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

The following is a discussion of our financial condition and results of operations as of and for the six-month periods ended June 30, 2004 and 2005, and of the material factors that we believe are likely to affect our consolidated financial condition. You should read this section together with our unaudited interim consolidated financial statements for the six-month periods ended June 30, 2004 and 2005, 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 50 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 five segments: Telecommunications; Technology; Insurance; Banking; and Other Businesses (which comprises our real estate, retail, media, travel services and miscellaneous businesses together with our other operations and central corporate functions). Given the scale, scope and market position of our existing operations, we are uniquely positioned to exploit the growth in consumer and corporate purchasing power in the countries in which we operate. Our consolidated revenues reached $3,355.0 million for the six-month period ended June 30, 2005 and $2,428.0 million for the six-month period ended June 30, 2004. Our total assets reached $11,574.6 million as of June 30, 2005, as compared to $7,348.6 million as of June 30, 2004. Net income from continuing operations before cumulative effect of accounting changes was $227.7 million for the six-month period ended June 30, 2005, compared to $206.5 million for the six-month period ended June 30, 2004.

Our revenues and total assets have increased through organic growth, as well as through acquisitions. Our major acquisitions during the six-month period ended June 30, 2005 included the purchase of Barash Communication Technologies, Inc. (BCTI), a leading provider of cellular services in the Republic Turkmenistan, the acquisition of controlling stakes in Mobile TeleSystems Komi, a telecommunication operator in the Komi region, Kvant, a manufacturer of personal computers and computer components, and in several producers of radio and satellite equipment, comprising Yaroslavl Radio Plant and MTU-Saturn. During this period we also increased our ownership shares in MTT, MBRD, Telmos and Gorizont-RT through acquisition of minority holdings and purchase of newly issued stock. Revenue growth in existing businesses for the six-month period ended June 30, 2005 was $671.7 million, or 27.7%. The consolidation of Kvazar-Micro, Uzdunrobita, Gorizont-RT and others in the six-month period ended June 30, 2005 contributed a total of $255.2 million to the increase. The Telecommunications segment's share of the Group's revenues continued to decline, from 87% to 80% period-to-period, as the Group benefited from continued growth across its non-telecom businesses.

We still 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 the six-month periods ended June 2005 and 2004 were $1,033.5 million (including $55.4 million paid for purchase of businesses) and $668.3 million (including $26.0 million paid for purchase of businesses), respectively. We have financed our cash requirements through our operating cash flows, borrowings and the recent initial public offering. Net cash provided by operating activities in the six-month periods ended June 30, 2005 and June 30, 2004 was $584.8 million, and $948.5 million, respectively. The proceeds from long-term borrowings for the respective periods amounted to $878.7 million and $359.3 million. As of June 30, 2005, we had indebtedness of $3,561.9 million, including capital lease obligations, and our interest expense for the six-month period ended June 30, 2005 was $122.5 million, net of amounts capitalized. In February 2005, we raised $1,284.6 million in cash during our initial public offering of 1,550,000 common shares, equivalent to 77,500,000 global depositary receipts (GDRs). Simultaneously with IPO, our certain shareholders sold 42,663 common shares in the form of 2,133,150 GDRs. Additionally, some shareholders further exercised their option to sell additional 238,900 shares in the form of 11,945,000 GDRs. The GDRs on our common stock were admitted to trade on the London Stock Exchange on February 14, 2005.

As a result of continued strengthening of our financial position, rating agencies reviewed our long- term corporate credit ratings in February and March 2005: Fitch upgraded us to "B+" and Standard & Poor's to "BB-" respectively. These agencies also withdrew our ratings from Credit Watch. The rating upgrade reflects the strong performance of the group's telecommunication subdivision, as well as the improved structure of our capital after the IPO.

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 and CIS markets. We employ a disciplined approach to our investment decisions with the aim of maximizing returns for our shareholders. Our internal performance benchmarks require that our businesses achieve certain operational, revenue and profitability targets, which also reflect the nature of these individual businesses. Progress against these targets is monitored and used to develop annual budgets, long-term business plans and capital allocation strategies. Companies that fail to achieve their objectives in a specified time frame generally cease to be beneficiaries of direct investments from JSFC Sistema and, should they continue to fall short of our objectives, may be sold. Similarly, we may dispose of businesses in industries that have largely fulfilled their growth potential.

In the six-month period ended June 30, 2005, 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 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 equity holdings as of June 30, 2005.

Segment	Company	Beneficial ownership[1]	Voting interest[2]
Telecommunications	MTS	51%	51%
	MGTS	46%	56%
	Comstar UTS[3]		
	MTU-Inform	76%	99%
	Comstar	77%	100%
	Telmos	82%	100%
	Sky-Link	42%	50%
	MTT	43%	50%
	Sistema Telecom	100%	100%
Technology	CSC	78%	78%
	Kvazar-Micro	50%	51%
	Mikron	60%	76%
	STROM telecom	52%	67%
	Sitronics	78%	100%
Insurance	ROSNO	49%	51%
Banking	MBRD	95%	99%
	East-West United Bank	49%	49%
Other Businesses			
Real Estate	Sistema-Hals	100%	100%
	Landshaft	100%	100%
Retail	Detsky Mir	75%	75%
	Detsky Mir Center	100%	100%
Mass Media	Sistema Mass Media	90%	90%
	MTU-Intel	87%	100%
	Golden Line	87%	100%
Travel Services	Intourist	72%	72%
International Operations	ECU GEST	100%	100%
Radio and Space Technology	RTI Systems	100%	100%
Pharmaceuticals and Biotechnology	Medical Technological Holding Company	69%	74%

(1) ''Beneficial ownership'' represents the percentage of ownership interests of the relevant entity that are beneficially owned by Sistema, directly or indirectly, based on Sistema's proportionate ownership of the relevant entity through its consolidated subsidiaries. Our ownership interests in the subsidiaries presented above are calculated based on shares owned by us as well as shares owned by certain companies affiliated but not owned by us, which we are required to consolidate under U.S. GAAP (FIN 46R). Excluding the ownership interests of these affiliated companies, our beneficial ownership interests in certain subsidiaries listed above would have been lower by the following amounts: CSC (2.2%), Mikron (1.7%), STROM telecom (1.5%), Sitronics (2.2%), ROSNO (1.6%), MBRD (28.4%), Detsky Mir (4.5%), Sistema-Hals (1.1%) and Landshaft (1.1%).

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

(3) The entities comprising the businesses of Comstar UTS are currently being restructured and combined into a single legal entity. References herein to ''Comstar'' are to our alternative fixed line subsidiary Comstar only.

Macroeconomic Factors Affecting Our Results of Operations

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

	Six months ended June 30,	
	2004	2005
GDP growth	7.4%	5.7%
Consumer price index	6.1%	8.0%
Unemployment rate	7.4%	7.5%
Nominal exchange rate (rubles per U.S. dollar) (1)	29.0	28.0
Real ruble appreciation against U.S. dollar(2)	7.7%	4.5%

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

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

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

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

Acquisitions and Divestitures

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

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

Below is a list of our major acquisitions during the year ended December 31, 2004 and the six-month period ended June 30, 2005.

Company	Principal activity	Date of acquisition	Stake acquired	Acquiring entity	Purchase price[1]
					(in millions)
Year ended December 31, 2004					
SCS-900	Mobile operator in Siberian region	March 2004	11.0%	MTS	$ 8.5
FECS-900	Mobile operator in Far East region	April 2004	40.0%	MTS	8.3
Primtelefon	Mobile operator in Far East region	June 2004	50.0%	MTS	31.0
Kvazar-Micro	Distributor of computer components and System integrator in Ukraine	July 2004	51.0%	ECU GEST	28.0
Uzdunrobita	Mobile operator in Uzbekistan	August 2004	74.0%	MTS	121.2
UDN-900	Mobile operator in Udmurtia Republic	August 2004	49.0%	MTS	6.4
TAIF Telcom	Mobile operator in the Tatarstan Republic and Volga region	September 2004	47.3%	MTS	63.0
MTT	Nationwide transit network operator	September 2004	29.8%	ECU GEST, Hurdsfield	39.8
MTT	Nationwide transit network operator	October 2004	0.2%	Sistema	0.1
Sibintertelecom	Mobile operator in Far East region	November 2004	93.53%	MTS	37.4
Telesot Alania	Mobile operator in the Republic of North Osetia (south of Russia)	December 2004	52.5%	MTS	6.2
Gorizont-RT	Mobile operator in the Republic of Sakha (Yakutia)	December 2004	76.0%	MTS	53.2
					$403.1
Six months ended June 30, 2005					
Telmos	Fixed line operator	February 2005	20.0%	Comstar	$ 8.5
MTS Komi	Mobile operator in Komi Republic	February 2005	74.0%	MTS	1.2
Sweet-Com	Holder of radio frequency	February 2005	74.9%	MTS	2.0
MBRD	Banking	February 2005	13.3%	Sistema	10.0
Kvant	Personal computers and components manufacturer	April 2005	52.8%	Sistemny proekt	6.0
MTU-Saturn	Designer of feeble current electric communications	May 2005	54.2%	Concern RTI	1.5
Barash Communication Technologies, Inc.	Mobile operator in Turkmenistan	June 2005	51.0%	MTS	28.1
Gorizont-RT	Mobile operator in the Republic of Sakha (Yakutia)	June 2005	24.0%	MTS	13.5
Yaroslavl radio plant	Producer of commercial payload for satellites and professional communications facilities	June 2005	51.0%	Concern RTI	6.1
					$ 76.9

(1) Excluding acquisition-related costs.

Recent Acquisitions

In August and October 2005, we effected the acquisition of a 28.17% stake in OJSC Novoil, 25.52% of the shares of OJSC Ufimsky NPZ, 22.43% of the shares of OJSC Ufaneftekhim, 25.00% of the shares of OJSC ANK Bashneft, 24.87% if the shares of OJSC Ufaorgsintez and 18.57% of OJSC Bashnefteproduct. The companies together comprise the majority of the energy sector in the region and are engaged in oil exploration and extraction, oil refining, petrochemical production and energy production and distribution. Taken as a whole, they are Russia's third largest oil refiner. Together with the management of these entities, we plan to build a modern, transparent and vertically integrated holding company, in order to maximize the value of the acquired companies and the entire holding through the implementation of best practice corporate governance, business process engineering and corporate finance activities. All the acquired companies are listed on the Russian Trading System (RTS) stock exchange, and the combined market value of the purchased equity shares on September 30, 2005 exceeded $1,220 million.

In August and September 2005, Detsky Mir acquired a retail network operating under the brand "Vyrastai-ka", a children's toys wholesale company LLC S-Toys (both based in Moscow), and a children's goods retailer CJSC Chudo-Ostrov-Neva based in Saint-Petersburg, for a total cash consideration of $3.0 million. The retail networks operate 4 stores in Moscow and 6 stores in Saint-Petersburg specializing in selling toys for children.

In July 2005, MTS increased its ownership interest in Uraltel to 100% by purchasing the remaining 0.16% stake for $0.1 million. The transaction was completed in compliance with MTS's strategy of consolidation of minority interests in subsidiaries.

