

Management's discussion and analysis of financial condition and results of operations

The following report contains a discussion and analysis of the financial condition of PJSC LUKOIL as of September 30, 2015 and the results of its operations for the three and nine month periods ended September 30, 2015 and 2014, as well as significant factors that may affect its future performance. It should be read in conjunction with our interim US GAAP consolidated financial statements and notes thereto.

References to "LUKOIL," "the Company," "the Group," "we" or "us" are references to PJSC LUKOIL and its subsidiaries and equity affiliates. All dollar amounts are in millions of US dollars, unless otherwise indicated. Tonnes of crude oil and natural gas liquids produced are translated into barrels using conversion rates characterizing the density of crude oil from each of our oilfields and actual density of liquids produced at our gas processing plants. Tonnes of crude oil purchased as well as other operational indicators expressed in barrels were translated into barrels using an average conversion rate of 7.33 barrels per tonne. Translations of cubic meters to cubic feet were made at the rate of 35.31 cubic feet per cubic meter. Translations of barrels of crude oil into barrels of oil equivalent ("BOE") were made at the rate of 1 barrel per BOE and of cubic feet – at the rate of 6 thousand cubic feet per BOE.

This report includes forward-looking statements – words such as "believes," "anticipates," "expects," "estimates," "intends," "plans," etc. – that reflect management's current estimates and beliefs, but are not guarantees of future results.

Key financial and operational results

	3 rd quarter of			9 months of		
	2015	2014	Change, %	2015	2014	Change, %
	(millions of US dollars)					
Sales.....	23,418	39,021	(40.0)	74,712	112,907	(33.8)
Net income attributable to LUKOIL.....	623	1,620	(61.5)	2,318	5,742	(59.6)
Adjusted net income attributable to LUKOIL ⁽¹⁾	750	1,805	(58.4)	2,769	6,447	(57.0)
EBITDA	3,646	5,338	(31.7)	10,025	14,770	(32.1)
Adjusted EBITDA ⁽¹⁾	3,773	5,523	(31.7)	10,476	15,475	(32.3)
Taxes other than income taxes, excise and export tariffs..	(4,600)	(9,246)	(50.2)	(14,745)	(26,926)	(45.2)
Earning per share of common stock attributable to LUKOIL (US dollars):						
Basic	0.84	2.15	(61.1)	3.08	7.61	(59.4)
Diluted	0.84	2.11	(60.4)	3.07	7.46	(58.8)
Hydrocarbon production by the Group including our share in equity affiliates (thousands of BOE).....	218,141	215,746	1.1	647,670	625,486	3.5
Daily hydrocarbon production by the Group including our share in equity affiliates (thousands of BOE)	2,371	2,345	1.1	2,372	2,291	3.5
Crude oil and natural gas liquids produced by the Group including our share in equity affiliates (thousands of barrels)	190,072	187,234	1.5	560,081	539,110	3.9
Gas available for sale produced by the Group including our share in equity affiliates (millions of cubic meters)	4,769	4,844	(1.5)	14,883	14,677	1.4
Refined products produced by the Group including our share in equity affiliates (thousands of tonnes)	16,507	16,678	(1.0)	45,300	47,772	(5.2)

⁽¹⁾Adjusted for loss on disposal of assets and dry hole write-offs.

During the nine months of 2015, net income attributable to LUKOIL decreased by \$3,424 million, or by 59.6%, while our EBITDA decreased by \$4,745 million, or by 32.1%, compared to the nine months of 2014. Our net income was significantly affected by a two-fold decrease in the hydrocarbon prices and by dry hole write-off related to exploration project in Romania in the amount of \$371 million and by a loss on disposal of our share in Caspian Investment Resources Ltd. in the amount of \$80 million. Our net income for the nine months of 2014 was affected by a loss on the expected disposal of assets in the amount of \$358 million and write-offs related to our exploration projects in West Africa in the total amount of \$347 million.

Business overview

The primary activities of LUKOIL and its subsidiaries are oil exploration, production, refining, marketing and distribution. The Company is the ultimate parent entity of a vertically integrated group of companies.

