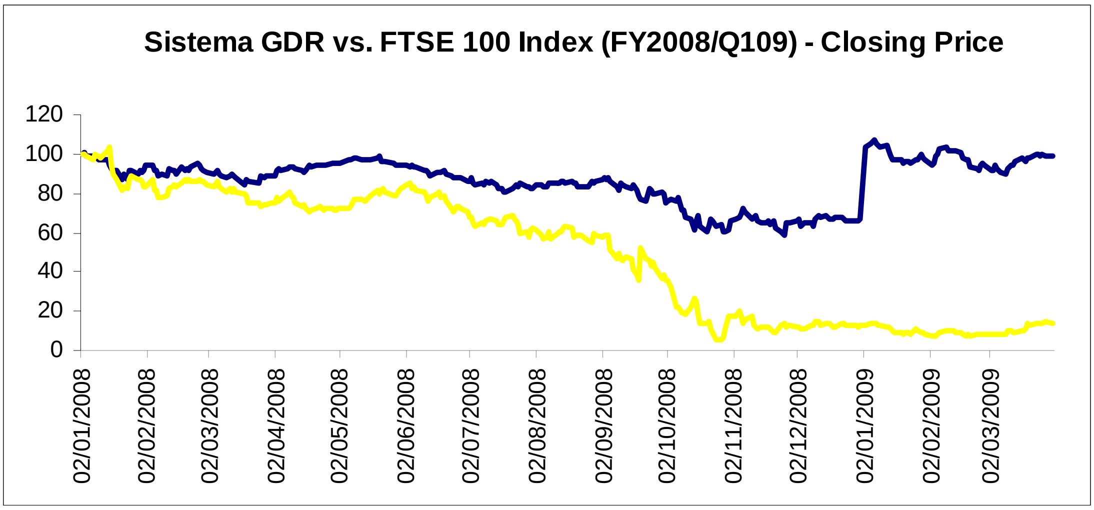


Share Price Performance

Since February 2005, when Sistema completed an initial public offering on the London Stock Exchange (LSE), 19% of the Corporation's outstanding shares have been in free-float in the form of global depositary receipts (GDRs).

Sistema's GDRs are listed on the LSE under the ticker 'SSA'. After the November 2007 share split was completed, one GDR represents 20 ordinary shares. Sistema's ordinary shares are traded on the Russian Trading System (RTS) under the ticker 'AFKS', the Moscow Stock Exchange (MSE) under the ticker 'SIST', and the Moscow Interbank Currency Exchange (MICEX) under the ticker 'AFKC'. Sistema's ordinary shares are a component of the MSE's technical index. On September 15, 2007, Sistema's ordinary shares were included in the list of stocks used to calculate the RTS Index.

The closing price for Sistema's shares on the first day of trading in 2008 closed at US$42.60. On the last day of trading, the closing price was US$5.50. The high of the year was reached on January 15th, when the closing price was US$44.00. The low of the year was achieved on October 27th, when the closing price was US$2.40. On March 31, 2009, the closing price was US$13.30.



Dividend Policy

Sistema's Board of Directors is guided by the Corporation's current dividend policy, as established in April 2008, in making its dividend recommendation to the Annual General Meeting. Dividends are determined according to the previous year's financial performance, and the payout level can be up to 40% of the Corporation's consolidated net income under US GAAP. This policy aims to both provide for a predictable sizeable dividend flow and maintain a dividend history while simultaneously giving the opportunity to reinvest profits to meet Sistema's capital requirements in order to maintain sustainable growth.

At the Annual General Meeting on June 28, 2008, the shareholders approved a cash dividend of RUB 2,512,500,000.00, or approximately US$106.4 million, for the 12 months ended December 31, 2007 to holders of Sistema shares. The dividend, which amounts to a payment of RUB 0.25 per share, or approximately US$ 0.21 per GDR, is more than five times higher than the dividend paid for the same period of 2006.

Share Structure and Performance of Subsidiaries

MTS

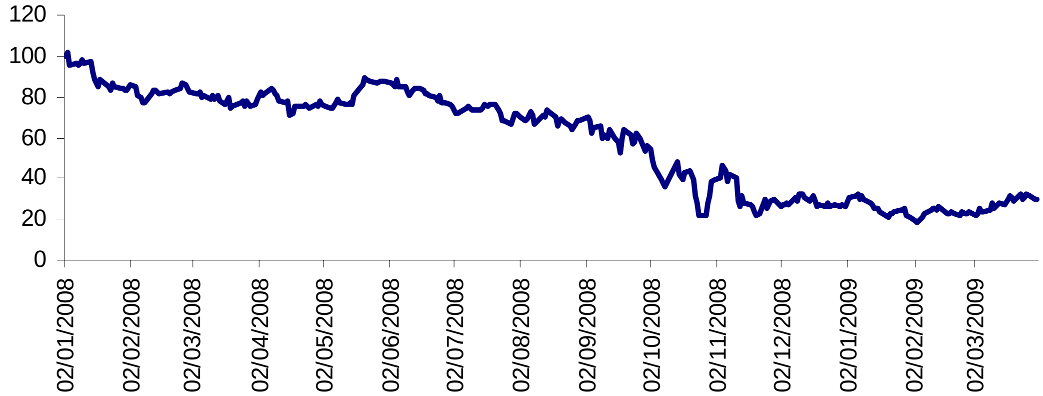
Mobile TeleSystems placed a Level III ADR issue through an IPO on the New York Stock Exchange (NYSE) on June 30, 2000. The current ADR to ordinary share ratio is 1:5, following a 1:4 ADR split in January 2005. MTS's major trading volumes are on the NYSE and trade under the symbol 'MBT'. MTS's shares are also traded on the RTS under the ticker 'MTSS' and as of March 17, 2008 had a relative weight of 0.67% on the RTS Index.

Ordinary shares of MTS are included on the MICEX under the ticker 'MTSI'. Currently the company has 1,993,326,138 ordinary shares with a nominal value of RUR 0.1 per share. As of December 31, 2008, Sistema owned 54, 7% of MTS's shares*.

The ADRs of MTS closed at US$100.07 on the first day of trading in 2008. The peak share price of US$101.90 was reached on January 3 and it closed at US$26.68 on the last day of trading of 2008. The company's market capitalization as of December 31, 2008 was US$10.6 billion. Its closing share price on March 31, 2009 was US$29.92 and its market capitalization was US$11.9 billion.

*Annex: * including active MTS shares.*

MTS ADR Closing Share Price on NYSE (FY2008/Q109)



Comstar UTS

In February 2006, Comstar UTS completed an IPO of 146,500,000 common shares. These shares included 139,000,000 newly issued shares and 7,500,000 shares sold by shareholders. The shares were admitted to trade on the London Stock Exchange in the form of GDRs at the ratio of 1 GDR per ordinary share. Approximately 34% of Comstar's shares are in free-float, traded as GDRs on the LSE under the ticker 'CMST'. Ordinary shares are traded on the RTS and the MSE under the ticker 'CMST'.

Currently, Comstar UTS has 417,940,860 outstanding shares with a nominal value of RUR 1 per share. As of December 31, 2008, Sistema directly or indirectly owned 53.6% of Comstar's common shares.

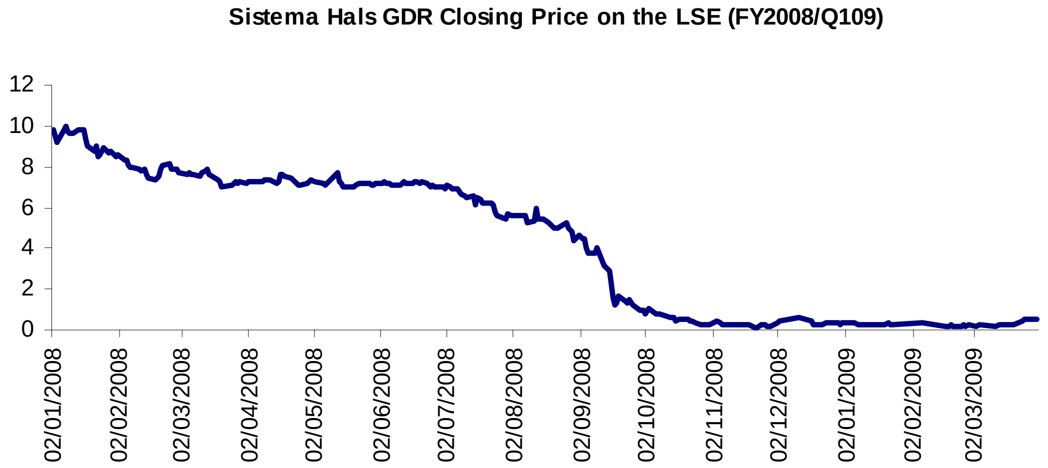
Comstar's GDRs closed at US$12.37 after the first day of trading in 2008. The year's peak share price of US$12.35 was reached on January 8, and it closed at US$3.95 on the last day of trading of 2008. The company's market capitalization as of December 31, 2008 was US$1.7 billion. The closing share price on March 30, 2009, was US$3.35 and its market capitalization was US$1.4 billion.

Comstar GDR Closing Share Price on LSE (FY2008/Q109)

Sistema Hals

Sistema Hals's shares were admitted to trading in the form of GDRs on the London Stock Exchange on November 8, 2006. The company offered 1,738,650 newly issued shares and 112,171 shares from selling shareholders. In addition, the underwriters exercised an option to purchase 168,256 ordinary shares in the form of GDRs to cover over-allotments in the offering. The shares were offered at $10.7 per GDR and $214.00 per ordinary share, representing a ratio of 20 GDRs per ordinary share. The shares of Sistema Hals are traded on the LSE in the form of GDRs under the symbol 'Hals'. Its ordinary shares have been included on the MICEX and MSE since 2006.

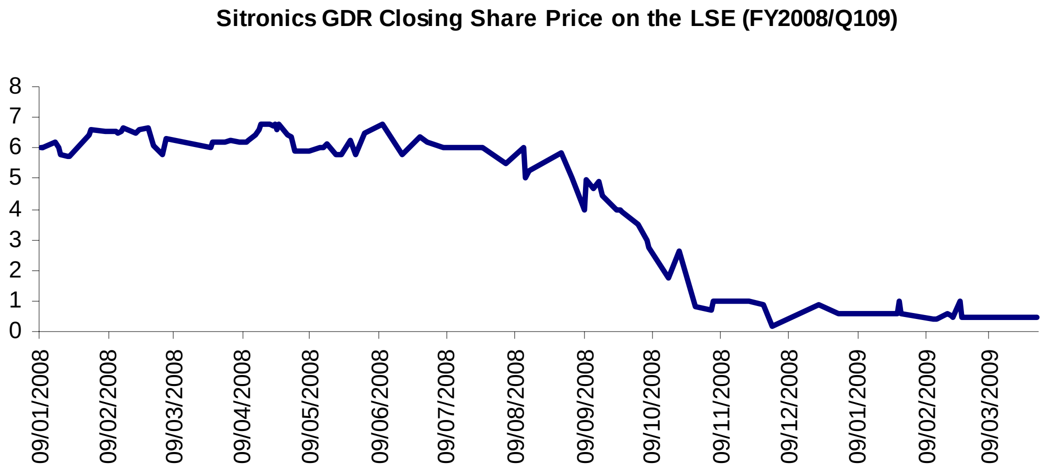
Currently, Sistema Hals has 11,217,094 ordinary shares. As of December 31, 2008, Sistema owned 80.8% of the ordinary shares of Sistema Hals and 18% were in free-float. After the first day of trading in 2008, the company's shares closed at US$9.85 per GDR, and they reached a high of US$10.00 on January 8, 2008. On December 31, 2008, the company's shares closed at US$0.32 per GDR and its market capitalization was 71789401 was US$72 million. On March 30, 2009, the closing share price was US$0.50 per GDR and its market capitalization was US$112 million.



Sitronics

On February 6, 2007, Sitronics completed an IPO in the form of GDRs on the London Stock Exchange, offering 1.675 billion ordinary shares under the ticker 'SITR'. This IPO confirmed its position as the leading high-tech firm in Russia, the CIS, and Central and Eastern Europe. The current GDR to ordinary share ratio is 1:50. Sitronics's shares are also traded on the RTS and MSE under the ticker 'SITR'.

Currently Sitronics has 9,547,087,190 ordinary shares with a nominal value of RUR 1 per share. As of December 31, 2008, Sistema owned 69.07% of Sitronics' shares and 17.55% of its shares were in free-float. After the first day of trading in 2008, the closing price of Sitronics' GDR was US$6.00. The peak GDR closing price was US$6.78 on April 21. On the last day of trading of the year, the company's GDR closed at US$0.60 and the company's market capitalization was US$114 million. The closing price on March 30, 2009, was US$0.47 and its market capitalization was US$89 million.



Asset structure

Company	Ordinary shares, owned by Sistema directly or indirectly	
	As of 31.12.2008	As of 08.04.2009
Business Unit "Telecommunications Assets"		
Mobile TeleSystems	54.7%*	54.7%*
Comstar-UTS	53.66%	53.66%
MGTS	66.88%	66.88%
Sky Link	50%	50%
MTT	50%	0%
Svyasinvest	25% + 1 share	25% + 1 share
Shyam Telelink (until 23.01.2009) Sistema Shyam TeleServices Limited (after 23.01.2009)	73.71%	73.71%
Sistema Mass Media	100%	100%
Russian World Studios	51%	51%
Business Unit "Technology & Industry Assets"		
Sitronics	69.08%	69.08%
Concern "RTI Systems"	97%	97%
Binnopharm	100%	100%
Business Unit "Consumer Assets"		
Sistema-Hals	80.8%	19.45%
Detsky Mir - Center	100%	100%
Detsky Mir	100%	100%
MBRD	94.57%	94.57%
East-West United Bank S.A.	100%	100%
Dalcombank	100%	100%
Intourist	66.2%	66.2%
Medsi	100%	100%
Petrochemicals		
Bashneft	21.4%	90.69%
Ufimsky Refinery	24.36%	87.67%
Novoil	26.93%	95.35%
Ufaneftekhim	23.13%	78.69%
Ufaorgsintez	22.8%	84.35%
Bashkirnefteprodukt	25.44%	79.1%

*Annex: * including active MTS shares.*

8. Risk Management

There are numerous risks that Sistema's business areas could face. They represent processes and factors that the company has little or no influence over. Therefore, effective evaluation and mitigation of these risks is an important component of Sistema's strategy.

Risk management is conducted in a centralized manner within the framework of the internal regulations that have been approved on a Sistema-wide level, as well as on a business area level. This process concerns all corporate activities, and is intended to reduce the probability and impact of any events that could negatively influence company operations. The corresponding measures are expected to provide a reasonable guarantee that the strategic goals of the company's activities will be achieved.

Political Climate
The political situation in Russia over the last year can be characterized as comparatively stable. At the same time, there has been increasing political instability in several neighboring CIS member states. This allows various political forces to influence all areas of these countries' economies, especially private companies.

Economic Situation
Russia's economic development was uneven in 2008. The first half of the year was represented by dynamic growth, due to record-high oil and commodities prices. However, the global economic crisis impacted the Russian economy in the second half of the year.

Russian GDP growth was 5.6% in 2008, according to Ministry for Economic Development, compared to 8.1% in 2007. At the same time, real disposable income, which is one of the key drivers of economic growth, grew by a marginal 2.7% in 2008, which is considerably lower than the 12.1% witnessed in 2007.

Consumer price inflation totaled 13.1% in January-December 2008, exceeding the figures seen for the previous five years. The acceleration of inflation in 2008 was mainly caused by significant growth in the global price of food and commodities. In the fourth quarter of 2008, however, inflation growth decelerated significantly, as a result of changes in the global economic environment.

In 2008, Russia's Balance of Payments showed a sharp trend reversal, compared to what has been witnessed in recent years. Total capital outflow in 2008 exceeded capital inflow in 2005-2007, which led to a decrease of foreign gold & currency reserves for the first time since 1998. This occurred despite a record-high positive current account balance. Nevertheless, Russian foreign reserves made it possible to compensate for the negative effects of trans-boundary capital movements, and to cope with the flight of foreign capital.

The value of Russian FX reserves had decreased by 10.8% by the end of 2008, and stood at $427.1 billion as of January 1, 2009. Russian FX reserves still remain the third largest in the world.

Russia and CIS countries continue to face the problem of being too dependent on oil prices. There is also the risk that strong macroeconomic trends may slacken in CIS countries, due to the growth of political instability or the increase of state involvement in the countries' economies.

Exchange Rate

Sistema faces exchange rate risks linked to changes in the value of the ruble, the euro and the grivna to the US dollar. The decrease in external trade, coupled with capital outflow caused by the deterioration of the global financial environment, may create pressure on the ruble. This can have a negative impact on the Sistema Group and its subsidiaries.

Capital Markets
There is the risk that Russian equities will underperform their counterparts in other developing markets. The two principle reasons for this possible weakness are the methods used to establish their fair value and the current level of liquidity in the global market as well as in Russia. There is also a risk that capital inflow will shrink as a result of tighter global liquidity, the impact of the credit crunch, political risks and a review of the market's growth prospects by the investors.

Interest Rates and Other Credit Risks
Changes in interest rates on the Russian and international markets caused by the credit crunch and tighter liquidity in the banking system could significantly affect the cost of borrowing and of raising additional capital. Sistema operates a number of capital-intensive businesses; therefore, any changes in borrowing costs could have a negative impact on the Corporation.

9. Social Responsibility

A primary contribution of Sistema's system of social responsibility can be found in the very core of its high technology business model: its contribution to the development of the country's economic potential, and the improvement of the quality of life for its consumers.

Sistema's philosophy of corporate social responsibility relies on the long-term and steady development of the Corporation. This makes it possible to harmoniously integrate a successful business with basic human values and the priorities of national development.

Creating favorable conditions for the innovative development of client-oriented business diversifies the Russian economy and strengthens its competitiveness in the global marketplace. Sistema also makes every effort to take into account both the interests of society as a whole and the expectations of stakeholders in its development strategy. This is a manifestation of its corporate social responsibility.

The Corporation maintains an ongoing dialogue with all stakeholders: state and government bodies, shareholders, regulatory organizations, clients, partners, employees and investors. This dialogue helps Sistema effectively respond to questions raised by stakeholders.

The position of Sistema regarding corporate social responsibility was reflected in the official document entitled "The Policy of Corporate Social Responsibility of Sistema." This document determines the principles and business lines of the Corporation in the sphere of social responsibility. It includes the management of social factors that support the sustainable development of the Corporation, the optimization of its contribution to national socio-economic development and the development of the regions where Sistema is present. It also strengthens the Corporation's reputation.

The basic principles of Corporate Social Responsibility (CSR) were determined and fixed in "the Policy." According to these principles, the Corporation's responsible approach to its business includes:

- improvement of life quality through innovative business development;
- the provision of a safe work environment and an investment in the development of human potential;
- protection of the environment;
- effective investments in production development, oriented to increase competitiveness of the Corporation in the interests of business and society as a whole;
- stakeholders' expectations and opinions, a systematic approach to building honest and mutually beneficial relations based on ethical principles;
- development of local communities, particularly by creating mutually beneficial social partnerships in the regions where the Corporation is present;
- transparency and development of social accountability.

Together with the introduction of "Principles from Policy," Sistema has undertaken measures to strengthen management systems by developing the CSR within the Corporation. A special department dealing with developmental processes has been created. Its purpose is to build effective management systems using the best practices within the structure of Sistema, including subsidiary companies, to propagate and implement the latest expertise for managing CSR. In addition, this department will incorporate practical training in CSR through a series of seminars engaging external experts in this sphere.

Since 2007, the Corporation has issued an Annual Social Report, in which its activity in the field of CSR is presented in both qualitative and quantitative terms according to conventional international and Russian standards of non-financial accountability. In line with the plan of the development of the unified non-financial accounting system in the Corporation, public companies will issue their Social Reports in 2009, and non-public companies will issue their Reports within the year.

Sistema's representatives are active members of the Committee of Corporate Responsibility of the Association of Russian Managers. They also actively take part in scientific research and practical developments in the field of CSR.

The Corporation became one of the first Russian companies to affiliate with the United Nations Global Compact (in 2002). In addition, Sistema adheres to the Conception of Social Responsibility that has been formulated by the Russian Union of Industrialists and Entrepreneurs (RSPP), and that has been set out in the Social Charter of Russian business.

One of the Corporation's significant social activities is charity, which is carried out within three main fields: Culture, Science and Education, and Social Development.

Sistema is implementing large-scale projects and programs in the area of Russian culture. These projects are directed towards protecting and popularizing Russia's cultural heritage.

Since 2003, Sistema has been the main sponsor of the State Russian Museum. The funds raised from the Corporation go to the museum's restoration, as well as to its publications and exhibitions. Sistema has provided technical and financial support for the innovative global project called "The Virtual World of the State Russian Museum," a virtual network of educational and cultural centers in Russia's regions and abroad.

Among the most important events in the past year which were carried out as part of the collaboration between Sistema and the State Russian Museum were the unique exhibition projects "Time to Gather…" and "The XX Century in the Russian Museum," held with great success in the State Museum-Reserve Tsaritsyno in Moscow, and the St Petersburg exhibitions "A Step Towards Bronze" and a festival of art in gardens and parks entitled "Imperial Gardens of Russia."

The Corporation supports to the development and popularization of domestic classical art such as music and ballet by sponsoring the festivals of The Mariinsky Theatre, including "The Easter Festival," "The Stars of the White Nights" and a series of concerts. In addition, the Corporation sponsors "The Musical Kremlin," held annually in the Armory Chamber of the Kremlin in Moscow, and the international ballet competition "Benois de la Danse," which presents one of the most prestigious ballet awards.

The Corporation gives special attention to the theatrical arts as well. Sistema maintains a close relationship with the "Moscow Sovremennik Theatre," which, thanks to the participation of the Corporation, was able to continue producing the play, "The Three Comrades." The Corporation continues to collaborate with the Studio of Theatrical Arts, where the funds of Sistema have supported plays such as "The River Potudan" and "The Battle of Life."

As a sponsor, Sistema participates in a number of major restoration projects. With its participation, reconstruction and restoration of the Marfo-Mariinskaya Monastery was completed. In September 2008, the re-consecration ceremony was held for the monastery.

The Corporation is aware of the importance of its support for young people's scientific and innovative development, and of the need for Sistema's participation in educational projects and programs. For many years now, Sistema has provided a scholarship program for outstanding students in a number of technical institutes. This program allows the students to obtain a scholarship and to have the chance to gain practical experience within the Corporation. In addition, Sistema sponsors the program, "A Step into the Future – Moscow," organized by Bauman Moscow State Technical University, and supports the university's robot technology team at international competitions.

The Corporation also acted as one of the sponsors of The Third International Festival of Science, organized by Lomonosov Moscow State University, where its advanced technologies were presented alongside the innovative student projects.

The Corporation successfully arranges masters programs, such as the Higher School of Management and Innovations, founded several years ago with the participation of Moscow State University. As part of this program, Sistema's employees have the opportunity to increase their qualifications and obtain a master degree. In addition, employees are provided with opportunities to enhance their abilities in various courses, using the facilities of the Corporate University of Sistema, which provides a wide spectrum of educational services.

Traditionally, Sistema has supported Russian sport: the Fund for Russian Olympic sportsmen, the Rugby Union of Russian, the Federation of Bicycle Sport, the Sport Federation of the Ministry of the Interior and a series of sport schools for children and youth.

The realization of projects in the social sphere is an important component of the charitable activities of the Corporation. Sistema renders aid to several orphanages and refuges, provides support to help children to become fully integrated in society, and offers children with limited possibilities the necessary training materials.

The Corporation also collaborates closely with several charitable foundations which provide aid to the disabled and veterans. Sistema contributes to the purchase of equipment and materials to assist in rehabilitation care for the disabled.

These numerous projects are being completed with the participation of the Corporate Charitable Foundation System, which was founded in 2003 for the efficient management of social investments of the Corporation and its subsidiaries.

PART 2 BUSINESSES OVERVIEW

10. Business Unit “Telecommunications Assets”

Vision & Strategy

The strategy in the Telecommunications Asset business area is focused on the following broad goals: winning and maintaining leading positions in key market segments and geographies, entering fast-growing segments and developing markets, exploiting synergies, the maximum integration of existing assets and diversification into media and R&D.

MTS and Comstar form the core of the telecoms assets and cover all segments of the telecoms marketplace. There has been a gradual exit from, or repositioning of, non-core assets, including the sale of MTT in the first quarter of 2009.

As the center of expertise and coordination of development in the telecommunications segment, the Telecommunications Asset business area is developing a long-term development strategy, and is improving the interaction of telecommunications and media assets in order to implement projects over the medium term to develop key aspects of the business.

First, the business area is focused on increasing operational efficiency. This includes the operational restructuring of telecoms assets and the joint construction and utilization of infrastructure, as well as the introduction of unified business processes and the exploitation of efficiencies of scale. Examples of this strategy include the acquisition of telecoms assets (Stream TV and Comstar Direct) by Comstar from SMM, as well as the joint utilization of network infrastructure by MTS and Comstar.

The strategy in the Telecommunications Assets business area also envisions the creation of an integrated operator with cooperation and coordination in the development of telecommunications and media assets. This will support the potential creation of a global telecommunications player based on MTS and Comstar fixed-mobile converged services. Such a business will be represented across all segments of the marketplace. This strategy already includes the completed transfer of the cable assets from SMM to Comstar, which will allow SMM to focus on developing a top content player to be present in traditional and new media segments.

The development of convergent services and combined businesses includes the transition to NGN networks, provision of convergent services to the consumer, the introduction of an umbrella brand and implementation of other key projects to create a single point of access to the full panoply of telecommunications services. Examples of this strategy include the adoption of the MTS brand by Sistema Shyam Teleservices in India, as well as the offering of combined service packages by MTS and Comstar.

In order to evaluate and lead the introduction of new technologies, Intellect Telecom is leading the creation of full-fledged research and testing centers for the Telecommunications Assets business area as a whole, and has developed projects for evaluating new technology and developing the network infrastructure of MTS, Comstar and Sistema Shyam Telecom. Collaboration with global partners and vendors remains another key source of innovation.

Selective international expansion will continue, with a focus on developing regions with substantial growth potential and utilizing new technologies. This strategy is demonstrated by the acquisition of Sistema Shyam Teleservices in India. The Indian project represents an important first step on the path to creating a global player by entering new markets with demonstrated growth potential, and it strengthens and diversifies the Corporation's portfolio of telecommunications assets.

These strategic approaches are helping the business area to increase returns from existing assets, and to optimize expenditure on their development within the framework of the Corporation's wider strategic priorities.

Mobile Telecommunications

Marketplace

The growth of the mobile telecommunications market has been a primary driver of the overall telecommunications sector in Russia in recent years. The combined mobile and wireless sectors accounted for 2.9% of Russian GDP in 2008, down from 3.1% in 2007[2], a result of the overall slowing of growth in the sector due to the global financial crisis and its impact on the Russian economy in the second half of 2008.

The market for mobile telecommunications was worth around US$23 billion in 2008, and the market has grown by an average annual rate of 39% in recent years. Voice services accounted for US$19.5 billion, data-exchange amounted to US$935 million, and value-added services (VAS) reached US$2.6 billion in 2008.

The level of mobile penetration in Russia reached 129.4%[3] at the end of 2008, equal to levels in the most developed telecommunications markets in the world. Mobile telephony accounted for a 45%[4] share of the total Russian telecommunications market in 2008. In 2009, the launch of third-generation (3G) services and the growth in the number of subscribers using these services is expected to increase revenues from data-exchange services. At the same time, an expected recession in Russia in 2009 is likely to lead to a short term slowing in growth in consumption of mobile services. Notably, the 3G market is expected to escape this trend and grow by at least 50%, according to Sky Link forecasts.

In recent years, the market for mobile telecommunications in Russia has developed at a rapid pace, with the number of subscribers doubling each year. Growth in subscriber numbers was driven by penetration of new target market segments and income groups, as well as by a reduction in prices for services and mobile devices.

Starting in 2006, as the market gradually approached saturation, the growth rate for new mobile-telephone subscribers began to fall. During 2008, the average rate of subscriber growth held steady at 2007 levels of around 3%. As the market has become saturated, mobile operators have shifted their focus to the quality of the subscriber base. The marketing resources of operators are no longer primarily focused on first-time subscribers. Instead, they are directed at retaining subscribers, increasing the average revenue per user (ARPU) and winning subscribers over from rival operators.

In the fourth quarter of 2008, Russian regional markets[5] accounted for around 78%[6] of subscriber growth, and the regions now provide the primary source of the subscriber base of operators through new subscribers. The regions have seen substantial growth in real household incomes in recent years, and these markets are now an important focus for mobile operators.

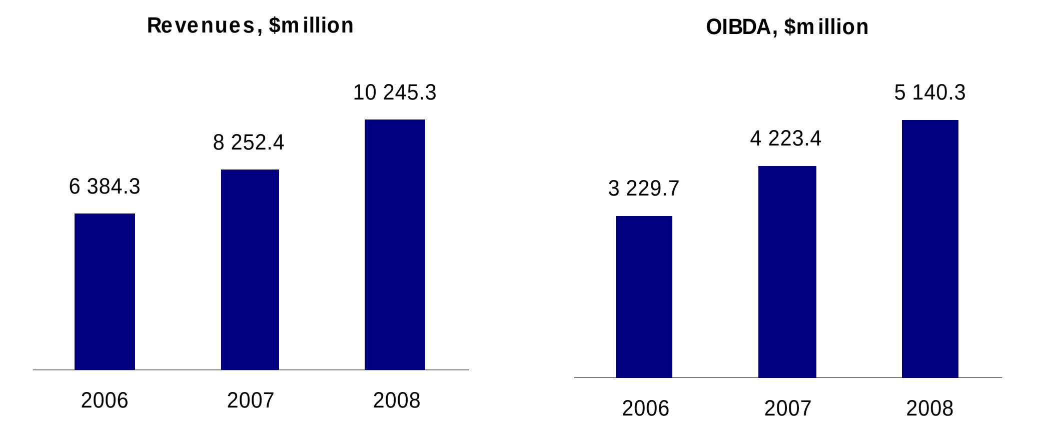
Data-exchange services are currently the fastest growing segment of the Russian and global mobile communications marketplaces. The volume of data on CDMA and UMTS (3G) networks in 2008 amounted to 1,636 terabytes, nearly three and half times the level in 2007. The market for mobile data-exchange, using a variety of technical standards, has grown by around 50%

[2] Source: Rosstat, Russian Ministry of Economic Development & Trade
[3] Source: AC&M Consulting
[4] Source: Rosstat, Russian Ministry of Economic Development & Trade
[5] Excluding Moscow, Moscow Region and St. Petersburg
[6] Source: AC&M Consulting

annually. One of the main trends in the global telecommunications market is the movement toward the integration of standards for terminal equipment and the emergence of multi-standard devices. This is erasing barriers between the different technologies currently in the marketplace.

In spite of the negative impact of the global financial crisis, the markets of the CIS retain substantial long-term growth potential for mobile operators due to rising income levels, generally poor fixed-line services and liberalization of the telecommunications sectors in several countries in recent years. Ukraine's level of mobile penetration has matured rapidly, and reached 121% at the end of 2008. Penetration in Belarus reached 86%, and 80% in Armenia. In Central Asia, penetration rates are far lower, but are growing rapidly. At the end of 2008, mobile penetration reached 44% in Uzbekistan, and 19% in Turkmenistan.[7]

Mobile TeleSystems (MTS)



Company in Brief

Mobile TeleSystems (MTS) is the largest mobile-phone operator in Russia and the CIS in terms of subscriber numbers, sales and market capitalization. MTS serviced over 95.66 million subscribers as of December 31, 2008. Founded in 1993, MTS today provides mobile communications in Russia, Ukraine, Uzbekistan, Turkmenistan, Armenia and Belarus, a territory with a total population of more than 230 million. MTS has been listed on the New York Stock Exchange since July 2000, and trades under the ticker 'MBT'. The Company's shares have been listed locally on Moscow Interbank Currency Exchange (MICEX) since November 2003 under the symbol MTSI. Sistema owns 52.8% of the shares of MTS. The free float of the Company's shares is approximately 46.7%.

Operational & Financial Results

MTS delivered strong results in difficult market conditions in 2008. Subscriber growth and increasing contributions from voice and data usage drove a 24.2% year-on-year increase in consolidated revenues to US$10.245 billion, compared to US$8.252 billion in 2007. Consolidated OIBDA increased by 21.7% to US$5.14 billion in 2008, with strong cost controls contributing to a 50.2% OIBDA margin.

Total consolidated subscriber numbers increased by 9.3 million in 2008 to 95.66 million. The Company added 7.2 million subscribers in Russia, 2.85 million in Uzbekistan, 640,000 in

[7] Source: AC&M Consulting, company data, national statistics

Armenia and 520,000 in Belarus. The Company saw its subscriber base fall by 1.88 million in Ukraine, while still maintaining overall market share.