In August 2005, Sistema Mass Media acquired Esta group, a leading Russian cable television operator in MMDS standard. Esta group owns cable networks in Tver, Kaluga and several other cities, and provides services to 217 thousand customers. The acquisition was carried out in line with the program of media assets expansion and development.

In September 2005, Comstar completed the purchase of 45% stake in Metrokom, a leading alternative fixed line operator in Saint-Petersburg, for a total cash consideration of $22.5 million, including the refinancing of a loan previously obtained by Metrocom with the support of Antel Holdings Ltd. The stake has been acquired from Antel Holdings Ltd., a subsidiary of MENATEP group. The remaining 55% of Metrocom is held by the Saint-Petersburg City Property Management Committee. The acquisition is expected to enhance Comstar UTS business operations through regional development.

In September 2005, the Group's affiliate Sky Link, issued 9,724,000 additional voting common shares with the par value of 100 RUR each to its shareholders in proportion to their existing shareholdings. The issue was fully paid in the amount equivalent to $34.0 million.

In September 2005, we announced our decision to consolidate our fixed-line telecommunications businesses under Comstar UTS, which will be effected through a merger with our other fixed-line telecommunications subsidiaries MTU-Inform and Telmos. MTU Intel, an internet provider, will become a subsidiary of Comstar UTS. JSFC Sistema will transfer 56% of its shares in MGTS, the incumbent fixed-line telecommunication service provider in Moscow, to Comstar UTS in exchange for new shares in the combined entity. The first legal steps in this consolidation process have been taken with the change in the legal status of CJSC Comstar to OJSC Comstar UTS and the acquisition of 20% stake in Telmos by Comstar UTS from JSFC Sistema. Additionaly, JSFC Sistema's Board of Directors has called an Extraordinary General Meeting of Shareholders in October 2005 to seek approval for the transfer of 56% of its shares in MGTS to OJSC Comstar UTS in exchange for new shares in the combined entity.

Other acquisitions

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

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

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

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

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

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

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

In June 2005, the Group contributed $20.9 million to share capital of MBRD by purchasing 130,000 newly issued shares of MBRD common stock in a closed subscription.

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

Divestitures

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

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

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

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

In January 2005, Intourist announced issue of new stock to its existing shareholders. Moscow Government purchased the first tranche of 3,120,516,875 shares in exchange for a 40% stake in Cosmos Hotel, a 1000-room hotel complex situated in Moscow, with a fair value of the contributed ownership interest of $20.1 million. In April 2005, JSFC Sistema paid an equivalent of $47.7 million for the remaining 6,961,052,632 newly-issued shares of Intourist. Upon completion of this transaction, our ownership interest in Intourist decreased to 72%.

Consolidated Financial Results Overview

The following table sets forth a summary of our financial results for the six-month periods ended June 30, 2005 and June 30, 2004. This financial information should be read in conjunction with our consolidated financial statements.

	Six months ended June 30,			
	2004	**% of revenue**	**2005**	**% of revenue**
	(Amounts in thousands, except percentages)			
Revenues	$ 2,428,045	100.0%	$ 3,354,950	100.0%
Costs of sales, exclusive of depreciation and amortization shown separately below	(879,986)	(36.2)	(1,379,072)	(41.1)
Selling, general and administrative expenses	(413,000)	(17.0)	(574,392)	(17.1)
Depreciation and amortization	(347,848)	(14.3)	(480,590)	(14.3)
Net other operating expenses	(21,267)	(0.9)	(13,531)	(0.4)
Income from equity investees	6,114	0.3	34,356	1.0
Net gain on disposal of subsidiaries	-	-	(452)	(0.0)
Operating income [1]	$ 772,058	31.8%	$ 941,269	28.1%
Interest income	9,616	0.4	35,712	1.1
Interest expense	(108,068)	(4.5)	(122,491)	(3.7)
Income tax	(198,901)	(8.2)	(260,626)	(7.8)
Foreign exchange (loss)/gain	9,084	0.4	(12,157)	(0.4)
Income from continuing operations before minority interests and cumulative effect of accounting changes	$ 483,879	19.9%	$ 581,707	17.3%
Minority interests	(277,333)	(11.4)	(354,052)	(10.6)
Cumulative effect of a change in accounting principle	(35,472)	(1.5)	-	-
Net income	$ 170,984	7.0%	$ 227,655	6.8%
OIBDA [2]	$ 1,119,906	46.1%	$ 1,421,859	42.4%

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

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

The following tables set forth a summary of revenues and operating income by reporting segment for the six-month periods ended June 30, 2004 and June 30, 2005. In our comparison of period-to-period results of operations, in order to analyze changes, developments and trends in revenues by reference to individual segment revenues, we present our revenues on an aggregated basis, which is revenues after elimination of intra-segment (between entities in the same segment) transactions, but before inter-segment (between entities in different segments) eliminations. Amounts attributable to individual companies, where appropriate, are shown prior to both intra-segment and inter-segment eliminations.

Revenues by segment:

	Six months ended June 30,			
	2004	**% of revenue**	**2005**	**% of revenue**
	(Amounts in thousands, except percentages)			
Telecommunications	$ 2,109,134	86.9%	$ 2,680,026	79.9%
Technology	82,990	3.4	426,541	12.7
Insurance	123,866	5.1	197,869	5.9
Banking	27,256	1.1	45,818	1.4
Other Businesses [1]	134,310	5.5	247,438	7.4
Aggregated revenue	$ 2,477,556	102.0%	$ 3,597,692	107.2%
Eliminations [2]	(49,511)	(2.0)%	(242,742)	(7.2)%
Total	$ 2,428,045	100.0%	$ 3,354,950	100.0%

(1) Other Businesses includes our real estate, retail and media businesses together with our other operations and central corporate functions.

(2) Eliminations of inter-segment revenue.

Operating income by segment:

	Six months ended June 30,					
	2004		% of operating income	2005		% of operating income
	(Amounts in thousands, except percentages)					
Telecommunications	$	777,738	100.7%	$	920,523	97.8%
Technology		13,173	1.7		109,942	11.7
Insurance		4,925	0.6		13,640	1.4
Banking		6,966	0.9		3,141	0.3
Other Businesses [1]		(18,700)	(2.4)		(3,940)	(0.4)
Aggregated revenue	$	784,102	101.6%	$	1,043,306	110.8%
Eliminations [2]		(12,044)	(1.6)%		(102,037)	(10.8)%
Total	$	772,058	100.0%	$	941,269	100.0%

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

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

Revenues

Our aggregated revenues increased by 45.2% to $3,597.7 million for the six-month period ended June 30, 2005 from $2,477.6 million for the six-months period ended June 30, 2004.

The growth in our revenues was attributable to the growth in our Telecommunications Segment of $570.9 million, in our Technology Segment of $343.6 million, in our Insurance Segment of $74.0 million, in our Banking Segment of $18.6 million and in our Other Businesses Segment of $113.1 million.

Growth in revenues for the six-month period ended June 30, 2005 compared with the six-month period ended June 30, 2004 was primarily due to organic growth, as well as to acquisitions made subsequent to June 30, 2004, including Kvazar-Micro, Sibintertelecom, Gorizont-RT and Uzdunrobita, the results of operations of which were not included in our consolidated financial statements for the six-month period ended June 30, 2004. The consolidation of Kvazar-Micro, Sibintertelecom, Gorizont-RT and Uzdunrobita contributed $163.4 million, $16.8 million, $16.2 million and $37.9 million, respectively, to the increase in aggregated revenues for the six-month period ended June 30, 2005. From our existing businesses, growth in our consolidated revenues for the six-month period ended June 30, 2005 amounted to $671.7 million, or 72.5% of the overall growth.

The Telecommunications Segment continued to be the largest revenue contributor for the six-month period ended June 30, 2005, though its share of the aggregated revenues decreased to 79.9% from 86.9% for the six-month period ended June 30, 2004 owing to accelerated growth and significant acquisitions in our other segments. In the six months ended June 30, 2005, MTS and MGTS were the largest contributors to the growth of the Telecommunications Segment revenue. Revenues of MTS and MGTS grew by $546.1 million (inclusive the effects of the acquisitions of Sibintertelecom, Gorizont-RT and Uzdunrobita), and $82.0 million, or by 31.3% and 36.2%, respectively, compared to the six months ended June 30, 2004. This increase was primarily due to the significant growth in MTS' subscriber base from 22.8 million as of June 30, 2004 to 44.1 million as of June 30, 2005. The increase in MGTS' revenues is primarily explained by the rise in subscription fees for residential and corporate subscribers that took effect in October 2004.

The increase in revenues of our Technology Segment was attributable to the organic growth of STROM telecom and Sitronics, as well as to the acquisition of Kvazar-Micro in July 2004. Revenues of STROM telecom and Sitronics for the six-month period ended June 30, 2005 increased by $126.6 million and $17.5 million, or by 320.1% and 219.6%, respectively, compared with the six-month period ended June 30, 2004. Revenues of STROM telecom increased mainly owing to sales of new billing systems to MTS and MGTS. Revenues of Sitronics increased as a result of increased production of consumer electronics under the Sitronics umbrella brand. The consolidation of Kvazar-Micro contributed $178.4 million to the increase in revenues of our Technology Segment for the six-month period ended June 30, 2005.

Revenues from our Insurance Segment grew by 59.7% for the six months ended June 30, 2005, compared with the six months ended June 30, 2004 due to ROSNO's promotion of new insurance products and the expansion of its client base following the overall growth of the insurance market in Russia and acquisition of new subsidiaries.

Our mass media, radio and retail businesses were the largest contributors to the organic growth in our Other Businesses Segment, with an increase in revenues of $5.8 million, $7.8 million and $10.4 million, respectively, for the six months ended June 30, 2005, compared with the same period in 2004. Our real estate business revenues decreased by $13.0 million as there were no sales of completed office buildings or residential property in the six month period ended June 30, 2005. The revenues of our tourism business have grown primarily due to an increase in the number of tourists, both inbound and outbound, served during the six months ended June 30, 2005 compared to six months ended June 30, 2004. The remaining part of the increase in revenues of our other businesses is attributable to the expansion of media business through commencement of operations in Ukraine and transfer of control over MTU-Intel and Golden Line, formerly accounted for in Telecommunications Segment, to mass media business.

Operating costs

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

For the six-month period ended June 30, 2005, our cost of sales increased as a percentage of revenues to 41.1% from 36.2% for the six-month period ended June 30, 2004, primarily as a result of the growth of operations in other segments which have significantly lower margins in comparison to Telecommunications segment, while the change in the cost of sales, as percentage of revenues, in our Telecommunications segment was insignificant. MTS experienced a slight growth in cost to sales ratio to 30.0% in the six months ended June 30, 2005 from 28.7% in the six months ended June 30, 2004, resulting from pursuing an aggressive marketing policy aimed at attraction of new subscribers.

Our selling, general and administrative expenses were 17.1% of revenue for the six-month period ended June 30, 2005 and 17.0% of revenue for the six-month period ended June 30, 2004. Depreciation and amortization remained at a constant level of 14.3% of revenues in the six-month period ended June 30, 2005 and in the six-month period ended June 30, 2004.