LUKOIL was established in accordance with Presidential Decree No. 1403, issued on November 17, 1992. Under this decree, on April 5, 1993, the Government of the Russian Federation transferred to the Company 51% of the voting shares of fifteen enterprises. Under Government Resolution No. 861 issued on September 1, 1995, a further nine enterprises were transferred to the Group during 1995. Since 1995, the Group has carried out a share exchange program to increase its shareholding in each of 24 founding subsidiaries to 100%. From formation, the Group has expanded substantially through consolidation of interests, acquisition of new companies and establishment of new businesses. Now LUKOIL is a global energy company operating through its subsidiaries in 34 countries on four continents.

In July 2015, the Company changed its legal form to Public Joint Stock Company (“PJSC”) following the requirements of the amended Russian Civil Code.

LUKOIL is one of the world’s largest energy companies in terms of hydrocarbon reserves that amounted to 17.6 billion BOE as of January 1, 2015 and comprised of 13.6 billion barrels of crude oil and 23.9 trillion cubic feet of gas.

Our operations are divided into four main business segments:

- **Exploration and Production** – which includes our exploration, development and production operations relating to crude oil and gas. These activities are primarily located within Russia, with additional activities in Azerbaijan, Kazakhstan, Uzbekistan, the Middle East, North and West Africa, Norway and Romania.
- **Refining, Marketing and Distribution** – which includes refining and transport operations, marketing and trading of crude oil, natural gas and refined products.
- **Chemicals** – which includes processing and trading of petrochemical products.
- **Power generation** – which includes generation, transportation and sales of electricity, heat and related services.

Each of our four main segments is dependent on the other, with a portion of the revenues of one segment being a part of the costs of the other. In particular, our Refining, Marketing and Distribution segment purchases crude oil from our Exploration and Production segment. As a result of certain factors considered in the “Domestic crude oil and refined products prices” section on page 9, benchmarking crude oil market prices in Russia cannot be determined with certainty. Therefore, the prices set for inter-segment purchases of crude oil reflect a combination of market factors, primarily international crude oil market prices, transportation costs, regional market conditions, the cost of crude oil refining and other factors. Accordingly, an analysis of either of these segments on a stand-alone basis could give a misleading impression of those segments’ underlying financial position and results of operations. For this reason, we do not analyse either of our main segments separately in the discussion that follows. However, we present the financial data for each in Note 19 “Segment information” to our interim consolidated financial statements.

Changes in Group structure

On April 15, 2014, a Group company entered into a contract with a Sinopec group company, to sell the Group’s 50% interest in Caspian Investment Resources Ltd., an exploration and production company operating in Kazakhstan. On June 3, 2015, a Group company made a substitute transaction with a Sinopec group company for the sale at a price of \$1,067 million. The transaction’s closing was subject to requisite governmental consents and approvals and was completed on August 20, 2015.

In April 2015, in line with the strategy to optimize downstream portfolio a Group company sold 100% of interest in LUKOIL Ukraine, a distribution company operating in Ukraine, to AMIC Energy Management GmbH. Also, in December 2014, Group companies sold 100% of shares in LUKOIL Slovakia s.r.o., LUKOIL Hungary Ltd. and LUKOIL Czech Republic s.r.o. to Slovnaft Česká Republica, Spol. s.r.o. and Norm Benzinkút Kft at the price of €98 million (approximately \$123 million).

In March 2015, a Group company closed a transaction to enter a project to develop the Etinde block offshore the Republic of Cameroon in the Gulf of Guinea. The Etinde project is being executed under the production sharing agreement. The project partners are LUKOIL (30% interest), New Age (African Global Energy) Ltd (30% interest, operator), Bowleven Plc (20% interest), and state-owned Societe Nationale des Hydrocarbures of Cameroon (20% interest). The license to develop the Etinde area was issued on July 29, 2014 and is valid for 20 years.

In December 2014, LUKOIL sold to Rosneft its 20% share in National oil consortium (“NOC”), established by Russian oil companies in 2008 within development of economic cooperation between Russia and Venezuela. In 2010, NOC and PDVSA, Venezuelan state-owned oil company, established a joint venture, PetroMiranda, to develop the “Junin-6” block in the Orinoko river basin.

West Qurna-2 project

On December 12, 2009, a consortium of a Group company and Statoil won the tender for development of the West Qurna-2 field in Iraq, one of the largest crude oil fields discovered in the world, with estimated recoverable oil reserves of 12.9 billion barrels (1.8 billion tonnes). The service agreement for West Qurna-2 field development and production was signed on January 31, 2010 and then ratified by the Ministry cabinet of the Iraq Republic. After Statoil withdrew from the West Qurna-2 project in May 2012, the parties of the project are Iraq’s state-owned South Oil Company and a consortium of contractors, consisting of a Group company (75% interest) and Iraq’s state-owned North Oil Company (25% interest).