The Company's sales in Russia grew by 27% in 2008 to US$7.84 billion, compared to US$6.18 billion in 2007. Strong sales growth was attributed to the inflow of new subscribers and growth in voice and data-exchange services. MTS maintained leading positions in the majority of markets where it is present: 34% market share in Russia; 33% in Ukraine; 46% in Uzbekistan; 87% in Turkmenistan, 79% in Armenia and 52% in Belarus.[8]

The company launched its 3G network in Russia in May 2008. At the beginning of 2009, the 3G network was active in 20 cities in Russia. The spread of 3G technology allows MTS to offer subscribers additional new and value-added mobile services, including wireless broadband access to Internet. The successful launch of the 3G network provides a new avenue for increasing customer loyalty and increasing ARPU. In December, MTS launched a 3G network in Uzbekistan, which will initially cover central Tashkent and which will be further deployed during 2009.

In October 2008, MTS initiated sales of iPhone 3G™ in Russia. Buyers of the iPhone 3G are able to sign onto existing MTS rate plans as well as special rate plans (i-Onliner and SIM) for active users of mobile Internet.

Also in October, the Company signed an exclusive, strategic non-equity partnership agreement with Vodafone. The four-year deal allows both companies, the number-one and number-two largest mobile operators in Europe[9], to combine their strengths in marketing and technology, and covers Russia, Ukraine, Uzbekistan, Turkmenistan and Armenia. In particular, the partnership will help MTS in a number of areas, such as obtaining advantageous procurement terms for equipment, advisory services on network development, CRM and key-account management. It also provides MTS with an exclusive range of products, services and devices with demonstrated track records of success in other markets.

The Company made important changes to its top-management team in 2008 in order to ensure the continued success of MTS and its continued future leadership of the Russian and CIS marketplace. Mikhail Shamolin was named president and Chief Executive Officer (CEO) of MTS in May 2008. In order to strengthen corporate governance, the Board of Directors was enlarged from seven to nine members, including three independent directors, in October 2008. The Company's established track record was recognized again in 2008 by ratings agency Standard & Poors in its Corporate Governance Rating, which assigned MTS one of the highest ratings of any Russian company, with a score of 7.3 on the Russian national scale.

In January 2008, the Company completed the redemption of a five-year US$400 million Eurobond issued in January 2003. During the year, MTS placed three ruble-denominated bonds worth RUB 30 billion. The funds raised are intended for general corporate needs.

During 2008, MTS continued to build upon its strong brand equity as one of the best-recognized and trusted brands in Russia and the CIS. In April 2008, MTS became the first and only Russian company named in the BRANDZ™ Top 100 Most Powerful Brands global survey, conducted by Millwood Brand and the *Financial Times*. In December, MTS reached an agreement with Indian mobile operator Sistema Shyam TeleServices to bring the MTS brand to the Indian market.

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[8] Source: AC&M Consulting

[9] Source: Informa Telecoms & Media, operator ranking based on proportionate subscribers.

The success of MTS in launching its 3G network and services and creating new possibilities for mobile communications was recognized at the Russian Mobile VAS (Value-Added Service) Awards 2008, when it received awards in five different categories: 'Best Mobile Operator in the Area of VAS,' 'Mobile Content,' 'Community and User Content' and 'User Convenience.'

MTS was also recognized in 2008 for its success in developing services and tariff plans to meet the needs of different customer segments, including youth, women, families, work migrants, small businesses and corporate clients. The Company received an award for 'Innovation in Marketing Strategy and Service Development' at the Global Telecoms Business Innovation Awards 2008.

Strategy & Outlook

The short-term and long-term strategy of MTS continues to be based on the formula '3+2,' and is focused on both strengthening the position of MTS as the leading communications brand in the CIS and increasing shareholder value.

The 3+2 formula is based on the following three goals:

(1) Provision of the best customer experience, including delivering superior quality at all touch points, increasing customer lifetime value and driving demand stimulation while focusing on CAPEX optimization and development of distribution.
(2) Driving data & content services, including compelling Internet user experience, innovative services & leading content portfolio and broad and rapid infrastructure deployment (3G).
(3) Expansion in the CIS and developing markets, provided necessary financing resources are available.

In turn, ensuring that these goals are met requires the application of the following approaches:

+1. Spending should be efficient and focused on optimizing operational costs and concentrating capital expenditure on supporting strategic projects.

+2. A focus on the development of the most efficient processes and organizational structure for MTS and its subsidiaries.

Sky Link

Company in Brief

Sky Link is the leader in the Russian 3G telecommunications market, providing high-speed mobile Internet access and voice communications based on CDMA 2000 1X EV-DO 3G technology operating with a 450 megahertz radio interface. Today, Sky Link provides 3G services in more than 5,000 cities and towns in 32 Russian regions. As of December 2008, Sky Link serviced more than 960,000 subscribers. The Company's strategy is based on strengthening its market positions while maintaining a balance of voice and data in the three primary 3G market segments: transit traffic, service development and device access. Sistema owns 50% of the shares of Sky Link.

Operational & Financial Results

Sky Link delivered a strong performance and enhanced OIBDA margin in 2008, enabled by the launch of new technology (such as EV-DO and EV-DO Rev. A[10]) and growth in both subscriber numbers and average revenue per user (ARPU). Revenues grew by 19.6% to US$333.94 million in 2008, compared to US$279.25 million in 2007. OIBDA increased significantly by 452% to US$66.00 million, and the OIBDA margin increased to 19.8% from 4.2%.

Despite deteriorating conditions in the global and Russian markets over the course of the year, the 3G market was largely unaffected. 3G remained the primary area of growth for all mobile-communications operators, and saw a steadily increasing demand. The total number of 3G subscriptions as of January 1, 2009, was 50% higher than a year earlier, and traffic increased two-fold.

During 2008, Sky Link maintained its position as the clear leader in the Russian 3G market, possessing the largest 3G network and an 82%[11] share of 3G traffic, despite the much larger mobile subscriber base of the 'big three' Russian mobile operators. It increased subscriber numbers by 130% year-on-year to 960,000. The Company increased its share in the total market for mobile Internet access (including all access technologies) to 12.5% in 2008[12], compared to 8.5% in 2007.

The level of ARPU for Sky Link reached US$35.2 in December 2008, and was US$44.2 in Moscow and US$27.5 in St Petersburg. It averaged US$25 for the regional operating companies at the CB rate. Data-exchange traffic per user increased by 70% to 303 megabytes in December 2008, compared to 171 megabytes in December 2007. Sky Link's ARPU level is the highest in mobile telecom industry.

In line with the Company's balanced-growth strategy, Sky Link was able to increase the share of mobile data-exchange in total revenues to 50%, compared to 35% in January 2008 (15% in January 2007), and this was made possible by the introduction of new technology. Data-exchange traffic levels generated by the Company's subscribers increased more than two-fold, from 207 terabytes in December 2007 to 470 terabytes in December 2008. December 2008 traffic levels were ten times higher than the volume in December 2006, reflecting an important shift in how and where people are accessing the Internet. Today, 55% of Sky Link users utilize

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[10] Evolution Data Optimized Revision A
[11] Source: Com News Research
[12] Source: Sly Link appraisal

laptops and USB interfaces to access the Internet, and 40% of personal computers sold in Russia are now laptops.

Beginning in 2008, Sky Link subscribers in Moscow, St Petersburg, Moscow and Leningrad Regions, Yekaterinburg and Chelyabinsk have been able to access data-exchange services using EV-DO Rev., a wireless technology. The use of this CDMA-based technology allows users to increase sending rates by an order of magnitude, from 1.8 megabits/second to 3.1 megabits/second. This rate of data speed allows subscribers to use video communications, interactive television and other multi-media services which require high data-exchange speeds. The share of Sky Link's total data-exchange traffic generated by the 3G (EV-DO) network reached 92%.

In order to best exploit this fast-growing marketplace, the Company moved to create a unified operating company with a network of affiliates in Russia's regional markets in 2008. A single system of financial planning and reporting was implemented, along with common policies on tariffs and products. In August 2008, a single call center was put into operation to serve Sky Link's clients across Russia, and in December, a single structure for rate plans was introduced across all of the markets where the Company is present. Going forward, Sky Link plans to gradually transform subscriber service to provide even better quality of service, simplify roaming options and ensure a single high standard of service across the entire territory covered by the Company.

In 2008, the Company continued to launch new products and services, further demonstrating its competitive advantage in being able to offer unique, integrated and packaged solutions. An IPM Content Billing solution was implemented, allowing for the management and billing of downloaded content. This represents a major and important shift towards being able to tailor tariffs and services to meet the needs of each user.

A new line of unlimited content rates and tariff options were developed and launched during the year that incorporated charging for Internet traffic based on its content and timing, including 'Unlimited Internet,' 'Unlimited LiveJournal,' 'Unlimited Weekends' and others. This solution allows for the charging of any data-exchange service in real time, while obtaining information about subscribers in order to deliver tailored products and tariff plans in the future.

In Moscow, new and unlimited content tariffs were implemented that can be activated as part of any rate plan, and they accounted for 20% of new subscriptions as of March 2009. From March 2009, content tariffs became available in Tver, and the Company plans to make them available in all regions in the near future. Low-cost national and international long-distance plans were expanded to six regions during 2008. In addition, new bonus programs were introduced, providing bonus voice minutes for active users of Internet traffic and vice versa.

New services were launched that allow Sky Link users to manage their accounts, services and devices, including Sky Balance (in 15 regions) and a regional version of the Sky Point Lite portal. For the 2008 presidential elections, a special Elections Mobile portal was launched, which provided subscribers with SMS messages providing updates on the election results. In Moscow and St Petersburg, the Mobile Rutube portal was launched, allowing the publication and exchange of user-generated video content in mobile formats. In Moscow, the Mobile Media Broadcasting service was launched commercially, providing live news updates via RSS channels. The Videocalls service was also tested in Moscow, permitting live video interaction through the Internet. This service was developed jointly with Videoport LLC.

In 2008, a deal was signed with Qualcomm Inc. to expand BREW hosting services to all of Russia as well as the CIS, the Baltic States and Central and Eastern Europe without additional technical support costs from Qualcomm. A video services catalogue based on BREW technology was supplemented by real-time access to 200 web cameras placed in cities and towns in 30 countries.

The development of 'packaged' video services using the EV-DO format is also an important mission for the Company. In 2008, it launched Dacha Guard, a service that allows users to maintain video surveillance of their country house and property by using high-speed data-exchange made possible by EV-DO technology. Going forward, the Company has also developed marketing material and a business case for VoIP telephone, VoIP roaming and VoIP office products.

Sky Link launched its 'Static Domain Name' service in 2008. It allows for the creation of a personal website with a dynamic IP address. The option is aimed primarily at Sky Link subscribers who use distance video surveillance. The service allows any Internet user to access the subscriber's website by using a fixed website name in place of a constantly changing IP address.

Also during 2008, the Company's SMS Banking service reached its 24^{th} Russian region. The mobile banking service, run in collaboration with MFMSolutions, added five additional leading Russian banks to its network.

In cooperation with Panda Security, Sky Link launched its 'Safe Internet' campaign, and provided free anti-virus software for Sky Link mobile Internet users.

Strategy & Outlook

In 2009, Sky Link aims to increase revenues by maintaining a balance between voice and data services. The Company's goal is to increase operating profit two-fold. The Company's management believes that the 3G marketplace will continue to grow rapidly, despite forecasts of an economic recession in Russia, as corporate and individual subscribers seek cost-effective and convenient mobile voice and data-access solutions.

As part of its strategy of creating a single operating company, the Company plans to complete the merger of subsidiary companies (Moscow Cellular Communications OJSC, Delta Telecom LLC, Astarta LLC and Sky Link LLC) into one company in 2009. At the same time, the operator will be streamlined in order to reduce costs and increase the efficiency of the business at the national and regional level.

The Company has put in place its 'Balance' strategy, which defines its business priorities, target indicators and development scenario for the period of 2009 to 2012. Sky Link's strategic priorities have been adjusted to reflect the current market situation and the operating results achieved during 2008. The strategy is focused on strengthening the market positions of Sky Link while maintaining the balance of voice and data services in the three main segments of the 3G market: traffic, services and devices.

A priority in this long-term strategy is investing in terminal technology, which allows the Company to efficiently integrate voice and data-service requirements. Sky Link is seeking to balance the development of traditional and alternative sales channels to optimize marketing expenditure and to promote Sky Link's clearly superior product offering. The Company also plans to expand its portfolio of integrated, 'packaged' products on the base of new, unlimited and content-oriented rate plans for voice and data.

Indian Mobile Telecommunications

Marketplace

The Indian telecommunications market is one of the biggest in the world. The number of mobile telephone subscribers reached 347 million by the end of 2008, compared to 38 million subscribers to fixed-line services. With market penetration for mobile telecommunications at 30%[1], India is among the telecommunications markets with the lowest penetration levels, and therefore has a high growth potential.

The number of mobile telecommunications users is projected to increase to 560 million over the next three years, with an average CAGR of 30% in 2008-2011[2]. The market for mobile telecommunications in India is expected to grow from $15 billion in 2008 to $26 billion in 2011[3].

Over the last several years, the market for mobile telecommunications services in India has developed rapidly. Annual growth in the number of mobile telecommunications subscribers was over 60%, due to the expansion of target segments and coverage, as well as the introduction of new tariff offers. The addition of new subscribers continued to grow in 2008, with a monthly average of over 9 million, compared to the monthly average of over 7 million new subscribers in 2007[4].

The average revenue per user (ARPU) for mobile telecommunications operators in 2008 was approximately $6[5]. The Indian market features one of the lowest ARPUs in the world, and could fall to $3-4 over the next six years as new segments of users subscribe and network coverage expands in rural areas.

The competitive environment in the mobile telecommunications market in India was notable for the fierce rivalry between existing players (primarily among GSM operators) that resulted in aggressive pricing. In 2008, there were six national operators. Bharti, Vodafone, Idea and the state-owned BSNL/MTNL used GSM networks, while Reliance used both CDMA and GSM networks and Tata used CDMA networks. In 2008, Tata received a GSM license and spectrum, and is planning to develop a GSM network. The ratio of subscribers to Indian operators with GSM/CDMA networks is 75:25.

The Big Four (Bharti, Vodafone, Reliance and BSNL/MTNL) dominate the market, with a market share of approximately 75%. After the Indian market crosses the 350 million subscribers threshold, a paradigm shift is expected to gradually change the operators' focus from subscriber market share to revenue market share[6].

After the issue of new pan-India licenses and frequency spectrums allocation in 2008, the Indian mobile telecommunications market is expected to witness increased competition. Regional operators Aircel and BPL are expanding their presence, and new players such as Sistema Shyam TeleServices, Etisalat (Swan Telecom), Telenor (Unitech Wireless), Datacom Solutions and Loop Telecom plan to build pan-Indian networks. The growth in the number of operators has created opportunities for M&A deals and for the further consolidation of the market.

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[1] Source: TRAI (Telecom Regulatory Authority of India)
[2] Source: Deutsche Bank, India Telecom Strategy, November 2008
[3] Source: Deutsche Bank, India Telecom Strategy, November 2008
[4] Source: TRAI
[5] Source: TRAI
[6] Source: Macquirie Capital Sequirities (India)

Sistema Shyam TeleServices

Company in Brief

Sistema Shyam TeleServices Ltd. (SSTL), previously known as Shyam Telelink Ltd., is a joint venture between Sistema and the Shyam Group. Sistema currently controls a 73.7% stake in SSTL. SSTL acquired a pan-India license and spectrum in 2008 that covers all of India, a country with a population of approximately 1.15 billion people. In 2008, the Company launched the new network in Rajasthan, a state with a population of more than 60 million people, and began to build a network in several Indian states with a combined population of 270 million people. SSTL's subscription base grew by 250,000 users in 2008. As of the end of 2008, the company had 500,000 users, including 250,000 mobile telecommunications subscribers.

Operational & Financial Results

In 2008, Sistema acquired a 73.7% stake of Shyam Telelink in three stages: 41% in January, 21% in May and 1.7% in June (through an additional stock emission). This acquisition has permitted Sistema to take control of the Indian company's management and begin to implement its program to create a pan-Indian mobile operator.

Sistema controls a majority of seats on the Board of Directors. A Working Group has been formed to manage the project in India, and it has developed the organizational structure of the operator, building its management team around executives from the side of Sistema.

With Sistema's backing, Shyam Telelink received a license in January 2008 to develop the operator across the whole of India, in all of its 22 telecommunications circles. Between April and August 2008, it received an 800 MHz frequency in these territories, giving the Company the resources needed for pan-Indian development.

Shyam Telelink signed infrastructure sharing contracts in 2008 with some of the largest telecom operators in India (Bharti, Idea and Tata), as well as with Indian infrastructure providers. It also signed interconnect agreements with the majority of Indian telecom operators.

In February 2008, a business plan was developed and approved in the operator's home state of Rajasthan. The plan called for a strategy and business plan for pan-Indian development to be written together with international consultants BCG by September 2008. The resulting strategy and plan for Shyam Telelink's development was approved by Sistema's Management Board in October 2008, and by Sistema's Board of Directors in November 2008.

A CDMA mobile communications network was built in Rajasthan and launched for commercial use on September 30, 2008. The launch of a network in one of India's 22 telecommunications circles was the first step in creating a pan-Indian network. New subscribers began to sign up with the operator.

In accordance with the approved system engineering project of the pan-Indian CDMA network, construction of the network began in the Indian state Tamil Nadu, including Chennai (launched on March 26, 2009) and Kerala (launched on March 30, 2009), as well as in West Bengal, Calcutta and Bikhar, including Jharkhand (with launch dates planned in May and June 2009).

A marketing plan, tariff plans and client offers were developed together with BCG and MTS. A distribution network was set up in Rajasthan and other states where Shyam Telelink was developing. It was decided to switch the operator to the MTS brand for pan-Indian expansion. The Company's rebranding took place in February-March 2009.

At the end of 2008, by decision of shareholders, the Company changed its name to Sistema Shyam TeleServices (SSTL).

Strategy & Outlook

SSTL's strategy focuses on rapid expansion of the market, an aggressive sales approach, the acquisition of primarily large numbers of low- and middle-income clients in cities and rural areas and further enlargement on all market segments.

In the short-term, SSTL's strategy is based on the following:

1. Preserving its timing advantage by launching before other new players.
2. Facilitating the commercial launch of networks in the maximum possible number of Indian telecommunications circles in 2009, aiming for no less than 11 of 22 circles. By 2010, networks should be built in all circles.
3. Aggressive pricing aimed at gaining market share.
4. Reaching 4.7 million subscribers in 2009, and 20 million in 2010.

The Company's long-term goal is to carve out a significant share of at least 8% of the Indian mobile telecommunications market. By 2014, SSTL plans to service no less than 56 million subscribers.

Fixed-Line Telecommunications

Marketplace

The total Russian telecommunications sector (fixed-line and mobile) grew by 12.8% in 2008 to a value of RUB 1,234.4 billion (US$43.4 billion[13]) in constant ruble prices, according to statistics from the Russian Ministry of Economic Development and Trade. This growth rate is slower than the 25% growth rate seen in 2007, with the fourth quarter of 2008 seeing slower growth in the market due to impact of the global economic crisis.

At the same time, several factors make the fixed-line market particularly resilient in the face of an economic downturn. In Russia, as in other relatively well-developed communications marketplaces, spending on telecommunications services is no longer seen as a luxury but as a near necessity, and surveys indicate that consumers will abandon other spending (including healthcare and the accumulation of savings) before severely cutting back or eliminating telecommunications services.

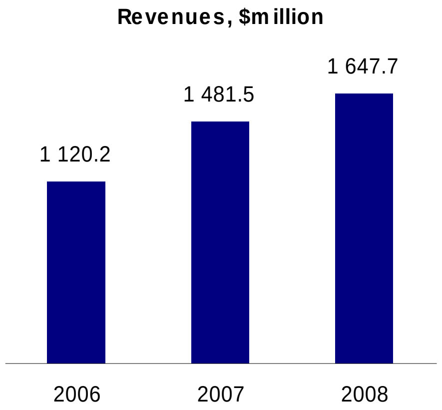
The crisis is expected to lead to a reduction in new start-ups and a reduction in investment and expansion by most operators. The Russian market may see slowing sales in new subscriber devices and a decline in the (previously very rapid) rate of market penetration of broadband Internet access, particularly in the regional markets. Despite the crisis, however, high-speed broadband will remain the primary driver of the fixed-line market in both Moscow and the regions. According to the most recent data, broadband penetration reached 62% of households in Moscow at the end of the third quarter of 2008[14]. The market is reaching the saturation point, and growth in market value will be driven by value-added services such as video-on-demand, HDTV and wireless access solutions.

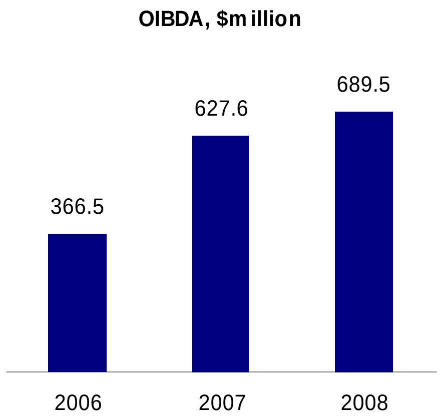
According to research by ITResearch, there were 9.5 million laptop computers in the country at the beginning of 2009, nearly one quarter of the roughly 40 million computers in use in Russia. Consumers increasingly use computers while on the move, and want broadband access outside of the home and office. This is leading growth in local WiMAX and WiFi solutions provided (primarily) by fixed-line players, as well as 3G solutions from mobile operators.

Overall broadband penetration outside of Moscow is estimated at between 10% and 15%[15]. Rates vary widely, with some as high as 50% in major regional cities, such as St. Petersburg, compared to single-digit penetration levels in some regions. Consultancy IKS estimates that 75% of Internet access in Russia as a whole will be through wire-line broadband in 2010, with a further 10% using wireless access.

[13] Based on the CBR average exchange rate for 2008 of RUB 28.46 per US$1
[14] Source: DirectInfo
[15] Source: J'son & Partners

Comstar-UTS





Company in Brief

Comstar-United Telesystems is a national fixed-line telecommunications provider with operations in 69 cities across Russia that cover a combined population of over 48 million people. Comstar is the number-one Russian broadband Internet provider, with more than one million residential subscribers and two million pay-TV subscribers. Through incumbent operator Moscow City Telephone Network (MGTS), the Group owns the 'last-mile' access to around 3.6 million households in Moscow, representing more than 97% of total households. Comstar is the leading broadband Internet provider in the capital and the preferred supplier of complete telecommunications products for Moscow corporate customers. Through Stream TV, acquired toward the end of 2008, the Group has access to a further 3.6 million households in Russia's regions. Sistema owns 53% of the shares of Comstar.

Operational & Financial Results

Comstar delivered robust top-line results in 2008, maintaining strong profitability in difficult market conditions through the implementation of tough cost control measures and improved efficiency. Comstar generated 11% growth for the twelve-month period, excluding the non-recurring compensation from the Federal budget that was received in the second and third quarters of 2007. The growth reflected the acquisition of DTN and RTC in the fourth quarter of 2007 and Interlink and UTC in 2008, growing 'Calling Party Pays' and long distance traffic volumes, as well as the development of the Group's broadband operations. The growth was partially offset by the 9% regulatory reduction in the price for the MGTS unlimited residential voice tariff plan from February 1, 2008, the regulator's cancellation of the compensation surcharge for long-distance calls from the beginning of 2008 and the regulatory change in the interconnect regime from March 1, 2008. The significant movement in the Russian ruble / US dollar exchange rate during the fourth quarter also adversely affected the Group's reported results for the period. Full year Group adjusted OIBDA, when excluding the US$ 36.5 million of Federal Budget payments received in 2007 and the stock-based compensation costs in 2007 and 2008, was up 14% year-on-year to US$ 682.6 million. This included an adjusted OIBDA margin of 41.4% due to the decrease in MGTS employee costs, reduced transportation costs and the optimization of selling and marketing costs in line with the movement toward the next phase of broadband strategy. In addition, the margin was partially offset by the consolidation of lower profitable regional operators, acquired in the fourth quarter of 2007 and in the second and third quarters of 2008, 9% regulatory reduction in the price for the MGTS unlimited residential voice tariff plan from February 1, 2008 and an increase in lower marginal CPP-traffic.

Traditional Segment

MGTS provides traditional fixed-line communications services to approximately 3.6 million residential and 747,000 corporate active access lines in Moscow. It accounts for 97% of residential installed access lines in Moscow, and provides infrastructure in the capital for the Comstar Group. Comstar owns 55.73% of MGTS.

Comstar is making a long-term investment in upgrading the MGTS network. At end of 2008, it had 4.85 million active lines in the city.

Since late 2007, the group has actively marketed broadband Internet services targeted at the mass market under the MGTS brand. It has used introductory and post-paid tariffs to attract first-time users. Under the Group's strategy, it aims to have more than 33% of MGTS voice users connected to broadband by 2011.

In 2008, substantial progress was carried out on the selective modernization of the network. Under the modernization drive announced in February, the network was 'sped up' from 6 to 24 Mbits/second by extending fiber-optic connections to curb (FTTC) and moving DSLAMs closer to the customer. Fiber to the home (FTTH) has also been installed in priority, high-traffic areas, with ADSL2+ equipment installed at the premises.

Since 2003, MGTS has increased the level of digitalization of its network from 13% to 63% at the end of 2008. This long-term project is due to be completed after 2012. As part of the digitization project, Comstar plans a selective upgrade using IMS (IP Multimedia Subsystem) technology, following the successful pilot test of the project in 2008.

The main driver of revenue growth for MGTS is growth in tariffs, which are regulated by the Federal Tariff Service. A 9% reduction in the regulated price charged by MGTS for its unlimited monthly tariff plan for residential voice services took effect on February 1, 2008. In addition, the Federal Tariff Service cancelled the fixed monthly interconnect service charge beginning on March 1, 2008, while a 25% increase in the weighted average per-minute charge for operators interconnecting to the MGTS network came into effect on July 1, 2008. On December 2, 2008, the Federal Tariff Service introduced new tariffs on MGTS's local connection services due to take effect on March 1, 2009. MGTS's regulated tariffs were increased by an average of 8%.

The number of residential fixed-line subscribers grew to 3,614,000. Subscribers' choice of voice tariff plans remained unchanged, with 50.5% of MGTS residential subscribers on the unlimited tariff plan, 28.0% on the per-minute plan, and the remaining 21.5% on a combination of the two plans at the end of the reporting period. Residential ARPU increased year-on-year to RUB 292.7, due to the mixed effect of the increase in CPP traffic volumes and the decrease in the price of the unlimited tariff plan in February 2008. CPP traffic levels for residential subscribers were up 32% to 1,745 million minutes.

The number of active corporate subscribers increased by 9% year–on-year to 73,000, and corporate ARPU was up 5% year-on-year to RUB 5,934.3. This reflected the ongoing increase in CPP traffic volumes, which were up 40% to 771 million minutes for the full year. As at December 31, 2008, 12.8% of MGTS corporate subscribers were on the unlimited tariff plan, 5.5% were on the per-minute plan, and the remaining 81.7% were on a combination of the two plans.

Moscow Alternative Segment

The number of residential subscribers to Stream and Comstar branded broadband, pay-TV and voice services increased by 8% year-on-year to 699 thousand subscribers. CPP traffic levels doubled, reaching 9 million minutes for the full year. The number of corporate subscribers declined by 8%, while CPP traffic levels were up 33% year-on-year to 339 million minutes for the full year.

Comstar is focused on increasing ARPU in the premium segment and retaining and expanding its client base in the Moscow broadband market. For instance, Comstar received the necessary access codes to be able to provide long distance telephony services in August. Some 90% of all corporate subscribers in alternative segments in Moscow had been switched to Comstar long-distance by the end of 2008.

With the rapid growth in the number of laptops and other mobile devices, Comstar moved in 2008 to deploy mobile broadband coverage in Moscow that is based on WiFi and WiMAX technologies. As part of a strategic partnership with FON International, backed by the Sistema/Coral fund, a range of international technology companies, Comstar started to build a WiFi network in Moscow. In January 2009, Comstar deployed an IEE 802.16e Mobile WiMAX network covering Moscow City on a test basis, ahead of the full commercial deployment later in the year. Previously, Comstar carried out a successful trial of mobile WiMAX technology in September 2008.

During 2008, Comstar continued to provide higher speeds to subscribers. In September, it introduced new speed tariff plans, allowing for data transmission speeds of up to 20 Megabits/second. In October 2008, Comstar launched HDTV services in Moscow. The launch of HDTV underlines how the ‘speeding up’ of the MGTS network will allow for the delivery of qualitatively new services to the home and office.

Alternative Segment in the Russian Regions and CIS

The number of residential subscribers in the Russian regions grew by six times in 2008 to 505,000, following the acquisitions of DTN and RTC in the fourth quarter of 2007, Interlink Group in June 2008, and UTC in July 2008. Residential ARPU reached RUB 240 during the year, compared to RUB 289 in 2007. The development in residential ARPU levels reflected the promotional subscriber acquisition campaigns, as well as the consolidation of regional operators with lower prevailing ARPU levels. CPP traffic levels for residential subscribers were up by four times year-on-year to 59 million minutes for the full year.

The number of corporate subscribers grew by six times in 2008 to 44,000. Corporate ARPU amounted to RUB 4,118 in 2008, compared to RUB 5,764 in the previous year. The same factors were reflected in the growing number of corporate subscribers and the ARPU development. CPP traffic levels for corporate subscribers were up by five times to 79 million minutes for the full year.

In 2008, Comstar was transformed from a Moscow operator with an emerging regional business into Russia’s leading national alternative fixed-line operator, with a presence in six of Russia’s seven Federal Districts. At the end of 2008, the regions accounted for 10% of the Group’s revenues, compared to 8% in 2007.

The acquisition of the regional assets of Stream TV was a “game changer” for the Group. Stream TV is the largest pay-TV operator in Russia, and provides cable TV and broadband Internet access services in 40 Russian cities with a combined population of over 15 million people. With the acquisition, the Group’s networks reach over 3.6 million households and have over 205,000 broadband Internet subscribers and over 1.8 million active pay-TV subscribers, representing 17% of the total Russian pay-TV market.

The integration of the regional operations of the Stream TV Group began in September. Entering 2009, the Group has put in place plans for the selective modernization of the Stream TV network using FTTB technology to bring Double and Triple-Play digital services to subscribers as quickly as possible. Management is planning to modernize up to 90% of the network and fully integrate it with Comstar’s existing regional network. ‘Stream’ will be rebranded as Comstar beginning in 2009.

Comstar also pursued its strategy of buying competitive local exchange carriers (CLECs) with leading positions in their markets and the most attractive long-term growth potential. In June 2008, Comstar purchased 100% of the Interlink group of companies, comprising Intersvyaz-Service CJSC and Inter-TV Media LLC, both operating under the Interlink brand in Ryazan in the Central Federal District. In July 2008, Comstar acquired a leading alternative telecommunications operator in the Urals Federal District.

In February 2009, after the reporting period, Comstar announced its restructuring plans for its regional business, directed at integrating the assets of Stream TV with its existing business. Around 80 legal entities are being consolidated to create a single legal entity, Comstar Regions CJSC, which in turn will be a 100% subsidiary of Comstar. Management of assets is being organized on the inter-regional level, with a head affiliate in each Federal District. (Comstar is currently present in six of seven districts.)

In the CIS, Comstar continued to strengthen its business in the rapidly developing Ukrainian and Armenian telecommunications market. In Ukraine, Comstar successfully upgraded its network in order to provide Triple-Play services to residential subscribers. In November, the Group announced the completion of its multi-service data network using NGN technology, and completed the construction of a mainline network linking its Ukrainian and Russian networks. In November, the first-ever launch of a national WiMAX network based on 802.16e standard WiMAX technology was carried out in Armenia at a ceremony attended by Russian President Dmitry Medvedev and Armenian President Serzh Sargsyan.

Strategy & Outlook

Comstar’s strategy is called the ‘Five Angles of Attack,’ and is based on the belief that in the battle for supremacy in the highly competitive global telecommunications sector, only the strongest players will survive. Today, in the midst of a major global financial crisis, companies must have a clear strategy if they are to lead the expected consolidation of the marketplace.

Originally approved in July 2007 and implemented throughout 2008, the ‘Five Angles of Attack’ represent Comstar’s strategy to 2011 and beyond. The five angles – Structure, Broadband, MGTS, Regions and Svyazinvest – are not just broad areas of focus for the Group’s management. Rather, each includes a specific set of projects that are accompanied by concrete goals and metrics. Each angle is designed to meet the core mission of Comstar: to serve its customers, retain their loyalty and increase revenues and profitability on a sustainable basis in order to increase the long-term value of the Group for its shareholders. Under the strategy, Comstar should become Russia’s number-one telecommunications operator by 2011, with undisputed leadership in the Moscow broadband and total fixed-line market and a position as the leading provider of fixed-line services in Russia's regions in the alternative segment.