Operating income

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

Our consolidated operating income margin comprised 28.1% of revenues for the six-month period ended June 30, 2005, compared with 31.8% of revenues for the same period ended June 30, 2004. MTS continued to be the main contributor to the operating margin with $788.6 million, or 83.8% of aggregated operating income, for the six-month period ended June 30, 2005.

Interest

Our consolidated interest expense for the six-month period ended June 30, 2005 increased by 13.3% to $122.5 million from $108.1 million for the six-month period ended June 30, 2004, primarily owing to an increase in our debt related to Sistema Capital's issuance of $350.0 million notes in January 2004, partially offset by the repayment of MTS' Floating Rate Notes in May 2004 for the amount of $300.0 million. In July 2004, MTS entered into a $500.0 million syndicated loan agreement with international financial institutions. In September 2004, MTS extended total amount available under the syndicated loan facility for an additional $100.0 million to total amount of $600.0 million. In January 2005, MTS Finance issued $400 million unsecured notes and in March 2005, MBRD entered into a loan facility with Dresdner Bank AG for the amount of $150 million.

Income tax

Our consolidated provision for income taxes for the six-month period ended June 30, 2005 increased by 31.0% to $260.6 million from $198.9 million for the six-month period ended June 30, 2004 following the increase of our pre-tax income. Our effective tax rate for the six-month period ended June 30, 2005 increased to 30.9%, compared to 29.1% for the year ended June 30, 2004 mainly as a result of the relatively higher amount of non-deductible expenses as a percentage of pre-tax income incurred during the six-month period ended June 30, 2005 as compared with the six-month period ended June 30, 2004.

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

Consolidated net income from continuing operations prior to minority interest and cumulative effect of accounting changes increased by 20.2% to $581.7 million for the six-month period ended June 30, 2005 from $483.8 million for the six-month period ended June 30, 2004. To arrive at this measure, we add interest income and foreign exchange gain to, and deduct interest expense and income taxes from, operating income. Net income margin from continuing operations prior to minority interests and cumulative effect of accounting changes was 17.3% for the six-month period ended June 30, 2005, compared with 19.9% for the six-month period ended June 30, 2004.

Minority interests

Minority interests in net income of our subsidiaries for the six-month period ended June 30, 2005 increased to $354.1 million from $277.3 million for the six-month period ended June 30, 2004 primarily due to the increase of net income attributable to MTS.

Segment Financial Results Overview

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

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

Telecommunications

We divide our Telecommunications Segment into two divisions: wireless services (MTS and its subsidiaries) and fixed line communications (MGTS and Comstar UTS).

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

	Six months ended June 30,			
	2004	**% of revenues**	**2005**	**% of revenues**
Revenues	$ 2,109,134	100.0%	$ 2,680,026	100.0%
Costs of sales, exclusive of depreciation and amortization shown separately below	(671,144)	(31.8)	(855,560)	(31.9)
Selling, general and administrative expenses	(323,672)	(15.4)	(454,767)	(17.0)
Depreciation and amortization	(341,054)	(16.2)	(462,515)	(17.3)
Net other operating income/(expenses)	(903)	(0.0)	(18,154)	(0.7)
Income from equity investees	5,677	0.3	31,493	1.2
Operating income	$ 777,738	36.9%	$ 920,523	34.3%
OIBDA [(1)]	$ 1,118,792	53.1%	$ 1,383,038	51.6%

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

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

Revenues

Telecommunications Segment revenues increased by 27.1% for the six-month period ended June 30, 2005 to $2,680.0 million compared to $2,109.1 million for the six-month period ended June 30, 2004. MTS and MGTS were the principal contributors to the growth, with an increase in revenues of $546.1 million and $82.0 million, respectively. The increase in revenues was partially offset by the effects of transfers of control over MTU-Intel and Golden Line from Telecommunications Segment to mass media business and over Mediatel to Technology Segment of approximately $17.9 million and $15.4 million, respectively.

Wireless services

Revenues of MTS for the six-month period ended June 30, 2005 were $2,293.6 million, an increase of 31.3% compared to $1,747.5 million for the six-month period ended June 30, 2004. This increase was primarily attributable to the significant growth in MTS' subscriber base from 22.8 million as of June 30, 2004 to 44.1 million as of June 30, 2005, including 34.1 million in Russia, 9.5 million in Ukraine, 0.4 million in Uzbekistan and 0.1 million in Turkmenistan. The growth was attributable to MTS' sales and marketing efforts and the expansion of its network, as well as improving general economic conditions and income levels in Russia and Ukraine. The increase in revenues from subscriber growth was partially offset by a decrease in tariffs in the Moscow license area and other highly competitive license areas, an increase of mass-market subscribers in MTS' subscriber mix and its continuing expansion into the regions of Russia outside the Moscow license area where tariffs are lower. As a result, average monthly service revenue per subscriber in Russia decreased by 35.7% from $14 per subscriber for the six-month period ended June 30, 2004 to $9 per subscriber for the six-month period ended June 30, 2005.

For the six-month period ended June 30, 2005, MTS' service revenues and connection fees increased by $553.6 million, or by 32.4%, to $2,261.5 million from $1,707.9 million for the six-month period ended June 30, 2004 due to growth in the number of its subscribers, as explained above. Revenues from sales of handsets and accessories decreased by $7.5 million, or 19.0%, for the six-month period ended June 30, 2005, compared to the six-month period ended June 30, 2004, due to decline in the average selling price for handsets.

Fixed line communications

MGTS' revenues grew by 36.2% in the six-month period ended June 30, 2005 to $308.3 million, compared to $226.3 million for the six-month period ended June 30, 2004. Revenues from monthly subscription fees increased by 37.9% in the six-month period ended June 30, 2005, compared to the same period in 2004, and reached $156.8 million. This increase was primarily due to an increase in monthly subscription fees for residential and government subscribers effective October 2004. The number of active lines was 4.2 million both as of June 30, 2005 and 2004. Revenues from local traffic fees, service activation fees and line rentals increased by 23.4% compared to the six-month period ended June 30, 2004, to $87.8 million.

MGTS is not licensed to provide domestic long distance, international long distance or DLD/ILD telecommunications services directly to its subscribers, but must route such traffic through a DLD/ILD licensed operator. As a result, DLD/ILD traffic originated by MGTS subscribers is carried by Rostelecom, which bills MGTS subscribers directly. MGTS has a revenue sharing agreement with Rostelecom pursuant to which Rostelecom pays MGTS a portion of the DLD/ILD revenues generated by MGTS customers. This amount is periodically revised. MGTS' revenues from Rostelecom amounted to $13.5 million for the six-month period ended June 30, 2005, compared to $14.5 million for the six-month period ended June 30, 2004.

Revenues of MTU-Inform slightly increased in the six-month period ended June 30, 2005 compared to the six-month period ended June 30, 2004 and were $49.0 million compared to $48.9 million for the same period in 2004, as a result of a moderate growth of business offset by a decrease in tariffs on services provided to mobile operators.

Telmos' revenues grew by 11.4%, to $25.4 million, for the six-month period ended June 30, 2005, compared with $22.8 million for the six-month period ended June 30, 2004. The increased traffic from fixed line operators contributed to revenue growth. The number of active lines in service slightly decreased to 67,106 as of June 30, 2005, from 67,983 as of June 30, 2004.

Comstar's revenues increased by 53.3% to $52.5 million for the six-month period ended June 30, 2005 from $34.3 for the six-month period ended June 30, 2004 as a result of growth in the number of active lines to 112,863.

Operating income

The operating income margin of the Telecommunications Segment was 35.4% in the six-month period ended June 30, 2005, compared to 36.9% in the six-month period ended June 30, 2004. This decline was primarily attributable to the decrease in the operating income margin of MTS.

Wireless services

MTS' operations contributed $788.6 million to our operating income from wireless services for the six-month period ended June 30, 2005.

MTS' operating income margin was 34.4% for the six-month period ended June 30, 2005, compared to 40.2% for the six-month period ended June 30, 2004. The decrease in MTS' operating income margin is due to increased cost of sales, advertising and marketing expenses and depreciation and amortization expenses as a percentage of revenues.

Fixed line communications

MGTS' operating income margin for the six-month period ended June 30, 2005 was 33.9%, compared to 20.8% for the six-month period ended June 30, 2004, primarily due to increase in tariffs. Operating costs increased by $26.7 million, or 15.1%, for the six-month period ended June 30, 2005.

MTU-Inform's operating income margin decreased to 31.7% for the six-month period ended June 30, 2005, compared with 43.2% in the same period in 2004. The lower operating income margin in the six-month period ended June 30, 2005 was attributable primarily to the significantly increased tariffs charged to MTU-Inform, especially by MGTS, while tariffs charged to mobile operators were unchanged.

Comstar's operating income was $1.9 million for the six-month period ended June 30, 2005 compared to operating income of $2.7 million for the six-month period ended June 30, 2004. The decrease is mostly explained by an increase in personnel costs owing to the transfer of employees from MTU-Inform and Telmos to Comstar as a part of the reorganization process to form Comstar UTS.

Telmos' operating income increased to $4.9 million for the six-month period ended June 30, 2005, compared to an operating income of $3.0 million in the same period of 2004 as a result of proceeds from insurance company following damage to its equipment and temporary disruption of services caused by a fire in 2003. Telmos' operating margin was 46.8% in the six-month period ended June 30, 2005.

Income from equity investees

Income from equity investees accounted for $31.5 million and $5.7 million for the six-month periods ended June 30, 2005 and and June 30, 2004, respectively. The increase in income from equity investees is primarily caused by the increase in the net income of MTS Belarus and growth of ownership interest in MTT, contributing $17.5 and $14.0 million, respectively, for the six-month period ended June 30, 2005.

Technology

As of June 30, 2005, our subsidiaries in the Technology Segment operated along four main divisions: telecommunications equipment manufacturing and software (STROM telecom, its subsidiaries and Mediatel), semiconductor design and manufacturing (Mikron, VZPP-Mikron, NIITM), electronic devices and consumer electronics (Sitronics, Elion, Elaks, Kvant and Koncel) and IT and systems integration (Kvazar-Micro). We added the fourth business division, IT and systems integration, in July 2004 through our acquisition of Kvazar-Micro, a company based in Ukraine with a presence throughout Eastern Europe. Kvazar-Micro, STROM telecom and Micron were the largest sources of revenue in the Technology Segment for the six-month period ended June 30, 2005.