The Group launched the “Mishrif Early Oil” stage on the West Qurna-2 field and reached the planned production of 120 thousand barrels per day in March 2014. According to the service agreement, costs are compensated after this level of production is achieved and maintained during any 90 days within a 120-day period. In June 2014, we met this term and from the second quarter of 2014 started to receive cost compensation.

Accounting for the cost compensation within the West Qurna-2 project in the Group consolidated statement of comprehensive income is as follows. The crude oil sales revenue is recognized after the Iraqi party has approved the actual invoice for the spending quarter. The invoice total amount depends on crude oil production volumes and the market prices for crude oil during the period. Subsequently, crude oil purchases are recognized based on actual crude oil shipments by the Iraqi party against its debt for cost compensation. Then this crude oil is either sold to third parties or supplied to the Group refineries and the respective sales revenues are recognized.

In the nine months of 2015, the Group accrued revenue from the West Qurna-2 project in the total amount of \$2,423 million, consisting of cost recovery of \$2,327 million and remuneration fee of \$96 million, compared to the revenue of \$2,629 million in the nine months of 2014. This revenue was classified as crude oil sales revenue. Attributable amount of 7,558 thousand tonnes, or 51,843 thousand barrels, of crude oil was included in Group’s crude oil production for the nine months of 2015 (3,902 thousand tonnes, or 26,761 thousand barrels in the nine months of 2014) that represented approximately 52% of total production from the field (58% in the nine months of 2014). In the nine months of 2015, we received 7,009 thousand tonnes of crude oil from the Iraqi party as a debt settlement within the cost compensation. This crude oil at cost of \$2,267 million was recognized in *Cost of purchased crude oil, gas and products*. Subsequently, we sold this crude oil to third party customers or delivered to our refineries. During the nine months of 2015, the cost compensation increased the Group’s EBITDA by \$1,779 million (\$2,264 million in the nine months of 2014).

The project’s target production level is 1.2 million barrels per day and the total term of the contract is 25 years.

The Group is exposed to political, economic and legal risks due to its operations in Iraq. Management monitors the risks associated with the projects in Iraq and believes that there is no adverse effect on the Group’s financial position that can be reasonably estimated at present.

Sectorial sanctions against the Russian companies

In July-September 2014, the United States (“US”), the European Union (“EU”) and other countries imposed a number of sectorial sanctions on Russian entities, including LUKOIL. These sanctions prohibit the US and the EU companies and individuals from the provision of goods, services or technology (except for financial services to LUKOIL) that can be used on the territory of the Russian Federation in deepwater exploration and production of crude oil, exploration and production of crude oil in Arctic offshore and shale projects. The Company considers these sanctions in its activities, continuously monitors them and analyses the effect of the sanctions on the Company’s financial position and results of operations.

Transition to IFRS

In line with the requirements of the Russian legislation, the Group’s consolidated financial statements for 2015 will be prepared in accordance with International Financial Reporting Standards (“IFRS”). Presentation currency of our IFRS financial statements will be Russian ruble.

Operational highlights

Hydrocarbon production

The table below summarizes the results of our exploration and production activities.