During 2008, Comstar made substantial progress along each angle of attack, executing major projects such as the construction of a proprietary long-distance network, construction of a WiMAX network in Moscow, active expansion in the regions through the acquisition of Stream-TV, the purchase of leading local operators in key regional markets, the consolidation of Comstar-Direct and many other steps that significantly strengthened the Group's position in the marketplace and long-term growth potential.

MTT

In March 2009, Sistema signed an agreement with Synterra Group CJSC to sell its 43.4% stake (50% of voting shares) in national and international long-distance operator MTT. In addition, Synterra Group will assume MTT's intercompany debt obligations to Sistema. The deal is expected to be reached for a total cash consideration of approximately US$54 million. The completion of the deal remains contingent upon the fulfilment of a number of conditions.

Media Content

Marketplace

In 2008, the Russian cinema market grew in comparison to 2007, reached a value of US$830 million[16]. Russian films accounted for 27% of the market. Domestic film producers make more than 100 full-length films each year. The average cost of producing 100 titles annually amounts to US$300 million, before taking into account advertising and marketing budgets. The market for DVDs is worth around US$1 billion, including pirated films.

The total Russian market for television content was around US$1.5 billion in 2008. The market for the production of television series amounted, according to various estimates, to US$500 million. The market for advertising on broadcast television, the primary driver of the market for serials, grew by around 20% in comparison with 2007.

The year saw Russian films gain in popularity in cinemas. The 81 domestic films to reach the box office saw total returns of US$212 million. The top-grossing film, the Irony of Fate 2 accounted for US$49.91 million.

The number of pay-TV channels showing Russian content approached the 100 mark, while the total number of channels on the pay-TV market, including foreign channels, exceeded 200. Russian producers of television content generated around US$70 million in revenue in 2008, according to IKS Consulting, with seven accounting for around 80% of the marketplace. According to TNS, Russian channels accounted for five of the top-10 non-terrestrial channels. The total audience of non-terrestrial TV channels reached 17.5 million in the first half of 2008. According to Discovery Research Group, strong growth in early 2008 helped the market deliver strong full-year numbers, but the market may fall by as much as 20% in 2009.

According to AKAR[17] data, the Russian advertising market grew by 17% in 2008, reaching a value of RUR 267 billion (US$9.4 billion[18]). This rate of growth was the lowest in eight years and compares to 24%-28% average growth rates between 2003 and 2007 and rates of 60% in 2001 and 2002 as the market recovered from the 1998 financial crisis. The fourth quarter of 2008, usually the strongest time of year for advertisers, was particularly weak and many companies have cut their marketing budgets for 2009.

The new media segment (including indoor advertising, non-terrestrial TV and advertising in theatres) of the market showed strongest growth in 2008, increasing by 48% to RUR 4.5 billion (US$158 million), according to AKAR. The non-terrestrial TV subsector grew by 100%. The Internet advertising segment grew by 23%, the billboard market grew by 13% and print mass media grew by 11%. Two sectors saw falling revenues, radio (-6%) and print publications (-1%).

Below-the-line advertising grew by 18%, according to AKAR and RAMU[19] data. Consumer promotions grew by 21% during the year to RUR 17 billion (US$597 million), while trade promotion (including merchandising) grew by 20% to RUR 16 billion (US$562). The direct-marketing segment (including CRM) grew by 18% to RUR 24

[16] Nevafilm Research.

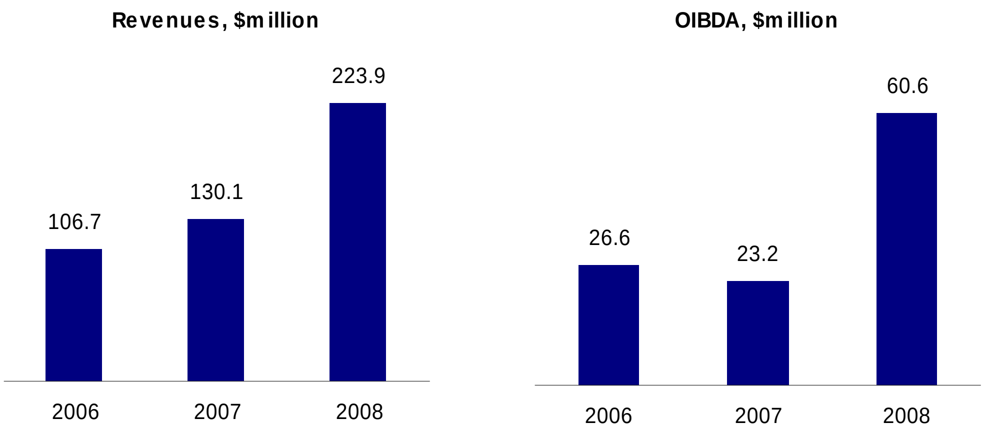
[17] Association of Russian Communications Agencies

[18] Based on the CBR average exchange rate for 2008 of RUR 28.46 to US$1

[19] Association of Russian Communications Agencies and Russian Association of Marketing Services

billion (US$843). Russian advertisers increasingly prefer the new information-technology mediums, such as on-line links and SMS, online databases, websites, interactive games and so forth.

Sistema Mass Media



Company in Brief

Sistema Mass Media (SMM) is one of the largest Russian companies in the market for the development and distribution of content for pay-TV networks and other media platforms and resources. The Company is focused on building an integrated content business. This includes the production of content, aggregating licenses from rights holders and the distribution of content for various platforms. In recent years, SMM has actively developed its advertising business, publishing business and broadcast television and telecommunications areas. As a result of the restructuring carried out between 2004 and 2007, the Company exited a number of business areas. This allowed it to concentrate its resources on high-technology segments of the media market, based on new technology platforms such as DVB-H and IPTV, which have been developed by CMM and other companies in the Sistema group.

SMM includes Russian World Studios (RWS), which was founded in 1998 and is one of the largest independent production companies and makers of television serials in Russia, as well as the Maxima Communications Group. It also includes Stream, one of the leading pay TV channels in Russia. Stream has five in-house channels for which it produces programming and also manages distribution and advertising. In total, Stream's channels reach 3.8mn households and over 12mn viewers. Stream also aggregates rebroadcasted TV channels and manages VOD services for Sistema's cable network operator Comstar. Sistema owns 100% of SMM

Operational & Financial Results

In 2008, SMM reported a 98% year-on-year increase in revenues to US$223.9 million, compared to US$130.1 million in 2007. OIBDA increased 183% to US$60.6 million.

The year saw major developments as SMM moved to complete restructuring in line with its long-term strategy. In June 2008, Andrei Smirnov was named general director of SMM and a new strategy for the development of SMM was put in place. As part of this strategy, the regional assets of Stream-TV, the leading pay-TV operator in Russia, were put under the management of Comstar and the sale of these assets was completed at the end of 2008. In January 2009, it was announced that Stream TV assets related to production and content distribution, including popular Stream TV channels, had been transferred to SMM Finance, a 100% subsidiary of SMM.

In 2008, work was carried out ahead of the re-launch in January 2009 all existing channels as well as the development and implementation of the concepts for two new channels, Psychology and Living World. In developing content for the channels, SMM is oriented towards market niches based on lifestyle and oriented towards different segments of middle-class pay-TV viewers, specifically well-off and socially mobile people aged 25-60. Clients include federal and regional pay-TV operators and the Company is targeting potential clients among mobile operators, Internet companies and terrestrial television channels.

During the year, a new corporate structure was created for RWS, following the arrival of its new shareholder, Sistema at the end of 2007. During the year, over 500 hours of serial production was completed, generating around US$500 million. In addition, development of the studio's cinema business rapidly got under way and top cinema talent were recruited, such as renowned producer Sergei Chliyants.

RWS productions during the year included the release of full-length film Antidur. Three more projects were also completed, including full-length feature Year of Deception and the serials Sea Patrol 2 and Love is Not What it Seems. In early 2009, Chameleon-Chimera was in production at the studio in St. Petersburg. Some 11 more projects were in preparation and three more were in production. .

In July 2008, the first stage of the new RWS St. Petersburg cinema complex was put into operation. It is the first world-class cinema studio built in Russia in 60 years. It provides unique cinema and multimedia production capacity for content for all current and developing media platforms, including Internet and mobile TV. The total space of the studio is 11,000m^2 and includes four sets with space of 750m2 each, including a pool for filming water scenes, two 350m^2 sets, a Dolby Premier studio, eight video-editing, three sound-editing and a re-recording bay. Around 4,000m^2 is dedicated to offices and support services.

The company is actively developing partner projects and the latest joint international project involving RWS was the short film Spirit, directed by Joseph Fiennes. The film won the Cinema for Peace award at the 2008 Berlin Film Festival. RWS provided services for such international productions as Leningrad, starring Gabriel Byrne, and PU-239 for HBO Films and Beacon Pictures. RWS also carried out line production for the Russian-language portion of the film Icon, by Hallmark Entertainment and starring Patrick Swayze.

Against a background of intensifying competition, Maxima Communications Group was able to maintain its positions in the marketplace in 2008. It remains the largest non-network Russian advertising agency and occupied 2.5% of the market in 2008, earning it a place in the Top 20 rating of Russian advertising agencies, including a second-place ranking in outdoor advertising. The Agency was ranked third in the Grand Prix at the Idea Festival in 2008.

During 2008, Maxima launched a new business area, Sales House, as part of SMM's wider strategy focused on content. As part of its expansion into fast-growing regional advertising markets, he Agency opened a new affiliate in Novosibirsk, Maxima Siberia. The Agency also developed and put in place its development strategy through 2012.

Also during the year, the Company continued to develop mobile broadcasting through its Digital Television and Radio Broadcasting (CTV) subsidiary. Work was carried out for the deployment of network for mobile broadcasting using the DVB-H format in 17 large Russian cities. The plan of the project has been delayed while the Company works with regulators to approve a frequency and territorial plan for digital broadcasting.

Strategy & Outlook

SMM's strategy is directed at creating Russia's leading media holding which creates and distributes content on four screens: TV, cinema, advertising and mobile and Internet content. The Company aims to achieve its strategic goals through a balanced mix of organic growth and carefully selected M&A of other media businesses.

On the base of its existing content, the Company plans create the largest Russian broadcaster of non-terrestrial TV, with a focus on the production, aggregation and distribution of TV content and services. In film, SMM's goal is to achieve leading positions in the creation and distribution of film, television and animated content, as well as increasing film-production capacity both in Russia and overseas. In advertising, the Company's goal is to achieve leading positions in the most innovative communications segments and sales of advertising capacity in traditional and new media. In mobile and Internet content, the strategy of SMM is aimed at securing a leading position in the emerging market for aggregating and distributing mobile and Internet content and creating cross-platform New Media content in order to most efficiently monetize content on both mobile and Internet platforms.

11. Business Unit “Consumer Assets”

Vision & Strategy

The Consumer Assets business unit (BU) was created in mid-2008. Its strategy is aimed at achieving sustainable growth in the shareholder value of the BU’s companies (MBRD, Intourist, Medsi, Detsky Mir and Sistema-Hals) at a rate exceeding the growth of the benchmark RTS index. The current economic environment has not led to a substantial change in strategy, but rather has served to emphasize the necessity of taking a number of important steps. The current strategy requires restructuring and optimizing debt loads, as well as instituting stringent requirements for operational efficiency and sales and marketing innovation by each company in the portfolio.

Part of achieving the Corporation’s strategic objectives for the business unit involves achieving and maintaining leading positions in target markets. In 2009, the primary goal will be to restructure the Corporation’s consumer businesses in light of new market conditions and the challenges and opportunities created by the global financial crisis. It is necessary to re-position a range of businesses to retain the customer base in an environment of falling consumer demand. Operational efficiency will be the key determinant of success. Sistema also recognizes that it should seek outside partners to support the development of all of its consumer businesses in order to bring extra expertise and competencies to its assets, with equity partnerships as one option.

Strategies and management teams are in place for each consumer business. The use of financial and operational resources by each subsidiary is being examined and re-evaluated. The Corporation is also examining non-organic growth strategies, ranging from finding strategic investors to carrying out carefully selected M&A transactions in order to strengthen an existing business segment or enter an emerging, fast-growth segment or geographic area.

Aggressive targets and accompanying motivational tools are being put into place to clearly identify criteria for success and to reward assets’ management teams for achievement. The most advanced management and financial reporting processes continue to be introduced in each business, along with a single high standard of corporate governance and operational management. Corporate governance standards at the subsidiary companies will meet or exceed the level required of publicly listed companies. In addition, more than US$50 million in investments are planned in IT, as this is a critical area for controlling expenditure and managing the business.

Opportunities for synergies are being explored across the Consumer Assets business unit to leverage Sistema’s existing 80 million-strong consumer base. In 2009 and 2010, the Corporation plans to put a universal bonus/loyalty program into place. This program would also include external companies, and would be supported by cross-selling and promotion among Sistema’s subsidiary companies. The business unit is exploring areas for combined efforts to improve customer experience through the introduction a single CRM system for the business unit. In addition, there is a strong focus on efficiency and scale in sourcing products and services and exerting quality control over the process of innovation.

The current environment requires a careful macroeconomic evaluation over the course of 2009, as well as ongoing monitoring to identify emerging risks and opportunities, particularly where the weakening or exit of less well-financed and managed competitors has left room to build market share and consolidate a particular market segment. Previous expansion schedules and targets must be reviewed in light of changing circumstances, and scarce resources must be carefully directed to areas of maximum return while maintaining financial stability.

The Consumer Assets business unit retains aggressive growth targets despite the current financial crisis. Combined capitalization of the businesses should exceed US$3 billion in 2012 and US$5 billion in 2015, while each business segment should have a capitalization greater than US$1 billion. Return on invested capital in existing businesses should be higher than 20% by 2012, and higher than 25% in 2015. In addition, BU's management believes its assets structure and the measures it is undertaking will help Sistema to reduce the currently applied "conglomerate discount" to zero.

Financial Services

Marketplace

The first half of 2008 saw robust growth of the Russian banking sector as the wider economy continued to grow. Russian GDP grew by 8.5% in the first quarter and 7.5% in the second quarter, driven by record export revenues, the expansion of bank credit, rising consumer demand and private- and public-sector investment. Beginning in the second half of the year, however, the developing global financial crisis had a negative impact on the economy. Russian financial institutions faced a number of major challenges, including the deterioration of the overall economy, a lack of available financing on the inter-bank market toward the end of 2008 and the beginning of 2009, and the decline of the Russian ruble against the US dollar and Euro.

During the year, the total value of assets in the Russian banking system grew by 39%, and their share of Russia's GDP increased from 60.8% to 67.5%. Funds from companies and organizations accounted for 31.3% of the total banking assets. The financial crisis reduced growth in lending to both consumers and the industry. The volume of lending to companies rose by 34.3% during the year, while the amount of loans issued to consumers grew by 35.2%, representing a significant slow down compared to 2007. The total growth in consumer deposits amounted to 14.5% in 2008, compared to 35.4% in 2007.

The global financial crisis precipitated a liquidity crisis in the Russian banking sector during the second half of the year. The issuance of credit to both corporate and consumer borrowers declined dramatically and interest rates increased. The level of loan defaults in the corporate credit market rose, primarily during the fourth quarter, with the percentage of non-performing loans in bank credit portfolios increasing from 0.9% to 2.1% during the year. The increase in 'bad loans' to consumers grew only marginally during 2008, increasing from 3.2% to 3.7% of total consumer lending.

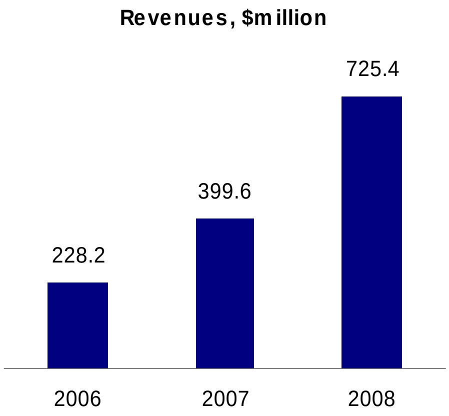
While 2008 was a very challenging year for the Russian banking sector – the combined profit of Russian credit organizations was down 30.4%, compared to 2007[20] – the situation did not deteriorate into a full-fledged banking crisis, due in large part to decisive and timely actions taken by the Central Bank of Russia (CBR). The CBR maintained the liquidity of the banking sector by providing credit. Its data[21] shows a 100-fold increase in 2008 in the credit and deposits provided by the CBR to financial institutions, primarily through the provision of unsecured credits.

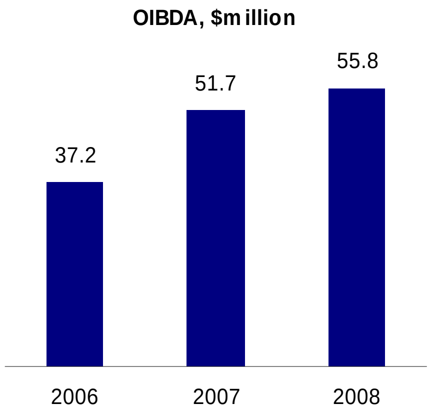
2009 will be most likely marked by the acquisition of troubled small and mid-sized banks by larger players. Small and medium enterprises (SMEs) and individual borrowers, which represented a source of rapid growth in the banking sector in recent years, have been most affected by limited liquidity. An increase in retail banking activity and consumer lending will be a key sign of recovery in the marketplace.

[20] Figures are taken from 1,050 credit organizations, representing 95% of all existing credit organizations as of January 1, 2009.

[21] Source: Bulletin of the Bank of Russia

MBRD





Company in Brief

MBRD (Moscow Bank for Reconstruction and Development) is one of Russia's largest universal banks, and it operates a leading national retail banking network. The bank offers a full range of services for corporate and consumer clients. The bank's retail banking business was launched in 2004, and is based on a model developed in consultation with international consulting group Deloitte & Touche CIS. Sistema owns 87% of the shares of MBRD.

Operational & Financial Results

The year 2008 posed huge challenges for the Russian banking sector, and MBRD demonstrated the strength of its strategy, delivering strong top-line growth through the development of its retail business, the launch of innovative banking products and careful management of its business in difficult and rapidly changing operating conditions. Revenues increased by 77% to US$725.4 million, compared to US$410.0 million in 2007. OIBDA grew by 8% to US$55.8 million. The Bank was able to limit the negative impact of the financial crisis on its business by taking quick action in September 2008 to halt the sales of most consumer credit and to accumulate funds from retail and inter-bank markets to support its liquidity.

During 2008, MBRD continued to implement its strategy of expanding its retail business, attracting new clients by offering a wide range of account types to meet the needs of individual depositors. The total deposits in personal time-deposit accounts increased by 7.8% to US$620.8 million in 2008, compared to US$575.9 million in 2007. Amounts held by customers on current accounts fell to US$14.8 million in 2008, from US$22.2 million in 2007. The number of personal accounts nearly doubled, rising to 16,851 from 8,602 the previous year. The portfolio of credit issued to individuals, including the securitization of the automobile financing portfolio, rose by 3.6% year-on-year to RUB 4.289 billion (US$172.5 million[22]).

The Bank continued to develop and implement its mortgage lending program as a key component of its comprehensive line of consumer banking products, and introduced a new land mortgage product in 2008. MBRD is a participant in the Federal Mortgage Program as part of an agreement with the state-owned Agency for Home Mortgage Lending and its regional operators. In October 2008, MBRD signed a new Strategic Cooperation Agreement with the Agency. The deal includes provisions for direct refinancing of issued mortgage loans with the Agency.

[22] Based on the CBR's average ruble/US dollar exchange rate of RUB 24.86/US$

During the year, MBRD issued 4,308 mortgage credits amounting to a total value of RUB 9.490 billion (US$381.7 million). As of January 1, 2009, the total portfolio of mortgage credits amounted to RUB 10.950 billion (US$440.5 million[23]), an increase of 63% compared to the previous year. According to RBC Ratings, the bank was ranked 11th among Russian banks in terms of the number of mortgage loans issued in 2008, and 14th in terms of value.

The Bank's credit portfolio of POS loans surpassed the RUB 1 billion mark (US$40.2 million) during 2008. The portfolio of issued consumer credit increased by 102.5% during 2008, reaching a total value of RUB 1.217 billion (US$41.7 million) as of January 1, 2009. The most dynamic growth came from the expansion of MBRD's range of express consumer credit products, attractive credit conditions during the first half of the year, increased number of points of sale and improved efficiency in servicing this segment.

The Bank's portfolio of car loans grew by 6.3% in 2008 to RUB 4.830 billion (US$194.3million) as it continued to launch new car-financing programs, simplify the loan application process and lower interest rates. Innovative programs in this segment included financing for consumer-to-consumer sales of used cars, and financing of mass-transit vehicle purchases and small water vessels.

Bank cards represented another important area of growth for MBRD, and the total number of MasterCard and Visa cards issued reached 155,370. The credit portfolio increased by 71% to RUB 1.045 billion (US$58.3 million). In February 2008, a new and simplified scoring system was put in place for corporate clients using bank cards for employee salary plans, helping to drive a 34% increase in this segment for the year. In August 2008, the Bank launched a new campaign for direct sales of credit cards, beginning at the Bank's affiliates in Tomsk and Yekaterinburg. At the end of 2008, in a key product launch driven by market demand, MBRD began to issue cards with grace periods. In December, bank customers were offered cards with initial discounted financing terms and credit limits equalling 85% of existing deposits.

Despite extremely challenging conditions in the corporate banking sector in the second half of 2008, the Bank achieved strong results for the year. The total deposits in corporate-client accounts reached RUB 22.9 billion (US$921.2 million), and the portfolio of credits issued to corporate borrowers reached RUB 36.7 billion (US$1.48 billion). MBRD significantly enhanced and diversified its corporate client base during 2008 through both the launch of new products, finding flexible solutions for the needs of clients and continually improving its level of service. This led to a 40% increase to RUB 688 million (US$27.68 million) of revenue from commissions for services to corporate clients.

Today, the Bank's client base includes companies from across the range of production and service industries. MBRD has also continued its long history of working with the Government of the City of Moscow, by providing credit facilities and guarantees to city institutions and programs. In addition, MBRD launched acquiring business in 2006 and, in the period of 2007 through 2008, increased its number of point-of-sale terminals by 200% and its revenues in this area by 400%.

Difficult conditions in global and Russian financial markets led MBRD to adopt a conservative position in its investment business in 2008. The Bank's priorities in this area included minimizing credit and market risk as well as assuring liquidity. This cautious strategy was reflected in the decision to form the investment portfolio only from instruments included on the

[23] Based on the CBR's ruble/US dollar exchange rate for January 1 2009 of RUB 29.20/US$1

Collateral List of the CBR, a significant reduction in the volume of REPO and unsecured transactions and constant monitoring and review of existing limits.

In 2008, the Bank focused on attracting and maintaining economic resources from the financial markets, and on making use of additional liquidity offered by the CBR in order to increase income from commissions for client services and maximize the range and volume of services available to clients. MBRD raised around RUB 1 billion (US$40.2 million) through the issuance of securities with terms ranging from three months to one year. The Bank also arranged the placement of two five-year ruble-denominated bond issues, which raised a total of RUB 6 billion (US$241.4 million). During the year, the Bank also attracted RUB 20.4 billion (US$820.6 million) from the CBR, with interest rates corresponding to the refinancing rate at the time the deals were closed (ranging from 8.25% to 12.00%).

In April, as part of its program to raise mid-term financing, it attracted an 18-month, US$75 million credit from Dresdner Bank. In July, despite challenging market conditions, MBRD attracted a syndicated loan from a consortium of banks led by WestLB for Euro 40 million with a 6+6-month tenure.

In 2008, MBRD strengthened its position in the brokerage market, increasing the volume of client deals carried out through the Bank by 50%, in comparison with 2007. The number of brokerage clients increased by 90% over the same period despite increased competition, reflecting the high quality of MBRD's service.

In February 2008, MBRD launched a car loan securitization transaction, whereby an interim funding totalling RUB 2.67 billion (US$107.4 million) was attracted throughout the year. However, as a result of instability in the financial markets, in December the cost of servicing these funds increased substantially, causing the Bank to cease the raising of external financing by way of redemption of the notes issued by the SPV.

Also at the end of 2008, MBRD embarked on structuring its mortgage-backed securities (MBS) transactions, providing for placement of bonds under Russian MBS law. Issuance of notes with a nominal value of up to RUB 3 billion is set for the first half of 2009.

The year also saw the Bank strengthen its position in the export and trade finance market, offering its clients highly competitive loans with five to 10-year tenures and low interest rates. The average portfolio size for such deals more than doubled in 2008 to US$187 million. Short-term financing clean limits were increased by 30% to U$350 million.

At the same time, the Bank undertook the successful reorganization of its affiliate network and opened a new Siberian Regional Directorate, which includes three affiliates in the Siberian Federal District. Today, MBRD covers six of Russia's seven federal regions. As of January 1, 2009, the bank was present in 31 oblasts, and its network includes 70 points of presence in 51 Russian cities.

The Bank's strong performance in 2007 and 2008 caused it to be recognized as a leading banking services provider to both corporate and consumer clients. International financial journal *Euromoney* recognized MBRD as Best Bank in the Area of Corporate Governance in Developing Europe in 2008. The Bank also received an award in the category 'Retail Bank' in the nomination for 'Dynamism and Development.'

Strategy & Outlook

The outbreak of the international financial crisis in 2008 and its negative repercussions for the Russian economy and banking sector have caused the Bank to adjust its priorities going forward in order minimize risks and ensure continued financial stability. Therefore, it is seeking to diversify its client base, restructure its credit portfolio, centralize decision-making regarding credit and finance issues and reduce costs by streamlining operations and optimizing staff numbers.

In order to achieve its goals, the bank is also implementing substantial changes in its management system. It is shifting to a management system that is appropriate for a large bank and that is based on careful, long-term business planning and budgeting, creating a new motivational system for managers and instituting a new and advanced system for management reporting. This will allow the bank to better analyze the financial performance of individual divisions of the bank, and to involve employees more closely in the process of reducing costs and increasing profitability.

As the bank's largest shareholder, Sistema has made a significant contribution to ensuring the financial stability of the Bank during the global financial crisis. At the end of 2008, the decision was made to centralize the system for managing the financial flows of the holding, using MBRD as a base. Sistema implemented a program for increasing the capital of the Banking Group[24] and putting its assets under MBRD's direct management. In addition, the Bank and Sistema have jointly developed a program of anti-crisis measures for 2009 that are aimed at ensuring liquidity and maintaining the profitability of the business and the quality of its credit portfolio.

In addition, the Bank is working with regulators and the government to help resolve the most critical issues facing the banking system and wider economy in 2009. In the beginning of 2009, MBRD resumed its work with the Agency for Home Mortgage Lending to provide mortgage loans, while working with the Agency to implement a program for restructuring loans taken out by clients who have seen their financial condition negatively affected by the crisis.

The financial crisis also represents an opportunity for the Bank to reshape its business and create a platform for future growth. MBRD is continuing to invest in updating its IT infrastructure. Despite some reductions in staff, the bank is not closing branches, and is instead converting credit and payment offices opened in large Russian cities into offices capable of providing clients with a full range of services. In seeking out new corporate clients, the Bank is now focusing on savings and payment products, rather than credit products.

The Bank remains committed to its long-term strategy aimed at developing a universal bank that offers classic personal and business banking services as well as investment services. As part of this strategy, the bank is targeting mid-sized and large corporate clients in both Moscow and the regions. To ensure stability, it is putting into place stricter requirements for borrowers, and is undertaking a range of measures to deal with bad loans. In the retail business, the focus is on increasing quality of service and customer loyalty. MBRD is also investing in technology to make it easier to deliver top-quality services while continuing to expand the geographic reach of its retail network. In addition, it is seeking to provide a sustainable level of credit to consumers while also increasing the requirements for borrowers and restructuring problem loans.

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[24] The Group includes MBRD, Dalcombank, East-West United Bank and leasing companies.

Travel

Marketplace

The total value of the Russian tourism market grew by 37% in 2008, reaching a value of US$17.9 billion[25]. In 2008, the inbound tourism market amounted to 1.69 million people[26], representing a 3.4% growth in comparison with 2007. For the period of 2001 to 2008, the average annual rate of growth in tourism reached 11.2%. According to expert forecasts, the flow of tourists to Russia is expected to decline by 17% to 1.4 million people in 2009. Slower growth in 2008 and the expected fall in tourist numbers in 2009 can be attributed to declining economic growth and dwindling consumer sentiment in Western Europe and the United States, the sources of the majority of tourists in Russia.

Over the longer term, the development of the inbound business traveler and tourism market will be aided by the ongoing improvement of Russia’s tourism infrastructure, including the construction of new hotels in regional tourist destinations, the creation of new tourist package products and international marketing campaigns promoting Russia as a tourist destination.

The outbound tourist market amounted to 8.56 million people[27] in 2008, an increase of 19.6% in comparison with 2007. For the period of 2001 to 2008, the average annual rate of growth in tourist numbers was 20.5%. Export forecasts see a 29% reduction in outbound tourist numbers to 6.1 million in 2009, due primarily to the fall in value of the exchange rate of the ruble against the US dollar and Euro, as well aw an expected recession in Russia.

The outbound market retains huge longer term potential, however. According to 2007 statistics, the ratio of tourist trips abroad to the total population in Russia was 5%, compared to 86% in Germany and 76% in the UK. The market is in a stage of consolidation, with the elimination of small and mid-sized players due to intense pricing competition and increasing requirements for financial guarantees. Consumers are demanding innovative and complete tour products of a higher quality, while regulators are enforcing stricter standards and guarantees on operators.

The market for domestic tourism within Russia was estimated at around 10 million people in 2008, representing a 10% year-on-year growth. Currently, experts are forecasting an 18% decline in the volume of domestic tourism in 2009, a development linked to the state of the economy. As the economy recovers, however, Russian tourism will benefit from improving infrastructure and changing travel habits, such as the growing popularity of ‘weekend breaks.’

The value of the Russian three-star hotel market in 2008 was approximately US$1.7 billion, up 15% compared to 2007. According to present forecasts, there will be a decline in the value of the hotel market of around 19% in 2009. The country requires continued investment in international standard hotels, as some 80% of existing capacity is below this standard. The expected decline in inbound and domestic tourism in 2009 will have a negative short-term impact on the continued development of the hotel sector, but the market will retain a strong demand for hotel services in key business centers and for the expansion of chains, which currently control around 22% of Russian hotel capacity.

[25] Intourist appraisal.
[26] This excludes countries with direct border links with Russia, including China, Poland, Finland, the CIS and Baltic States.
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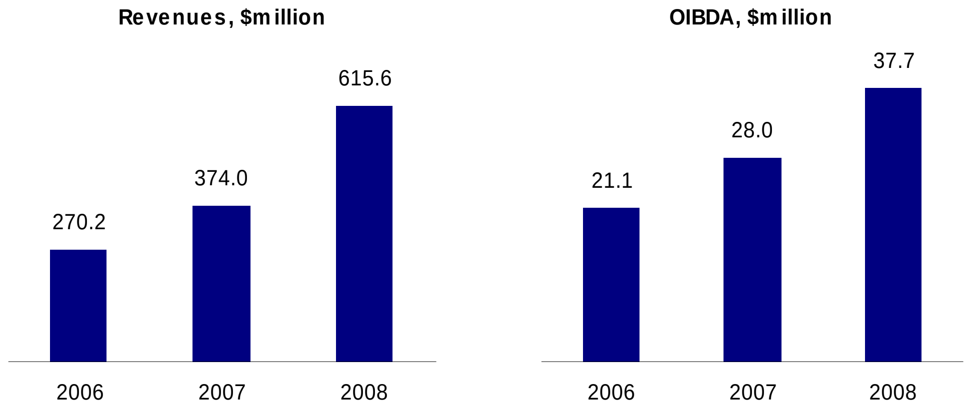
Intourist



Company in Brief

Intourist was founded in 1929. Over many decades, Intourist has provided a gateway for Russia and the Soviet Union for foreign visitors and for domestic tourists alike. Some eight decades since its inception, Intourist remains the flagship of the Russian tourist industry, and is present in all major segments of the tourism and hospitality industry, from packaged tours to VIP and corporate services. Today, Intourist is a vertically integrated tourist holding, managed by the Intourist management company and four business divisions: NTK Intourist (tour operations), Intourist Hotel Group, Intourist Travel Store and Intourist Transport Services. The Company is present in 80 Russian regions and works with 7,000 partners in 168 countries worldwide. It is the established leader in the market for inbound tourists, welcoming visitors from 70 countries. Its hotel-management group includes owned and third-party hotels in Russia, Czech Republic, Italy and Turkey. Sistema owns 65.1% of the shares of Intourist.

Operational & Financial Results

Intourist delivered a very strong performance across all of its business divisions in 2008. Turnover grew by 73.7% to US$896.6 million in 2008, compared to US$516.3 million in 2007. Revenues increased 64.6% in 2008 to US$615.6 million, compared to US$374.0 million over the same period. OIBDA increased by 34% to 37.7 million in 2008.