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

	Six months ended June 30,			
	2004	% of revenue	2005	% of revenue
Revenues	$ 82,990	100.0%	$ 426,541	100.0%
Costs of sales, exclusive of depreciation and amortization shown separately below	(54,692)	(65.9)	(294,979)	(69.2)
Selling, general and administrative expenses	(12,640)	(15.2)	(16,317)	(3.8)
Depreciation and amortization	(1,032)	(1.2)	(5,462)	(1.3)
Net other operating expenses	(1,453)	(1.8)	159	0.0
Operating income	13,173	15.9%	109,942	25.8%
OIBDA (1)	14,205	17.1%	115,404	27.1%

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

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

Revenues

The revenues of our Technology Segment increased by $343.6 million, or by 414.0%, to $426.5 million for the six-month period ended June 30, 2005. The acquisition of a controlling stake and consolidation of Kvazar-Micro revenues contributed $178.4 million to the increase of our Technology Segment revenues for the six-month period ended June 30, 2005. Exclusive of the effects of the Kvazar-Micro acquisition, segment revenues would have increased by $165.2 million, or 199.0%, for the six months ended June 30, 2005. Revenues of the telecommunications equipment manufacturing and software division grew by 320.1% to $166.1 million, or 66.9% of the total segment revenues, net of the effects of the Kvazar-Micro acquisition, in the six-month period ended June 30, 2005, compared to $39.5 million, or 47.6% of the segment revenues in the six-month period ended June 30, 2004. The increase of revenues in the telecommunications equipment manufacturing and software division was primarily attributable to the sales of new billing systems to MTS and MGTS. Revenues of the telecommunications equipment manufacturing and software division for the six-month period ended June 30, 2005 include revenues of Mediatel, which was part of Telecommunications Segment in the six months ended June 30, 2004. Mediatel contributed $13.3 million to revenues of telecommunications equipment manufacturing and software division for the six months ended June 30, 2005. Revenues of the semiconductor design and manufacturing division insignificantly decreased by 1.1% to $27.3 million, or 11.1% of segment revenues, net of the effects of the Kvazar-Micro acquisition and intra-segment sales, in the six-month period ended June 30, 2005 compared to $27.6 million, or 33.2% of the segment revenues in the six-month period ended June 30, 2004. The electronic devices and consumer electronics division demonstrated considerable growth in the six-month period ended June 30, 2005, with revenues increasing to $59.0 million, or 23.8% of the segment revenues, net of the effects of the Kvazar-Micro acquisition, from $15.9 million, or 19.2% of the segment revenues, for the same period in 2004. The increase of revenues in the electronic devices and consumer electronics division was a result of the increased sales of consumer electronics under the Sitronics umbrella brand during the six-month period ended June 30, 2005, following the extensive advertising campaign.

Operating income

Operating income increased to $109.9 million, or 25.8% of segment revenues, for the six-month period ended June 30, 2005 from an operating income of $13.2 million in the same period of 2004. The consolidation of the low-margin Kvazar-Micro business contributed $2.6 million to the operating income for the six months ended June 30, 2005. The increase in operating income was primarily attributable to the sales of telecommunications equipment to our Telecommunication Segment. Telecommunications equipment manufacturing and software division continued to be the main contributor to the operating margin with $94.7 million, or 86.2% of aggregated operating income, for the six-month period ended June 30, 2005. For the same period in 2004 operating income of Telecommunications equipment manufacturing and software division was $14.1 million or 106.8% of aggregated operating income. Electronic devices and consumer electronics division and Semiconductor design and manufacturing division contributed $3.8 million and $12.0 million to our operating income for the six-month period ended June 30, 2005 compared to operating loss of $0.5 and $0.4 million for the six-month period ended June 30, 2004, respectively. Net of the effects of the Kvazar-Micro acquisition, cost of sales increased by 128.6%, to $125.0 million, for the six-month period ended June 30, 2005 compared to $54.7 million for the same period in 2004. Selling, general and administrative expenses decreased as a percentage of sales, net of the effects of the Kvazar-Micro acquisition, to 4.1% for the six-month period ended June 30, 2005 from 15.2% for the same period in 2004 mainly due to the increased volume of production and sales and improved cost efficiency.

Insurance

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

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

	Six months ended June 30,			
	2004	% of revenues	2005	% of revenues
Revenues from financial services	$ 123,866	100%	$ 197,869	100%
Financial services related costs, exclusive of depreciation and amortization shown separately below	(85,902)	(69.4)	(145,176)	(73.4)
Selling, general and administrative expenses	(31,733)	(25.6)	(38,953)	(19.7)
Depreciation and amortization	(1,929)	(1.6)	(1,871)	(0.9)
Other operating income	468	0.4	1,464	0.7
Gain from equity investees	155	0.1	307	0.2
Operating income	$ 4,925	4.0%	$ 13,640	6.9%

Voluntary medical insurance, motor own damage insurance and property insurance historically have been the largest contributors to our gross premiums written, or GPW. However, the share of voluntary medical insurance, a major component of the total GPW, was decreasing throughout the year ended December 31, 2004 and the six-month period ended June 30, 2005, from 36% in the six-month period ended June 30, 2004 to 26% in the six-month period ended June 30, 2005. Revenues from obligatory motor third party liability policies slightly decreased from 9.5% of total GPW in the six-month period ended June 30, 2004 to 8.8 % in the six months ended June 30, 2005. Motor own damage insurance increased from 12.5% to 13.8% of total GPW in the six-month period ended June 30, 2005 as compared to the same period in 2004. Revenues from property insurance increased from 11.1% of the total GPW for the six-month period ended June 30, 2004 to 40.7% for the six-month period ended June 30, 2005. GPW for non-life insurance products is equal to the total gross premiums to be paid over the term of the insurance policies issued by ROSNO during the period, while GPW for life insurance is equal to premiums due under the policies during the period. Premiums for non-life insurance are recorded as revenue primarily on a pro-rata basis over the terms of the related policies whereas life insurance premiums are recognized as revenue when due from the policyholder.

The adjustments necessary to reconcile GPW to revenue derived from the relevant policies are set forth in change in provision in unearned premiums, net of reinsurance, in the table below.

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

	Six months ended June 30,	
	2004	**2005**
	(Amounts in thousands)	
Voluntary medical insurance	72,578	82,583
Motor third-party liability	793	1,278
Motor own damage insurance	25,117	44,016
Property	22,302	129,299
General third-party liability	2,271	4,452
Marine, aviation and transport	5,136	9,935
Personal accident	2,596	4,288
Other non-life liability	4,265	7,173
Life insurance	631	2,179
Obligatory motor third-party liability	19,203	28,093
Reinsurance inward	46,568	4,609
Total gross premiums written	201,460	317,905
Reinsurance outwards	(19,848)	(70,839)
Change in provision in unearned premiums, net of reinsurance	(71,407)	(63,876)
Net premiums earned	110,205	183,190
Commission income	3,402	1,550
Medical services income	3,954	5,324
Net gains/(loss) on operations with securities	3,657	498
Interest income	521	6,352
Other income	2,127	955
Total revenue	$123,866	$197,869

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

Revenues

In the six-month period ended June 30, 2005, our Insurance Segment revenues grew by $74.0 million, or 59.7%, compared to the six-month period ended June 30, 2004. Voluntary medical insurance, motor own damage and property insurance together accounted for $255.9 million, or 80.5%, of GPW for the six-month period ended June 30, 2005. GPW on obligatory motor third-party liability insurance accounted for $28.1 million, or 8.8%, of our GPW for the six-month period ended June 30, 2005.

GPW on property insurance increased to $129.3 million for the six-month period ended June 30, 2005, or by 479.8%, compared to $22.3 million for the six-month period ended June 30, 2004, primarily due to the consolidation of operations of Leader which we acquired from RAO UES in October 2004. As a result, GPW on energy business (being a part of property insurance in the six month period ended June 30, 2005) grew from $44.0 million in the six-month period ended June 30, 2004 (being a part of reinsurance inward then) to $93.7 million in the same period of 2005.

Overall, GPW increased by 57.8%, to $317.9 million in the six-month period ended June 30, 2005, in comparison with $201.5 million in the six-month period ended June 30, 2004 owing to insurance business expansion and new subsidiaries purchased.

Operating income

As a result of the growth of ROSNO's business, the operating income of our Insurance Segment increased to $13.6 million in the six-month period ended June 30, 2005 from $4.9 million in the six-month period ended June 30, 2004. The operating income margin increased to 6.9% in the six-month period ended June 30, 2005 from 4.0% in the six-month period ended June 30, 2004. General and administrative expenses of the Insurance segment increased to $39.0 million in the six-month period ended June 30, 2005 from $31.7 million in the six-month period ended June 30, 2004 primarily due to an increase in payroll costs and advertising and marketing expenses.

Total assets

The total assets of our Insurance Segment increased to $608.5 million as of June 30, 2005 from $324.2 million as of June 30, 2004, or by 87.7%. This growth is primarily attributable to an increase in cash and bank deposits of $89.7 million, in receivables from insurance operations of $64.6 million, and in loans and notes receivable of $117.4 million.

Banking

Our Banking Segment is represented by MBRD, which provides a broad range of services. Historically, MBRD mainly performed treasury functions for companies in or related to our consolidated group. Accordingly, MBRD's revenues are primarily derived from our subsidiaries and related parties. We are currently focusing on developing and expanding MBRD's retail banking business in Moscow and major cities throughout Russia. As of June 30, 2005, MBRD operated in Moscow and in six additional regions, as compared to four regions besides Moscow as of June 30, 2004. The volume of revenues from our subsidiaries and related parties as a percentage of total MBRD revenues was declining throughout the year ended December 31, 2004 and the six-month period ended June 30, 2005 as a consequence of the expansion of third-party operations.

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

	Six months ended June 30,			
	2004	% of revenues	2005	% of revenues
	(Amounts in thousands, except percentages)			
Revenues from financial services	$ 27,256	100%	$ 45,818	100%
Including:				
Revenues from consolidated companies	9,165	33.6	12,770	27.9
Revenues from related parties	942	3.5	1,459	3.2
Financial services related costs, exclusive of depreciation and amortization shown separately below[(1)]	(16,782)	(61.6)	(28,360)	(61.9)
Selling, general and administrative expenses	(3,675)	(13.5)	(13,312)	(29.1)
Depreciation and amortization	(533)	(2.0)	(1,005)	(2.2)
Income from equity investees	700	2.6	-	-
Operating income	$ 6,966	25.6%	$ 3,141	6.9%

(1) Includes interest expense on deposits.

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

Revenues

For the six-month period ended June 30, 2005, compared with the six-month period ended June 30, 2004, MBRD's revenues increased by 68.1%, to $45.8 million. Interest income grew by $12.1 million in the six-month period ended June 30, 2005 and amounted to $38.7 million. This growth was primarily attributable to interest on loans to customers. As of June 30, 2005, loans to customers, net of allowances for loan losses, increased by 58.4% compared with June 30, 2004 to $476.5 million, including $202.0 million, or 42.4%, of inter-company loans and $27.8 million, or 5.8%, of loans to our related parties. As of June 30, 2005, the weighted average interest on inter-company loans was 11.6% on U.S. dollar-denominated loans (which totaled $136.3 million) and 12.7% for ruble-denominated loans (which totaled $65.7 million). The weighted average interest rate on U.S. dollar-denominated loans to related parties was 11.5% (which totaled $24.4 million) and 11.0% for ruble-denominated loans (which totaled $3.4 million). Loans to third-party customers, net of allowance for loan losses, increased by $139.2 million to $246.7 million as of June 30, 2005 as compared to $107.5 million as of June 30, 2004. The weighted average interest rate on loans to third-party customers was 12.2% for ruble-denominated loans and 12.2% for U.S. dollar-denominated loans as of June 30, 2005.

Non-interest income increased to $7.1 million in the six-month period ended June 30, 2005 from $0.7 million in the six-month period ended June 30, 2004 primarily due to the growth in commissions received and gain from trading securities and foreign currency operations.