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
Crude oil and natural gas liquids production⁽¹⁾	(thousand BOE per day)			
Consolidated subsidiaries				
Western Siberia	901	966	923	972
Timan-Pechora	340	319	335	312
Ural region	317	308	316	308
Volga region.....	136	136	139	135
Other in Russia.....	38	38	37	38
Total in Russia.....	1,732	1,767	1,750	1,765
Iraq ⁽²⁾	235	158	190	98
Other outside Russia.....	47	56	57	60
Total outside Russia.....	282	214	247	158
Total consolidated subsidiaries	2,014	1,981	1,997	1,923
Our share in equity affiliates				
in Russia	16	13	15	10
outside Russia.....	36	41	39	42
Total share in equity affiliates.....	52	54	54	52
Total crude oil and natural gas liquids	2,066	2,035	2,051	1,975
Natural gas production available for sale⁽³⁾				
Consolidated subsidiaries				
Western Siberia	169	183	174	185
Timan-Pechora	13	14	12	14
Ural region	15	15	20	17
Volga region.....	6	7	6	6
Total in Russia.....	203	219	212	222
Total outside Russia.....	94	82	100	85
Total consolidated subsidiaries	297	301	312	307
Share in equity affiliates				
in Russia	1	1	1	1
outside Russia.....	7	8	8	8
Total share in production of equity affiliates.....	8	9	9	9
Total natural gas available for sale.....	305	310	321	316
Total daily hydrocarbon production	2,371	2,345	2,372	2,291
				(US dollar per BOE)
Hydrocarbon extraction expenses	4.12	6.12	4.37	5.84
- in Russia	3.51	5.56	3.57	5.49
- outside Russia	7.15	9.80	8.78	8.69
				(millions of US dollars)
Hydrocarbon extraction expenses	883	1,288	2,767	3,558
- in Russia	627	1,013	1,910	2,970
- outside Russia.....	256	275	857	588
Exploration expenses	164	207	552	476
- in Russia	18	21	103	144
- outside Russia	146	186	449	332
Mineral extraction tax	2,034	3,200	6,319	9,369
- in Russia	2,031	3,187	6,307	9,323
- outside Russia.....	3	13	12	46

⁽¹⁾ Natural gas liquids produced at the Group gas processing plants.

⁽²⁾ Compensation oil that represented approximately 52% of production from the West Qurna-2 field in the nine months of 2015 and 58% in the nine months of 2014.

⁽³⁾ Including petroleum gas sold to third parties.

We undertake exploration for, and production of, crude oil and natural gas in Russia and internationally. In Russia, our major oil producing subsidiaries are LUKOIL-Western Siberia, LUKOIL-Komi and LUKOIL-PERM. Currently, the Group is restructuring its international upstream segment that includes stakes in PSA's and other projects in Kazakhstan, Azerbaijan, Uzbekistan, Romania, Iraq, Saudi Arabia, Egypt, Ghana, Cote d'Ivoire, Norway, Cameroon and Nigeria.

Crude oil production. In the nine months of 2015, we produced (including the Company's share in equity affiliates) 75.3 million tonnes, or 550.5 million barrels, of crude oil.

The following table represents our crude oil production in the nine months of 2015 and 2014 by major regions.

(thousands of tonnes)	Change to 2014				
	9 months of 2015	Total, %	Change in structure	Organic change	9 months of 2014
Western Siberia.....	33,428	(4.9)	–	(1,705)	35,133
Timan-Pechora.....	12,649	7.6	–	896	11,753
Ural region.....	11,215	3.2	–	351	10,864
Volga region.....	5,057	2.6	–	126	4,931
Other in Russia.....	1,425	(0.4)	–	(6)	1,431
Crude oil produced in Russia.....	63,774	(0.5)	–	(338)	64,112
Iraq ⁽¹⁾	7,558	93.7	–	3,656	3,902
Other outside of Russia.....	2,047	(5.1)	(94)	(15)	2,156
Crude oil produced internationally.....	9,605	58.6	(94)	3,641	6,058
Total crude oil produced by consolidated subsidiaries.....	73,379	4.6	(94)	3,303	70,170
Our share in crude oil produced by equity affiliates:					
in Russia.....	536	50.6	–	180	356
outside Russia.....	1,360	(6.3)	–	(92)	1,452
Total crude oil produced.....	75,275	4.6	(94)	3,391	71,978

⁽¹⁾ Compensation oil that represented approximately 52% of production from the West Qurna-2 field in the nine months of 2015 and 58% in the nine months of 2014.

The main oil producing region for the Company is Western Siberia where we produced 45.6% of our crude oil in the nine months of 2015 (50.1% in the nine months of 2014).

Crude oil production in Western Siberia continued to decline due to natural depletion of reserves and an increase in water cut. Nevertheless, this was compensated for by the development of greenfields and successful employment of new technologies.

The increase in our international production related to the West Qurna-2 oilfield in Iraq where we commenced commercial production in the second quarter of 2014 (for details see p. 3). The structural decrease in production elsewhere outside Russia refers to the sale of our share in Caspian Investment Resources Ltd. in August 2015.

The increase in our share in crude oil produced by equity affiliates in Russia was due to the commencement of production at the Trebs and Titov oilfields by Bashneft-Polus, where the Group holds a 25.1% interest.