In 2008, Intourist continued to occupy a leading position in the market for incoming tourism with a share of 9.8%, compared to 10.8% in 2007. The Company's market share in this segment declined due to lower rates of growth compared to the average rate for excursion-educational tourism, an area of specialization for Intourist. During the year, Intourist focused on the development of its higher margin business and VIP packages.

In the outbound market, Intourist significantly strengthened its position, increasing its market share to 8.3% in 2008, compared to 5.6% in 2007. The Company has established positions in the market for mass-market destinations (Turkey and Egypt) as well as the sub-mass market destinations for Russian tourists (Spain, Italy, Greece, Czech Republic, Bulgaria, Thailand, Tunisia, etc.). In the 2008-2009 winter season, NTK Tourist offered new international tour destinations, including Goa (India), Indonesia, Malaysia, Singapore, Vietnam and Cambodia. The growth in tour destinations allows the Company to diversify its operating business and minimize risk exposure to any single market, while making use of synergies between its tour operating and transportation divisions.

The mass-market destinations of Turkey and Egypt accounted for 34% and 45%, respectively, of total outbound sales. Moscow and St Petersburg were the sources of 70% of total sales in 2008, while the Company continued to focus on regional markets, with tours originating from Stavropol, Samara, Rostov-on-Don, Yekaterinburg, Chelyabinsk, Novosibirsk, Perm and Krasnodar.

Intourist entered the mass market for domestic tourism with the acquisition of one of the leading players in its segment, Orient, during 2008. The Company's share in this market was 1.5% in 2008. Previously, Intourist had operated tours in Moscow, St Petersburg and the Golden Ring, but had not penetrated the mass market in recent years.

During 2008, Intourist maintained its status as the country's leading hotel-management company, with a total of 5,700 rooms in management by the end of the year. Of this total, 3,200 rooms were in Russian hotels and 2,500 rooms were abroad. In comparison, total room count by the end of 2007 was 2,400 rooms, of which 2,300 rooms were in Russia. The majority of its Russian hotel rooms are located in Moscow, where Intourist operates the landmark Peking and Cosmos hotels in the city center. At the same time, it is developing rapidly in the regions. In July 2008, Intourist Hotel Group signed a 15-year lease to manage the Elets Hotel in Lipetsk Region. During the year, the Hotel Group undertook a rebranding to strengthen its image as Russia's number one hotel operator.

The number of hotel rooms outside of Russia managed by Intourist rose from around 100 to 2,500 during the year. In May, Intourist obtained a five-year lease for the five-star Justiniano Club Belek in Belek, Turkey. Management of the hotel is being performed by local subsidiary Intourist Hotel İşletmesi, with the aim of providing the Company's tour operations with access to hotel capacity in Turkey's most popular tourist destinations. Also in May, Intourist signed a deal with International Hotel Investments (IHI) plc, a subsidiary of Corinithia Palace Hotel Company Limited Malta, to create a joint-venture development of four- and five-star hotels in Russia.

In April 2008, Intourist concluded a club deal to obtain a US$50 million credit. The credit was organized by the Moscow offices of HSBC Bank and Raiffeisenbank. In October 2008, Commerzbank AG joined the club loan as a third creditor, providing an additional US$17 million. The credit term is three years, and the interest rate ranges between 5% and 5.25% annually. The loan is intended for general corporate needs, including the financing of current operational activity, CAPEX for hotel construction projects and M&A.

In May 2008, Intourist acquired 100% of the shares of Intourist USA. The company was originally founded in 1930 as the American representative office of the Soviet-era Intourist, before becoming an independent operator in 2001. Once again a subsidiary of the Company, Intourist USA has an established brand identity and a well-established presence in the US marketplace.

In June 2008, Intourist appointed its first independent director with international experience to its board of directors. The appointment of John Theodore Lindquist signals the Company's commitment to improving its corporate governance systems by increasing its transparency and adherence to international standards of business conduct.

In July 2008, Intourist and Tver region signed a cooperation deal for development of the tourism infrastructure of Tver region. The agreement was signed as part of the Program for the Development of the Hotel Network in the central cities of the Central Federal District, which was approved in 2007.

At the end of 2008, Intourist Travel Store completed a deal to acquire 74% of the shares of RossTour, a leading chain of tour agencies in the Urals Region. This acquisition enhances the Company's retail business, while at the same time allowing it to strengthen the position of its tour operations business in the Urals.

On the basis of its performance in 2008, Intourist was named 'Largest Tourist Company in Russia' for the third year in a row by TurInfo. In September 2008, in the Top 1,000 Russian Managers rankings assembled by *Kommersant* and the Association of Russian Managers, Intourist President Alexander Artunov was named top manager in the category of 'Service.'

Strategy & Outlook

Going forward, Intourist is committed to maintaining its leading position in the Russian tourism market. It plans on solidifying its positions in the inbound, outbound and domestic travel segments while exploiting synergies among its business divisions. In 2009, the Company's goal in the tour operations business is to increase market share in the falling outbound market in order to benefit the Company when the segment returns to growth in 2010 or 2011. In its hotel management business, it aims to improve the efficiency of its existing facilities in order to reduce costs in a difficult operating environment. In the retail sector, Intourist is focused on optimizing the performance of its point-of-sales chains, and will take advantage of the consolidating sector with the intention of acquiring market share and existing points-of-sale in attractive locations.

Intourist's longer-term strategic goal is to be the established leader in the Russian and CIS tourist industry and in the top 10 of all European operators. Its strategic approach includes further vertical integration to capture more of the value chain while promoting Intourist as a single umbrella brand across all areas of its business. The Company aims to occupy 15% of the outbound market and 20% of the inbound market. The hotel management business will develop with a focus on the geographic requirements of the tour business in order to utilize its existing networks. The Company's point-of-sales chain will continue to grow, and Intourist will move aggressively to realize the potential of online sales. The strategic outlook also envisions the potential for creating a charter airline in partnership with a large airline, as well as the potential for an alliance with a large European player.

Retail

Marketplace

During 2008, the Russian marketplace for retail of children's products saw two radically different trends – reflecting consumer spending patterns and confidence before and after the impact of the global financial crisis was felt in the country. Before September 2008, the retail market demonstrated robust growth and was on track to increase by around 20%. Continued growth was being driven by the increased birth rate and growth in real household incomes. This growth reflected a stable pattern seen since the beginning of the decade, with retail as a whole shifting away from traditional markets and single shops to national and regional chains.

After years of decline in the 1990s and the beginning of this decade, Russia's birth rate is increasing. In 2008, it rose by 8% and exceeded 12 children per 1,000 residents. The birth rate is the primary driver of the market for children's products, as it increases the number of consumers who need to be fed, clothed and reared. An extremely positive phenomenon for children's retail is the fact that the number of children in the under-4 age segment, which accounts for more than half of the market in value terms, has increased by around 20% over the last five years.

During the first nine months of 2008, real disposable household incomes rose by 7.1%, compared to the same period in 2007. This rise was accompanied by increased spending, with the non-food segment of the retail sector growing by between 20% and 30% annually. [28]

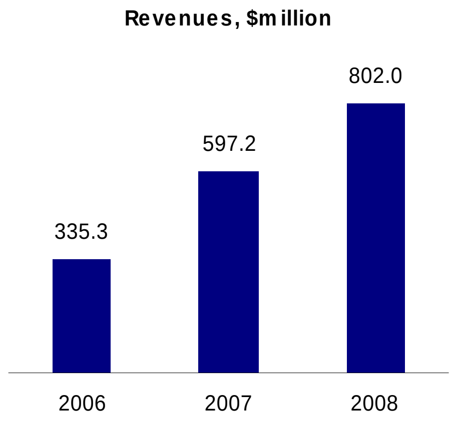
The market situation shifted dramatically in September and October. In the fourth quarter, there was a 5.8% reduction in disposable wage income. For the year as a whole, growth in this indicator was only 2.7%, compared to 12.1% in 2007. Combined with a sharp fall in consumer sentiment – Rosstat's index of consumer sentiment fell to a six-year low – the net effect was a substantial slow down (although not a decline) in non-food retail market growth to approximately 10% year-on-year.

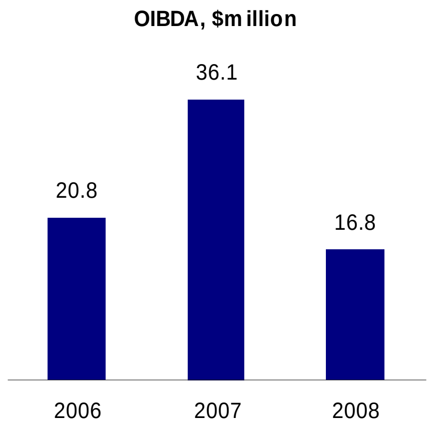
According to research carried out by Detsky Mir and data from independent research groups, around one quarter of the consumer segment targeted by Detsky Mir in the children's retail sector reported that they were reducing spending on their children as a result of the present economic situation. This ratio is substantially lower than the level adults plan to cut back on spending for themselves, indicating the relative resilience of the market for children's products. According to Comcon data, the share of consumers planning to economize on purchases of adult clothing and shoes is approximately 50% higher.

The most stable marketplace in 2008, as might be expected, was children's food, with fewer than 20% of buyers choosing to cut back in this area. The most typical approach to cutting costs for consumers is to switch to a cheaper pricing segment rather than returning to traditional markets. These local shops continue their long-term trend of ceding overall market share to organized retail, particularly chains, which account for around 30-35% of the market for children's products.

[28] Source: all retail and spending data from Rosstat

Detsky Mir





Company in Brief

Detsky Mir is the leading retailer of children's goods in Russia. With a 50-year history, it is one of the country's best-known and trusted retail brands. Today, the Group includes the Detsky Mir national retail chain, C-Toys and the Yakimanka Children's Gallery luxury center. The Group has more than 220,800 m^2 of retail space. C-Toys is one of the leading distributors of children's products in Russia, and engages in licensed production and distribution of toys and children's clothing for such well-known international players as The Walt Disney Company, Warner Bros., Nickelodeon, Sony Pictures, Marvel and others, as well as producing its own licensed party costumes. The Yakimanka Children's Gallery luxury center is a full-concept shop in Moscow, with products for children under 14 years old and a total trading area of 3,560m^2. The head company of the Group is Detsky Mir Center, which is 100% owned by Sistema.

Operational & Financial Results

Detsky Mir delivered a strong top-line performance in 2008, despite very difficult market conditions in the latter part of the year. The Group achieved a robust increase in sales through organic growth in existing stores and continued expansion. Detsky Mir increased its revenues by 34% year-on year in 2008 to US$802.0 million, compared to US$597.2 million in 2007. OIBDA declined by 53% to US$16.8 million. Same-store sales rose by 27%.

The Group celebrated its 100th store in May, with the opening of a new outlet in Magnitogorsk. At the end of 2008, the Group had 130 stores, and total retail space reached 220.8 thousand m^2. Around 70% of this space was accounted for by stores outside of Moscow and Moscow Region. Average store space in 2008 was 1,700m^2.

Detsky Mir opened 40 stores during 2008, with a total retail space of 62.3 thousand m^2. In December, the Yakimanka Children's Gallery luxury center, with 3.6 thousand m^2, was opened in Moscow. The flagship Detsky Mir store in Lubyanka Square in Central Moscow was shut in July 2008 for a major reconstruction. Including the Lubyanka store, a total of six stores were shut or relocated during the year, accounting for a total of 15.4 thousand m^2 of retail space.

The flexibility of Detsky Mir's format and experience in operating in regional markets and targeting a range of consumer income groups allows it to quickly adapt its product matrix to changing consumer requirements. This flexibility proved particularly important in 2008, as the retail sector began to feel the impact of the slowdown in consumer spending. The crisis has also provided opportunities for Detsky Mir to consolidate its leadership in the market for children's products, winning over new customers and in some cases taking over leases in attractive locations previously occupied by competitors.

A key strategic goal for Detsky Mir during 2008 was to improve and streamline its management and corporate structure. New and highly experienced managers joined the top-management team. A system of key performance indicators (KPIs) was developed and installed for the Group.

During 2008, the Group concluded major restructuring work to make its lines of management and reporting more efficient and transparent. A three-level system of management has been created, with stores reporting to regional trading representative offices, which in turn report to the Corporate Center. Some 11 regional trading representative offices have been created, which carry out management of stores according to their geography. The Detsky Mir Center management company was streamlined through the consolidation of five subsidiary companies, making it both more transparent and efficient.

In 2008, the Group also moved to reorganize its logistics with the transfer of logistics operations to the Group's Wholesale and Logistics company, which is consolidating all such operations in the Group into a 21.4 thousand m^2 leased Class A warehouse at the Kreshkino logistic park.

Relationships with suppliers have also been streamlined, with 99% of suppliers to C-Toys now accredited with post-financing. More than 30% of turnover of Detsky Mir's suppliers has been moved to factoring. In July, the Group signed a deal with Swiss Group SGS to carry out a quality audit of suppliers and of the Group's own products. Detsky Mir has also introduced its own 'mark of quality,' ensuring that goods meet the strict requirements set out by the company and Russian regulators for product quality and safety.

The Group also obtained additional financing this year to invest in expanding and restructuring the existing debt load. These funds included a US$20.5 million loan from Raiffeisenbank Austria, a US$20 million loan from UniCredit Bank and a US$50 million loan from the European Bank for Reconstruction and Development (EBRD). In addition, a contract was signed with Raiffeisenbank for the refinancing of EUR 50 million in rubles. Nomos Bank approved an uncovered credit limit for RUB 300 million, and MetallInvest Bank has provided a factoring limit of RUB 478 million.

The Group remained a committed corporate citizen in 2008, and donated cash and goods worth nearly RUB 16 million to charitable causes for children. Also during the year, the Group was one of the founders of the Association of Enterprises in the Industry for Children's Goods charity, which consolidates the largest players in the domestic market for children's products.

In February 2008, Detsky Mir's leadership in the sector was recognized when it was named 'National Leader in Children's Product Retail' at the annual Russian Retail Olympics, which is organized by top government and industry bodies. It was also named in the categories 'First among Equals' and 'Most Go-getting' at the 2008 Retailer Best awards.

The company was ranked 33rd in April 2008's ratings of Russia's Top-50 retailers by *Kommersant* newspaper. It was also ranked among the Top-200 most transparent companies in Russia, ranking 16th among all retailers, in a survey by *Sekret Firmy* magazine, published in May.

Strategy & Outlook

Detsky Mir's development strategy is based on the development of its national chain of Detsky Mir brand children's stores, increasing the efficiency of all of its operations to reduce costs and strengthening the Group's competitive advantages in the marketplace.

The continued national expansion of the retail business will be based on a carefully pinpointed store-opening plan for 2009. This plan is based on the most attractive locations, particularly those vacated by the departure or reduction of other companies in the marketplace. In order to make the best use of scarce financing in the current environment, very strict criteria will be applied when selecting which stores and projects will be funded in 2009.

The Group is applying both new management approaches and IT solutions in order to improve efficiency. It is putting an enterprise resource planning (ERP) system in place to help managers make more informed and rapid decisions. Logistics continue to be reorganized to reduce costs, prevent stockpiling and streamline dealings with suppliers. Overall business processes are being improved in line with the restructuring completed in 2007, and management is focused on the most efficient use of working capital.

The Group will also leverage its existing competitive advantages. It will continue to adjust its product mix to changing consumer demand in an uncertain economic environment. It is developing private-labels, which have a higher margin but are also generally cheaper alternatives for consumers. The Group is also developing its CRM systems to build upon its own consumer base as well as the wider consumer base of the companies in Sistema's Consumer Assets business unit.

Healthcare

Marketplace

The Russian market for paid medical services increased by 20.6% year-on-year in 2008[29]. The market for voluntary medical insurance is forecast to decline in value in 2009-2010 by around 20% due to the impact of the financial crisis, while the market for individual consumption for paid medical services is expected to fall by 10%. Before 2008, the market for paid medical services had grown by 25% to 30% per year.

Nonetheless, the market retains strong long-term growth potential, with current forecasts of 29.1% growth in the voluntary medical insurance market and 16.1% for individual consumption in 2011. The voluntary healthcare insurance market has been growing faster than the state-backed mandatory health insurance market, although the mandatory system is five-times larger. Total government financing in the healthcare sector is nearly 10-times larger than the market for paid medicine.

Moscow remains the largest market for paid medical services in Russia. The share of supplementary medical insurance in the total Moscow market for paid medical services was around 50% in 2008. In regional markets, only around 20% of clients are covered by insurers, 80% of clients are covered by other arrangements or pay out of pocket.

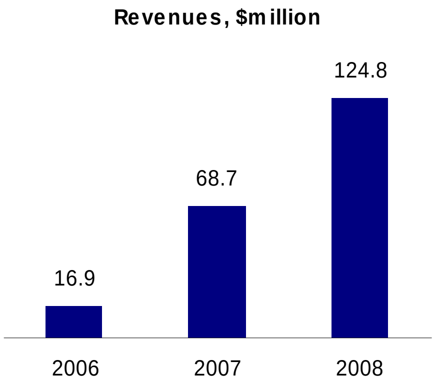
In 2008, the market saw a fall in consumption of high-cost medical services (such as VIP policies). Insurance companies sought to limit the volume of medical services covered by policies to make them cheaper. A number of small and mid-sized healthcare providers, often with large debt loads, failed, allowing the largest players to drive the consolidation process in the marketplace and acquire high-quality healthcare facilities, equipment and staff from failed companies.

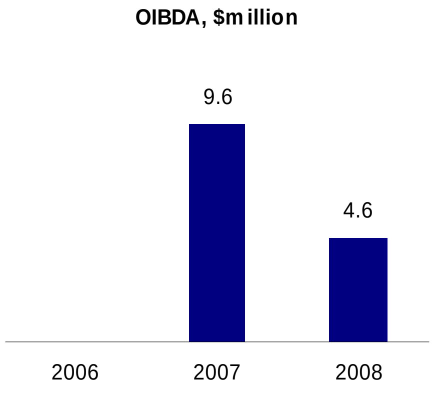
At the same time, the dynamic growth in the paid medicines sector has been driven by such factors as increasing healthcare awareness, provision of voluntary policies by employers as an added benefit for workers, company healthcare services and demand for specialized treatment. Before the negative impact of the economic crisis was felt in 2008, the most active growing segments of the paid medicine market were specialized clinics, primary-care center services, service under voluntary medical-insurance policies and services for individuals.

The global market for fitness and wellness services was worth an estimated US$81 billion, with a margin of 18%, according to Deloitte & Touche. In Russia, the market is worth around US$750 million and turnover grown by an average rate of 21,5%, although margins in the sector have been falling due to increasing competition. The present financial crisis has led to a fall in sector, by an average of 18% to 22%. The premium segment of the market in Moscow and large cities is the most saturated, while the low budget end of the market is currently the least crowded.

[29] Source: Discovery Research

Medsi





Company in Brief

The Medsi Group of Companies is Russia's largest national chain of private medical clinics by number of clients and revenues. It provides medical treatment, preventative care, dental, fitness and other health-enhancing services in Moscow and different regions around the country. Today the Group includes more than 30 clinics providing medical services for adults, the Medsi-American Medical Center VIP Center, two children's polyclinics, a hospital, an emergency medical service as well as a chain of fitness and wellness clubs. The Group is 100% owned by Sistema.

Operational & Financial Results

Medsi continued to deliver strong revenue growth during the year, while investing in regional expansion and the fitness segment of the marketplace. In 2008, revenues increased to US$124.8 million in 2008, compared to US$68.7 million in 2007. OIBDA decreased to US$4.6 million. Revenue per square meter increased by 21% year-on-year. The number of clinics and clubs increased to 37 from 28. The number of visits increased by 25.0% to 2,761,000, while the total number of clients increased by 86.4% to 328,000. The number of services delivered rose by 56.5% to 4,913,000.

Medsi's share of the highly fragmented market for paid medical services reached 1,2% in 2008, compared to 0,85% in 2007. The Group predicts that its market share will reach 1.7% in 2009. In the market for voluntary medical insurance, Medsi's market share reached 2.2% in 2008, compared to 1.9% in 2007, while the Group predicts that its share of this market will reach 3.2% in 2009.

In 2008, the Group moved all of its operations under the umbrella brand, the Medsi Group of Companies. A rebranding was carried out across the company and a single brand identity and accompanying brand book and logotype were adopted. A major marketing campaign to position the brand is planned for 2009. Integral to the brand's concept is promoting the idea of a healthy lifestyle and developing areas such as wellness, fitness and spa services.

During the year, Medsi expanded its network in both Moscow and the regions. Three new first-referral Clinics were opened in Moscow and Moscow Region during the year. A hospital was opened on the base of the Central Union Hospital in Moscow and an emergency-care station was opened on Novorizskoe Highway in Moscow Region. In addition, a first-referral clinic was opened in Yuzhno-Sakhalinsk in Russia's Far East.

Despite difficult market conditions for the sector as a whole, Medsi benefitted from consolidation in the sector, obtaining highly qualified personnel, including specialists and doctors and easing difficulties in recruiting such staff in the Russian market. As other clinics exited the market, their patients went to other providers, including Medsi. From the beginning of 2009, Medsi was conducting active negotiations with a number of clinics to potentially acquire them or run them under management.

In 2008, Medsi continued to innovate to better serve its patients and corporate clients while also becoming more efficient and enhancing business processes as the Group expands. During the year, the decision was made to introduce a single register of services. The move gives Medsi a clear competitive advantage and transparency in working with insurance companies. A single, high standard was introduced for equipping the offices of primary-care doctors at each clinic with the latest medical equipment as well as computers and printers. The standard surpasses federal requirements and builds upon Medsi's experience and expertise in delivering the highest standards of medical services.

During the year, work was begun to create a CRM (customer relations management) system to support the Group's sales department. The system has made it possible to unite all of the client databases of the Medsi Group in one place. Work was begun on the introduction of a Medicine Information System (MIS), a program which automates all aspects of the activity of a modern clinic and allows a doctor at any Medsi clinic to access data about any Medsi patient. The system gives doctors all of the information they require regarding the patient's medical history and current treatments at their fingertips. The use of the MIS will allow the Group to better manage the activity of each medical establishment and obtain the latest medical and management data.

The MIS is closely tied to another Group project, the client's Personal Office. The Personal Office is a highly secure portal which allows the client to see the entire history of his or her interactions with Medsi, book appointments or correspond with their care manager. The personal data secured in the portal is protected by state-of-the-art encryption.

During 2008, Medsi responded to market demand and launched the Treatment Abroad project to provide services using international clinics and specialists in Europe and Israel. The target client base for this project includes voluntary insurance patients and employees of Russian and Western companies which are serviced by Medsi clinics. The launch of the project allows the Group to ensure it can provide the complete cycle of treatment and continuity of care for its treatment. Although the impact of the financial crisis meant that the flow of patients was lower than forecast during 2008, the project remains a significant and developing business area for the Group.

The Group focused its resources on developing its infrastructure and integrating Medsi's existing assets in 2008 Cost-cutting plans were put into effect to help mitigate the impact of the crisis. Despite these constraints, the Group acquired the Family Medicine Corporation, a company which represents a unique market model for servicing VIP clients, including personal doctor-care managers.

In addition, the Group acquired a large hospital with a total floor space of 10,000m2 and 150 beds for providing care to patients within the Medsi network. This multi-use care institution provides a wide range of operations, including endoscopic care. The hospital has been linked to the total information network of the Medsi clinic.

In December 2008, Medsi was recognized for 'Contributions to Maintaining the Health of the Nation' at the annual Company of the Year awards.

Strategy & Outlook

The primary strategic goal of Medsi is to become the leader of the market for private medical care in Russia and build upon its leading position in the marketplace and presence in key market segments, including its chain of clinics, hospital, VIP clinics, children's clinics, fitness and additional services, including treatment abroad.

An important component of the strategy for 2009 is to take advantage of the opportunities created by the crisis to build market share and lead the consolidation of the marketplace. At the same time, in light of the increased cost of obtaining outside financing, the Group has scaled back its immediate expansion plans. The Group is focused on completing the construction and launch into service of seven first-referral Clinics and a clinical and diagnostic center begun in 2007 while focusing financing on further developing its competitive strengths.

Taking into account the crisis, the Group's marketing strategy is focused primarily on insurance companies, as they provide longer-term (from six months to one year) guaranteed revenue streams for corporate policies. For children, the share of insurance companies accounts for 50%, while 50% are accounted for by individual clients, as many company policies do not include children under voluntary medical insurance policies.

Real Estate

Marketplace

During the first half of 2008, the Moscow market for office real estate continued to develop at a similar pace to that of the previous few years. Demand for office space exceeded supply, despite the fact that, beginning in 2005, the amount of quality office space in Moscow increased at an annual rate of 25% to 35%. The scale of projects continued to increase (exceeding 100,000m^2), as did the complexity, with several formats combined in a single project and in the development of the accompanying infrastructure. The process of decentralization progressed, including projects beyond the limits of the Moscow Circular Highway (MKAD).

During the third quarter of 2008, the pace of development of the office market slowed. The quantity of new, high-quality property to come onto the market declined, as did the number of new construction projects. In the fourth quarter, as the impact of the global financial crisis on the Russian economy became apparent, several development companies announced that they were halting projects already in progress. Potential leasing clients began to review expansion plans and preliminary lease agreements. A market for subleasing emerged, and leasing rates fell between 5% and 15%.

The market for retail property also saw a continued boom period in the first half of the year, followed a by a sharp slowdown in the third and fourth quarters of 2008. At the beginning of the year, a large number of new, high-quality retail premises came onto the market, a significant portion of which had already been leased due to high levels of demand from Russian and international retailers.

In the fall of 2008, the retail market felt the impact of the global financial crisis. The market reacted to the crisis by slowing the pace of new construction. There was a reduction in demand from potential leasing clients, as a number of retailers announced the closure of outlets and scaled back plans to expand into other cities. Developers concentrated on completing the construction of projects already in advanced stages of readiness, and other projects were put on hold. Regional projects were frozen, due to problems with financing.

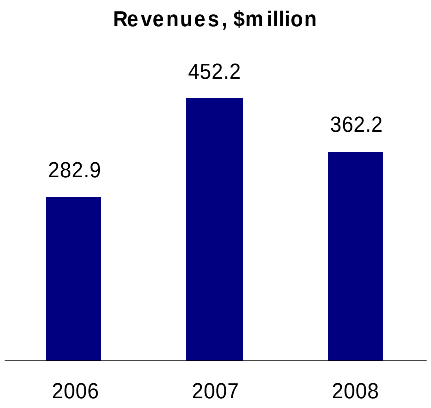
Despite the crisis, consumer demand remained relatively stable until the end of the year. However, a reduction in purchasing is anticipated from the beginning of 2009, with growth in retail turnover expected to fall to 3.4%, compared to 13.6% in 2008. A shift to lower-cost goods will mean greater stability in the market for hypermarkets and discounters. The crisis is expected to accelerate the process of consolidation in retail markets as well as in retail property markets.

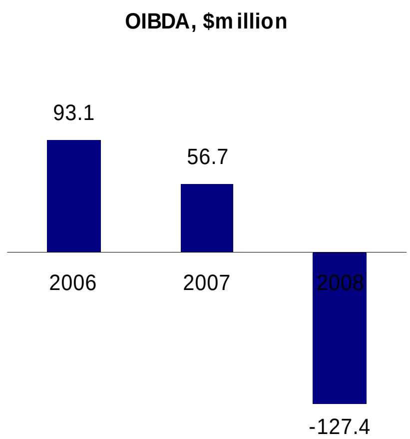
One of the main trends in the Moscow market for hotel properties in recent years has been the retirement of a range of properties of various classes without adequate replacement. Nearly all new projects have been concentrated in the uppermost segment of the market, due to the reduced payback period of properties in this class. The growth of new hotels in the middle-market category has been minimal. Out of 25 projects due to be completed and put into service in 2008, only eight were finished. In addition, a number of new hotels will enter the market with significant delays, as was the case before the crisis. Out of around 2,500 new hotel rooms forecasted for the year, around 1,000 actually came into service. A number of mixed-use projects with a hotel element that were due to be finished in 2009 will likely be delayed, and the market will see slower growth over the medium term.

In the residential market, the primary market trends in 2008 included limited volumes of new properties, a fall in purchasing activity and the diversification of the activity of developers previously focused on residential properties. Purchasing activity during the year peaked in March and April, and prices continued to rise during the first half of the year. Prices for elite housing in newly-built projects in the center of Moscow rose by 9.0% during the first hal,f and prices in the secondary market grew by 15.2%. During the first half of the year, however, not a single significant new property came onto the marketplace, as sales in large new projects were scheduled to begin in the second half.

Beginning in August, demand in the marketplace began to fall. At the same time, prices for elite newly-built housing in the center of the city rose by 2.4% in the third quarter, and by 3.2% in the secondary market over the same period. In the third and fourth quarter, the market for residential housing retained its general trend of development, and the market was less affected by the crisis. This is in part due to the fact that a unique project is always an attractive asset and the market for elite housing remains relatively small. Buyers can usually be found, even in a down market. At the same time, few new properties that came onto the market as existing projects were halted due to the impact of the financial crisis.

Sistema-Hals





Company in Brief

The Sistema-Hals Group is one of Russia's leading real-estate development companies, with primary business areas of Real Estate Development, Asset Management and Facility Management. Its broad range of development services allows the company to operate a clear system of control across the full lifecycle of a property, from the conceptual design stage through to the management of the completed property. Since it was founded in 1994, Sistema-Hals has successfully completed around 40 projects with a total area of about 340,000 m^2. These include the headquarters of DaimlerChrysler, the Hals-Tower office building, the headquarters of the Pipe Metallurgical Company (TMK), a hotel for the international MaMaison chain (Orco Property Group), the Detsky Mir retail and entertainment center in Kazan and a range of residential complexes in Moscow's Kuntsevo District.

Sistema-Hals shares have been traded on the Moscow Interbank Currency Exchange (MICEX) under the ticker HALS since 2006, as well as in the Russian Trade System (RTS) since 2007. Global Depository Receipts of Sistema-Hals have been traded on the main market of the London Stock Exchange since November 2006 under the ticker HALS.

In April 2009, Sistema signed an agreement with VTB Bank to sell a portion of its shares in Sistema-Hals. Following the exercise of the transaction and the call option, VTB will own 51%

of Sistema-Hals. Sistema will continue to participate in the development of Sistema-Hals through its 20% minority stake.

Operational & Financial Results

In deeply challenging conditions in the Russian property sector, Sistema-Hals' consolidated revenues for 2008 decreased by 20% to US$362.2 million, compared to US$452.2 million in 2007. The company posted negative OIBDA of US$(127.4) million.

According to an independent analysis conducted by Cushman & Wakefield Stiles & Riabokobylko (C&WS&R), the value of Sistema-Hals' holding in properties and development projects stood at US$2.05 billion as of January 1, 2008.

At the end of 2008, the Group's diversified portfolio consisted of 104 projects and properties. The combined planned area consisted of 80 projects amounting to 4.5 million m^2 and around 500 hectares of land, and 25 properties amounting to around 117,000 m^2 and more than 350 hectares of land. This portfolio includes Class A and Class B office buildings, multi-use complexes, elite and business-class residential buildings and villa communities, hotel and multi-use complexes and land development.

During 2008, the primary area for the Group's Real Estate Development business was the sale of apartments and houses in the developments on Simferopolsky Thoroughfare, Michurinsky Prospect, Dnepropetrovskaya Street and Rublevskoe Highway. As of the end of 2008, the Group had sold 77% of the apartments in the Primavera apartment complex on Simferopolsky Thoroughfare 18 and 18/1, 100% of the apartments in Dnepropetrovskaya Street 25A, 72% of the apartments in the Diplomat development on Michurinsky Prospect 39A, 91% of the apartments in the Emerald Valley development on Rublevskoe Highway 111A, a standing parking garage on Aviator Street 9 and 80% of the plots in the Aurora villa complex in Stepankovo, Moscow Region.

In 2008, as part of the process of optimizing the Group's portfolio, it sold a project for the construction of an administrative building in central Moscow on Rochdelskaya Street, as well as a complex of buildings on 8th of March Street.

The primary revenue from the Group's Asset Management business came from leasing cottages in the Serebryany Bor area. In 2008, the company started to lease cottages, which were built during the second stage of the project Serebryany Bor. Those premises consist of 20 cottages with a total space of 4 774 m^2. In 2008, the Group leased 99 cottages with a total space of 26 536 m^2 overall. During the year, the Group achieved an average rate of around US$1,000 per m^2. In August, the asset-management portfolio was enhanced with the addition of the Danilovsky Fort Business Center, located on Novodanilovskaya Embankment, 8, Moscow.

Also in 2008, Sistema-Hals, together with its French partner Apsys, began to lease retail space at its Leto (Summer) retail and entertainment complex. During the year, lease agreements were signed with major retails including Media Markt, Russky Led, Monex Trading (Mothercare, Claire's, Next, the Body Shop and Starbucks), Lady and Gentleman, KFC, L'Etoile, Sephora, and nearly 30 others.