Operating income

Banking Segment's operating income amounted to $3.0 million in the six-month period ended June 30, 2005, compared to $7.0 million for the same period in 2004, mostly due to an increase in the volume of MBRD's operating expenses following the expansion of retail business and interest accrued on additional debt.

Selling, general and administrative expenses as a percent of revenues increased to 29.1% in the six-month period ended June 30, 2005 from 13.5% in the same period of 2004 as a result of increased workforce and other costs related to roll-out of retail operations.

Total assets

Total assets of the Banking Segment increased to $983.6 million as of June 30, 2005 from $460.9 million as of June 30, 2004 primarily owing to the increase in loans issued to banks to $263.0 million as of June 30, 2005 compared to $69.6 million as of June 30, 2004, and in loans to customers, net of allowance for loan losses, to $476.5 million as of June 30, 2005 compared to $300.9 million as of June 30, 2004. In March 2005, MBRD secured additional financing for the amount of $150.0 million through a loan from Dresdner Bank AG, which issued respective loan participation notes admitted to trade on the Luxembourg Stock Exchange. These additional funds allowed MBRD to expand its' loan portfolio.

Other Businesses

In this segment we include our real estate, retail, media, travel services and miscellaneous businesses, as well as operations of our parent company, Sistema. Thus, costs of our corporate function (other than Sistema Telecom) are included in the operating costs of this segment. These costs amounted to $12.9 million for the six-month period ended June 30, 2005, compared to $11.3 million in the same period of 2004.

	Six months ended June 30,			
	2004	% of revenues	2005	% of revenues
	(Amounts in thousands, except percentages)			
Revenues	$ 134,310	100.0%	$ 247,436	100.0%
Cost of sales, exclusieve of depreciation and amortization shown separately below	(80,397)	(59.9)	(173,135)	(70.0)
Selling, general and administrative expenses	(49,523)	(36.9)	(73,674)	(29.8)
Depreciation and amortization	(3,300)	(2.5)	(9,737)	(3.9)
Net other operating (expenses)/income	(19,372)	(14.4)	3,066	1.2
(Loss)/income from equity investees	(418)	(0.3)	2,556	1.0
Net loss on disposal of subsidiaries	-	-	(452)	(0.2)
Operating income/(loss)	$ (18,700)	(13.9)%	$ (3,940)	(1.6)%

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

We operate our retail business through Detsky Mir, the largest retailer of children's goods in Russia. Detsky Mir is among the most recognized brands in Russia. As of June 30, 2005, we operated twelve stores in Moscow, including the flagship Detsky Mir store in central Moscow, and five stores outside of Moscow with a total retail space of 47,971 sq.m. We plan to expand Detsky Mir by opening new stores in Moscow and other Russian cities and to undertake a significant refurbishment of our flagship store.

We operate our media businesses mainly through Sistema Mass Media, a holding company that is active in three main areas: advertising, print distribution and other media, which includes a number of companies that operate in other segments such as publishing, film production and news services. Following a strategic review of our media assets in 2003, we are primarily focused on developing distribution platforms and content for pay-TV and multi-media services initially in Moscow and subsequently in other parts of Russia. In the six-month period ended June 30, 2005, MTU-Intel (a provider of internet access services) and its subsidiary Golden-Line, previously included in Telecommunications segment, operated as a part of our mass media businesses.

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.

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

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

Revenues

Total operating revenues of the Other Businesses Segment increased to $247.4 million for the six-month period ended June 30, 2005, compared to $134.3 million for the six-month period ended June 30, 2004.

Real estate revenues decreased by $13.0 million, to $10.9 million, for the six-month period ended June 30, 2005 compared to the same period in 2004. The reason for the decrease is the continued construction of real estate projects during the six months ended June 30, 2005, which resulted in no sales of completed premises in that period.

In our retail business, revenues increased by 49.7%, to $45.2 million, for the six-month period ended June 30, 2005 from $30.2 million for the six-month period ended June 30, 2004. The increase was mostly generated by revenues of our new retail outlets.

Mass media revenues increased to $93.5 million, or by 360.2%, during the six-month period ended June 30, 2005 compared to $20.3 million in the six-month period ended June 30, 2004, primarily due to an increase in print distribution revenues. In addition, $42.5 million and $8.7 million in the total revenues relate to MTU-Intel and Golden Line respectively, which previously were included in our Telecommunication segment. In addition, we commenced operations in Ukraine through establishing direct subsidiaries, Maxima Kiev and Lingway, which contributed $1.7 million and $13.5 million, respectively, to the total revenues of mass media business.

MTU-Intel's revenues increased by 45.5%, from $29.2 million for the six-month period ended June 30, 2004 to $42.5 million for the same period in 2005, owing to the growth in the number of active subscribers of ADSL Internet services. In February 2004, MTU-Intel introduced a new residential focused brand, STREAM, and later reduced ADSL tariffs by 50%, which increased the number of subscribers as of June 30, 2005 by 598.1% to 180,568, as compared to June 30, 2004.

The total operating revenues of our travel services business for the six-month period ended June 30, 2005 were $37.6 million compared with $35.3 million for the six-month period ended June 30, 2004, representing growth of 6.3%. During the six-month period ended June 30, 2005, the number of inbound tourists served decreased to 57,639 or by 17.6% compared to the six-month period ended June 30, 2004, while the number of outbound tourists decreased to 29,275, or by 13.1%, compared to the six-month period ended June 30, 2004. The growth in revenues simultaneously with the decline in the number of clients is explained by relatively higher prices on travel services in the six-month period ended June 30, 2005 compared with the six-month period ended June 30, 2004.

Operating loss

In the Other Businesses Segment, operating losses decreased during the six-month period ended June 30, 2005 to $3.9 million from $18.7 million in the six-month period ended June 30, 2004, due to significant charity expenses of $16.4 million incurred by our corporate office during the six-month period ended June 30, 2004.

In the real estate business, operating income for six-month period ended June 30, 2005 decreased to $3.2 million, from $7.9 million in the same period of 2004. The decrease resulted from completion and sale of real estate projects during the six-month period ended June 30, 2004 and the absence of such sales owing to continued construction in the six months ended June 30, 2005.

In our retail business, operating income during the six-month period ended June 30, 2005 increased to $3.8 million, compared with $2.2 million in the six-month period ended June 30, 2004, as a result of an increase in the number of retail outlets.

In the media business, our operating income during the six-month period ended June 30, 2005 increased to 0.5% of total revenue, or $0.5 million, from an operating loss of $2.0 million in the six-month period ended June 30, 2004. This trend is explained by the inclusion of MTU-Intel in mass media operations with an operating income of $2.9 million in the six-month period ended June 30, 2005.

In our travel services business, operating income, as a percentage of revenues, insignificantly decreased to 2.0% during the six-month period ended June 30, 2005, compared to an operating income of 3.7% in the six-month period ended June 30, 2004.

Telecommunications Operating Data

Our revenues and operating income for the six-month periods ended June 30, 2005 and 2004 were influenced by trends in the principal businesses included in our Telecommunications Segment: MTS, MGTS and Comstar UTS. The following discussion contains certain operating data relating to each of the principal businesses in our Telecommunications Segment.

MTS

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

	At June 30,	
	2004	2005
	(Amounts in thousands, except average monthly service revenue per subscriber)	
Subscribers [(1)]		
Russia	18,146	34,090
Moscow license area	6,120	8,820
Telecom XXI	2,094	2,080
Kuban-GSM	1,707	3,223
Russian regions	8,225	19,967
UMC	4,634	9,521
Uzbekistan (Uzdunrobita)	n/a	398
Turkmenistan	n/a	60
Total	22,780	44,069
Average monthly service revenue per subscriber		
Russia	$ 14	$ 9
Ukraine	$ 14	$ 10

(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.

In the six-month period ended June 30, 2004, the subscriber base increased by 36.5% to 22.8 million as of June 30, 2004. As of June 30, 2005, MTS' subscriber base increased to 44.1 million, or by 93.5% compared to June 30, 2004. A portion of the growth in the subscriber base was due to acquisitions during the year ended December 31, 2004 and the six-month period ended June 30, 2005, including Uzdunrobita, Primtelefon, Gorizont RT, Telesot Alania, Barash with 0.3, 0.2, 0.1, 0.1 and 0.1 million subscribers, respectively. MTS' organic growth in revenues amounted to $466.9 million, or 26.7% in the six-month period ended June 30, 2005 as compared to the six-month period ended June 30, 2004, while MTS acquisitions contributed $79.2 million to our revenues for the six-month period ended June 30, 2005.

Average monthly service revenue per subscriber in Russia fell from $14 in the six-month period ended June 30, 2004 to $9 in the six-month period ended June 30, 2005, due to the decrease in tariffs in the Moscow license area, an increase of mass-market subscribers in MTS' subscriber mix and its continued expansion into the regions of Russia outside of the Moscow license area where tariffs are lower. In the first half of 2005 more than half of MTS' subscriber growth occurred outside of the Moscow license area. However, as a result of competition and the tariff structure in the Russian regions outside of the Moscow license area, MTS' average revenue per subscriber in the Russian regions remains lower than in the Moscow license area, though costs are generally lower there as well. MTS generally expects to see a continued decline in average monthly service revenue per subscriber due to the introduction of lower tariff plans in connection with its marketing efforts.

UMC has experienced subscriber growth from 4.6 million subscribers as of June 30, 2004 to 9.5 million subscribers as of June 30, 2005, and we expect this trend to continue, assuming the Ukrainian economy continues to grow. Average monthly service revenue per subscriber decreased in the six-month period ended June 30, 2005 as a result of an extensive marketing campaign focused on penetration to the mass-market.

	Six months ended June 30,	
	2004	2005
Subscriber churn [1]		
Russia	17.4%	13.5%
Ukraine	11.0%	10.8%

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

MTS' subscriber churn in Russia decreased from 17.4% in the six-month period ended June 30, 2004 to 13.5% in the six-month period ended June 30, 2005 as a result of MTS marketing initiatives, targeted to raise subscriber loyalty. Although its subscriber churn in Russia decreased for the six-month period ended June 30, 2005, MTS believes that subscriber churn is highly dependent on competition and the number of mass-market subscribers in its overall subscriber mix. Mass-market subscribers generally choose to prepay their mobile phone usage by purchasing pre-paid packages and are more likely to switch providers to take advantage of low-tariff promotions. As a result, competition for these subscribers will likely lead to sustained downward pressure on tariffs. The other reasons for increases in subscriber churn are the absence of service contracts with subscribers in Russia that contain minimal periods of usage and the absence of connection fees, which generally prevent a subscriber's early churn. In order to decrease subscriber churn, in 2004 MTS launched a new marketing campaign that provides a 15% discount for services rendered to certain contract subscribers if they do not terminate their contracts within one year of activation. Churn, as MTS uses it, includes internal churn within its subscriber base, i.e., MTS' subscribers switching between different tariff plans we offer.