In addition to our production, we purchase crude oil in Russia and on international markets. In Russia, we primarily purchase crude oil from affiliated producing companies and other producers. Then we either refine or export purchased crude oil. Crude oil purchased on international markets is normally used for trading activities, for supplying our international refineries or for processing at third party refineries.

	3 rd quarter of			
	2015		2014	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Purchases in Russia.....	3,540	483	1,231	168
Purchases for trading internationally.....	24,240	3,307	27,994	3,819
Purchases for refining internationally	27,620	3,768	30,156	4,114
The West Qurna-2 compensation crude oil.....	16,419	2,240	6,274	856
Total crude oil purchased.....	71,819	9,798	65,655	8,957

	9 months of			
	2015		2014	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Purchases in Russia.....	10,394	1,418	4,493	613
Purchases for trading internationally.....	103,001	14,052	84,193	11,486
Purchases for refining internationally	65,567	8,945	68,653	9,366
The West Qurna-2 compensation crude oil.....	51,376	7,009	6,274	856
Total crude oil purchased.....	230,338	31,424	163,613	22,321

A significant part of our crude oil purchases is for refining. Compared to the nine months of 2014, our purchases for refining at international refineries decreased by 4.5%. The volume of our purchases for trading increased by 22.3%. Moreover, in the nine months of 2015, the Group received 7,009 thousand tonnes of compensation crude oil from Iraq's state-owned South Oil Company as cost compensation within the West Qurna-2 project (in the nine months of 2014, the Group received 856 thousand tonnes).

Production of gas and natural gas liquids. During the nine months of 2015, we produced 14,883 million cubic meters (87.6 million BOE) of gas available for sale (including our share in equity affiliates), that is 1.4% more than in the nine months of 2014.

Our major gas production field is the Nakhodkinskoe field, where we produced 5,598 million cubic meters of natural gas in the nine months of 2015 (6,150 million cubic meters in the nine months of 2014). Our international gas production increased by 15.8%, compared to the nine months of 2014, largely resulting from the increase in production in Uzbekistan and Azerbaijan.

In the nine months of 2015, the output of natural gas liquids at the Group gas processing plants in Western Siberia, Ural and Volgograd regions of Russia was 9.6 million BOE, compared to 10.6 million BOE in the nine months of 2014.

Refining, marketing and trading

Refining. We own and operate four refineries located in European Russia and three refineries located outside of Russia – in Bulgaria, Romania and Italy. Moreover, we have a 45% interest in the Zeeland refinery in the Netherlands.

Compared to the nine months of 2014, the total volume of refined products produced by the Group (including our share in production at the Zeeland refinery) decreased by 5.2%. Production volumes decreased by 8.9% at our Russian refineries, but increased by 2.9% internationally. In Russia, the decrease was a result of amendments in the tax legislation that decreased the refining margins. At the same time, in June 2015, we put in operation a preliminary distillation unit at our refinery in Volgograd with a capacity of 6 million tonnes per year.

Along with our own production of refined products we refine crude oil at third party refineries depending on market conditions and other factors. In the periods considered, we processed our crude oil at third party refineries in Belarus and Kazakhstan.

The following table summarizes key figures for our refining activities.

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(thousand barrels per day)			
Refinery throughput at the Group refineries	1,285	1,310	1,189	1,268
- in Russia	891	926	842	916
- outside Russia ⁽¹⁾	394	384	347	352
Refinery throughput at the Zeeland refinery ⁽¹⁾	97	84	97	68
Refinery throughput at third party refineries	24	44	19	34
Total refinery throughput	1,406	1,438	1,305	1,370
	(thousands of tonnes)			
Production of the Group refineries in Russia	10,597	11,148	29,791	32,695
Production of the Group refineries outside Russia	4,698	4,476	11,923	12,535
Production of the Zeeland refinery	1,212	1,054	3,586	2,542
Refined products produced by the Group including our share in the Zeeland refinery	16,507	16,678	45,300	47,772
Refined products produced at third party refineries	277	511	683	1,159
Total refined products produced	16,784	17,189	45,983	48,931
	(millions of US dollars)			
Refining expenses at the Group refineries	364	545	1,081	1,543
- in Russia	200	305	530	807
- outside Russia	164	240	551	736
Refining expenses at the Zeeland refinery	42	44	121	134
Refining expenses at third party refineries	14	25	33	51
Capital expenditures	216	629	910	1,827
- in Russia	174	482	694	1,296
- outside Russia	42	147	216	531

⁽¹⁾ Including refined product processed.