During the year, Sistema-Hals undertook a number of major projects for clients within the Sistema group. In May, the Group began construction of the first phase of a film and television-studio complex in St. Petersburg for RWS. In July, Sistema-Hals began the restoration of the landmark Detsky Mir building on Lubyanka Square in Central Moscow.

In 2008, the Group's Facility Management business portfolio included objects with a total space of around 288,000m^2 that are located in six Russian regions. Clients include large Western and Russian corporations: Japan Airlines, Metromedia International Group, Raiffeisenbank, Scandinavian Airlines, Siemens, Western Union, Sistema, MTS, Detsky Mir, Intourist, Rosno, Mosdachtrust, MGTS, Nafta-Moscow, Mobile Drilling Systems, Uralsib Leasing Company, Chibo CIS, Warley Parsons International, Stelt Telecom, Trabond Limited and Oscar Service.

In order to optimize its business structure, the Group made the decision in 2008 to dispose of the Infrastructure-Construction segment as a non-core business. Therefore, in November 2008, it undertook the sale of 51% of the shares of Organizator LLC and 51% of the shares of PSO Sistema-Hals CJSC.

On April 7, 2009, after the end of the reporting period, Sistema signed an agreement with VTB Bank to sell a portion of its shares in Sistema-Hals. The transaction is being carried out in two stages. In the first stage, which is already completed, VTB acquired a 19.5% stake in Sistema-Hals, and also received a call option to acquire a further 31.5% stake in the company. VTB may exercise its call option, subject to receiving the necessary approvals from the regulatory authorities. Following the exercise of the call option, VTB will own 51% of Sistema-Hals. Furthermore, both parties have agreed to the terms for the restructuring of Sistema-Hals' debt to VTB.

Strategy & Outlook

Following the sale of a portion of its stake in Sistema-Hals, Sistema will continue to participate in the development of Sistema-Hals through its 20% minority stake, contributing its deep expertise aimed at enhancing the shareholder value of the Group.

In December 2008, the Board of Directors of Sistema-Hals adopted an anti-crisis program. Sistema-Hals plans to maintain revenue flows through the sale of projects in order to finance production programs as well as to pay off current debt. Key high-margin projects and those involving existing partnership commitments have been identified for priority financing. Lesser projects are to be sold and the revenues concentrated on core business areas. A cost-cutting program aims to reduce commercial and administrative costs by 50%. The Group will continue to seek external financing and will re-finance existing debt as necessary.

In 2009, the Group plans to complete the sale of flats in the apartment buildings on Simferopolsky Thoroughfare, Michurinsky Prospect and Rublevskoe Highway, and will carry out the sale of land plots in the Aurora villa complex as well. These projects are in the final phase and do not require significant additional financing. In addition, Sistema-Hals plans to begin the sale of apartments as part of the program of redeveloping the former MGTS buildings located at Vsevolozhsky Lane 5 and Milyutinsky Lane 5/1. In May, an agreement was signed with leading Italian architecture design firm Giugiaro Architettura to design the interior of the apartment-hotel portion of the Milyutinsky Lane 5/1 development.

Over the longer term, the strategic goal of Sistema-Hals is to occupy the leading position among Russian property companies through achieving a stable financial position and implementing a range of unique projects. The strength and ability of its team and its property pipeline will allow it to increase its long-term market value. It plans to build upon the strong foundation that it has created over the past 15 years, and will use its considerable experience and expertise to build a more diverse and profitable property portfolio.

In order to realize its strategic goal, the Group aims to create a diversified portfolio of properties in all key market segments, including Class A and B office properties, retail and entertainment complexes, hotels and business-class residential properties. In particular, the Group plans to concentrate its resources on current projects in the Class A and B office market, and will increase the share of profitable assets by maintaining unique and high-margin properties in its portfolio. At the same time, residential property will remain one of the primary sources of income for the implementation of the Group's long-term commercial property projects, and will finance current operations.

Sistema-Hals also plans to take advantage of the increased support and proficiency provided by its international strategic partnerships. Through its partnership with Apsys, the Group has a range of unique competitive advantages in developing retail property projects. The Group plans to develop this partnership and increase the number of projects underway. The Group will also build upon its relationship with Saudi-Arabian company Saraya to develop projects in the hotel segment. The Group will continue to seek strategic relationships with top international property and construction companies.

12. Business Unit “Technology and Industry”

Vision & Strategy

The mission of the High Technology and Industry business area is to efficiently manage and develop the high-technology and industrial assets of Sistema. The business area intends to continue the development of its key subsidiary companies in this area-Sitronics, RTI Systems and Binnofarm-while focusing on unlocking and exploiting synergies between these businesses.

In order to fulfill this strategic mission, a number of long-term objectives have been established. The market positions of the high-technology businesses of Sistema will be strengthened in the developing markets of Russia, the CIS and Eastern Europe, while also entering Asian markets. The management of the subsidiary companies in this business area will be strengthened. New areas of production and technological development will be created and, where appropriate, M&A will be undertaken to increase synergies between the companies. Stable monetary flows will be maintained, and there will be effective and targeted investment in projects to promote organic growth.

The High Technology business unit is carrying out active work to attract state financing through the implementation of joint projects with the Russian government by way of state-private-sector partnerships, as well as through participation in federal target investment programs and national projects. The business area is acting to initiate and develop joint projects with leading Russian state-owned corporations.

Another, no less important, area for Sistema in the High Technology and Industry arena is cooperation with the state in fields of innovation such as the development of Technoparks and Special Economic Zones (SEZs). The business area has participated in the development of these zones of innovation for several years, and in the context of a number of major programs and projects.

Global economic uncertainty has led the Corporation to develop several anti-crisis strategies in this sector. These include finding alternative investment opportunities made possible by the crisis itself, and maintaining positive cash flow while reducing the debt load of each business. The success of these anti-crisis measures will be ensured, where needed, by direct management of subsidiary companies.

High Technology

Marketplace

The growth in demand for next-generation data and convergent services is driving the advancement of both developed and emerging telecommunications markets. Mobile and fixed-line operators are seeking to gain market share and increase average revenue per user (ARPU) by offering services such as high-speed wire-line and mobile broadband Internet access, streaming video and online gaming, as well as Internet telephony (VoIP), triple-play services (voice + data + TV) , high-definition television (HDTV) and more.

These factors are driving the demand for data-exchange equipment, broadband infrastructure, routers and other related products in the target markets in Russia and the CIS, as well as in Eastern Europe, the Middle East, Africa and the Asia-Pacific Region.

In order to deliver a wider range of convergent services, telecommunications operators worldwide are focusing their investment on building and expanding networks based on IP protocols and IP Multimedia Subsystem (IMS) networks. There is an ongoing shift towards combining next-generation networks (NGNs) by using soft-switch exchanges capable of simultaneously supporting both wire-line and wireless access to a full range of services for voice, data and video.

As service providers look to reduce costs by moving to Internet Protocol (IP) networks, streamlining their operations and better managing their network assets, the need for new business support systems (BSS) increases. Gartner predicts that the customer billing management market will continue its positive trend by being the mission critical parts of the telecom operations. The latest Gartner Telecom Operations Management Systems study states that the billing and charging systems in Eastern Europe - where a high percentage of revenues comes from the Russian market - is expected to grow between 4-6% over the next two years.

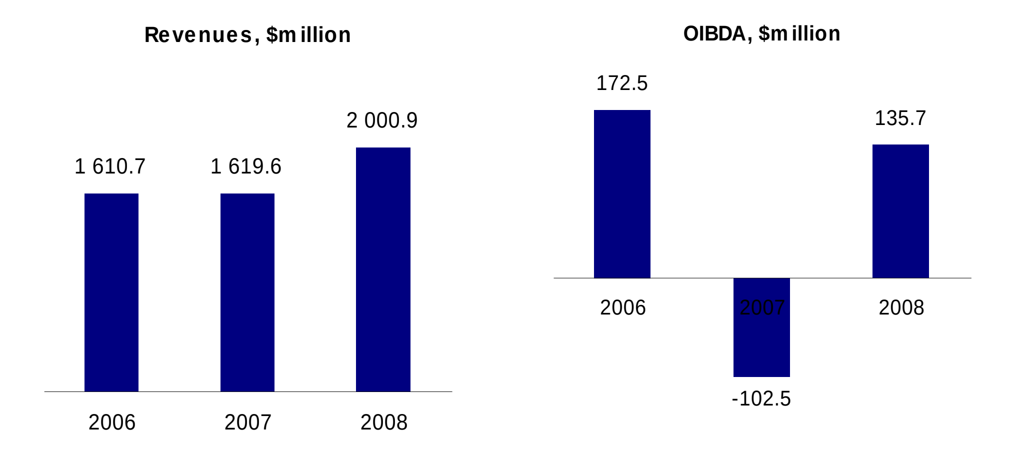
According to the research by the Semiconductor Industry Association, the value of the microelectronic market totaled USD$248.6 in 2008, which is 2.8% less than in 2007. The market posted growth in the first three quarters of the year, but declined in December 2008, falling 22% lower than in the same period last year. This was the first semiconductor market decline since 2001, and was directly affected by the banking crisis and global economic slowdown.

The market for smart cards in Russia remains stable. This market is affected by two opposite trends – the decrease of average prices and the growth of volume demand. The market is still far from saturation, so the transport cards and banking cards segments showed positive movement in 2008 despite an overall demand decrease.

According to the Gartner IT Market forecast summary, the dollar-valued global IT spend is estimated to grow by 7.52% in 2008 and by 2.17% in 2009, with an average of 5.07% annual growth from 2007 to 2012. Growth will be driven by the development of the emerging markets in the Middle East and Africa. These regions will have an estimated CAGR of 9.8% from 2007 to 2012, followed by APAC and Central and Eastern Europe, which will have a CAGR of 8.4% and 6.2%, respectively, between 2007 and 2012.

The telecoms market in Russia is consolidating after a period of tremendous growth in the last 5 years. According to a Gartner study, mobile connections have grown from 36 million in 2003 to 162 million in 2007. According to ACM Consulting, growth will continue, though at a slower pace, with mobile connections reaching 181 million at the end of 2008. Though the mobile market may seem to be saturated, other parts of the telecoms market maintain substantial potential for growth. In Gartner's study, only 5% of households had consumer broadband connections, a figure which is predicted to grow to 14% in the next five years.

Sitronics



Company in Brief

JSC SITRONICS is a leading provider of telecommunications, information technology and microelectronic solutions in Russia and the CIS, with a growing presence in other EEMEA emerging markets. The company has offices in 32 countries, servicing more than 3,500 clients and exporting to 62 countries worldwide. Today, the company has more than 10,000 employees. In 2007, Sitronics carried out an IPO of its shares on the London Stock Exchange, and its shares are also listed on the RTS and MSE exchanges in Moscow. Sistema owns 61.33 % of Sitronics.

Operational & Financial Results

During 2008, Sitronics continued to optimize its existing product line in each area of business, and implemented its strategy of focusing on the fastest-growing and highest margin segments of the high-technology marketplace. Despite unprecedented challenges in the global high-technology marketplace, the Company delivered strong sales growth and OIBDA margins. Revenues grew over 24% year-on-year to US$2.001 billion in 2008, compared to US$1.620 billion in 2007. OIBDA profits reached US$135.7 million, compared to OIBDA losses of US$ 102.5 million in 2007. The company therefore delivered OIBDA margins of 6.8% for the full year in 2008.

Telecommunications Solutions

During 2008, the Telecommunications Solutions strengthened its position in the marketplace through new contracts, new products and cost optimization programs. Sitronics successfully expanded its geographical footprint and strengthened its position in high-growth markets such as Africa, the Middle East and Asia.

In 2008, Sitronics Telecommunication Solutions and Intracom Telecom (a subsidiary of Sitronics) won new contracts with the largest telecommunication operators all over the world, including: Vodafone Czech, T-Mobile (Slovakia), Globul (Bulgaria), Mediacom (Poland), Smart Telecom (Ireland), MTS (Russia, Ukraine, Belarus, Uzbekistan), Comstar UTS, K-Telecom (Armenia), Kazakhtelecom (Kazakhstan), Warid Telecom (Uganda and Congo), and Shyam Teleservices (SSTL).

Information Technologies

During 2008, Sitronics Information Technologies maintained its status as the leading systems integrator in the CIS. In June 2008, Sitronics subsidiary Kvazar-Micro was brought under the Sitronics umbrella brand, and the company was renamed Sitronics Information Technologies. This integration and rebranding followed an increase in Sitronics' shareholding of Kvazar Micro to 100% in June. During 2008, Sitronics Information Technologies continued to implement and carry out IT-infrastructure projects for manufacturing, financial and governmental companies in Russia and the CIS. The Company announced the launch of new solutions such as the mobile data-processing centers called Sitronics Daterium™, which were jointly developed with the experts from the Russian Atomic Energy Corporation (Rosatom). Also in 2008, the company commenced the project for Comstar UTS to deploy the first wireless WiMAX network in Russia.

Sitronics Information Technologies continue to work on a number of large state-sponsored infrastructural projects, including: "Global Navigation System," in cooperation with the Federal Space Agency and the Transport Ministry; "Electronic Russia 2002-2010," in cooperation with the Ministry for Economic Development; and "Education development for 2006-2010," in cooperation with the Ministry of Education and Science. The company deployed a Multiservice Information and Communications Educational Network solution (known as MIOS) in Russia (Moscow, St Petersburg, Kazan, Sochi, Astrakhan) and the CIS.

In 2008, Sitronics Information Technologies obtained a license from the Federal Security Service for the development of certified solutions for the protection of confidential information.

Microelectronics

In 2008, Sitronics Microelectronics remained the leading Russian manufacturer of microelectronics according to any national standard. The company is also one of the key participants in a partnership between the government and private enterprise that carries out R&D initiatives. In 2008, Sitronics became the first microelectronics company in Russia to achieve ISO 14000 certification for its management of the environmental impact of its activities. During the year, the Company continued its successful cooperation with the Moscow Metropolitan, supplying around 25 million contactless (RFID) transportation cards each month. RFID cards were also used by transport companies in Magnitogorsk and Tumen. In 2008, the company developed 25 new types of microcircuits. Using 0.18-micrometer technology, three new products were introduced: chips for ID cards and electronic passports, RFID chips for contactless cards and memory sticks.

Sitronics Smart Technologies controls around 25% of the market and is the largest supplier to providers of GSM services in the CIS.

Consumer Services and Products

In 2008, the restructuring of the Sitronics Consumer Services and Products department continued, in line with the Company's strategy of focusing on higher margin products and services and adapting to changing market conditions. As part of the restructuring process, the Company ceased the assembly of consumer electronics at Zelenograd. Revenues from this business area were comparatively low as production of unprofitable products was terminated.

Strategy & Outlook

Sitronics has developed its strategy to mitigate the current negative effect of the global economic crisis and to build upon long-term trends in the Russian and global high-technology marketplace. The Russian government and state-owned companies are playing a larger role in the Russian economy, and are channelling investments into major infrastructure projects. In the broader marketplace, public and private-sector clients are demanding integrated and complete technology solutions. Meanwhile, global manufacturing and R&D in the high-technology sector are continuing to shift to Eastern Europe and the Asia-Pacific region. All of these factors provide unique opportunities for Sitronics in the high-technology marketplace, both in Russia and abroad.

In order to provide consistent and comprehensive solutions, Sitronics will leverage its partnerships with top global technology companies as well as its combination of scientific R&D capacity. Other development opportunities for the Company are based upon its existing position in fast-growing markets. The Company will use its geographic presence, its global experience, and the expansion of its portfolio of competitive prices and services to enter new, emerging markets by offering an efficient price-quality combination. In addition, Sitronics will expand its business through the existing ecosystems of major clients by offering them new and fully integrated solutions.

Radar & Aerospace

Marketplace

The Russian market for state defense contracts in 2008 amounted to US$32.68 billion, while the market for arms and military technology was worth US$19.61 billion over the same period. The market is developing dynamically due to major ongoing investments by the Russian government in upgrading and modernizing the country's military capabilities, while civilian projects such as the GLONASS satellite navigation system are witnessing the civilian application of advanced technology that was originally developed in the defense sector.

In 2008, the radio-technology and information systems segment of the Russian defense sector was worth US$1.90 billion dollars. It has seen stable growth rates of 15% per year. Information systems and complexes are a key priority area of development over the coming years under the Russian State Armaments Program for the period of 2006 to 2015.

The market for aerospace systems and avionics devices amounted to US$486 million. Growth in this market segment is likely to slow sharply in 2009-2010 due to the deterioration in the overall economy, and will weaken by 10-15% per year. The market for mechanotronics and robotics accounted for US$3 billion, of which around 30% was accounted for by electric motors, and the remainder by actuator technology. Currently, this market segment is expected to see a sharp decline of 20-25% in 2009-2010.

The market for navigation and telematics can be separated into two major segments: the regulated market (including state and local government clients as well as large corporate clients) and the commercial segment. The regulated market was worth an estimated US$510 million in 2008. According to data from the Mobile Research Group, the commercial market for navigation and telematics will be worth US$2.7 billion by 2010, and has grown by as much as 50% per year. This market remains one of the most promising in the wider technology sector. Despite negative economic conditions, the demand from the regulated marketplace for navigation and telematics products and services is expected to remain high.

The Russian market for ground-based ballistic missile defense systems has an estimated value of around US$200 million per year, while other long-range radar systems have a combined market value of around US$125 million. The market for short-range radar for civilian and specialized applications is forecasted to range between a value of US$200 and US$300 million over the next five years.

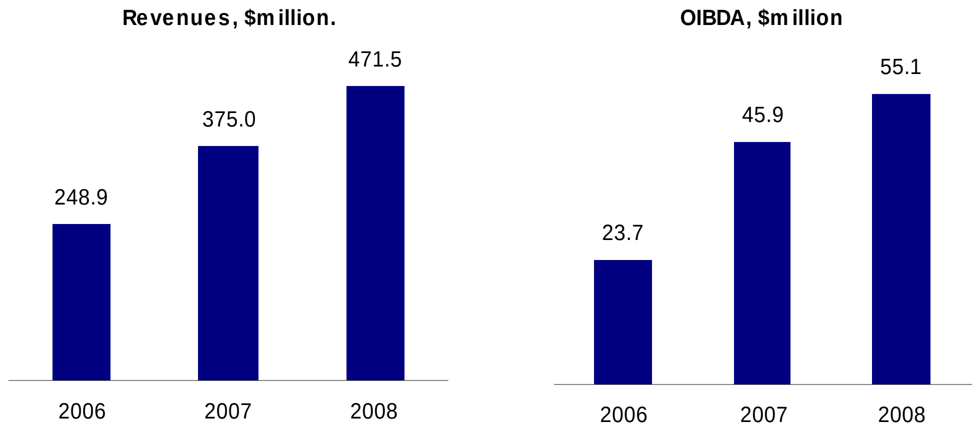
The market for information communications systems and devices that are primarily destined for various corporate users in Russia and the CIS is also growing rapidly, as are opportunities in other developing markets. The potential market for Russian companies in this segment is estimated at around US$1.5 billion over the course of the next five years.

The demand for integrated Management-Center solutions for both the military and civil sectors is likely to grow by 20-25% per year over the coming decade. A substantial part of this market includes navigation and telematics-related solutions, which are also predicted to see growth rates in the range of 20-25% per annum.

The level of demand for informational devices, including measurement and diagnostic equipment, is dependant on the rate of growth of the overall economy. The market has an estimated value of US$350 million over the coming five years. The market for broadcasting equipment, in accordance with the government's Concept for the Development of the

Telecommunications Market of the Russian Federation, should amount to around US$2.5 billion over the next five years.

Concern "RTI Systems"



Company in Brief

Concern RTI Systems OJSC is one of Russia's largest defense-industrial holdings, and it directs Russian companies with enormous scientific and production potential and experience in successfully executing highly complex, high-technology projects. RTI Systems specializes in the development and implementation of large system projects in such fields as radio technology, aerospace and ground-control systems, mechanotronics and robotics. It also acts as lead contractor for the creation of information elements for ground-based ballistic missile defense systems, and organizes technical operations of the current group of anti-missile defense systems (AMDS) and space surveillance systems (SSS). Its primary clients include the Russian Ministry of Defense, the Emergency Situations Ministry, the Federal Security Service, the State Corporation for Atomic Energy and the Ministry for Internal Affairs. Major projects carried out by RTI Systems include the Voronezh next-generation radar and creation of the National Emergency Situations Control Center (NESCC), ordered by the Emergency Situations Ministry. Sistema owns 100% of RTI Systems.

Operational & Financial Results

RTI Systems delivered impressive growth in revenue and OIBDA during 2008. Sales increased by 26% to US$471.5 million in 2008, compared to US$375.0 million in 2007. OIBDA grew by 20% to US$55.1 million in 2008, compared to US$45.9 million in 2007. The contract portfolio of RTI Systems was worth US$5.1 billion as of December 31, 2008.

Defense contracts from the Russian state continued to account for a significant share of RTI Systems' revenues. According to the Center for Analysis of Strategy and Technology, it ranked 11th nationwide among defense-sector companies in terms of total revenues, and 10th in terms of sales of military and dual-use technology. In terms of revenue per employee, the Concern ranked among the top five companies and among the top ten in terms of net profitability.

In 2008, as part of a contract with the Russian Ministry of Defense, RTI Systems fulfilled a systems project for the development of information equipment and prepared proposals for the draft State Armaments Program for the period of 2011-2020. Also in 2008, RTI Systems signed a contract valid through 2011 to produce equipment for the Factory Assembled Ready (FAR) for Set-Up Radar Voronezh-M.

In April 2008, RTI Systems handed over the NESCC to the Emergency Situations Ministry for trial operations. Visiting the center, then-President Vladimir Putin noted that the center was virtually unmatched anywhere in the world in terms of technological capabilities.

In 2008, RTI Systems acquired 74.9% of the shares of Austrian company Watt Drive. The deal allowed the Concern, working jointly with UralElectro, to carry out the development and manufacture of high-technology electric engines and actuators for both the Russian and export markets.

Also during the year, a cooperation agreement was signed between RTI Systems and the A.F. Mozhaiskiy Military Space Academy to develop new technology to fulfill state contracts through the mutually beneficial sharing of scientific and technical work and human resources.

On the order of the Russian Ministry of Industry and Trade, the Concern's specialists took part in the preparation of a number of documents regarding the future development of arms and military technology for the Russian Armed Forces for the period of 2020-2025. These included surveys identifying both scientific breakthroughs and critical technologies that must be developed for the future needs of the military.

Also during 2008, RTI Systems carried out preliminary planning work on the project 'Aeropost Zonal Security and Communications,' one of the pilot projects being developed as part of the Agreement for the Development of the Strategic Partnership of the Russian State Corporation for Atomic Energy (Rosatom) and Sistema, which was signed in May 2008.

New products delivered in 2008 included the Voronezh-DM FAR for Set-Up Radar, which entered into trial duty. State testing was completed on the Voronezh-M radar in Lekhtusi. Preliminary testing was completed of the updated Daryal radar. Assembly of the Podslnukh radar was completed.

Strategy & Outlook

The strategic goal for RTI Systems in 2009 is to concentrate resources on key state contracts while simultaneously increasing the efficiency of R&D and production work. The Concern sees opportunities for increasing the volume of state defense contracts, especially considering existing plans to reduce the size of the armed forces and shift the functions of operating and maintenance of the radio-technology equipment used in missile-defense facilities to outside contractors.

The Concern will participate in additional tenders being carried out for key Federal Target Programs (FTPs) including the FTP ”Reducing Risks and Mitigating the Consequences of Emergencies,” which is linked to the expansion of the network of NESCC for the Russian Emergency Situations Ministry. It will also seek to participate in a number of FTPs for the first time, such as the program 'Development of Systems for State Management in Risk Minimization of Emergency and Catastrophic Situations.'

RTI Systems is also seeking to develop its emerging geoinformatics and radio-navigation segment, and to participate in developing and exploiting technology for the GLONASS satellite navigation system.

The Concern intends to integrate and develop its capabilities in the mechanotronics segment through Watt Drive and UralElectro by launching Watt Drive products in Russia and exploring the export potential for the products of UralElectro.

Over the longer term, the development strategy of RTI Systems is based on the focused development of its own innovative technologies, as well as its ability to make use of both Russian and international experience to provide the Concern with a competitive advantage in the global marketplace.

The Concern is focused on the further integration of the radio engineering and aerospace communications and control systems divisions in order to achieve qualitative growth, and is focused on the intensive development of its own R&D potential to create new products to meet the needs of the Russian and international marketplaces.

In the mechanotronics segment, RTI Systems will seek to occupy a leading position in the marketplace as a systems integrator, offering efficient engineering solutions based on its own unique breakthroughs and integrated systems solutions.

In the geoinformatics and radio navigation segment, which was launched in 2008, the Concern's aim is to become the largest player in the marketplace for products and services, based on its partnership with the Russian state.

Pharmaceuticals

Marketplace

The total Russian pharmaceutical market was worth around RUB 450 billion (around US$18.1 billion[30]) in 2008, according to preliminary data from DSM Group, representing year-on-year growth of 27%. Excluding para-pharmaceutical products, the market for medicines was estimated at approximately RUB 350 billion (around US$14.1 billion), up 26% year-on-year in ruble terms. Volume consumption growth increased by 12%, according to DSM, the first increase in volume sales in two years. At the same time, pharmaceutical prices grew by 12%, compared to a 3.6% increase recorded in 2008. During the year, the average medicine package price increased by 10% to RUB 57 (US$2.30) and per capita expenditure on medicines reached RUB 1,670 (US$67.17).

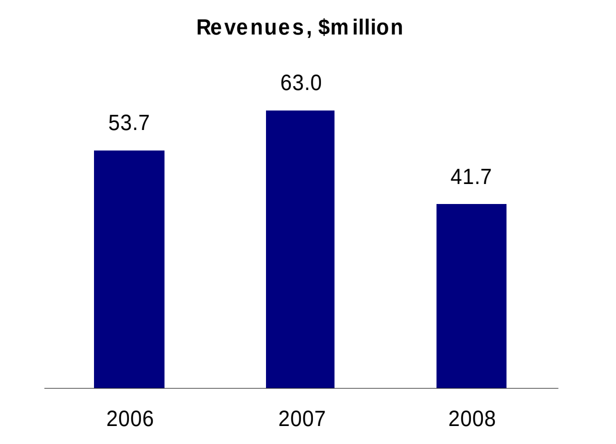
The retail market and out-of-pocket spending by consumers continue to be the primary driver of the Russian pharmaceutical market. Since the late 1990s, pharmaceutical chains have begun to replace traditional pharmacies as the primary sales point for medicines, as well as medicines dispensed as part of the Supplementary Medicines Provision (known as the 'DLO' in Russian) program. In 2008, the largest pharmaceutical chains, which have expanded in regional markets in recent years, ceased increasing store numbers and focused on enhancing the profitability of existing stores. Commercial sales of medicines grew by 24% in ruble terms during the year to RUB 235 billion (US$9.5 billion)

The Russian pharmaceutical market has grown by around 120% in value terms since 2005, according to market-research group Pharmexpert, while volume growth has actually fallen over the same period, by 2.7%. In part this is due to the replacement of older and less effective medicines by newer original and generic treatments. It is also the result of the dominance of the market (in value terms) by foreign manufacturers, which account for up to 80% of sales in the overall market and around 90% of the DLO market. Domestic manufacturers account for a far larger share of the market in volume terms, given the significant price difference between Russian and foreign medicines.

The Russian government has committed to increasing healthcare spending and medicines provision and has announced its intention to launch a new, universal mandatory medicines insurance program as early as 2010. It has pledged to increase the market share of Russian manufacturers, in particular such critical areas as vaccines and hormones. In the short term, the Russian pharmaceutical market may decline in 2009 in US dollar terms, due to the fall in the value of the ruble, which will hurt importers while also increasing the cost of imported active pharmaceutical ingredients (APIs). But higher public spending, increased health awareness and long-term increases in personal income should drive long-term growth in the marketplace.

Binnopharm

[30] Based on the CBR's average ruble/US dollar exchange rate of RUB 24.86/US$1 [verify x-rate used by company]



Company in Brief

Binnopharm was founded in 2006 aimed at becoming one of Russia's leading biotechnology companies. Binnopharm is responsible for the development and production of extemporaneous medicines with priority in Rx medicines for the hospital sector.

The group is developing genetically engineered treatments in bottles and syringe tubes for the treatment of illnesses which have a significant social impact, including cancers, liver disease, viral infections, neurodegenerative diseases and others. Binnopharm has already launched industrial production of a full-cycle vaccine against the hepatitis B virus and the Company's research and development team are working to create new and innovative treatments.

In 2009, the Company plans to open Russia's largest Good Manufacturing Practice (GMP) compliant pharmaceutical manufacturing facility in Zelenograd, Russia's 'silicon valley'. The new factory will produce medicines in tablet, capsule, aerosol and ampoule form. Binnopharm intends to move the overall production facilities to GMP with increase of production capacity afterward.

Binnopharm is 100% owned by Sistema.

Operational & Financial Results

Binnopharm's revenues amounted to US$41.7 million in 2008, compared to US$63.0 million in 2007. The Company had a negative OIBDA margin. The year's financial results reflect investments made in developing new medicines products and the closure of production facilities in order to build capacity for reconstruction and the development of future production.

During 2008, the Company registered an additional 14 finished pharmaceutical products and substances. At year end, an additional 39 medicines and substances were in the process of registration and six were in the final stage of development, including genetically engineered products. Also during the year, a new CEO and management team was put into place to lead the Company in the next phase of its development.

The company began the development of several large strategic projects within the framework of state-sector/private-sector partnerships. It worked to expand its R&D base by attracting talented scientific personnel while cooperating with educational and research institutions in order to lead the consolidation of the Russian pharmaceutical biotechnology sector. Also during 2008, the Company began the registration of a Russian-made vaccine for hepatitis B in five African countries including Nigeria, as well as Russia and Tajikistan.

Binnopharm continues to build on its competitive advantages and position itself for future growth. It pretends to be the only company in Russia to carry out the industrial production of biotechnological, genetically engineered, full-cycle medicines, which generally enjoy higher margins compared to other types of medicines. It has concentrated on the production of ampoules, which are a cost-effective medicines form sought by hospitals.

Today, the Company possesses fully equipped laboratory for the quality control of biotechnology medicines. Its team of scientists and biotechnology experts provides the R&D capacity to develop new biotechnology medicines; its R&D and production base are well placed to develop new markets for the prevention and treatment of viral illnesses.

Strategy & Outlook

In 2009, Binnopharm will complete the construction of a production and logistics center in Zelenograd which pretends to be the largest GMP-compliant production facility in Russia. The factory will have one of the largest GMP-compliant ampoule productions capacity in Russia and almost the only such production of 10ml ampoules. One of the first products to be made on an industrial scale at the new facility will be aerosol preparations for the treatment of respiratory illnesses. It will be made using a production line for aerosols and sprays using a technology which protects the ozone layer, a unique technology for the Russian market.

Binnopharm's strategy is based on developing and registering generic equivalents for medicines as they come of patent as well as biotechnology medicines, specifically biogenerics and their substances. In particular it will develop the import-substitution market by producing biogenerics and substances in therapeutic areas dominated by foreign analogues. It will develop new formulations and new combinations for medicines.

The Company's strategy is based on continually expanding the range of its own products, and those of its strategic partners, that it produces and markets, including medicines targeted at the hospital market, vaccines, anti-bacterial treatments, treatments of respiratory illnesses and more. At the same time, it will reduce or eliminate the distribution of lower-value medicines.

With the opening of a new R&D center, Binnopharm will leverage the R&D capacity being carried out by the scientists and technicians of Company as well as in partnership with scientific research and production organizations in the biotechnology sphere.

The primary product strategy of Binnopharm in economic uncertainty is to focus on the hospital market for injection preparations and to launch the maximum number of biotechnology products, specifically biogenerics, primarily aimed at the hospital market. The Company will extend its activities with a focus on the development of branded generics in order to achieve leading positions in target therapeutic classes in the retail and hospital sectors of the pharmaceutical market. .

13. Petrochemicals

Marketplace

On the global scale petroleum products remain an irreplaceable source of energy and the consumption of petroleum products is growing in a stable manner. Recent falls in the price of oil are unprecedented and over the long term, virtually all independent analysts expect long- term price growth. Extreme volatility in oil prices in 2008 reflected a complex combination of factors, including disruption to supplies and current and potential conflicts in several key oil producing regions globally and the global financial crisis.

The price per barrel of Brent crude rose above US$100 briefly in January 2008 and returned to that level later in February. Oil prices rose to over US$145 in July, before peaking at US$147.27. Declining demand in the US linked to high gasoline prices and economic uncertainty helped push down the price in the late summer, with the price falling below US$100 in mid-September. The oil price hit US$33.87 in late December.