MGTS

MGTS' revenues are dependent on the regulated tariffs approved by the Federal Tariff Service. The following table illustrates MGTS' regulated tariff development in the periods under review:

Service	Effective August 1, 2003	Effective October 1, 2004
Monthly subscription fee		
Residential subscribers [1]	4.6	5.8
Public sector subscribers [2]	4.6	5.8
Corporate subscribers [2]	5.5	6.8
Local call charges		
Public sector subscribers [3]	0.005	0.005
Corporate subscribers [3]	0.013	0.014
Exchange rate (rubles per U.S. dollar) [4]	30.28	29.22

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

Comstar UTS

Comstar UTS services three segments of subscribers: corporate, operators and residential. The following table shows the number of Comstar UTS subscribers and active service lines as of the dates indicated.

	At June 30,	
	2004	2005
Total subscribers	20,112	23,090
Corporate	15,626	17,797
Operators	171	279
Residential	4,315	5,014
Active service lines	520,753	556,504

The number of subscribers increased during the six-month periods ended June 30, 2005 and 2004. The increase in the total number of subscribers equaled to 14.8% as of June 30, 2005 compared to June 30, 2004.

The total number of active service lines increased by 6.9% as of June 30, 2005 compared to June 30, 2004. A line is considered to be "active" if the subscriber has used the service within the last 30 days.

Liquidity and Capital Resources

We use a variety of sources to finance our operations, both external and internal. In addition to net cash provided by operations, our companies use short- and long-term borrowings to fund capital expenditures and strategic investments. Short- and long-term funding sources may change with time, but currently include notes issued in the international and Russian capital markets and credit facilities with international and Russian banks, denominated in both rubles and foreign currencies. In January 2004, January and March 2005, we (including MTS) raised approximately $350.0 million, $400.0 million and $150.0 million, respectively, through U.S. dollar-denominated bond offerings in the international capital markets. MTS repaid its $300.0 million notes in May 2004 with the proceeds of a short-term bridge loan and operating cash flows. In September 2004, MTS entered into a $600.0 million syndicated loan facility provided by international financial institutions. In December 2004, MTS repaid 10.95% notes due 2004 in principal amount of $300 million from drawings on the syndicated loan facility, which significantly improved our working capital position as the notes were included in short-term liabilities.

Our parent company, 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. In February 2005, JSFC Sistema completed its initial public offering on the London Stock Exchange. The amount of proceeds, net of related expenses, equaled to $1,284.6 million. We intend to invest the proceeds from the offering primarily in the purchase of long-term assets.

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

Working capital

Working capital is defined as current assets less current liabilities. As of the date hereof, we believe our working capital is sufficient for our present requirements. As of June 30, 2005, we had a positive working capital of $1,471.7 million, compared to a deficit of $347.0 million as of June 30, 2004.

Our working capital turned to positive as we refinanced a portion of our short-term debt with the proceeds from long-term borrowings and the initial public offering.

Credit Ratings

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

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

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

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

Capital Requirements

We need funding to finance the following:

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

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

Our capital expenditures in the six-month periods ended June 30, 2004 and June 30, 2005 were $650.3 million and $981.5 million, respectively. We expect to continue to finance most of our capital expenditure needs through our operating cash flows, and to the extent required, to incur additional indebtedness through borrowings or additional capital raising activities. Historically, a significant portion of our capital expenditures have been related to the installation and build out of our telecommunication networks and expansion into new license areas. Our future expenditures may be higher, in particular if licenses relating to new telecommunication technologies become available and our investment program for expansion and full digitalization of the Moscow public switch telephone network will be implemented. We expect that capital expenditures will remain a large portion of our cash outflows in connection with the continued installation and build out of our networks.

In addition to our capital expenditures, we spent $26.0 million and $55.4 million in the six-month periods ended June 30, 2004 and June 30, 2005, respectively, to acquire businesses. We may continue to expand our business through acquisitions. Our cash requirements relating to potential acquisitions can vary significantly based on market opportunities.

We expect to refinance most of our existing debt when it becomes due. In May 2004, MTS retired $300 million in principal amount of our Floating Rate Notes due August 2004 with the proceeds of a

$200.0 million short-term bridge loan from Credit Suisse First Boston International and operating cash flows. This $200.0 million bridge loan was repaid from MTS' operating cash flows and drawings on the syndicated loan facility described above. In December 2004, MTS repaid its 10.95% notes due 2004 in principal amount of $300.0 million from further drawings on the syndicated loan facility.

Capital Resources

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

At June 30, 2005, our debt was comprised of the following:

	Currency	Annual interest rate (Actual at June 30, 2005)	(000's) June 30, 2005
Sistema Finance Notes	USD	10.3%	$ 349,094
Sistema Capital Notes	USD	8.9%	350,000
MTS Finance Notes due 2012	USD	8.0%	400,000
MTS Finance Notes due 2010	USD	8.4%	400,000
MTS Finance Notes due 2008	USD	9.8%	400,000
MGTS Bonds	RUR	8.3%-10.0%	104,631
MBRD Bonds	USD	8.6%	150,000
Total Corporate Bonds			**2,153,725**
Syndicated Loan	USD	LIBOR+2.5% (6.2%)	600,000
EBRD	USD	LIBOR+3.1% (6.8%)	150,000
HSBC Bank and ING-BHF-Bank	USD	LIBOR+0.4% (4.1%)	162,688
ABN AMRO N.V.	USD	LIBOR/EURIBOR+0.35% (4.05/2.45%)	88,860
Commerzbank (Eurasia)	USD	LIBOR+1.4%-5.0% (5.1%-8.7%)	51,184
Hermes Credit Facility	EUR	EURIBOR+0.7% (2.8%)	50,291
ING-Bank (Eurasia)	USD	LIBOR+2.3%-4.2% (6.0%-7.9%)	33,333
Vendor Financing	Various	Various	27,682
Barclays Bank PLC	USD	LIBOR+0.15% (3.86%)	23,459
Citibank	USD	LIBOR+1.6% (5.3%)	20,714
Vneshtorgbank	USD, EUR	LIBOR+4.9% (8.6%), EURIBOR+5.35% (7.45%), 13%	18,947
Commerzbank Belgium S.A.	USD, EUR	LIBOR+0.4% (4.1%), 3.75%	16,344
Raiffeisenbank	USD	LIBOR+7.0% (10.7%)	14,786
WestLB	USD, EUR	LIBOR+6.8% (10.5%), EURIBOR+2.0% (4.1%)	14,400
Credit Suisse Bank	USD	LIBOR+3.45% (7.15%)	13,491
HSBC	USD	LIBOR+2.8% (6.5%)	12,500
DONAU-BANK	USD	9.0%	9,701
Ericsson Project Finance	USD	LIBOR+4.0% (7.7%)	9,450
Sberbank	RUR	10.0%-15.0%	6,566
Nordea Bank Sweden	USD	LIBOR+0.4% (4.1%)	4,875
Loans and promissory notes from related parties	Various	Various	35,152
Other	Various	Various	40,426
			3,558,574
Less amounts maturing within one year			(527,529)
Total			**$ 3,031,045**

The following table presents the aggregate scheduled maturities of debt principal outstanding as of June 30, 2005:

Payments due in the year ended June 30,		(In thousands)
2006	$	527,529
2007		416,098
2008		638,920
2009		587,653
2010		66,240
Thereafter		1,322,134
Total	**$**	**3,558,574**

In addition, we had capital lease obligations in the amount of $3.3 million as of June 30, 2005. The terms of our material debt obligations and capital lease obligations are described in Notes 20, 21 and 22, respectively, to our unaudited consolidated financial statements.

Our ability to incur further indebtedness is limited by the covenants in our outstanding notes, including (i) consolidated indebtedness to consolidated EBITDA test (as defined in the indenture relating to the notes), (ii) MTS' debt/cash flow incurrence test. The covenants in our outstanding notes also limit our ability to grant liens on our properties and to enter into mergers, acquisitions, sales and sale-leaseback transactions.

The following table presents a summary of our cash flows and cash outlays for capital expenditures and acquisitions of subsidiaries:

	Year ended June 30,			
	2004		2005	
	(Amounts in thousands)			
Cash flows				
Net cash provided by operating activities	$	948,487	$	584,766
Net cash used in investing activities		(644,477)		(1,766,838)
Net cash (used in)/provided by financing activities		(150,858)		1,764,348
Net increase in cash		153,152		582,276
Cash outlays for				
Capital expenditures[1]		(642,276)		(978,142)
Acquisition of subsidiaries, net of cash acquired		(26,046)		(55,405)

(1) Includes acquisition of property, plant and equipment, intangible assets and principal payments on capital lease obligations.

During the periods under review, our operating activities generated positive cash flows due to growth through organic growth and acquisitions. During the same periods, our investing activities generated negative cash flows due primarily to increases in capital expenditures in connection with the development of our telecommunications network and the acquisitions of new businesses. We expect for the foreseeable future to continue to use cash in investing activities as we continue to expand our telecommunications network in the Moscow region, into the regions outside of Moscow and into other CIS countries. We also intend to continue to expand our business through acquisitions. We intend to finance our future investments primarily through net cash flows from operations and the incurrence of additional indebtedness. The availability of financing is influenced by many factors, including our profitability, operating cash flows, debt levels, contractual restrictions and market conditions. For the six-month period ended June 30, 2005 our financing activities generated positive cash flows following the receipt of proceeds from our initial public offering in February 2005.

Liquidity

As of June 30, 2005 and June 30, 2004, we had total cash and cash equivalents of $1,086.0 million and $436.3 million, respectively. In addition, as of June 30, 2005 and June 30, 2004, we had short-term investments of $1,193.2 million and $217.3 million, respectively, mostly in corporate and municipal bonds and bank deposits.

For details of external financing refer to Notes 20, 21 and 22 to our audited consolidated financial statements. For subsequent events related to our external financing, refer to Note 31 to our audited consolidated financial statements.

Because most of our operating subsidiaries are incorporated in Russia, their ability to pay dividends to us is limited by provisions of Russian law. For example, Russian law requires that, among other things, dividends can only be paid in an amount not exceeding net profits as determined under Russian accounting standards. In addition, dividends may only be paid if the value of the company's net assets is not less than the sum of the company's charter capital, the company's reserve fund and the difference between the liquidation value and the par value of the issued and outstanding preferred stock of the company, if any, as determined under Russian accounting standards. In May 2005, MTS's Board of directors recommended to the shareholders to approve cash dividends of RUR 5.75 (equivalent of $0.21 as of the announcement date) per share for the year ended December 31, 2004, for the total of approximately $402.6 million, which was approved by the Shareholders' meeting on June 21, 2005. This is an almost two-times increase from $218.8 million announced and paid for the year ended December 31, 2003.

In June 2005, the shareholders of JSFC Sistema approved cash dividends of RUR 26.0 (equivalent of $0.91 as of the announcement date) per share for the year ended December 31, 2004, for the total of approximately $8.8 million. Whereas the dividends paid by JSFC Sistema for the year ended December 31, 2003 amounted to $5.2 million.

In August 2005, the Board of Directors of JSFC Sistema approved its dividend policy, which describes recommendations on the size of dividends as well as JSFC, Sistema's obligations on dividend payments and relevant disclosures. The policy determines the recommended dividend rate at 2% of our consolidated net income.

Competition

We operate in some of the most competitive industries in Russia, including telecommunications, technology, insurance and banking. Our businesses confront aggressive pricing practices, evolving customer demand patterns and changing technologies.