Marketing and trading. Our marketing and trading activities mainly include wholesale and bunkering operations in Western Europe, South-East Asia, Central America and retail operations in the USA, Central and Eastern Europe, the Baltic States and other regions. In Russia, we purchase refined products on occasion, primarily to manage supply chain bottlenecks.

The Group retails its refined products in 23 countries through nearly 5.1 thousand petrol stations (including franchisees). Most of the stations operate under the LUKOIL brand.

The table below summarizes figures for our trading activities.

	3 rd quarter of		9 months of	
	2015	2014 ⁽¹⁾	2015	2014 ⁽¹⁾
	(thousands of tonnes)			
Retail sales	5,251	5,501	14,382	14,848
Wholesale sales	27,508	24,738	78,980	72,624
Total refined products sales	32,759	30,239	93,362	87,472
Refined products purchased in Russia	360	556	1,253	1,375
Refined products purchased internationally	17,609	14,096	51,380	43,306
Total refined products purchased	17,969	14,652	52,633	44,681

⁽¹⁾ From the first quarter of 2015, our international volumes of small wholesales are included in retail sales. Figures for 2014 were adjusted accordingly.

In April 2015, in line with the strategy to optimize its downstream operations, a Group company sold 100% of the Group's interest in LUKOIL Ukraine, a distribution company operating in Ukraine. Also, in December 2014, Group companies sold 100% of shares in LUKOIL Slovakia, LUKOIL Hungary and LUKOIL Czech Republic that together operated approximately 140 petrol stations.

Exports of crude oil and refined products from Russia. The volumes of crude oil and refined products exported from Russia by our subsidiaries are summarized as follows:

	3 rd quarter of			
	2015 (thousands of barrels)	(thousands of tonnes)	2014 (thousands of barrels)	(thousands of tonnes)
Exports of crude oil to Customs Union	7,015	957	6,890	940
Exports of crude oil beyond Customs Union	48,297	6,589	48,686	6,642
Total crude oil exports	55,312	7,546	55,576	7,582
Exports of refined products.....		5,215		5,284

	9 months of			
	2015 (thousands of barrels)	(thousands of tonnes)	2014 (thousands of barrels)	(thousands of tonnes)
Exports of crude oil to Customs Union	21,198	2,892	20,370	2,779
Exports of crude oil beyond Customs Union	168,223	22,950	143,067	19,518
Total crude oil exports	189,421	25,842	163,437	22,297
Exports of refined products.....		15,618		17,730

Following the amendments in tax legislation in the Russian oil industry, we increased our exports of crude oil and decreased the refined products exports. During the nine months of 2015, the volume of our crude oil exports from Russia increased by 15.9%, and we exported 40.5% of our domestic crude oil production (34.8% – in the nine months of 2014), including 1,200 thousand tonnes of crude oil purchased from our affiliates and third parties (485 thousand tonnes in the nine months of 2014). The volume of our refined products exports decreased by 12% compared to the nine months of 2014. Primarily, we export diesel fuel, fuel oil and gasoil. These products accounted for approximately 78% of our exported refined products volumes.

Substantially, we use Transneft infrastructure to export our crude oil. Nevertheless, during the third quarter and the nine months of 2015, we exported 1,937 thousand tonnes and 5,626 thousand tonnes of crude oil, respectively, through our own infrastructure (1,662 thousand tonnes and 4,954 thousand tonnes during the third quarter and the nine months of 2014, respectively) that represented approximately 20% of our total crude oil export in each of the periods considered. All the volume of crude oil exported that bypassed Transneft was routed beyond the Customs Union.

During the nine months of 2015, the Company exported 1,165 thousand tonnes of light crude oil through the Eastern Siberia – Pacific Ocean pipeline. This allowed us to preserve the premium quality of crude oil and thus increased the efficiency of exports, compared to exports to traditional Western markets.

During the nine months of 2015, our revenue from export of crude oil and refined products from Russia both to Group companies and third parties amounted to \$9,318 million and \$5,894 million, respectively (\$15,615 million for crude oil and \$12,982 million for refined products in the nine months of 2014).