Volatility in the oil price – as with other commodities in the present economic environment -- is expected in the short term, but the price is expected to rise over the longer term as global consumption increases by as much as 35%-40% by 2035, driven by demand from large developing economies such as India and China, while Russia's domestic demand for petroleum products has grown significantly since the beginning of the decade.

Russia is the world's second largest oil producer, after Saudi Arabia, and produces around 9.8 million barrels today, around 7.0 million of which is exported[31]. The sector saw strong increases in production growth, especially after world oil prices began to rise substantially in 2002 and Russia accounted for around 80% of growth outside of OPEC between 2002 and 2006.[32] However, production increases were more muted in 2007 and 2008, due in part to capacity constraints.

Russia has 40 oil refineries whose capacities fit well with domestic demand, which is focused mainly towards low-octane fuel. However, demand growth for high-octane fuel and tougher regulatory requirements is driving the modernization process at most oil refineries. Russia currently exports around 70% of its crude-oil production and refines around 30%.[33] Throughput of refining grew by 4% in 2007.[34] In the retail gasoline sector, the market remains fragmented among regional lines, with the single largest market share among large companies amounting to 20%.

Bashkir Oil & Energy Group

Company in Brief

In 2005, Sistema acquired minority shareholdings in six crude oil processing and oil extracting companies located in the Russian Republic of Bashkortostan that form the Bashkir Oil & Energy Group. At the end of March 2009, Sistema announced that it was increasing its ownership in the group and its companies to controlling stakes. The Group covers the full petroleum cycle, from production through refining to retail sales. The Group consists of oil-production company Bashneft, refining companies Ufaneftekhim, Novoil, Ufaorgsintez and Ufimsky Refinery and petroleum retail company Bashkirneftprodukt, as well a chain of 317 gasoline service stations in the Republic of Bashkortostan. The Group is one of Russia's Top-10 oil producers and Top-5 oil

[31] Source: Oil & Gas Journal 2008 Survey
[32] Source: Citibank
[33] Source: Oil & Gas Journal 2008 Survey
[34] Source: Energy Intelligence

refiners. It has the fourth largest reserves among Russian oil companies. Along with sales in Russia, the Group exports its products to Ukraine, Poland, Czech Republic, Germany, Slovakia and Hungary. It has 20,000 employees.

Operational & Financial Results

The Group produced 11.7 million tons of oil 2008, compared to 11.6 million tons in 2007. Proven reserves stood at 310 million tons at the beginning of 2008. It refined 21 million tons of petroleum in 2008 out of a total capacity of 32 million tons, representing nearly 66% capacity utilization.

During 2008, Sistema, as a strategic investor, continued to work with the Group to develop a transparent, vertically integrated holding with the goal of maximizing the shareholder value of each company as well as the overall Group. Return on capital invested at the Group was 18% in 2008.

In late March 2009, after the accounting period, Sistema acquired additional shares in the six companies which make up the Group for US$2.5 billion, consisting of an initial US$2.0 billion payment at the closure of the deal and US$500 million to be paid in 14 months. The acquisitions provide Sistema with majority control of the Bashkir Oil & Energy Group.

The deal also gives Sistema control over the Group's subsidiary businesses, such as Bashkirenergo, (50.17% of the ordinary shares are owned by the Group), a major power utility in the Republic of Bashkortostan and the wider Urals Region which produces 2.6% of Russia's electricity energy and 2.3% of its heating energy. In addition, the Group controls a number of transport, power, telecommunications and hotel businesses.

Company	***% shares acquired***	***Total % shareholding post transaction***
Bashneft	55.04%	76.52%
Ufaneftekhim	42.24%	65.78%
Novoil	60.26%	87.23%
Ufaorgsintez	50.23%	73.02%
Ufimsky Refinery	53.68%	78.49%
Bashkirnefteprodukt	47.89%	73.33%

Following the deal, Sistema will be making a mandatory offer to remaining shareholders. Financing for the offer was provided via a seven year, US$2 billion credit provided by VTB Bank. The acquired shares and 17% of the shares of MTS guarantee the loan. Other borrowed funds for the future payment and potential acquisitions of additional shares from minority shareholders may amount to US$1 billion.

For Sistema and its shareholders, the deal represents a means for creating additional shareholder value for the Corporation through increased asset values and dividend flows. Control of the Group has been acquired for its long-term development and Sistema's management believes that there is significant potential for growth in the value of the assets through the creation of a vertically integrated oil company. The assets provide important diversification for the Corporation, reduce risks and provide a unique opportunity to gain exposure to an industry with demonstrated long-term growth potential.

Strategy & Objectives

The Group's strategy following Sistema's acquisition of majority control is based on creating the most efficient and technologically advanced vertically integrated company in the Russian oil industry with a focus on refining and petrochemicals. A concrete strategic plan has been developed to increase transparency and efficiency across the Group.

On the Group level, new policies are being established for investment and financing and monetary flows are being made more optimal. Information disclosure levels will be brought up to the level of other Sistema subsidiaries and decision-making will be made more publicly, in the interests of all stakeholders. Within the Group, a single communications platform will be put in place to link the companies along with a single IT network and policy. A new organizational structure will be introduced along with new financial and management reporting procedures and systems.

In oil production, the strategy is to increase the efficiency and reduce costs. The Group will seek to develop new deposits to increase proven and potential reserves. In refining, it is seeking an optimal balance between volume of crude oil produced by the Group and crude oil provided by other producers, while making most efficient use of refining capacity. It is seeking to increase the depth of refining and develop new product, while also developing its petrochemicals production. The strategy also entails finding the right balance between sales through partners and through its own retail network. It is also studying the potential for its exports of finished petroleum products. In its retail network, the Group will move to a single brand for all of its gasoline stations. It will look to develop new channels for both sales and purchasing

PART 3 MANAGEMENT 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, 2008 and 2007, 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, 2008 and 2007, 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 with a combined customer base of over 100 million customers 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 seven segments: Telecommunications; Technology; Banking; Retail; Real Estate; Mass Media; Corporate and Other Businesses category comprises our 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 $16,670.8 million for the year ended December 31, 2008 and $13,410.7 million for the year ended December 31, 2007. Net income for the year ended December 31, 2008 amounted to $62.0 million as compared to $1,571.9 million in the year ended December 31, 2007. Our total assets have grown to $29,158.8 million as of December 31, 2008, as compared to $28,396.7 million as of December 31, 2007.

Our revenues and total assets have increased through organic growth during year ended December 31, 2008. The Telecommunications segment's share of our total revenues from sales to external customers decreased, from 72.0% in the year ended December 31, 2007 to 71.2% in the year ended December 31, 2008.

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 2008 and 2007 were $4,270.9 million and $3,062.5 million, respectively. In addition, in the years ended December 31, 2008 and 2007 we paid $1,940.7 million and $1,459.1, respectively, for purchases of businesses. We have financed our cash requirements through our operating cash flows and borrowings. Net cash provided by operating activities in 2008 and 2007 was $3,825.8 million and $2,723.1 million, respectively. The proceeds from long-term borrowings, net of debt issuance costs, for the years ended December 31, 2008 and 2007 amounted to $4,353.5 million and $2,448.5 million, respectively. As of December 31, 2008, we had indebtedness of $10,661.7 million, including capital lease obligations, and our interest expense for 2008 was $554.9 million, net of amounts capitalized.

We continue 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, CIS markets and other countries. 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.

In some of our segments such as Telecommunications, Technology and Retail we developed our international expansion. Though we still consider our natural prime markets to be Russia and CIS countries, in order to support our positions in such a highly competitive market we strive to become global players, which requires international expansion to achieve scale and to provide access to new clients and technologies. Additionally, following our strategy to concentrate on businesses with a high technology component, we accelerated our development in business lines requiring significant know-how. A number of strategic alliances were put in place which should provide us access to cutting edge global technologies.

In the year ended December 31, 2008, we have reiterated our positioning as a diversified business focused on the consumer sector. With ongoing growth across our portfolio, we remain committed to investing in market-leading businesses in the service sector, where growth continues to be driven by the improving macro picture resulting in increasing spending power of our customers. We believe that through our geographical and sectoral diversification we are best positioned to capture this growth. Our fundamental goal remains unchanged - we plan to continue to invest in profitable growth in the areas of our expertise, and grow both organically and through mergers and acquisitions, as well as ensure the most efficient use of our available resources.

The following table illustrates our ownership interests in our principal consolidated subsidiaries and affiliates as of December 31, 2008.

Segment	Company	Beneficial ownership(1)	Voting interest(2)
Telecommunications	MTS	56%(1)	56%
	Comstar UTS(3)	59%	59%
	Sistema Shyam TeleServices Limited	74%	74%
Technology	SITRONICS	70%	70%
Banking	MBRD	100%	100%
	Dalcombank	100%	100%
	EWUB	99%	100%
Real Estate	Sistema-Hals	80%(1)	80%(1)
Retail	DM-Center	100%	100%
	Detsky Mir	95%(1)	95%
Mass Media	Sistema Mass Media	100%	100%
Other Businesses			
Travel Services	Intourist	66%	66%
International Operations	Sistema International	100%	100%
Radio and Space Technology	Concern RTI	97%	97%
Pharmaceuticals and Biotechnology	Binnofarm	100%	100%
Medical services	Medsi	100%	100%

(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: MBRD (25.7%).

(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) Comstar UTS holds our 25.0%+1 share of Svyazinvest.

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. Below is a summary of several key macroeconomic factors that may have a substantial impact on our business:

	Years ended December 31,	
	2007	2008
GDP growth	8.1%	5.6%
Consumer price index	11.9%	13.3%
Unemployment rate	6.1%	7.7%
Nominal exchange rate (rubles per U.S. dollar) (1)	25.58	24.98
Real ruble appreciation against U.S. dollar(2)	15.0%	(5.3)%

Sources: Central Bank of Russia, Rosstat, 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.

A significant portion of our expenditures and liabilities, including capital expenditures and borrowings (including our U.S. dollar denominated notes), are either denominated in, or closely linked to, the U.S. dollar and/or euro, while substantially all of our revenues are denominated in local currencies of the countries where we operate. As a result, the devaluation of local currencies against the U.S. dollar and/or euro can adversely affect our revenues reported in U.S. dollars and increase our costs in terms of local currencies. If local currencies decline against the U.S. dollar and/or euro and price increases cannot keep pace, we could have difficulty repaying or refinancing our U.S. dollar and/or euro-denominated indebtedness, including our U.S. dollar denominated notes. In addition, local regulatory restrictions on the sale of hard currency in Turkmenistan and Uzbekistan may delay our ability to purchase equipment and services necessary for network expansion which, in turn, may cause difficulty in expanding our subscriber base in those countries. Further, a portion of our cash balances is held in jurisdictions outside Russia, and as a result of exchange controls in those jurisdictions, these cash balances may not always be readily available for our use.

Acquisitions and Divestitures

During the years 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 date of acquisition. Before January 1, 2008 we consolidated revenues and expenses of newly acquired entities from the beginning of the year in which we obtained a controlling interest. 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 the years ended December 31, 2007 and December 31, 2008.

Company	**Principal activity**	**Date of acquisition**	**Stake acquired**	**Acquiring entity**	**Purchase price[1] (in millions)**
Year ended December 31, 2008					
Sistema Shyam TeleServices	Mobile services provider	January –April 2008	63.7%	Sistema	449.3
CJSC Sahles	Holder Perm Motor Group	February 2008	18.0%	RTI	51.1
Kvazar-Micro Corporation B.V	IT company	March 2008	49%	Sitronics	174.8
Comstar UTS	Telecommunication provider	November 2008	6.8%	MGTS Finance S.A	463.6
MTS	Mobile services provider	January-December 2008	2.1%	MTS	1,059.8
Year ended December 31, 2007					
RTC	Telecommunications operator	December 2007	88.0%	Comstar UTS	$ 26.4
Bashcell	Mobile services provider	December 2007	100.0%	MTS	6.7
Digital Telephone Networks South	Telecommunications operator	November 2007	100.0%	Comstar UTS	167.2
Dalcombank	Banking	November 2007	98.7%	Sistema	130.1
K-Telecom	Mobile services provider	September 2007	80.0%	MTS	402.6
Shyam Telelink Ltd	Mobile services provider	September 2007	10.0%	Sistema	11.4
Uzdunrobita	Mobile services provider	June 2007	26.0%	MTS	250.0
Sitronics	Holding company of the Group's Technology segment	January 2007	3.1%	Sitronics	36.0
MBRD	Banking activities, securities transactions and foreign currency transactions	December 2007	49.0%	EWUB	57.6

[1] Excluding acquisition-related costs.

In June 2008, we increased our stake in Shyam Telelink from 72.0% to 73.7% as a result of a pro rata charter capital increase of Shyam Telelink in the total amount of $470.0 million with our contribution being $348 million, including $11.8 million paid for a stake acquired.

Divestitures

In February 2008, the Group acquired an additional 18.8% of CJSC Sahles from an unrelated party for $51.1 million in cash. As a result of this transaction, the Group's ownership has increased to 100%. In March 2008, the Group completed the sale of 100% in CJSC Sahles to CJSC Saturn, a subsidiary of OPK Oboronprom, for a total cash consideration of $190.0 million. The transaction resulted in a loss from disposal of $2.1 million.

Consolidated Financial Results Overview

The following table sets forth a summary of our financial results for the years ended December 31, 2008 and 2007. This financial information should be read in conjunction with our consolidated financial statements.

	Years ended December 31,			
	2007	% of revenues	2008	% of revenues
	(Amounts in thousands of USD, except percentages)			
Revenues	13,410,655	100.0	16,670,810	100.0
Costs of sales, exclusive of depreciation and amortization shown separately below	(5,945,794)	(44.3)	(6,999,984)	(42.0)
Selling, general and administrative expenses	(2,368,554)	(17.7)	(3,435,934)	(20.6)
Depreciation and amortization	(1,747,171)	(13.0)	(2,316,295)	(13.9)
Provision for doubtful accounts	(122,995)	(0.9)	(270,069)	(1.6)
Net other operating expenses	(231,613)	(1.7)	(269,341)	(1.6)
Equity in net income of investees	66,076	0.5	4,925	0.0
Loss from impairment	(20,719)	(0.2)	(240,780)	(2.2)
Gain on disposal of interests in subsidiaries and affiliates	155,069	1.1	29,960	0.2
Operating income [1]	3,194,942	23.9	3,173,292	19.0
Interest income	80,405	0.6	72,487	0.4
Change in fair value of derivative instruments	(145,800)	(1.1)	(47,559)	(0.3)
Interest expense, net of amounts capitalized	(409,826)	(3.0)	(554,912)	(3.3)
Currency exchange and translation gain	289,833	2.1	(894,539)	(5.4)
Income tax expense	(971,766)	(7.2)	(857,462)	(5.1)
Minority interests	(1,093,095)	(8.4)	(1,019,870)	(6.1)
Equity in net income of energy companies in the Republic of Bashkortostan	109,855	0.8	192,680	1.2
Income from continued operations	1,054,548	7.8	64,117	0.4
(Loss) from discontinued operations	(4,612)	0.0	(4,194)	0.0
Gain from disposal of discontinued operations	521,963	3.9	2,053	0.0
Net income	1,571,899	11.7	61,976	0.4
OIBDA [2]	4,942,113	36.9	5,489,587	32.9

(1) Operating income is calculated as revenues less operating costs, plus equity in net income of investees (excluding equity in net income of energy companies in the Republic of Bashkortostan) and gain on disposal of interests in subsidiaries and affiliates. 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 service 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 and business units for the years ended December 31, 2007 and 2008. 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. Intra-segment dividends are exluded from both revenues and operating income. Amounts attributable to individual companies, where appropriate, are shown prior to both intra-segment and inter-segment eliminations:

The principal activities of our significant entities are as follows:

Significant Entities	Principal Activity
JSFC Sistema	Investing and financing activities
Telecommunications Business Unit:	
MTS and subsidiaries	Wireless telecommunication services
Comstar UTS and subsidiaries	Fixed line telecommunication services, data transmission and internet services
Sistema Shyam TeleServices Limited	Wireless telecommunication services
Sistema Mass Media and subsidiaries	Cable television, advertising, production and distribution of periodicals, movie production
Consumer Assets:	
Moscow Bank for Reconstruction and Development and subsidiaries Dalcombank	Banking activities, securities transactions and foreign currency transactions
Detsky Mir and subsidiaries Detsky Mir-Center and subsidiaries	Retail and wholesale trading
Sistema-Hals and subsidiaries	Development and marketing of real estate projects
VAO Intourist and subsidiaries	Sale of tour packages in the RF and abroad, hotel business
Medsi and subsidiaries	Healthcare services
Technology & Industry Business Unit:	
Concern RTI Systems and subsidiaries	Manufacturing of radiotechnical equipment, research and development
SITRONICS and subsidiaries	Production and marketing of integrated circuits, wafers, electronic devices and consumer electronics, research and development, IT and systems integration, computer hardware and software distribution
Binnofarm and subsidiaries	Production and distribution of pharmaceuticals

Revenues by Business unit:

	Years ended December 31,			
	2007	% of revenues	2008	% of revenues
	(Amounts in thousands, except percentages)			
Telecommunications	$ 9,748,542	72.7	$ 12,081,513	72.4
Technology & Industry	2,082,796	15.5	2,532,448	15.2
Consumer Assets	1,844,466	13.7	2,596,507	15.5
Corporate and Other	61,031	0.4	60,973	0.4
Eliminations [(2)]	(326,180)	(2.3)	(600,631)	(3.5)
Total	$ 13,410,655	100.0	$ 16,670,810	100.0

(2) Eliminations of inter-segment revenue.

Revenues by segment:

	Years ended December 31,			
	2007	% of revenues	2008	% of revenues
	(Amounts in thousands, except percentages)			
Telecommunications[(1)]	$ 9,648,978	72.0	$ 11,877,453	71.2
Technology [(2)]	1,619,604	12.1	2,019,527	12.1
Banking	410,048	3.1	725,429	4.4
Real Estate	452,198	3.4	362,237	2.2
Retail	597,224	4.4	801,969	4.8
Mass Media	130,071	0.9	223,984	1.3
Other Businesses [(3)]	969,696	7.2	1,320,216	7.9
Aggregated Revenue	$ 14,118,119	103.1	$ 17,330,815	104.0
Eliminations [(4)]	(417,164)	(3.1)	(660,005)	(4.0)
Total	$ 13,410,655	100.0	$ 16,670,810	100.0

(1) Telecommunications does not include Mass Media
(2) Technology does not include radio and space technology and Binnopharm and subsidiaries but includes Videophone
(3) Other Businesses includes our travel services, radio and space technology, healthcare services, pharmaceuticals and biotechnology businesses together with our other operations and central corporate functions.
(4) Eliminations of inter-segment revenue.

Operating income by Business unit:

	Years ended December 31,			
	2007	% of operating income	2008	% of operating income
	(Amounts in thousands, except percentages)			
Telecommunications	$ 3,260,597	104.6	$ 3,564,994	105.4
Technology & Industry	(120,821)	(3.9)	96,320	2.8
Consumer Assets	141,549	4.5	(159,362)	(4.7)
Corporate and Other	(163,881)	(5.2)	(118,350)	(3.5)
Total	$ 3,117,444	100.0	$ 3,383,602	100.0

Operating income by segment:

	Years ended December 31,			
	2007	% of operating income	2008	% of operating income
	(Amounts in thousands, except percentages)			
Telecommunications[(1)]	$ 3,260,413	102.7	$ 3,577,145	112.7
Technology [(2)]	(158,918)	(4.9)	63,498	2.0
Banking	43,039	1.3	41,014	1.3
Real Estate	41,855	1.3	(151,715)	(4.8)
Retail	25,637	0.8	1,987	0.1
Mass Media	184	0.0	(5,784)	(0.2)
Other Businesses [(3)]	(97,036)	(3.1)	(54,698)	(1.5)
Aggregated operating income	$ 3,115,174	98.1	$ 3,471,447	107.4
Eliminations [(4)]	79,768	1.9	(298,155)	(7.4)
Total	$ 3,194,942	100.0	$ 3,173,292	100.0

(1) Telecommunications does not include Mass Media
(2) Technology does not include radio and space technology and Binnopharm and subsidiaries but includes Videophone
(3) Other Businesses includes our travel services, radio and space technology, healthcare services, pharmaceuticals and biotechnology businesses together with our other operations and central corporate functions.
(4) Eliminations of inter-segment revenue.

Year ended December 31, 2008 compared to year ended December 31, 2007

Revenues

Our consolidated revenues increased by 24.3% to $16,670,8 million for the year ended December 31, 2008 from $13,410.6 million for the year ended December 31, 2007.

The growth in our consolidated revenues was attributable to the growth in our Telecommunications Segment of $2,228.5 million, in our Technology Segment of $399.9 million, in our Banking Segment of $315.4 million, in our Retail Segment of $204.7 million, in our Mass Media Segment of $93.9 million and in our Other Businesses Segment of $350.5 million, partially offset by the decrease in our Real Estate Segment of $90.0 million.

The Telecommunications Segment continued to be the largest revenue contributor for the year ended December 31, 2008, and its share of the aggregated revenues from sales to external customers decreased to 71.2% for the year ended December 31, 2008 from 71.8% for the year ended December 31, 2007 owing to a growth and significant acquisitions in our other segments. Revenues of MTS and Comstar UTS grew to $10,245.2 million and $1,647.7 million, or by 24.2% and 11.2%, respectively, compared to the year ended December 31, 2007. This increase was primarily due to the significant growth in MTS' subscriber base from 82.0 million as of December 31, 2007 to 91.6 million as of December 31, 2008. The growth reflected the acquisition of DTN and RTC in the fourth quarter of 2007 and Interlink and UTC in 2008, growing 'Calling Party Pays' and long distance traffic volumes, as well as the development of the Group's broadband operations. The growth was partially offset by the 9% regulatory reduction in the price for the MGTS unlimited residential voice tariff plan from February 1, 2008; the regulator's cancellation of the compensation surcharge for long-distance calls from the beginning of 2008; and the regulatory change in the interconnect regime from March 1, 2008. The significant movement in the Russian ruble / US dollar exchange rate during the fourth quarter also adversely affected the Comstar UTS's reported results for the period.

The increase in revenues of our Technology Segment was attributable to the organic growth of the Microelectronic Solutions and IT Solutions divisions.

The Banking segment provides corporate and retail banking services in Russia and Luxembourg. The segments' revenues increased by 76.9 %, in the year ended December 31, 2008, as a result of the strong growth of the segment's retail and corporate lending portfolios. The loan portfolio, including leases, grew by 11.3 % to $4.9 billion as at December 31, 2008, whilst interest income received from retail and corporate lending increased by 57.4% year on year.

Our Real Estate Segment revenues decreased by $90.0 million as the financial crisis in the second half of 2008 made potential customers defer significant investments in real estate.

Revenues from our Mass Media Segment grew by $93.9 million, or 72.2%, for the year ended December 31, 2008, compared with the year ended December 31, 2007 due to acquisitions of new subsidiaries in the regions.

Revenues from our Retail Segment grew by 34.3%, or $204.7 million, for the year ended December 31, 2008, compared with the year ended December 31, 2007 primarily due to an increase in the number of stores.

Our radio and space technology business as well as travel services business were main contributors to the growth in Other Businesses with revenues of $471.4 million and $615.6 million for the year ended December 31, 2008, compared to $374.9 and $374.0 respectively for the prior year. The increase in revenues for the year ended December 31, 2008 was mainly attributable to organic growth.

Operating costs

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

For the year ended December 31, 2008, our gross margin increased to 58.0% from 55.7% for the year ended December 31, 2007.

Our selling, general and administrative expenses increased to 20.6% of revenues for the year ended December 31, 2008 as compared to 17.7% for the same period of 2007. Depreciation and amortization increased to 13.9% of revenues in the year ended December 31, 2008 from 13.0% in the year ended December 31, 2007 following the growth in the depreciable assets.

As of December 31, 2008, we recorded non-cash impairment losses totaling $113.5 million related to goodwill recorded in connection with acquisitions completed in 2007 and 2008. Of the total impairment losses, $63.6 million related to acquisition of Dalkombank and $49.9 million related to acquisition of UCN. As of December 31, 2008, the Group recorded a $75.0 million non-cash impairment loss with respect to MTT as of December 31, 2008 resulting from the decrease in fair value of the stake as indicated by the selling price of the stake in the transaction in March 2009. We also recognized a non-cash impairment charge relating to its investments in real estate developed for sale and income producing property in the amount of $ 37.2 million and $ 4.7 million, respectively.

Operating income

Operating income is revenues less operating costs, plus equity in net income of investees (excluding equity in net income of energy companies in the Republic of Bashkortostan) and gain on disposal of interests in subsidiaries and affiliates.

Our consolidated operating income margin comprised 19.0% for the year ended December 31, 2008, compared with 23.8% for the year ended December 31, 2007. MTS continued to be the main contributor to the operating margin with $3,203.5 million, or 94.0% of aggregated operating income, for the year ended December 31, 2008.

Change in fair value of derivative instruments

An expense of $47.5 million was recorded in the year ended December 31, 2008 due to an increase in fair value of the call and put option on Comstar UTS shares that we issued in connection with our acquisition of the 25.0%+1 share of Svyazinvest, put option has been exercised.

Interest expense, net of amounts capitalized

Our consolidated interest expense, net of amounts capitalized, for the year ended December 31, 2008 increased by 35.4% to $554.9 million from $409.8 million for the year ended December 31, 2007, primarily owing to the increase in our indebtedness by $2,312.0 million or 27.7% as of December 31, 2008 compared to December 31, 2007.

Currency exchange and translation gain

Currency exchange and translation loss for the year ended December 31, 2008 amounted to $894.5 million compared to a gain of $289.8 million for the year ended December 31, 2007, resulting primarily from depreciation of the Russian Rouble against the U.S. Dollar in 2008.

Equity in net income of energy companies in the Republic of Bashkortostan

Our share in the net income of affiliated energy companies in the Republic of Bashkortostan (including Bashneft, Novoil, Ufimsky NPZ, Ufaneftekhim, Ufaorgsintez, Bashnefteproduct) amounted to $192.7 million in the year ended December 31, 2008 compared to $109.9 million in the year ended December 31, 2007. The increase was due to oil price increases in 2008 in comparison with 2007.

Minority interests

Minority interests in net income of our subsidiaries decreased from $1,093.1 million for the year ended December 31, 2007 to $ 1,019.9 million for the year ended December 31, 2008 due to the decrease of profitability of our significant subsidiaries caused by foreign exchange losess.

Segment Financial Results Overview

The following analysis concentrates on our seven reporting segments: Telecommunications, Technology, Banking, Real Estate, Retail, Mass Media, and Other Businesses category. We include the discussion of our travel services, radio and space technology, pharmaceuticals and biotechnology businesses together with our other operations and central 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 three divisions: wireless services (MTS) and fixed line communications (Comstar UTS) and the Indian project.

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

	Years ended December 31,			
	2007	% of revenues	2008	% of revenues
	(Amounts in thousands, except percentages)			
Revenues	$ 9,648,978	100.0%	$ 11,877,453	100.0%
Costs of sales, exclusive of depreciation and amortization shown separately below	(3,230,904)	(33.5)	(3,503,863)	(29.5)
Selling, general and administrative expenses	(1,392,240)	(14.4)	(2,290,732)	(19.3)
Depreciation and amortization	(1,611,253)	(16.7)	(2,092,079)	(17.6)
Provision for doubtful accounts	(64,318)	(0.7)	(156,172)	(1.3)
Net gain on disposal of subsidiaries	3,216	0.0	-	0.0
Impairment loss	-	0.0	(76,333)	(0.6)
Net other operating expenses	(171,491)	(1.7)	(197,005)	(1.6)
Equity in net income of investees	78,425	0.8	15,876	0.1
Operating income	$ 3,260,413	33.8	$ 3,577,145	30.1
OIBDA [1]	$ 4,871,666	50.5	$ 5,669,224	47.7

(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 service 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, 2008 compared to year ended December 31, 2007

Revenues

Telecommunications Segment revenues increased by 23.1% to $11,877.5 million for the year ended December 31, 2008 compared to $9,649.0 million for the year ended December 31, 2007. MTS and Comstar UTS contributed $10,245.2 million and $1,647.6 million, respectively, to the growth in segment revenues.

Wireless services

Revenues of MTS for the year ended December 31, 2008 were $10,245.2 million, an increase of 15.1% compared to $8,252.4 million for the year ended December 31, 2007. This increase was primarily attributable to the growth in MTS' subscriber base from 82.0 million as of December 31, 2007 to 91.3 million as of December 31, 2008, including 64.6 million in Russia, 18.12 million in Ukraine, 5.64 million in Uzbekistan, 0.93 million in Turkmenistan and 2.0 million in Armenia. The growth was attributable to MTS' acquisitions, sales and marketing efforts and the expansion of its network. As a result of MTS marketing initiatives average monthly service revenue per subscriber in Russia increased by 33.3 % from $9 per subscriber for the year ended December 31, 2007 to $12 per subscriber for the year ended December 31, 2008.

For the year ended December 31, 2008, MTS' service revenues and connection fees increased by $2,003.7 million, or by 24.5 %, to $ 10,176.3 million from $8,172.6 million for the year ended December 31, 2007 due to growth in the number of its subscribers, as explained above. Revenues from sales of handsets and accessories decreased by $10.7 million, or 13.4 %, for the year ended December 31, 2008, compared to the year ended December 31, 2007, due to a decrease in the number of sold handsets.

Fixed line communications

Comstar UTS's revenues increased by $166.1million, or by 11.2 %, to $1,647.6 million for the year ended December 31, 2008 from $1,481.5 for the year ended December 31, 2007 mostly as a result of acquisitions made in the end of 2007 and beginning of 2008.

MGTS' revenues grew by 2.1 % in the year ended December 31, 2008 to $ 1,135.8 million, compared to $1,112.5 million for the year ended December 31, 2007. Revenues from residential subscribers decreased by 3.3% in the year ended December 31, 2008, compared to the year ended December 31, 2007, and decreased to $514.2 million.

Operating income

The operating income margin of the Telecommunications Segment was 30.1% in the year ended December 31, 2008, compared to 33.8% in the year ended December 31, 2007. The decrease in the operating income margin was primarily due to an increase in depreciation and amortization expenses as well as a decrease of profitability of our equity investments.

MTS' operating income margin was 31.3 % for the year ended December 31, 2008, compared to 33.1% for the year ended December 31, 2007.

Comstar UTS' operating income margin for the year ended December 31, 2008 did not change significantly and was 30.0 %, compared to 30.8 % for the year ended December 31, 2007.

Equity in net income of investees

Equity in net income of investees accounted to $15.9 million and $78.4 million for the years ended December 31, 2008 and December 31, 2007, respectively. The decrease in equity in net income of investees is primarily caused by the significant increase in net loss of Sky-Link amounted to $60.0 million for the year ended December 31, 2008, compared to $29.0 million for the year ended December 31, 2007. Equity in net income of MTT decreased by $34.2 million for the year ended December 31, 2008.

Technology

As of December 31, 2008, our subsidiaries in the Technology Segment operated along four main divisions: Telecommunication Solutions (SITRONICS Telecom Solutions and Intracom Telecom), IT Solutions (Kvazar-Micro), Microelectronic Solutions (Mikron, VZPP-Mikron, NIITM), Consumer Services and Products (Sitronics, Kvant, Elion, Elaks, Koncel).

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

	Years ended December 31,					
		2007	% of revenues		2008	% of revenues
	(Amounts in thousands, except percentages)					
Revenues	$	1,619,604	100.0%	$	2,019,527	100.0 %
Costs of sales, exclusive of depreciation and amortization shown separately below		(1,381,922)	(85.3)		(1,600,142)	(79.2)
Selling, general and administrative expenses		(259,544)	(16.0)		(263,718)	(13.0)
Depreciation and amortization		(56,453)	(3.5)		(73,845)	(3.6)
Provision for doubtful accounts		54,859	(3.4)		(4,263)	(0.2)
Net gain on disposal of subsidiaries		4,625	0.3		6,244	0.3
Net other operating expenses		(30,303)	(1.9)		(20,302)	(1.0)
Equity in net income of investees		(66)	(0.0)		(3)	(0.0)
Operating income/(loss)	$	(158,918)	-	$	63,498	3.1
OIBDA [1]	$	(102,465)	-	$	137,343	6.8

(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 service 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, 2008 compared to year ended December 31, 2007

Revenues

The revenues of our Technology Segment increased by $399,9 million, or by 24.7 %, to $2,019.5 million for the year ended December 31, 2008.

Operating income

Our Technology Segment has operating income of $63.5 million for the year ended December 31, 2008 compared to an operating loss of $158.9 million in the year ended December 31, 2007. Operating expenses net of depreciation were down 17.1% year on year to $282.0 million for the full year following the cost saving measures implemented during 2008. Selling, general and administration expenses, net of stock option expenses and bad debt provisions, represented 13.0% of revenues for the full year, compared to 16.0% for the respective period of 2007.