For example, in the Telecommunications Segment, our wireless business is subject to increasing competition from a number of existing and emerging companies, resulting in pricing pressures and lower margins. We compete with at least one other mobile cellular operator in each of our markets. The competition has evolved in recent years to exist primarily between MTS, Vimpelcom and MegaFon, each of which has effective national coverage in Russia. Competition is based largely on local tariff prices and secondarily on network coverage and quality, the level of customer service provided, roaming and international tariffs and the range of services offered.

We compete with a number of alternative fixed line operators servicing Moscow, 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
Six months ended June 30,				
2001	29.16	28.16	28.82	29.07
2002	31.48	30.14	31.09	31.45
2003	31.88	30.32	31.15	30.35
2004	29.45	28.49	28.73	29.03
2005	28.68	27.46	28.01	28.67

(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
Six months ended June 30,				
2001	5.43	5.38	5.42	5.38
2002	5.33	5.30	5.33	5.33
2003	5.33	5.33	5.33	5.33
2004	5.33	5.32	5.33	5.32
2005	5.31	5.05	5.17	5.06

(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 and the euro relative to the U.S. dollar. As a result of inflation in Russia and Ukraine, we link our monetary assets and transactions, when possible, to the U.S. dollar. We have not entered into any significant currency hedging arrangements.

A significant part of our capital expenditures and operating and borrowing costs are either denominated in U.S. dollars or tightly linked to the U.S. dollar exchange rate. These mostly include salaries, capital expenditures and borrowings. In order to hedge against a significant portion of this risk, we also denominate tariffs for our unregulated telecommunication services in Russia, which are payable in rubles, in units linked to the U.S. dollar and require accounts to be settled at the official rate of the Russian Central Bank on the date of payment.

If the ruble or the hryvnia decline against the U.S. dollar and tariffs for our telecommunication services cannot be maintained for competitive or other reasons, our operating margins could be adversely affected and we could have difficulty repaying or refinancing our U.S. dollar-denominated indebtedness. Our investment in monetary assets denominated in rubles and hryvnias is also subject to risk of loss in U.S. dollar terms. In particular, we are unable economically to hedge the risks associated with our ruble and hryvnia bank or deposit accounts. Generally, as the value of the ruble or the hryvnia declines, our net ruble and hryvnia monetary asset position results in currency remeasurement losses.

A portion of our capital expenditures and operating and borrowing costs are denominated in euro. These include capital expenditures and certain borrowings. We currently do not hedge against the risk of decline in the U.S. dollar against the euro because settlements denominated in euros are not significant.

In December 2004, MTS entered into two variable-to-fixed interest rate swap agreements to manage its exposure to changes in fair value of future cash flows of its variable-rate long term debt, which is caused by interest rate fluctuations. In March 2005, we also purchased several short-term USD forward agreements to hedge the fair value of its investments in Ruble-denominated financial instruments. Interest rate swap is designated as a cash flow hedge, while currency exchange forward agreements are classified as a fair value hedge. Both hedge instruments have been effective through the six months ended June 30, 2005.

Inflation and Exchange Rates

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

Six months ended June 30,	Inflation rate
2001	12.7%
2002	9.0%
2003	7.9%
2004	6.1%
2005	8.0%

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

Six months ended June 30	Inflation rate
2001	5.3%
2002	(1.8)%
2003	4.6%
2004	4.4%
2005	6.3%

Over the past several years, the rate of increase in the consumer price index in Russia has steadily declined, due to conservative fiscal and monetary policies and the resulting federal budget surpluses. However, inflation remains high in comparison to developed countries.

We link the unregulated tariffs of our telecommunications business to the U.S. dollar. While a majority of our costs are denominated in U.S. dollars or are closely tied to the U.S. dollar, certain of our costs, including salaries and utility costs, are sensitive to rises in the general price level in Russia. During the year ended December 31, 2004 and the six-month period ended June 30, 2005 the ruble appreciated against the U.S. dollar, both in terms of the nominal exchange rate and real appreciation. We would expect increases in ruble-denominated costs, driven by real appreciation of the ruble to put pressure on our margins. While we could seek to raise our prices and tariffs to compensate for such increases in costs, competitive pressures may not permit increases that are sufficient to preserve our operating margins. Accordingly, high rates of inflation in Russia relative to the nominal rate of devaluation could materially adversely affect our results of operations.

Overall, while the sharp decline in the value of the ruble in both nominal and real terms in the immediate aftermath of the 1998 financial crisis supported business growth and helped us to achieve positive results across most of our business lines, the subsequent appreciation of the ruble in real terms and in nominal terms has increased our costs in Russia.

Interest Rate Risk

We are exposed to variability in cash flow risk related to our variable interest rate debt and exposed to fair value risk related to our fixed-rate notes. As of June 30, 2005, approximately $1,285.0 million, or 36.1% of our total indebtedness, including capital leases, was variable interest rate debt, while $2,276.9 million, or 63.9% of our total indebtedness, including capital leases, was fixed interest rate debt. In December 2004, we entered into two interest rate swap agreements with respect to $250.0 million of variable-rate indebtedness. We continue to consider other financial instruments available to us on the market to mitigate exposure to variability in the interest rates.

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 June 30, 2005.

Contractual Maturity Dates as of June 30, 2005:

		June 30,							
	Currency	2006	2007	2008	2009	2010	Thereafter	Total	Average rate at June 30, 2005
Syndicated Loan.	USD	280,000	280,000	40,000	–	–	–	600,000	LIBOR+2.5% (6.2%)
EBRD	USD	23,077	23,077	23,077	23,077	23,077	34,615	150,000	LIBOR+3.1% (6.8%)
HSBC Bank and ING-BHF-Bank	USD	19,509	19,509	19,509	19,509	19,509	65,143	162,688	LIBOR+0.4% (4.1%)
ABN AMRO N.V..	USD	10,457	10,457	10,457	10,457	10,457	36,575	88,860	LIBOR+0.35% (4.05%)
ING-Bank (Eurasia)	USD	26,667	6,666	–	–	–	–	33,333	LIBOR+2.3%-4.2% (6.0%-7.9%)
Commerzbank (Eurasia) . . .	USD	18,684	12,500	–	–	–	–	31,184	LIBOR+1.4-3.5% (5.1%-7.2%)
Barclays Bank PLC	USD	2,850	2,850	2,606	2,606	2,606	9,941	23,459	LIBOR+0.15% (3.86%)
Citibank	USD	4,208	5,550	5,402	4,518	1,036	–	20,714	LIBOR+1.6% (5.3%)
Commerzbank (Eurasia) . . .	USD	20,000	–	–	–	–	–	20,000	LIBOR+5.0% (8.7%)
Vneshtorgbank	USD	5,244	4,929	3,007	3,007	2,760	–	18,947	LIBOR+4.9% (8.6%)
Raiffeisenbank	USD	2,291	2,396	2,596	2,801	2,269	2,433	14,786	LIBOR+7.0% (10.7%)
Credit Suisse Bank	USD	1,021	1,098	1,181	1,271	1,376	7,544	13,491	LIBOR+3.45% (7.15%)
Commerzbank Belgium S.A.	USD	2,663	2,663	2,663	2,663	2,662	–	13,314	LIBOR+0.4% (4.1%)
HSBC	USD	10,000	2,500	–	–	–	–	12,500	LIBOR+2.8% (6.5%)
Ericsson Project Finance . .	USD	9,450	–	–	–	–	–	9,450	LIBOR+4.0% (7.7%)
Nordea Bank Sweden	USD	3,250	1,625	–	–	–	–	4,875	LIBOR+0.4% (4.1%)
Commerzbank Belgium S.A.	USD	1,458	1,458	114	–	–	–	3,030	LIBOR+1.4% (5.1%)
Total USD variable debt		440,829	377,278	110,612	69,909	65,752	156,251	1,220,631	
Weighted average USD interest rate		6.1%	5.9%	5.7%	5.6%	5.4%	5.2%	5.9%	
Hermes Credit Facility	EUR	12,573	12,573	12,573	12,573	–	–	50,292	EURIBOR+0.7% (2.8%)
West LB International S.A.	EUR	10,400	4,000	–	–	–	–	14,400	EURIBOR+2.0% (4.1%)
Total EUR variable debt . . .		22,973	16,573	12,573	12,573	–	–	64,692	
Weighted average EUR interest rate		3.0%	2.9%	2.8%	2.8%	–	–	2.9%	

We would experience an additional interest expense of approximately $9.5 million in the year ended June 30, 2006, $5.3 million in the year ended June 30, 2007, $2.9 million in the year ended June 30, 2008, $2.0 million in the year ended June 30, 2009 and $1.3 million in the year ended June 30, 2010 on an annual basis as a result of a hypothetical increase in the LIBOR/EURIBOR by 1% over the current rate as of June 30, 2005. The fair value of our publicly traded long-term notes as of June 30, 2005 ranged from 101.3% to 108.1% of the principal amount. At June 30, 2005, 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 June 30, 2005.

Critical accounting policies

Critical accounting policies are those policies that require the application of management's most challenging, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods. Critical accounting policies involve judgments and uncertainties that are sufficiently sensitive to result in materially different results under different assumptions and conditions. We believe that our most critical accounting policies are those described below.

Consolidation of variable interest entities

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

Following the adoption of FIN 46R, we reevaluated the relationships with our related parties: Promtorgcenter, Notris, Laminea, Finescort-M, Kuntsevo-Invest, Putney Assets and Mosdachtrest. Kuntsevo-Invest and Mosdachtrest are engaged in our construction activities; Promtorgcenter, Notris, Laminea, Finescort-M and Putney Assets possess shareholdings and provide financing through intercompany loans to other entities of our Group. Mosdachtrest was accounted for under equity method for the periods prior to January 1, 2004. We determined these entities were variable interest entities and that it was their primary beneficiary. Accordingly, the we consolidated these companies effective January 1, 2004. All intercompany balances have been eliminated in consolidation and the results of these VIEs have been included in the consolidated statement of operations and statement of cash flows for the six-month period ended June 30, 2004. In accordance with the provisions of FIN 46R, the Group recorded a charge for the cumulative effect of this accounting change of $35.5 million, net of income tax of nil, in the six-month period ended June 30, 2004. This charge reflects the cumulative impact to the Group's results of operations had these VIEs been consolidated since their inception.

Revenue recognition

Telecommunications

Telecommunications Segment earns revenues from the provision of wireless telecommunication services, local telephone and data transmission services and usage of its local exchange networks and facilities. Revenues are recognized on an accrual basis, when services are actually provided or title to equipment passes to the customer, regardless of when the resulting monetary or financial flow occurs. Segment revenue sources consist of the following: (a) subscription fees, (b) usage fees, (c) value-added service fees, (d) roaming fees charged to other operators for guest roamers utilizing our network, (e) connection fees and (f) sales of handsets and accessories.

We defer initial connection fees paid by subscribers for the first time activation of network service, as well as one time activation fees received for connection to various value-added services. These fees are recognized as revenue over the estimated average subscriber life. The Group periodically reviews its estimates of the expected subscriber relationship period.

Local telephone services provided by MGTS, totaling approximately 4% and 5% of our consolidated revenues for the six-month periods ended June 30, 2005 and June 30, 2004, respectively, are regulated tariff services, and changes in rate structure are subject to approval by the Federal Tariff Service.