Main macroeconomic factors affecting our results of operations

Changes in the price of crude oil and refined products

The price at which we sell crude oil and refined products is the primary driver of the Group's revenues. Compared to the nine months of 2014, crude oil price dropped nearly two-fold and in the nine months of 2015, the price for the Brent crude oil fluctuated between \$42 and \$66 per barrel and reached its maximum of \$66.7 in the middle of May.

Substantially all the crude oil the Group exports is Urals blend. The following table shows the average crude oil and refined product prices in the periods considered.

	3 rd quarter of		Change,	9 months of		Change,
	2015	2014	%	2015	2014	%
	(in US dollars per barrel, except for figures in percent)					
Brent crude.....	50.47	101.93	(50.5)	55.31	106.52	(48.1)
Urals crude (CIF Mediterranean) ⁽¹⁾	49.92	101.53	(50.8)	55.01	105.39	(47.8)
Urals crude (CIF Rotterdam) ⁽¹⁾	49.19	100.73	(51.2)	54.20	104.69	(48.2)
	(in US dollars per metric tonne, except for figures in percent)					
Fuel oil 3.5% (FOB Rotterdam).....	243.76	558.95	(56.4)	280.34	569.60	(50.8)
Diesel fuel 10 ppm (FOB Rotterdam)	482.89	878.57	(45.0)	529.98	907.96	(41.6)
High-octane gasoline (FOB Rotterdam).....	599.03	974.15	(38.5)	605.51	984.34	(38.5)

Source: Platts.

⁽¹⁾ The Company sells crude oil on foreign markets on various delivery terms. Thus, our average realized sale price of oil on international markets differs from the average prices of Urals blend on Mediterranean and Northern Europe markets.

Domestic crude oil and refined products prices

Substantially all crude oil produced in Russia is produced by vertically integrated oil companies such as ours. As a result, most transactions are between affiliated entities within vertically integrated groups. Thus, there is no concept of a benchmark domestic market price for crude oil. The price of crude oil that is produced but not refined or exported by one of the vertically integrated oil companies is generally determined on a transaction-by-transaction basis against a background of world market prices, but with no direct reference or correlation. At any time there may exist significant price differences between regions for similar quality crude oil as a result of the competition and economic conditions in those regions.

Domestic prices for refined products are determined to some extent by world market prices, but they are also directly affected by local demand and competition.

The table below represents average domestic wholesale prices of refined products in the periods considered.

	3 rd quarter of		Change,	9 months of		Change,
	2015	2014	%	2015	2014	%
	(in US dollars per metric tonne, except for figures in percent)					
Fuel oil.....	116.73	281.00	(58.5)	118.94	274.60	(56.7)
Diesel fuel.....	475.54	777.32	(38.8)	490.27	794.51	(38.3)
High-octane gasoline (Regular)	565.84	929.47	(39.1)	539.57	868.88	(37.9)
High-octane gasoline (Premium)	584.45	940.95	(37.9)	560.02	892.53	(37.3)

Source: InfoTEK (excluding VAT).

Changes in the US dollar-ruble exchange rate and inflation

A substantial part of our revenue is either denominated in US dollars or is correlated to some extent with US dollar crude oil prices, while most of our costs in the Russian Federation are settled in Russian rubles. Therefore, ruble inflation and movements of exchange rates can significantly affect the results of our operations. In particular, a depreciation of the ruble against the US dollar generally causes our costs to decrease in US dollar terms, and vice versa. The appreciation of the purchasing power of the US dollar in the Russian Federation calculated on the basis of the ruble-dollar exchange rates and the level of inflation in Russia was 30.8% in the nine months of 2015, compared to the nine months of 2014, while the nominal ruble depreciation against the US dollar was 40.3%, compared to the nine months of 2014.

The following table gives data on inflation in Russia and the change in the ruble-dollar exchange rate.

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
Ruble inflation (CPI), %	1.7	1.4	10.4	6.3
Average exchange rate for the period (ruble to US dollar)	62.98	36.19	59.28	35.39
Exchange rate at the end of the period (ruble to US dollar)	66.24	39.39	66.24	39.39

Tax burden

Starting from January 1, 2015, the method for calculation of certain tax and duty rates applied to oil companies in Russian Federation is amended. The mineral extraction tax rate increased significantly along with simultaneous decrease in export duty rates and excises.