Banking

Our Banking Segment is represented by MBRD, East West United Bank and Dalcombank. In the year 2008 MBRD's business included 101 points of sales, including 31 outlet in Moscow and 70 outlets in thirty regions of Russian Federation. The Dalcombank business included 79 points of sales in six Russian regions in 2008.

Devaluation of the Russian ruble against US dollar, the decrease in value of financial instruments and the decline in borrowers' ability to meet payments' schedules caused worse financial results of the Banking Segment compared to the results of the year 2007. In order to minimize the adverse effect of the financial and economic crisis the Banking Segment focused on the liquidity of transactions and improvement of the credit risk and arrears management in its operating activity.

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

	Year ended December 31,					
		2007	% of revenues		2008	% of revenues
	(Amounts in thousands, except percentages)					
Revenues from financial services	$	410,048	100%	$	725,429	100
Including:						
Revenues from consolidated companies		15,882	3.9		34,518	4,8
Revenues from related parties		5,855	1.4		23,971	3,3
Financial services related costs, exclusive of depreciation and amortization shown separately below[1]		(235,035)	(57.3)		(456,501)	(62,9)
Selling, general and administrative expenses		(123,306)	(30.1)		(217,202)	(29,9)
Depreciation and amortization		(8,668)	(2.1)		(14,828)	(2,0)
Other operating income (purchase price allocation)		-	-		4,116	0,6
Operating income	$	43,039	10.5%	$	41,014	5,7%

(1) Includes interest expense on deposits.

Year ended December 31, 2008 compared to the year ended December 31, 2006

Revenues

For the year ended December 31, 2008, compared with the year ended December 31, 2007, the segments' revenues increased by 76.9 %, to $725.4 million. Interest income grew by 57.4% in the year ended December 31, 2008 and amounted to $655.2 million. As of December 31, 2008, loans to customers increased by 22.9 % compared with December 31, 2007 to $3,981.4 million, including $379.1 million, or 9.52 %, of inter-company loans and $219.3 million, or 5.51 %, of loans to our related parties. As of December 31, 2008, the weighted average interest on MBRD's inter-company loans was 14.0% for ruble-denominated loans and 9.7% on non-ruble-denominated loans. The weighted average interest rate on ruble-denominated loans to related parties was 12.1% and 11.3% for non-ruble-denominated loans. Loans to third-party customers increased by $766.0 million to $3,383.0 million as of December 31, 2008 as compared to $2,617 million as of December 31, 2007. The weighted average interest rate on loans to third-party customers was 16.8% for ruble-denominated loans and 9.2% for non-ruble-denominated loans as of December 31, 2008.

MBRD's non-interest income decreased to $74.0 million in the year ended December 31, 2008 from $78.6 million in the year ended December 31, 2007 primarily due to a decline in gains on operations with securities and financial instruments.

Operating income

The Banking Segment's operating income decreased by 4.7 % and amounted to $41.0 million in the year ended December 31, 2008, compared to $43.0 million for the year ended December 31, 2007. The decrease in operating income is explained by a decline in net interest income caused by the decrease in interest margin at the end of the year 2008 and an increase in provisions for impairment on loans and other assets.

Total assets

Total assets of the Banking Segment increased to $6,227.5 million as of December 31, 2008 from $5,624.6 million as of December 31, 2007 primarily owing to the increase in loans issued to customers and loans and advances to banks.

In the year 2008 MBRD issued two tranches of bonds denominated in Russian ruble amounting to $102.1 million each, maturing in March and April of the year 2013 respectively. In March 2008 MBRD repaid $150.0 million of Eurobonds.

Real Estate

In our Real Estate Segment, represented by Sistema-Hals, 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 40 projects totaling over 340,000 sq.m. of space.

	Years ended December 31,			
	2007	% of revenues	2008	% of revenues
	(Amounts in thousands, except percentages)			
Revenues	$ 452,198	100.0%	$ 362,237	100.0 %
Cost of sales, exclusive of depreciation and amortization shown separately below	(223,676)	(49.5)	(256,468)	(70.8)
Selling, general and administrative expenses	(161,604)	(35.7)	(88,706)	(24.5)
Depreciation and amortization	(14,872)	(3.3)	(24,313)	(6.4)
Provision for doubtful accounts			(42,916)	(11.8)
Impairment of construction projects	-	-	(76,504)	(21.1)
Equity in net income of investees			(11,446)	(3.2)
Net gain on disposal of subsidiaries			(3,398)	(0.1)
Net other operating income/(expenses)	(10,191)	(2.3)	(10,201)	(2.8)
Operating income	$ 41,855	9.3%	$ (151,715)	-

Year ended December 31, 2008 compared to year ended December 31, 2007

Revenues

The Real Estate segment, represented by Sistema Hals, reported almost 19.9% revenue decrease year on year to $362.2 million in 2008. The real estate development division contributed most to the decrease of the segment and accounted for 75.8 % of total segment's revenues compared to 84.0% in 2007. The volume of sales of the division amounted to $274.3 million in 2008 compared to $356.0 million in 2007.

In 2007 two strategic deals - the sale of the Company's 50% share in the Sochi based project "Kamelia" to Saraya and the sale of the Company's 50% share in the St. Petersburg based project "Leto" to Apsys in December 2007 - contributed approximately $146.4 million to the revenue while in 2008 no such significant transactions took place. The decrease was partially offset by continuing sales of units in the ongoing "Dnepropetrovskaya", "Nahimovskiy", "Michurinskiy" and "Rublevskoe highway" residential projects. "Dnepropetrovskaya" and "Nahimovskiy" residential projects were completed by the year end.

Sistema Hals's asset management division revenues increased by $9.7 million compared to 2007 or by 21.7% year on year to $ 54.4 million in 2008 primarily as a result of an increase in house sales and rental revenues from single family houses.

The Facility Management division reported year-on-year revenue growth of 45.2 % to $33.1 million for the full year of 2008. The growth was primarily due to an increase in revenues from services provided to our subsidiaries.

During 2008 the segment disposed of its Project and construction management division which contributed approximately $28.6 million to revenues in 2007.

Operating income

Operating income of the Real Estate Segment for the year ended December 31, 2008 decreased to a loss of $151.7 million from an income of $41.9 million in the year ended December 31, 2007. The decrease in selling, general and administrative expenses was largely due to stock-based compensation in the amount of $99.8 million accounted for in 2007. Impairment of construction projects was caused by recognition of a loss from a contract with Siemens for a total amount of $25.4 million, and impairment provisions for the excess of fair value of certain construction projects over their book value for $51.1 million. Provision for bad debts for $42.9 million also contributed to the decrease of operating income.

Total assets

Total assets of the Real Estate Segment increased from $1,770.0 million as of December 31, 2007 to $1,984.5 million as of December 31, 2008, or by 12%. This growth is primarily due to an increase of a number of construction projects in the segment's portfolio.

Retail

We operate our retail business through Detsky Mir, the largest retailer of children's goods in Russia and the CIS. Detsky Mir, through its subsidiary, S-Toys, is also the leading Russian children's goods importer and exclusive distributor of world-class children's brands.

Through the year Detsky Mir had been implementing its strategy approved in December 2006. The strategy is to continue opening new retail outlets in Moscow and other large cities of Russia and the CIS taking advantage of limited competition in the sector of large format nationwide children's goods retail chains. Detsky Mir plans to continue offering a broad selection of children's toys, goods for babies, clothes and footwear, stationery and sporting goods targeted at middle-income consumers. In 2008 Detsky Mir launched a pilot project Children Gallery Yakimanka, a luxury store in the centre of Moscow.

As of December 31, 2008 Detsky Mir operated 130 stores in 67 cities of the Russian Federation and 2 cities in Ukraine adding 35 stores during the year. The company increased its retail space from 173.6 thousand sq.m. to 220.8 thousand sq.m.

	Years ended December 31,					
		2007	% of revenues		2008	% of revenues
	(Amounts in thousands, except percentages)					
Revenues	$	597,224	100.0%	$	801,969	100.0 %
Cost of sales, exclusive of depreciation and amortization shown separately below		(350,174)	(58.6)		(467,902)	(58,3)
Selling, general and administrative expenses		(199,670)	(33.4)		(318,178)	(39.7)
Depreciation and amortization		(10,494)	(1.8)		(14,805)	(1.8)
Net other operating income/(expenses)		(11,249)	(1.9)		903	0.1
Operating income	$	25,637	4.3%	$	1,987	0.2

Revenues

Our Retail segment increased its revenues by 34.3 % year on year to $802.0 million in 2008. The stores opened during the year contributed $83.5 million, or 10.4%, to the segment revenues in 2008. Wholesale operations accounted for $45.7 million, or 5.7% of the annual revenues.

Operating income

Operating income of the Retail Segment for the year ended December 31, 2008 decreased to $2.0 million, from $25.6 million in the year ended December 31, 2007. The decrease resulted from a financial crisis in the Russian Federation which prevented the segment from achieving targeted sales volumes.

Mass Media

We operate our Mass Media Segment through Sistema Mass Media, a holding company that is active in three main areas: pay-TV, advertising and other media sectors, such as publishing, film production and news services. Following a strategic review of our media assets, we primarily focus on developing distribution platforms and content for pay-TV and multi-media services initially in Moscow and subsequently in other parts of Russia. Starting from the year ended December 31, 2005, our Mass Media Segment is actively developing cable television network throughout Russia.

	Years ended December 31,					
		2007	% of revenues		2008	% of revenues
	(Amounts in thousands, except percentages)					
Revenues	$	130,071	100.0%	$	223,984	100.0%
Cost of sales, exclusive of depreciation and amortization shown separately below		(77,313)	(59.3)		(85,797)	(38.3)
Selling, general and administrative expenses		(42,832)	(32.8)		(82,289)	(36.7)
Depreciation and amortization		(21,097)	(16.2)		(66,345)	(29.6)
Net other operating income		11,355	8.4		4,663	2.1
Gain on disposal of interests in subsidiaries and affiliates		-	0.0		-	0.0
Operating income	$	184	0.1%	$	(5,784)	-

Revenues

The Mass Media segment, which comprises our Pay-TV business, operating under the brand name Stream-TV, as well as advertising, print and other media operations, generated 72.2% year on year revenue for the year 2008 primarily as a result of the increase in Stream-TV and Internet ARPU and subscriber growth. Stream-TV's revenues increased by 31 % year on year to $118 million in 2008. The Stream-TV subscriber base increased by 18 % year on year to 2 million subscribers, while its Internet subscriber base has nearly doubled to 0.2 million subscribers. Pay-TV ARPU increased from $4.2 to $4.7 in 2008. Internet ARPU decreased from $15.0 in 2007 to $14.6 in 2008. The Maxima Group, an advertising agency, which operates in Russia, Ukraine, Kazakhstan and Belarus, contributed $11.9 million to segment revenues in 2008.

Operating income

Operating income of the segment decreased to a loss $5.8 million from a gain $0.2 million in the year ended December 31, 2007.

Radio and Space Technology

Our radio and space technology division represented by RTI Systems is primarily involved in the design and production of radars and radar systems, space control systems and telecommunications equipment for both governmental agencies and corporate clients.

Revenue

The total operating revenues of our radio and space technology division for the year ended December 31, 2008 were $471.5 million compared to $374.5 million for the year ended December 31, 2007, representing growth of 25.9 %. The growth in revenues is explained by an increase in the volume of contracts with governmental agencies.

Operating income

In our radio and space technology division, operating margin decreased to 10.5 % during the year ended December 31, 2008 from 11.2% in the year ended December 31, 2007.

Travel Services

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 more than 40 Russian and several foreign subsidiaries.

Revenue

The total operating revenues of our travel services business for the year ended December 31, 2008 were $615.6 million compared to $374.0 million for the year ended December 31, 2007, representing growth of 64.6 %. The growth in revenues is explained by the strong performance of our tour operating division which developed faster than the rest of the market, particularly on routes to Turkey and Egypt. The segment serviced 1,124,446 customers in 2008 compared to 888,683 in 2007. The hotel group, which comprises 19 hotels, increased the total number of rooms by 234 % to nearly 5,753 rooms as of December 31, 2008.

Operating income

In our travel services business operating margin also slightly decreased to 5.0 % for the year ended December 31, 2008 from 5.5% in the year ended December 31, 2007 as a result of the overall decline in the economy.

Corporate and Other

In this category we include our central corporate functions. Thus, costs of our corporate function are included in the operating costs of this segment. These costs (being mostly attributable to personnel costs (including share awards and bonuses granted) decreased to $103.0 million for the year ended December 31, 2008, compared to $159.5 million in the year ended December 31, 2007.

	Years ended December 31,			
	2007	% of revenues	2008	% of revenues
	(Amounts in thousands, except percentages)			
Revenues	$ 61,896	100.0%	$ 60,973	100.0 %
Cost of sales, exclusive of depreciation and amortization shown separately below	(26,598)	(42.2)	(6,993)	(11.5)
Selling, general and administrative expenses	(159,481)	(253.6)	(103,120)	(169.1)
Provision for doubtful accounts	-	(0.0)	(64,122)	(105.2)
Depreciation and amortization	(8,395)	(13.3)	(9,265)	(15.2)
Other operating income			4,177	6.9
Operating income/(loss)	$ (163,881)	-	$ (118,350)	-
Equity in net income of energy companies in the Republic of Bashkortostan before minority interest	123,856	12.6	241,867	396.7

Year ended December 31, 2008 compared to year ended December 31, 2007

Revenues

Total operating revenues of the Other Businesses Segment decreased to $61.0 million for the year ended December 31, 2008, compared to $61.9 million for the year ended December 31, 2007.

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Operating income/(loss)

In the Other Businesses Segment operating losess for the year ended December 31, 2007 amounting to $163.9 million decreased to $118.4 million in 2008. The decrease in selling, general and administrative expenses was largely due to non-recurring compensation cost in the amount of $23.0 million incurred in the year ended December 31, 2007.

Telecommunications Operating Data

Our revenues and operating income for the years ended December 31, 2008 and 2007 were influenced by trends in the principal businesses included in our Telecommunications Segment: MTS 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.

	At December 31,		
	2006	2007	2008
		(in millions)	
Subscribers[1]			
Russia	51.2	57.4	64.6
Ukraine	20.0	20.0	18.1
Uzbekistan	1.5	2.8	5.7
Armenia	-	1.4	2.0
Turkmenistan	0.2	0.4	0.9
Total consolidated	72.9	82.0	91.3
MTS Belarus (unconsolidated)	3.2	3.8	4.3

(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.

We had approximately 65 million subscribers in Russia at December 31, 2008, of which 15 million were in the Moscow license area that encompasses the City of Moscow and the Moscow region. According to AC&M-Consulting, approximately 17% of all mobile cellular subscribers in Russia reside in the Moscow license area, where penetration stood at approximately 185% as of December 31, 2008. Penetration in all of Russia was approximately 129%, according to AC&M-Consulting. Our subscribers in Russia outside of the Moscow license area totaled approximately 50 million as of December 31, 2008. According to AC&M-Consulting, as of December 31, 2008, we had a leading 34% market share of total mobile cellular subscribers in Russia. Our market share in the Moscow license area was higher at 47 % as of December 31, 2008, according to AC&M-Consulting. We had approximately 18 million subscribers in Ukraine as of December 31, 2008, and according to AC&M-Consulting, a 32.5 % market share of total mobile cellular subscribers in Ukraine. We had approximately 6 million subscribers in Uzbekistan, representing a 46 % market share, according to our estimates. Additionaly, we had approximately 2 million subscribers in Armenia, representing a 78.8 % market share, according to AC&M-Consulting.

Subscriber Churn

We define our churn as the total number of subscribers who cease to be a subscriber 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. We view the subscriber churn as a measure of market competition and customer dynamics. The following table shows our Russian and Ukrainian subscriber churn for the periods indicated.

	Year Ended December 31,		
	2006	2007	2008
Subscriber Churn			
Russia	23.3%	23.1%	27.0%
Ukraine	29.9%	49.0%	47.3%

The churn rate is highly dependent on competition in our license areas and those subscribers who migrate as a result of such competition. We believe that the increase in our churn rate in Russia to 27.0% during the year ended December 31, 2008 as compared to 23.1% for the year ended December 31, 2007 is in line with regular fluctuations in subscriber numbers attributable to the strong competitive environment intensified by increased subscriptions during 2007 and 2008.

Although the churn rate in Ukraine slightly decreased to 47.3% for the year ended December 31, 2008 from 49.0% for the year ended December 31, 2007, it significantly increased to 49.0% in 2007 as compared to 29.9% in 2006 and remains high. This increase is primarily represented by the churn of prepaid subscribers, which increased from 30% in 2006 to 51% in 2007. Churn of contract, or postpaid, subscribers increased from 25% in 2006 to 29% in 2007.

We calculate our average monthly service revenue per subscriber by dividing our service revenues for a given period, including guest roaming and interconnect fees, by the average number of our subscribers during that period and dividing by the number of months in that period. The following table shows our average monthly service revenue per Russian and Ukrainian subscriber and average monthly minutes of use per Russian and Ukrainian subscriber for the periods indicated.

	Year Ended December 31,		
	2006	2007	2008
Average monthly service revenue per subscriber			
Russia	$8[1]	$9[1]	$11
Ukraine	$7	$7	$ 7
Uzbekistan	$11	$10	$ 7.7
Average monthly minutes of use per subscriber			
Russia	129	157	209
Ukraine	142	154	279
Uzbekistan	437	516	536

(1) As of June 30, 2006, we changed the methodology for reporting average revenue per user for its Russian subscribers, a common calculation used throughout the telecommunications industry as a measure of company effectiveness and performance. Whereas previously we had excluded interconnect fees, we are now including all network revenue in our calculation.

Average monthly service revenue per subscriber in Russia increased to $11 for the year ended December 31, 2008, from $9 for the year ended December 31, 2007. Average monthly service revenue per subscriber in Ukraine is stable in the year ended December 31, 2008 as a result of the aggressive pricing policies of competitors.

Comstar UTS

Comstar UTS had near 1,204,020 residential subscribers in its alternative fixed-line communications segment as at December 31, 2008, of which the number of broadband and pay-TV (StreamTV) subscribers increased by 118..8% and 122.9%, respectively, year on year. The broadband subscriber base grew strongly during the year and had reached near 737,000 by the end of the year. The number of dial-up subscribers declined by 29.2 % in 2008, which was in line with the general market trend of subscribers switching to broadband services.

The corporate client base in the alternative fixed-line telecommunications segment grew to nearly 73,694 subscribers as at December 31, 2008. The numbering capacity in the alternative fixed-line telecommunications segment was more than 1,125,000 numbers by the year end, whilst the number of ADSL and data transmission channels increased by 7.0 % during the year. Local connections still account for the majority of the traffic.

The total numbering capacity in the traditional fixed-line telecommunications segment was 4,850,872 numbers, of which over 3.6 million numbers were provided to residential subscribers and near 746,680 numbers were provided to corporate subscribers. Comstar UTS provided traditional fixed-line telecommunications services to 3,613,679 residential customers and more than 73,000 corporate customers as at December 31, 2008.

Alternative Fixed-Line Business

	Years ended December 31,	
	2007	**2008**
Number of subscribers	**1,115,759**	**1,278,203**
Residential subscribers	1,048,933	1,204,020
Broadband subscribers	618,298	736,642
Dial-up subscribers	109,096	77,233
Voice subscribers	232,202	277,151
Pay-TV subscribers	122,288	145,283
Corporate subscribers	66,398	73,694
Operators	428	489

	Years ended December 31,	
	2007	**2008**
Active telephone lines		
Corporate subscribers	240,748	265,135
Operators	132,779	131,047
Mobile operators	333,677	308,395
Residential subscribers	232,197	276,896
Total	**939,131**	981,473
Installed capacity / telephone lines	**1,051,871**	**1,125,788**
ADSL and data transmission channels	**50,275**	**52,473**

Traditional Fixed-Line Business

	Years ended December 31,	
	2007	**2008**
Number of current subscribers		
Residential subscribers	3,585,967	3,613,679
Corporate subscribers	67,469	73,454
Operators	227	247
Total	**3,653,663**	**3,687,380**
Active telephone lines		
Residential subscribers	3,585,967	3,613,679
Corporate subscribers	766,725	746,680
Total	**4,352,692**	**4,360,359**
Installed capacity / telephone lines	**4,795,333**	**4,850,872**
Access nodes / lines rented		
Corporate subscribers	31,823	29,491
Operators	229,959	222,926
Total	**261,782**	**252,417**

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 2008, MTS issued three ruble-denominated bonds in the amount of 10 billion rubles each (equivalent in aggregate to $779.1 million as of December 31, 2008). MTS also entered into Euro- and U.S. dollar-denominated loan agreements with various banks in 2008 for aggregate borrowings equivalent to $1,010.9 million as of December 31, 2008. In March 2008, JSFC Sistema issued ruble-denominated bonds in the amount of 6 billion rubles each (equivalent to $204.2 million as of December 31, 2008). In 2008, MBRD issued two ruble-denominated bonds in the amount of 3 billion rubles each (equivalent in aggregate to $208.2 million as of December 31, 2008). In July 2008, JSFC Sistema entered into a credit line facility with Sberbank for the amount of $450 million. As of December 31, 2007, $80.0 million under the facility remains undrawn. In March 2008, JSFC Sistema signed a credit arrangement with The Royal Bank of Scotland. The amount drawn under the facility in 2008 was $255.0 million. In November 2008, MGTS issued Access Telecommunications Cooperatief U.A. a $363.6 million USD-denominated promissory note as part payment of its obligation under the put option. In July 2008, SITRONICS signed a credit arrangement with VTB bank. The amount drawn under the facility in 2008 was 150.0 million Euro (equivalent to $211,575 million as of December 31, 2008). In December 2008, SITRONICS entered into a USD-denominated loan agreement with Vnesheconombank. As of December 31, 2008, the amount outstanding under this agreement comprised $155.0 million. Our other borrowings in 2008 amounted to approximately $1,100.0 million.

Our parent company, JSFC 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 JSFC 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.

We expect to repay all long-term debts as they become due from our operating cash flows or through re-financings. See Notes 20 and 21 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 December 31, 2008, we had a working capital deficit of $1,407.6 million, from positive working capital of $633.4 million as of December 31, 2007. The increase in working capital deficit was mainly attributable to an increase in the current portion of our debt, and an increase in trade payables, partially offset by an increase in our cash and cash equivalents balance as of December 31, 2008.

We expect to repay all long-term debts as they become due from our operating cash flows or through re-financings. We believe that our working capital together with our plans for external financing will provide us with sufficient funds for our present requirements.

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	April 01, 2009	BB	CW Negative
	Fitch	March 31, 2009	BB-	RW Negative
	Moody's	April 22, 2009	B1	RW Negative
MTS	Standard & Poor's	April 01, 2009	BB	CW Negative
	Moody's	April 2, 2009	Ba2	Stable
	Fitch	March 31, 2009	BB+	RW Negative
Sitronics	Fitch	March 31, 2009	B-	RW Negative
	Moody's	October 17, 2008	B3	Negative
Comstar UTS	Standard & Poor's	April 01, 2009	BB	CW Negative
	Moody's	October 24, 2007	Ba3	Stable
MGTS	Standard & Poor's	April 01, 2009	BB	CW Negative
	Moody's	January 19, 2006	Ba3	Stable
MBRD	Fitch	April 01, 2009	B+	RW Negative
	Moody's	October 20, 2008	B1	RW Negative
Sistema Hals	Fitch	April 09, 2009	B	RW Evolving
	Moody's	December 22, 2008	B3	RW Negative

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 the years ended December 31, 2007 and December 31, 2008 were $3,062.5 million and $4,270,9 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 as licenses relating to new telecommunication technologies became available and our investment program for expansion and full digitalization of the Moscow public switch telephone network is being 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 $1,459.1 million and $1.940.7 million in the years ended December 31, 2007 and December 31, 2008, 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.

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, 2008, our debt was comprised of the following:

	Interest rate (Actual at December 31, 2008)		December 31, 2008 (In thousands)
USD-denominated:			
Access Telecommunications Cooperatief S.A.	16%	$	263 552
Gazprom Bank	9.5%		200 000
Vnesheconombank	LIBOR+7% (8.8%)		155 000
Alfa Bank	LIBOR+5.5%-6.0% (7.5%-8.0%)		90 001
Alexandria Capital plc	9.3%		75 000
Raiffeisen Bank	LIBOR+6.6% (8.4%), 12%		80 091
Standard Bank	LIBOR+6% (7.8%)		50 000
HSBC Bank	LIBOR+2.5%-8.5% (4.3%-10.3%), 10.7%		27 054
The Royal bank of Scotland	LIBOR+0.9% (2.7%)		15 000
Melrose Holdings S.A.	17%		7 000
Other	Various		51 750
			1 014 448
EUR-denominated:			
Societe Generale – Geniki Bank	EURIBOR+1.5% (4.5%)		14 105
ING Bank	EURIBOR+1.3% (4.3%)		6 428
Hellenik Bank	LIBOR+4% (5.8%)		4 253
			24 786
Borrowings in other currencies:			
Raiffeisen Bank	MosPrime+5.5% (28.3%)		34 036
Sberbank	8.0-12.0%		23 206
HSBC	MosPrime+2.5% (25.3%)		13 546
Promsvyazbank	14.0%		8 169
Other	Various		166 616
			245 574
Loans from related parties	Various		233 705
Capital leases			20 492
Vendor financing			1 267
Other borrowings			66 036
Total		**$**	**1 606 307**

	Currency	Interest rate (Actual at December 31, 2008)	December 31, 2008 (In thousands)
MTS Finance Notes due 2012	USD	8.0%	399,463
MTS Finance Notes due 2010	USD	8.4%	400 000
Sistema Capital Notes due 2011	USD	8.9%	345 000
MTS Finance Notes due 2018	RUR	8,70%	268 533
MTS Finance Notes due 2013	RUR	14.0%	255 272
MTS Finance Notes due 2015	RUR	14.0%	255 272
MBRD Bonds due 2013	RUR	10%-11.5%	208 226
JSFC Sistema Bonds due 2013	RUR	9.5%	204 218

SITRONICS Bonds due 2010	RUB	10.0%	102 109
MBRD Capital Notes due 2009	USD	8.8%	99 694
MBRD Loan Participation Notes due 2016	USD	8.9%	60 491
DM-Center Bonds due 2015	RUB	8.5%	39 142
Intourist Bonds due 2010	RUB	9.0%	34 036
MGTS Bonds due 2009	RUB	7.1%	5 233
MGTS Bonds due 2010	RUB	7.1%	5 202
Total notes and corporate bonds			**2 681 890**

	Maturity	Interest rate (Actual at December 31, 2008)	December 31, 2008 (In thousands)
USD-denominated:			
Syndicated Loan Facility to MTS	2009	LIBOR+0.8%-1.2% (2.6%-3%)	1 168 462
VTB	2010-2011	6.2%-8.5%	602 271
Sberbank	2010-2013	10.5%	370 000
The Royal Bank of Scotland	2010-2014	LIBOR+0.4%-2.7% (2.2%-4.5%)	243 936
EBRD	2013-2014	LIBOR+1.5%-3.3% (3.3%-5%)	233 333
Skandinaviska Enskilda Banken AB	2017	LIBOR+0,2% (2%)	159 047
Vnesheconombank	2009-2014	LIBOR+3.0%(4.8%,), 8.9%	113 320
Commerzbank AG, ING Bank AG and HSBC Bank plc	2009-2014	LIBOR+0.3% (2.1%)	110 726
HSBC Bank plc and ING BHF Bank AG	2009-2013	LIBOR+0.4% (2.2%)	108 048
HSBC Bank plc, ING Bank AG and Bayerische Landesbank	2009-2014	LIBOR+0.3% (2.1%)	92 789
Raiffeisenbank	2009	LIBOR+5.25% (7%) 8%	86 560
Citibank International plc and ING Bank N.V.	2009-2014	LIBOR+0.3% (2.1%)	81 348
Barclays Bank plc	2009-2014	LIBOR+0.2% (2%)	72 360
Merrill Lynch International	2011	LIBOR + 11.4% (13.2%)	70 000
HSBC Bank plc	2011	5.2%	67 000
Unicredit	2011-2015	LIBOR + 4.2%-7.0% (6.2%-9.0%)	45 938
Commerzbank (Eurasia)	2009-2010	LIBOR+3.5% (5.3%)	30 826
Gazprombank	2011	12,50%	26 000
Other	2009-2015	Various	32 463
			3 714 427
EUR-denominated:			
Gazprombank	2009-2011	12%	423 150
Syndicated Loan to Sitronics	2009-2011	EURIBOR+1.2% (4.2%)	211 575
The Royal Bank of Scotland	2009-2013	EURIBOR+0.4% (3.4%)	24 406
VTB	2010-2012	EURIBOR+3.8%-8.9% (6.8%-11.9%)	7 614
ING BHF Bank and Commerzbank AG	2009	EURIBOR+0.7% (3.7%)	7 356
Other	2009-2010	Various	20 096
			694 197
RUR-denominated:			
Sberbank	2012	7.6%	892 167
VTB	2012	15%-17.5%	801 849
RussBank	2010	14.1%	56 787
Unicredit	2011	MosPrime+1.8% (24.6%)	25 958
InvestTorgBank	2011	14,50%	22 819
Other	Various	Various	47 057
			1 846 637
Other currencies	2009-2018	Various	118 246
Total			**6 373 507**

The following table presents the aggregate scheduled maturities of debt principal outstanding as of December 31, 2008:

Year ended December 31,		
2009	$	3 700 154
2010		3 208 487
2011		1 635 970
2012		1 517 876
2013		282 171
Thereafter		317 047
Total	$	10 661 705

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,	
	2007	**2008**
	(Amounts in thousands)	
Cash flows		
Net cash provided by operating activities	$ 2,723,142	$ 3,825,761
Net cash used in investing activities	(5,753,948)	(5,874,833)
Net cash provided by financing activities	3,378,278	3,269,613
Net increase in cash	463,352	929,592
Cash outlays for		
Capital expenditures[1]	(3,061,486)	(4,270,900)
Acquisition of subsidiaries, net of cash acquired	(1,459,149)	(1,940,700)

(1) Includes acquisitions 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 organic growth and acquisitions. During the same periods, our investing activities generated negative cash flows due primarily to 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. 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. For the year ended December 31, 2008, our financing activities generated positive cash flows following the receipt of proceeds from initial public offerings of Sitronics and an increase of borrowings needed to finance our investing activities.

Liquidity

As of December 31, 2008 and December 31, 2007, we had total cash and cash equivalents of $1,991.3 million and $1,061.7 million, respectively. In addition, as of December 31, 2008 and December 31, 2007, we had short-term investments of $617.4 million and $909.2 million, respectively, mostly in corporate and municipal bonds and bank deposits.

For details of external financing refer to Notes 19 and 20 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 profit 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.

Competition

We operate in some of the most competitive industries in Russia, including telecommunications, technology 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, Saint-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,				
2004	29.45	27.75	28.73	27.75
2005	29.00	27.46	28.32	28.78
2006	28.78	26.18	27.09	26.33
2007	26.58	24.26	25.58	24.55
2008	29.38	23.13	24.98	29.38

(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.

	Hryvnias per U.S. dollar			
	High	**Low**	**Average(1)**	**Period End**
Year ended December 31,				
2004	5.33	5.31	5.32	5.31
2005	5.31	5.05	5.11	5.05
2006	5.05	5.05	5.05	5.05
2007	5.05	5.05	5.05	5.05
2008	7.58	4.84	5.27	7.58

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

Our principal exchange rate risk involves changes in the value of the ruble, hryvnia and the euro relative to the U.S. dollar.

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.

Inflation and Exchange Rates

The Russian economy has been characterized by high rates of inflation:

Year	Inflation rate
2004	11.7%
2005	10.9%
2006	9.0%
2007	11.9%
2008	13.3%

The Ukrainian economy has been characterized by high rates of inflation:

Year	Inflation rate
2004	12.3%
2005	10.3%
2006	11.6%
2007	16.6%
2008	25.2%

Over the past several years, except for 2008, 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.

Certain of our costs, including salaries and utility costs, are sensitive to rises in the general price level in Russia. Over the past 15 years, the ruble has fluctuated, at times substantially over short periods of time, against the U.S. dollar and, in particular, it has significantly depreciated against the U.S. dollar in 2008 as a result of the ongoing global financial crisis. For example, on December 31, 2008, the official exchange rate published by the Central Bank of Russia, or CBR, was 29.38 rubles per one U.S. dollar, as compared to 24.55 rubles per one U.S. dollar on December 31, 2007.

A majority of our capital expenditure and liabilities and borrowings are either denominated in or tightly linked to the U.S. dollar. Conversely, a majority of our revenues are denominated in rubles. As a result, devaluation of the ruble against the U.S. dollar can adversely affect us by increasing our costs in rubles, both in absolute terms and relative to our revenues, and make it more difficult to comply with our financial ratios or timely fund cash payments on our indebtedness. A decline in the value of the ruble against the U.S. dollar will also result in a translation loss when we translate the ruble revenues into U.S. dollars for inclusion in our audited consolidated financial statements. It also reduces the U.S. dollar value of tax savings arising from tax incentives for capital investment and the depreciation of our property, plant and equipment, since their basis for tax purposes is denominated in rubles at the time of the investment. Increased tax liability would also increase total expenses.