Prior to January 1, 2005, MGTS was required to grant discounts ranging from 20% to 100% on installation and monthly fees to certain categories of residential subscribers, such as pensioners, military veterans and disabled individuals, and was entitled to reimbursement from the federal budget for these discounts. Due to the lack of certainty of reimbursement, MGTS accounted for such revenues upon collection. According to the new Law on Telecommunications, effective January 1, 2005, all MGTS' subscribers are required to pay the full price for residential service, and those entitled to discounts are to receive reimbursement from the government rather than discounts from MGTS.

Technology

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

During the six-month periods ended June 30, 2005 and 2004, STROM telecom did not sell installation, training or post-contract customer support services, as well as upgrades or enhancements to existing software products, separately from other elements of its software arrangements. The vendor-specific objective of fair value of installation, training and post-contract customer support services, as well as upgrades or enhancements to existing products, has been established by management having the relevant authority. The management believes that it is probable that the established price (based on rates per hour) for such services will not change before their separate introduction into the market place.

Insurance

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

Banking

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

Other businesses

Revenues on construction contracts are recognized under the completed-contract method. Our other entities recognize revenues when products are shipped or when services are rendered to customers.

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

Management estimates

The preparation of our consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses for the reporting period. Actual results could differ from those estimates. Examples of significant estimates include the provision for doubtful accounts and valuation allowance on deferred tax assets.

License Costs and Other Intangible Assets

We capitalize the cost of licenses acquired in business combinations and directly from the government. As the telecommunications industries in Russia, Ukraine and Uzbekistan do not have sufficient experience with renewal of licenses or extensions of license terms, we amortize each license on a straight-line basis over the term of the license commencing from the date such license becomes commercially operational. We review these licenses and their remaining useful life and, if necessary, revise the useful lives based on our actual utilization. The estimated useful lives of licenses may vary depending on market or regulatory conditions, and any revision to the estimated useful lives may result in a write off or an increase in amortization costs.

Most of our current licenses provide for payments to be made to finance telecommunications infrastructure improvements, which in the aggregate could total approximately $103.0 million, as of June 30, 2005. According to the terms of licenses, such contributions are to be made during the license period upon the decision and as defined by the Board of Directors of the Association of GSM-900 Operators (the “Association”). The Association is a nongovernmental, not-for-profit association, and their Board of Directors comprises representatives of the major cellular communications companies, including MTS. The Association has not adopted any procedures enforcing such payments and no such procedures have been established by Russian legislation. To date, MTS has not made any such payments pursuant to any of the current operating licenses issued to MTS and its consolidated subsidiaries. Further, the management of MTS believes that MTS will not be required to make any such payments in the future. In relation to these uncertainties, the Group has not recorded a contingent liability in the accompanying consolidated financial statements.

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

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

Useful Lives of Property, Plant and Equipment

We calculate depreciation expense for property, plant and equipment on a straight-line basis over their estimated useful lives. We establish useful lives for each category of property, plant and equipment based on our assessment of the use of the assets and anticipated technology evolution. We review and revise if appropriate the assumptions used in the determination of useful lives of property, plant and equipment at least on an annual basis.

Impairment of Long-Lived Assets

We periodically evaluate the recoverability of the carrying amount of our long-lived assets in accordance with SFAS No. 144, ‘‘Accounting for the Impairment or Disposal of Long-Lived Assets.’’ Whenever events or changes in circumstances indicate that the carrying amounts of those assets may not be recoverable, we compare undiscounted net cash flows estimated to be generated by those assets to the carrying amount of those assets. When these undiscounted cash flows are less than the carrying amounts of the assets, we record impairment losses to write the asset down to fair value, measured by the estimated discounted net future cash flows expected to be generated from the use of the assets.

Translation Methodology

We follow a translation policy in accordance with Statement on Financial Accounting Standards (‘‘FAS’’) No. 52, ‘‘Foreign Currency Translation.’’

Management has determined that the functional currency of MGTS, Rosno, Kuban-GSM, CSC, Detsky Mir, DM-Center, Sistema Mass Media and Concern RTI is the Russian Ruble ("RUR"). Commencing January 1, 2005, MBRD's functional currency was changed to RUR following the increased ratio of RUR-denominated transactions in the MBRD's operations. The functional currency of UMC is the Ukrainian Hryvnia ("UAH") and the functional currency of STROM telecom is the Czech Krona. Management believes that USD is the appropriate functional currency for the other subsidiaries of the Group due to the pervasive use of the U.S. dollar in their operations.

We have selected the U.S. dollar as our reporting currency and have translated financial statements of subsidiaries with a different functional currency into U.S. dollars. Assets and liabilities are translated at the exchange rates current at the balance sheet date, while income and expense items are translated at average rates of exchange prevailing during the period. The resulting translation adjustments in the amount of $9.1 million gain, net of minority interest of $5.9 million, and $11.8 million loss, net of minority interest of $4.5 million, are recorded as a separate component of other comprehensive income for the six-month period ended June 30, 2004 and the six-month period ended June 30, 2005, respectively.

The ruble is not a fully convertible currency outside of the territory of the Russian Federation. The translation of ruble-denominated assets and liabilities into U.S. dollars for the purpose of these financial statements does not indicate that we could or will in the future convert the reported values of the assets and liabilities in U.S. dollars.

Taxation

We are subject to a variety of taxes levied in the Russian Federation, including income taxes, payroll taxes, VAT, property taxes and other, and our foreign subsidiaries are subject to taxation in their respective jurisdictions.

The taxation system in Russia is subject to frequent changes, varying interpretations and inconsistent enforcement at the federal, regional and local levels. In some instances, new tax regulations have been given retroactive effect, while under the Tax Code only laws benefiting the taxpayer may have retroactive effect. In addition to our substantial tax burden, these conditions complicate our tax planning and related business decisions. For example, tax laws are unclear with respect to the deductibility of certain expenses and at times we have taken a position that may be considered aggressive by tax authorities, but that we consider to be in compliance with current law. Tax declarations, together with other legal compliance areas (for example, customs and currency control matters), are subject to review and investigation by a number of authorities, which are enabled by law to impose extremely severe fines, penalties and interest charges. These facts create tax risks in Russia that are more significant than those typically found in countries with more developed tax systems.

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

Income taxes

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

Value-added tax

During the six-month periods ended June 30, 2005 and 2004 the VAT rate in Russia was 18%.

New accounting pronouncements

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

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

In May 2005, the FASB issued FAS No. 154, "Accounting Changes and Error Corrections", which replaces APB Opinion No. 20, "Accounting Changes" and FAS No. 3, "Reporting Accounting Changes in Interim Financial Statements". FAS No. 154 changes the requirements for the accounting and reporting of a change in accounting principle and is applicable to all voluntary changes and to changes required by an accounting pronouncement if such pronouncement does not specify transition provisions. FAS No. 154 requires retrospective application to the prior periods' financial statements of changes in accounting principle. In cases when it is impracticable to determine the period-specific or cumulative effects of an accounting change, the statement provides that the new accounting principle should be applied as of the earliest period for which retrospective application is practicable or, if impracticable to determine the effect of a change to all prior periods, prospectively from the earliest date practicable. This Statement shall be effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005.

In June 2005, the Emerging Issues Task Force ("EITF") reached a consensus on EITF Issue No. 05-2, "The Meaning of 'Conventional Convertible Debt Instrument' in EITF Issue No. 00-19, 'Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock." Issue No. 00-19 is used to evaluate whether embedded derivatives should be bifurcated under FASB Statement No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended. Specifically, Statement 133 provides guidance as to when an issuer is required to bifurcate a conversion option that is embedded in convertible debt. However, Issue 00-19 does not define "conventional convertible debt instrument." Given the development of numerous contractual terms that may be included in a convertible debt instrument, it is not clear when a convertible debt instrument is "conventional." The consensus reached by EITF No. 05-2 is effective for new instruments entered into and instruments modified in reporting periods after June 29, 2005. We do not anticipate the adoption of EITF No. 05-2 to have a material impact on our financial position and results of operations.

In June 2005, the EITF reached a consensus on EITF Issue No. 05-6, "Determining the Amortization Period for Leasehold Improvements." As part of a business combination, the acquiring entity will often assume existing lease agreements of the acquired entity and acquire the related leasehold improvements. The issues are whether the "lease term" should be reevaluated at consummation of a purchase business combination and whether the amortization period for acquired leasehold improvements should be reevaluated by the acquiring entity in a business combination. The consensus reached by EITF No. 05-6 is effective for leasehold improvements that are purchased or acquired in reporting periods beginning June 29, 2005. We do not anticipate the adoption of EITF No. 05-6 to have a material impact on our financial position and results of operations.

Off-balance sheet arrangements

Obligations under guarantee contracts

As of June 30, 2005, MTS has issued guarantees for MTS-Belarus, an equity investee, for the total amount of $12.0 million. Under these guarantees the Group could be potentially liable for a maximum amount of $12.0 million in case of the borrower's default under the obligations. The guarantees expire by April 2007.

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

Additionally, MBRD guaranteed loans for several companies, including related parties, which totaled $20.6 million as of June 30, 2005.

These guarantees would require payment by us only in the event of default on payment by the respective debtor. Under these guarantees, we could be potentially liable for a maximum amount of $53.7 million in the case of the borrower's default under the obligations. As of June 30, 2005, no event of default has occurred under any of the guarantees issued by us.

Obligations under derivative contracts

In connection with MTS' acquisition of 74% of the shares in Uzdunrobita in August 2004, it entered into call and put option agreements with the existing shareholders of the company to acquire the remaining 26% of the shares. The exercise period for the option is 48 months from the acquisition date. The call and put option agreements stipulate a minimum purchase price of $37.7 million plus 5% per annum commencing from the acquisition date. The fair value of the put option was approximately $5.5 million as of June 30, 2005.

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 June 30, 2004:

	July 1, 2005 - June 30, 2006	July 1, 2006 - June 30, 2007	July 1, 2007 - June 30, 2008	July 1, 2008 - June 30, 2009	July 1, 2009 - June 30, 2010	July 1, 2010 - thereafter	Total
			(Amounts in thousands)				
Contractual obligations:							
Notes payable	196,518	196,518	671,161	626,815	96,750	1,246,750	3,034,513
Bank loans	593,468	452,710	159,914	97,043	76,363	180,443	1,559,942
Capital lease	2,561	1,109	57	22	17	48	3,814
Operating leases and services agreements	39,021	28,893	19,628	15,662	21,019	48,321	172,544
Committed Investments:							
Purchases of property, plant and equipment	181,100	–	–	–	–	–	181,100
Construction contracts	39,200	–	–	–	–	–	39,200
Total	1,051,868	679,231	850,761	739,542	194,149	1,475,562	4,991,113

In December 2003, MGTS announced its long-term investment program for the period from 2004 through 2012. The program was approved by a resolution of the Moscow City Government in December 2003 and provides for total capital expenditures of approximately $1.6 billion during the years 2004-2012, including for the expansion and full digitalization of the Moscow telephone network, the reconstruction of 350 local telephone stations and the installation of 4.3 million new phone numbers. We expect to finance approximately 50% of the capital expenditures under the investment program.