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, 2008, approximately $ 3,158 million, or 29.7 % of our total indebtedness was variable interest rate debt, while $ 7,484 million or 70.3 % of our total indebtedness was fixed interest rate debt.

In January 2006, MTS entered into a variable-to-fixed interest rate swap agreement with HSBC Bank Plc to hedge MTS' exposure to variability of future cash flows caused by the change in EURIBOR related to the ABN AMRO Bank. MTS agreed with HSBC Bank plc to pay a fixed rate of 3.3% and receive a variable interest of EURIBOR on EUR 26.0 million for the period from April 2006 up to October 2013.

In December 2007, MTS entered into several variable-to-fixed interest rate swap agreements with HSBC Bank plc, Rabobank, Citibank N.A. and ING Bank N.V. to hedge MTS' exposure to variability of future cash flows caused by the change in LIBOR related to our outstanding debt. MTS agreed with HSBC Bank plc to pay a fixed rate of 4.14% and receive a variable interest of LIBOR on $96.1 million for the period from March 31, 2008 to September 30, 2014. The agreement with Rabobank was to pay a fixed rate of 4.16% and receive a variable interest of LIBOR on $86.1 million for the period from April 9, 2008 to April 9, 2014. MTS agreed with Citibank N.A. to pay a fixed rate of 4.29% and receive a variable interest of LIBOR on $53.5 million for the period from September 28, 2007 September 30, 2013. Two agreements were signed with ING Bank N.V. Under the first agreement, MTS will pay to ING Bank N.V. a fixed rate of 4.19% and receive a variable interest of LIBOR on $92.6 million for the period from February 29, 2008 to February 28, 2014. According to the terms of the second agreement, MTS will pay ING Bank N.V. a fixed rate of 4.41% and receive a variable interest of LIBOR on $67.0 million for the period from July 16, 2007 to January 15, 2014.

As of December 31, 2008, we recorded a liability of $20.9 million in relation to the above hedge contracts in the accompanying consolidated balance sheet and a loss of $16.7 million, net of tax of $4.2 million, to other comprehensive income in the accompanying consolidated statement of changes in shareholders equity in relation to the change in fair value of these agreements.

We continue to consider other financial instruments available to us on the market to mitigate exposure to variability in interest rates.

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, 2008.

Contractual Maturity Dates as of December 31, 2008:

	Currency	December 31, 2009	2010	2011	2012	2013	Thereafter	Total	Average rate at December 31, 2008
Syndicated Loan Facility to MTS	USD	845 384	215 384	107 694	-	-	-	1 168 462	2,8%
The Royal Bank of Scotland	USD	95 645	95 645	52 646	-	-	-	243 936	3,4%
EBRD	USD	33 333	33 333	33 333	33 333	83 333	16 668	233 333	4,2%
Skandinaviska Enskilda Banken AB	USD	30 000	28 096	18 824	18 824	18 824	44 479	159 047	2,0%
Vnesheconombank	USD	60 000	-	-	-	-	-	60 000	4,8%
Commerzbank AG, ING Bank AG and HSBC Bank plc	USD	19 740	19 740	19 740	19 740	19 740	12 026	110 726	2,1%
HSBC Bank plc and ING BHF Bank AG	USD	21 798	21 798	21 798	21 798	20 856	-	108 048	2,2%
HSBC Bank plc, ING Bank AG and Bayerische Landesbank	USD	16 609	16 609	16 609	16 609	16 609	9 744	92 789	2,1%
Raiffeisenbank	USD	20 500	-	-	-	-	-	20 500	7,0%
Citibank International plc and ING Bank N.V.	USD	14 790	14 790	14 790	14 790	14 790	7 398	81 348	2,1%
Barclays Bank plc	USD	13 156	13 156	13 156	13 156	13 156	6 580	72 360	2,0%
Merrill Lynch International	USD	-	-	70 000	-	-	-	70 000	13,2%
Unicredit	USD	-	-	20 000	9 567	-	16 371	45 938	7,6%
Commerzbank (Eurasia)	USD	15 413	15 413	-	-	-	-	30 826	5,3%
Vnesheconombank	USD	155 000	-	-	-	-	-	155 000	8,8%
Alfa Bank	USD	90 001	-	-	-	-	-	90 001	7,8%
Raiffeisen Bank	USD	55 105	-	-	-	-	-	55 105	8,4%
Standard Bank	USD	50 000	-	-	-	-	-	50 000	4,1%
HSBC Bank	USD	20 000	-	-	-	-	-	20 000	7,3%
The Royal bank of Scotland	USD	15 000	-	-	-	-	-	15 000	7,8%
Total USD variable debt		**1 571 474**	**473 964**	**388 590**	**147 817**	**187 308**	**113 266**	**2 882 419**	
Weighted average USD interest rate		**3,7%**	**3,7%**	**3,6%**	**3,0%**	**3,1%**	**3,2%**	**3,6%**	
Syndicated Loan to Sitronics	EUR	21 158	21 158	169 259	-	-	-	211 575	4,2%
The Royal Bank of Scotland	EUR	8 135	8 135	8 136	-	-	-	24 406	3,4%
VTB	EUR	2 175	2 175	2 175	1 088	-	-	7 614	9,4%
ING BHF Bank and Commerzbank AG	EUR	7 356	-	-	-	-	-	7 356	3,7%
Societe Generale – Geniki Bank	EUR	14 105	-	-	-	-	-	14 105	4,5%
ING Bank	EUR	6 428	-	-	-	-	-	6 428	4,3%
Hellenik Bank	EUR	4 253	-	-	-	-	-	4 253	5,8%
Total EUR variable debt		**63 610**	**31 468**	**179 570**	**1 088**	**-**	**-**	**275 737**	
Weighted average EUR interest rate		**4,3%**	**4,3%**	**4,3%**	**9,4%**	**0,1%**	**0,0%**	**4,3%**	

We would experience an additional interest expense of approximately $23.4 million in the year ended December 31, 2009, $12.7 million in the year ended December 31, 2010, $7.3 million in the year ended December 31, 2011, $3.8 million in the year ended December 31, 2012, $2.1 million in the year ended December 31, 2013 and $1,1 million thereafter as a result of a hypothetical increase in the LIBOR/EURIBOR by 1% over the current rate as of December 31, 2008.

The fair value of our publicly traded long-term notes as of December 31, 2007 ranged from 80.0% to 99.3% of the principal amount. At December 31, 2007, 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, 2008.

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.

Revenue recognition

Telecommunications

The 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) monthly subscription fees, (b) usage fees, (c) value-added telecommunication service fees, (d) roaming fees charged to other operators for guest roamers utilizing our network, (e) connection fees, (f) revenues from use of prepaid phone cards and (g) 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. We periodically review our estimates of the expected subscriber relationship period.

Technology

The Technology Segment earns revenues from (a) sale of consumer electronic, semiconductor products and other electronic devices; (b) manufacturing and distribution of software products; and (c) computer hardware sale and systems integration services. 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:

Electronic and semiconductor products are generally sold with a limited warranty of product quality. The product return reserves, warranty and other post-contract support obligations are accrued at the time of sale. We accrue for known warranty if a loss is probable and can be reasonably estimated, and accrue for estimated incurred but unidentified issues based on historical activity.

In those cases where we buy components from and subsequently sell the assembled devices to the same counterparty or where our responsibility to the customer is limited solely to assembly services, we record only the net amount retained as our revenues.

Revenues from the sale of software products are multiple-element arrangements, involving provision of related services, including customization, implementation and integration services, as well as ongoing support and maintenance provided to customers.

If the services element of the arrangement is deemed essential to the functionality of the software arrangement, the accounting for performance of construction-type contracts is applied. Revenue on such arrangements is recognized applying the percentage-of-completion method. The measurement of progress towards completion is based on the ratio of hours or costs to date to estimated total hours or costs at completion.

If the service element of the arrangement is not deemed essential to the functionality of the software, the service revenues are accounted for separately from the software revenues. In such multiple-element arrangements, the software component is accounted for using the residual method.

In cases where extended payment terms exist, license and related customization fees are recognized when payments are due, unless a history of collection, without providing concessions, has been established under comparable arrangements.

Due to frequent sales price reductions and rapid technology obsolescence, revenues from computer hardware sales to dealers under agreements allowing price protection are deferred until the dealers sell the merchandise.

The arrangements regarding systems integration services typically include multiple elements, such as equipment and software, installation services and post-contract support.

If evidence of the fair value of the undelivered elements of the arrangement does not exist, all revenue from the arrangement is deferred until such time that evidence of fair value does exist, or until all elements of the arrangement are delivered. Fees allocated to post-contract support are recognized as revenue on a pro rata basis over the support period. Fees allocated to other services are recognized as revenues as services are performed.

Revenue and cost of sales from contracts involving solutions achieved through modification of telecommunications equipment and software are recognized by reference to the stage of completion of the contract at the balance sheet date when the outcome of a contract can be estimated reliably. Where the outcome of a contract cannot be estimated reliably, equal amounts of revenue and costs are recognized until results can be estimated more precisely. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognized immediately.

Banking operations

Interest income of the Banking Segment is recognized on the 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 the allowance for loan losses in case of uncollectibility of loans and advances, including through repossession of collateral.

Real estate

The Real Estate Segment earns revenues from (i) real estate development, (ii) project and construction management, (iii) asset management and investments, (iv) facilities management. We record revenues as follows:

(i) Revenues from real estate development activities are recognized in accordance with the provisions of FAS No. 66, "Accounting for Sales of Real Estate" and AICPA Statement of Position No. 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts" ("SOP 81-1").

When we undertake real estate development projects at its own risk, we recognise revenues from sales of real estate when a) a sale is consummated; b) the buyer's initial and continuing investments are adequate to demonstrate a commitment to pay; c) our receivable is not subject to future subordination; d) we have transferred to the buyer the usual risks and rewards of ownership and does not have a substantial continuing involvement with the project. A sale is not considered consummated until (a) the parties are bound by the terms of a contract; (b) all consideration has been exchanged; (c) any permanent financing for which we are responsible has been arranged; and (d) all conditions precedent to closing have been performed. Revenues from development of office and residential buildings are recognized prior to consummation of sale by the percentage-of-completion method if (a) construction is beyond a preliminary stage; (b) the buyer is committed to the extent of being unable to require a refund except for non-delivery of the property; (c) sales prices are collectible; (d) aggregate sales proceeds and costs can be reasonably estimated.

In those instances, when we act as a contractor under construction contracts with third parties, we apply the percentage-of-completion method to the respective contracts where and as soon as we are able to reliably estimate the stage of progress to completion of the project, costs to complete the project and contractual revenues. Progress towards completion is measured by the percentage of costs incurred to date to the estimated total costs at completion for each contract (the "cost-to-cost" method). On most contracts, we are not able to reliably estimate costs to complete the project and contractual revenues until the project is at least 30% complete. In such cases, until the 30% completion point, we carry the projects at cost. We do not recognize revenue on contracts until reasonably dependable estimates of costs to complete the project and contractual revenues can be made.

(ii) We provide project and construction management services to municipal governments on certain socially important infrastructure projects. Our remuneration for such services was determined as a percentage of project costs incurred by third parties and approved by the municipal government. Based upon the guidance in Emerging Issues Task Force Consensus No. 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent" ("EITF 99-19"), we have concluded that our services under such contracts do not transfer to us the full risks and rewards associated with the projects. Therefore, we recognise as revenues only our fees from project management services. Fees are recognized as the project costs are incurred and approved by the municipal government.

(iii) Revenues from asset management and investments include rental revenues, revenues from sale or assignment of rights to land plots and residential units. Rental revenues are recognized over the lease term on a straight-line basis. Revenues from the sale or assignment of rights over real estate are recognized when substantially all the risks and rewards of ownership have been passed to the buyer.

(iv) Revenues from service contracts for facilities management are recognized on the accrual basis over the periods when services are provided.

Other businesses

Our other segments 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 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.

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. 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 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 ten 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 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, 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 FAS No. 52, "Foreign Currency Translation."

Management has determined that the functional currencies of the Group's significant subsidiaries for the year ended December 31, 2008 are the currencies of the countries of their domicile, with the exception of Intourist, a company incorporated in the RF, Kvazar-Micro International Ltd., a company incorporated in the United Kingdom, and Uzdunrobita, MTS subsidiary in Uzbekistan, whose functional currency is the U.S. dollar ("USD") due to the pervasive use of the USD in their operations.

The impact of the change in functional currency on the financial statements was an increase in the opening translated carrying values of the following non-monetary assets and liabilities and the related deferred taxes as of January 1, 2008:

		January 1, 2008
Inventories and spare parts	$	21,433
Property, plant and equipment, net		60,413
Other intangible assets, net		9,223
Investments in associates and joint ventures		730
Accrued expenses and other current liabilities (advances received under development projects)		(23,980)
Deferred taxes		(2,023)
Minority interest		(6,067)
Total increase	$	59,730

This increase has been reflected in shareholders equity as a part of other comprehensive income as of January 1, 2008.

The Group has selected the USD as its reporting currency and translated into USD 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.

Transactions in foreign currencies are recorded at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in effect at the balance sheet date. Revenues, costs and expenses are recorded using average exchange rates prevailing during the reporting period.

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.

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 (profits tax), a number of turnover-based taxes, and payroll (social) taxes, together with others. Laws related to these taxes have not been in force for significant periods, in contrast to more developed market economies; therefore, the government's implementation of these regulations is often inconsistent or nonexistent. Accordingly, few precedents with regard to tax rulings have been established. Generally, tax declarations remain open and subject to inspection for a period of three years following the tax year. As of December 31, 2006, our tax declarations for the preceding two fiscal years were open to further review.

In the ordinary course of business, we may be party to various legal and tax proceedings, and subject to claims, certain of which relate to the developing markets and evolving fiscal and regulatory environments in which we operate. We consider that our liability, if any, in all pending litigation, other legal proceedings or other matters will not have a material effect upon our financial condition, results of operations or liquidity. We have adequately provided for tax liabilities in our financial statements; however, the risk remains that the authorities could take a different position with regard to interpretive issues.

Income Taxes

Income taxes of our Russian entities have been computed in accordance with RF laws. Income tax rate in the RF equals 24%. The income tax rate on dividends paid within Russia is 9%. Our foreign subsidiaries are paying income taxes in their jurisdictions. As of December 31, 2008, the income tax rate in Ukraine is 25%.

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 we will be able to realize the benefit, or the future deductibility is uncertain.

We provide for income taxes in accordance with Statement FAS No.109, “Accounting for Income Taxes” and Financial Accounting Standards Board (“FASB”) Interpretation No. 48, “Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109” (“FIN 48”).

Uncertain tax positions are recognized in the consolidated financial statements for positions which are considered more likely than not of being sustained based on the technical merits of the position on audit by the tax authorities. The measurement of the tax benefit recognized in the consolidated financial statements is based upon the largest amount of tax benefit that, in management’s judgment, is greater than 50% likely of being realized based on a cumulative probability assessment of the possible outcomes.

Deferred tax assets and liabilities are recognized for differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the tax bases of assets and liabilities that will result in future taxable or deductible amounts. The deferred tax assets and liabilities are measured using the enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

We recognize interest relating to unrecognized tax benefits and penalties within income taxes.

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 as VAT receivable in the accompanying financial statements.

New Accounting Pronouncements

In September 2006, the FASB issued FASB Statement No. 157, "Fair value measurements" ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands disclosure requirements of fair value measurement. SFAS No. 157 is applicable to other accounting pronouncements that require or permit fair value measurement, and accordingly, does not require any fair value measurement. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We adopted SFAS No. 157 as of January 1, 2008. The adoption of SFAS No. 157 did not have a material impact on our financial position, results of operations and cash flows.

SFAS No. 157 also established a hierarchy that classifies the inputs used to measure fair value. This hierarchy prioritizes the use of inputs used in valuation techniques into three levels based on observable and unobservable inputs. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of us. Unobservable inputs, which require more judgment, are those inputs described above that reflect management's assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The hierarchyis broken down into three levels based on the reliability of inputs: 'Level 1' – quoted prices in active markets for identical assets or liabilities; 'Level 2' – significant other observable inputs; and 'Level 3' – significant unobservable inputs.

In February 2008, the FASB issued FSP FAS 157-2, "Effective Date of FASB Statement No. 157" ("FSP FAS 157-2"). FSP FAS 157-2 delays the application of SFAS No. 157 for all non-financial assets and liabilities that are measured at fair value on a non-recurring basis. FSP FAS 157-3 is effective for interim and annual periods beginning after November 15, 2008. Therefore, in accordance with the aforementioned FSP, we have only partially applied SFAS No. 157. Beginning January 1, 2009, we will also apply SFAS No. 157 to all non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a non-recurring basis as required by SFAS No. 157.

In October 2008, the FASB issued FSP FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active" ("FSP FAS 157-3"). FSP FAS 157-3 clarifies the application of SFAS No. 157 in a market that is not active and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. FSP FAS 157-3 was effective upon issuance, including prior periods for which financial statements have not been issued, and therefore was effective for the financial statements for the year ended December 31, 2008. The adoption of FSP FAS 157-3 had no material effect on our financial statements.

In February 2007, the FASB issued FASB Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities"—including an amendment of FASB Statement No. 115" ("SFAS No.159"), which permits an entity to measure certain financial assets and financial liabilities at fair value. SFAS No. 159 offers an irrevocable option to carry the vast majority of financial assets and liabilities at fair value, with changes in fair value recorded in earnings (the fair value option, or FVO). The Statement's objective is to improve financial reporting by allowing entities to mitigate volatility in reported earnings caused by the measurement of related assets and liabilities using different attributes, without having to apply complex hedge accounting provisions. SFAS No.159 is effective as of the beginning of an entity's first fiscal year beginning after November 15, 2007. We do not expect that the adoption of SFAS No. 159 will have a material impact on the consolidated financial statements.

In December 2007, the FASB issued FAS No. 141R, "Business Combinations" ("SFAS No. 141R"), and FAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51" ("SFAS No. 160"). These statements substantially elevate the role played by fair value and dramatically change the way companies account for business combinations and noncontrolling interests (minority interests in current GAAP). SFAS No. 141R and SFAS No.160 will require among other changes: (a) more assets acquired and liabilities assumed to be measured at fair value as of the acquisition date; (b) liabilities related to contingent consideration to be re-measured at fair value in each subsequent reporting period; (c) an acquirer to expense acquisition-related costs; and (d) noncontrolling interests in subsidiaries initially to be measured at fair value and classified as a separate component of equity. Both Statements are to be applied prospectively (with one exception related to income taxes) for fiscal years beginning on or after December 15, 2008. However, SFAS No.160 requires entities to apply the presentation and disclosure requirements retrospectively (e.g., by reclassifying noncontrolling interests to appear in equity) to comparative financial statements, if presented. Both standards prohibit early adoption. We are currently evaluating the impact the adoption of SFAS No. 141R and SFAS No. 160 may have on our financial position and results of operations.

In connection with the issuance of SFAS No. 160, the SEC revised EITF Topic D-98 "Classification and Measurement of Redeemable Securities" ("Topic D-98") to include the SEC Staff's views regarding the interaction between Topic D-98 and SFAS No. 160. The revised Topic D-98 indicates that the classification, measurement, and earnings-per-share guidance required by Topic D-98 applies to noncontrolling interests (e.g., when the noncontrolling interest is redeemable at a fixed price by the holder or upon the occurrence of an event that is not solely within the control of the issuer). This includes noncontrolling interests redeemable at fair value. The revisions to Topic D-98 that are specific to accounting for noncontrolling interests should be applied no later than the effective date of SFAS No. 160. We are currently evaluating the impact that adoption of SFAS No. 160 and Topic D-98 will have on the accounting and disclosure of our minority interest.

In March 2008, the FASB issued SFAS No. 161, “Disclosures about Derivative Instruments and Hedging Activities” (“SFAS No. 161”). The new standard is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity’s financial position, financial performance, and cash flows. It is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. We are currently evaluating the potential impact, if any, of the adoption of SFAS No. 161 on our financial position, results of operations and cash flows.

In April 2008, the FASB issued Staff Position (FSP) No. FAS 142-3, “Determination of the Useful Life of Intangible Assets.” The FSP amends the factors an entity should consider in developing renewal or extension assumptions used in determining the useful life of recognized intangible assets under SFAS No. 142 “Goodwill and Other Intangible Assets.” The FSP affects entities with recognized intangible assets and is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. The new guidance applies to (1) intangible assets that are acquired individually or with a group of other assets and (2) both intangible assets acquired in business combinations and asset acquisitions. We are currently evaluating the impact that adoption of the FSP will have on our financial position, results of operations and cash flows.

In November 2008, the FASB issued EITF Issue No. 08-6, “Equity Method Investment Accounting Considerations” (“EITF Issue No. 08-6”). EITF Issue No. 08-6 considers the effects of the issuances of SFAS No. 141R and SFAS No. 160 on an entity’s application of the equity method under Opinion 18, “The Equity Method of Accounting for Investments in Common Stock,” i.e. determination of the initial carrying value of an equity-method investment, impairment assessment of an underlying indefinite-lived intangible asset of an equity-method investment, accounting for issuance of shares by an equity investee, and accounting for a change in an investment from the equity method to the cost method. EITF No. 08-6 is effective for transactions occurring in fiscal years beginning on or after December 15, 2008 and interim periods within those fiscal years. Early adoption is not permitted. We do not expect the adoption of EITF No. 08-6 to have a significant impact on our financial position, results of operations and cash flows.

In November 2008, the FASB issued EITF Issue No. 08-7, “Accounting for Defensive Intangible Assets” (“EITF Issue No. 08-7”). EITF Issue No. 08-7 applies to all acquired intangible assets in situations in which an entity does not intend to actively use the asset but intends to hold (lock up) the asset to prevent others from obtaining access to the asset (a defensive intangible asset), except for intangible assets that are used in research and development activities. The EITF reached a consensus that a defensive intangible asset should be accounted for as a separate unit of accounting and should be assigned a useful life that reflects the entity's consumption of the expected benefits related to the asset, noting that it would be rare for a defensive intangible asset to have an indefinite life. This EITF Issue No. 08-7 is effective for intangible assets acquired on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. We expect EITF Issue No. 08-7 will have an impact on our accounting for future acquisitions of intangible assets once adopted, but the materiality of this impact will depend upon the type of acquisitions we make.

In November 2008, the FASB issued EITF Issue No. 08-6, “Equity Method Investment Accounting Considerations” (“EITF Issue No. 08-6”). EITF Issue No. 08-6 considers the effects of the issuances of SFAS No. 141R and SFAS No. 160 on an entity’s application of the equity method under Opinion 18, “The Equity Method of Accounting for Investments in Common Stock,” i.e. determination of the initial carrying value of an equity-method investment, impairment assessment of an underlying indefinite-lived intangible asset of an equity-method investment, accounting for issuance of shares by an equity investee, and accounting for a change in an investment from the equity method to the cost method. EITF No. 08-6 is effective for transactions occurring in fiscal years beginning on or after December 15, 2008 and interim periods within those fiscal years. Early adoption is not permitted. We do not expect the adoption of EITF No. 08-6 to have a significant impact on its financial position, results of operations and cash flows.

In November 2008, the FASB issued EITF Issue No. 08-7, “Accounting for Defensive Intangible Assets” (“EITF Issue No. 08-7”). EITF Issue No. 08-7 applies to all acquired intangible assets in situations in which an entity does not intend to actively use the asset but intends to hold (lock up) the asset to prevent others from obtaining access to the asset (a defensive intangible asset), except for intangible assets that are used in research and development activities. The EITF reached a consensus that a defensive intangible asset should be accounted for as a separate unit of accounting and should be assigned a useful life that reflects the entity's consumption of the expected benefits related to the asset, noting that it would be rare for a defensive intangible asset to have an indefinite life. This EITF Issue No. 08-7 is effective for intangible assets acquired on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. We expect EITF Issue No. 08-7 will have an impact on its accounting for future acquisitions of intangible assets once adopted, but the effect is dependent upon the acquisitions that are made in the future.

In December 2008, the FASB issued FSP No. 132(R)-1, "Employers' Disclosure about Postretirement Benefit Plan Assets." This FSP provides guidance on an employer's disclosures regarding plan assets of a defined benefit pension or other postretirement plan. The objectives of the disclosures required under this FSP are to provide users of financial statements with an understanding of (a) how investment allocation decisions are made; (b) the major categories of plan assets; (c) the inputs and valuation techniques used to measure the fair value of plan assets; (d) the effect of fair value measurements using significant unobservable inputs on changes in plan assets for the period; and (e) significant concentrations of risk within plan assets. The disclosures about plan assets required by this FSP are required for fiscal years ending after December 15, 2009, and earlier application is permitted. This FSP is not expected to have a material impact on our financial statements.

Off-balance sheet arrangements

Obligations under guarantee contracts

MBRD guaranteed loans for several companies, including related parties, which totaled $125.2 million as of December 31, 2008. EWUB issued guarantees to several companies and individuals, which totaled $16.2 million as of December 31, 2008.

The issued guarantees are recorded at fair value in the accompanying consolidated balance sheet.

These guarantees would require payment by us only in the event of default on payment by the respective debtor. As of December 31, 2008, no event of default has occurred under any of the guarantees issued by us.

Obligations under derivative contracts

In December 2007, Intracom Holdings S.A. entered into a flexible forward agreement with EFG EUROBANK to eliminate the foreign currency exposure risk. At the beginning of 2008, the forward agreement was closed without any impact on cash flow. In January 2008, Intracom Holdings S.A. entered into a second flexible forward agreement with EFG EUROBANK. The arrangements did not qualify for hedge accounting. In relation to these instruments we recorded a loss of $0.2 million for the year ended December 31, 2008.

SITRONICS Telecom Solutions (Czech Republic) – During the year ended December 31, 2008, STS (Czech Republic) recognized a loss of $0.4 million on derivative instruments embedded in other contracts.

Call and put option

Simultaneously with the acquisition of the 25% stake plus one share in Svyazinvest (see Note 26), MGTS Finance S.A. and "2711 Centerville Cooperatief U.A." ("2711 UA"), an affiliate of Mustcom Limited, signed a call and put option agreement, which gives 2711 UA a right to purchase 46,232,000 shares of Comstar UTS, representing 11.06% of total issued shares, from MGTS Finance S.A and sell them back to MGTS Finance S.A. The call option acquired by 2711 UA could be exercised at a strike price of USD 6.97 per share at any time following the signing of the agreement with respect to 10.5% of Comstar UTS' shares. The call option for the remaining 0.56% stake could be exercised at any time beginning from April 1, 2007. The call option was to expire in one year from the date of signing of the agreement. 2711 UA had a right to exercise its put option at any time within two years from the date of exercising the call option at a strike price, which will be calculated based on a weighted average price of Comstar UTS' GDRs during the 90 trading days period preceding the exercise of the put option.

The fair value of the call and put option as of December 11, 2006, the grant date, was estimated at $90.0 million and included in cost of investment in Svyazinvest. We were estimating the fair value of the respective liability using an option pricing model and was re-measuring it as of each balance sheet date. Respective gains and losses were included in the statement of operations for the period.

On December 7, 2007, Access Telecommunications Cooperatief U.A. ("Access", previously known as 2711 UA) has exercised the call option for 46,232,000 shares and paid $322.2 million in cash to the Group.

On August 25, 2008, Access has initiated the process of exercising the put option, and on November 26, 2008 has sold MGTS Finance S.A. 46,232,000 shares of Comstar UTS for the total of $463.6 million, $100.0 million of which had been paid on November 26, 2008 in cash, and the remaining portion had been restructured in the form of an interest-bearing promissory note repayable in four monthly installments.

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, 2008:

	January 1, 2009 - December 31, 2009	January 1, 2010 - December 31, 2010	January 1, 20011 - December 31, 2011	January 1, 2012 - December 31, 2012	January 1, 2013 - December 31, 2013	January 1, 2014 - thereafter	Total
	(Amounts in thousands of USD)						
Contractual obligations:							
Notes payable	853,337	1,355,666	401,063	424,711	8,711	108,344	3,151,832
Bank loans	3,625,583	2,259,245	1,521,072	1,221,990	303,415	212,273	9,143,578
Operating leases and services agreements	309,794	139,692	125,106	118,842	114,588	160,563	968,585
Committed investments:							
Purchases of property, plant and equipment	400,700	0	0	0	0	0	400,700
Construction contracts	203,067	0	0	0	0	0	203,067
Total	5,392,481	3,754,603	2,047,241	1,765,543	426,714	481,180	13,867,762

As of December 31, 2008, MTS had executed non-binding purchase agreements in the amount of approximately $400.7 million to subsequently acquire property, plant and equipment.

In December 2003, MGTS announced its long-term investment program for the period from 2004 to 2012 providing for extensive capital expenditures including expansion and full digitalization of the Moscow telephone network. The program was approved by the resolution of Moscow City Government of December 16, 2003. At the inception of the investment program, capital expenditures were estimated to be approximately $1,600 million and include reconstruction of 350 local telephone stations and installation of 4.3 million of new phone numbers. As a result of implementation of the investment program, new digital equipment will be installed in the buildings housing the telephone nodes, and a substantial amount of floor space will become available after the replacement of analogue switching equipment. The additional free floor space after reconstruction is expected to be sold to third parties or rented out. There are 113 automatic telephone station buildings which are to be reconstructed or rebuilt in the course of the investment program. Currently, the management had not made a decision whether to sell the free floor space created in the course of the investment program or to rent it out.

Sistema-Hals has contracted for construction works and other general construction expenditures under its development project “Leningradsky 39”. Aggregate commitments under these contracts amounted to $181.5 million as of December 31, 2008. In addition, in connection with one of these projects, Sistema-Hals undertook obligations to provide the Central Army Sports Club (“CSCA”) with residential housing. As of December 31, 2008 the remaining obligation amounted to an approximate market value of $34.8 million.

Sistema-Hals has obligations to manage a number of construction projects which will be completed subsequent to the balance sheet date. The Moscow City Government has the obligation to finance these construction projects, with Sistema-Hals generating commissions based on the agreed upon budget cost of the project.

Sistema-Hals additionally has an agreement for reconstruction works of Detsky Mir Lubyanka. Commitment under the contract amounts to $315.8 million.

Other Contingencies

Siemens project. - In 2003, Sistema-Hals entered into a fixed price contract with Siemens to develop an office building in Moscow. During 2006-2008, there was significant growth in the prices of materials, labor and other construction costs. As a result of this, Sistema-Hals is unable to complete the project within the original budget cost estimates. In 2007 Sistema-Hals initiated negotiations with Siemens to revise the contract price to recover the increased costs. Due to the uncertainties connected with the results of the negotiations, Sistema-Hals was not able to reasonably determine or estimate the likely outcome of the project and hence no losses were provided in the financial statements for the year ended December 31, 2007.

In 2008 the negotiations about the contract price continued. The parties discussed the possibility to increase the contract price by the amount sufficient to cover the cost overruns. Ultimately, no agreement was reached. One of the reasons was the worsening economic environment and turmoil in financial and real estate markets. In October 2008 Siemens drew on the guarantee with Deutsche Bank in the amount of the construction advance received by Sistema-Hals from Siemens (EUR 64,000 thousand). This amount was then repaid by Sistema-Hals to Deutsche Bank using financing from JSFC Sistema. In November 2008 construction was suspended.

In the beginning of 2009 the parties agreed to terminate the contract on condition of payment to Siemens of compensation of $25.3 million. As a result we recognized a provision for loss for the contract in this amount. The loss was recorded as a part of operating expenses.

Recent activities

Acquisitions

In April 2009, we acquired controlling stakes in energy companies in the Republic of Bashkortostan from Agidel-Invest LLC, Ural-Invest LLC, Inzer-Invest LLC and Yuryuzan-Invest LLC for the total cash consideration of $2,5 billion. As a result of this transaction, we own a 76.52% stake in ANK Bashneft JSC, a 65.78% stake in Ufaneftechim JSC, a 87.23% stake in Novoil JSC, a 73.02% stake in Ufaorgsintez JSC, a 78.49% stake in Ufimskiy NPZ JSC and a 73.33% stake in Bashkirnefteproduct JSC.

Disposals

In March 2009, we sold a 50% stake in MTT for a total cash consideration of $41.2 million.

In April 2009, we have signed an agreement with JSC VTB Bank ("VTB") to sell a portion of our shares in Sistema-Hals. In accordance with the agreement VTB acquired 19.5% stake in Sistema-Hals for RUR 30 and also received a call option to acquire a further 31.5% stake in the company for RUR 30.

Other

In April 2009, Sistema-Hals completed the placement of its rouble bonds in the amount of RUR 3 billion ($89,6 million). The bonds mature in 2014.

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