The following table represents average enacted rates for taxes specific to the oil industry in Russia for the periods considered.

		3 rd quarter of		Change, %
		2015	2014	
Export tariffs on crude oil	\$/tonne	128.68	380.54	(66.2)
Export tariffs on refined products				
Light and middle distillates	\$/tonne	61.70	251.12	(75.4)
Fuel oil	\$/tonne	97.73	251.12	(61.1)
Gasoline	\$/tonne	100.33	342.43	(70.7)
Straight-run gasoline	\$/tonne	109.34	342.43	(68.1)
Diesel fuel	\$/tonne	61.70	247.29	(75.0)
Mineral extraction tax				
Crude oil	RUR/tonne	6,263.00	5,839.93	7.2
Crude oil	\$/tonne ⁽¹⁾	99.45	161.36	(38.4)

⁽¹⁾ Translated to US dollars using average exchange rate for the period.

		9 months of		Change, %
		2015	2014	
Export tariffs on crude oil	\$/tonne	129.75	384.59	(66.3)
Export tariffs on refined products				
Light and middle distillates	\$/tonne	62.22	253.80	(75.5)
Fuel oil	\$/tonne	98.57	253.80	(61.2)
Gasoline	\$/tonne	101.17	346.08	(70.8)
Straight-run gasoline	\$/tonne	110.25	346.08	(68.1)
Diesel fuel	\$/tonne	62.22	250.38	(75.2)
Mineral extraction tax				
Crude oil	RUR/tonne	6,721.17	6,017.08	11.7
Crude oil	\$/tonne ⁽¹⁾	113.38	170.03	(33.3)

⁽¹⁾ Translated to US dollars using average exchange rate for the period.

The rates of taxes specific to the oil industry in Russia are linked to international crude oil prices and are changed in line with them. The methods to determine the rates for such taxes are presented below.

Crude oil extraction tax rate is determined by adjusting the base rate depending on the international market price of Urals blend and the ruble-dollar exchange rate. The tax rate is zero when the average Urals blend international market price for a tax period is less than or equal to \$15.00 per barrel. Each \$1.00 per barrel increase in the international Urals blend price over the threshold (\$15.00 per barrel) results in an increase in the tax rate by \$2.93 per tonne extracted (or \$0.40 per barrel extracted using a conversion factor of 7.33) above the base rate.

During the nine months of 2015, the base rate was 766 rubles per metric tonne extracted (493 rubles in the nine months of 2014).

The crude oil extraction tax rate varies depending on the development, depletion and complexity of a particular oilfield. The tax rate is zero for extra-heavy crude oil and for crude oil produced in certain regions of Eastern Siberia, the Caspian Sea, the Nenetsky Autonomous District and some other regions, depending on the period and volume of production.

The Group produces crude oil in the Caspian Sea and extra-heavy crude oil in Timan-Pechora, where a zero extraction tax rate is currently applied.

Natural gas extraction tax rate. The mineral extraction tax on natural gas produced by independent producers in Russia was calculated using a flat rate until July 1, 2014. During the first half of 2014, the rate was 471 rubles per thousand cubic meters.

Starting from July 1, 2014, the base rate amounts to 35 rubles per thousand cubic meters and is adjusted depending on average wholesale natural gas price in Russia, share of gas production in total hydrocarbon production of particular taxpayer, and complexity of particular gas field. In the nine months of 2015, actual average natural gas extraction tax rate calculated for our major gas field – Nakhodkinskoe in Western Siberia amounted to 159.97 rubles per thousand cubic meters. (134.68 rubles per thousand cubic meters in the third quarter of 2014).

Crude oil export duty rate is calculated on a progressive scale. The rate is zero when the average Urals blend international market price is less than or equal to approximately \$15.00 per barrel (\$109.50 per metric tonne). If the Urals blend price is between \$15.00 and \$20.00 per barrel (\$146.00 per metric tonne), each \$1.00 per barrel increase in the Urals blend price over \$15.00 results in an increase in the crude oil export duty rate by \$0.35 per barrel exported. If the Urals blend price is between \$20.00 and \$25.00 per barrel (\$182.50 per metric tonne), each \$1.00 per barrel increase in the Urals blend price over \$20.00 results in an increase in the crude oil export duty rate by \$0.45 per barrel exported. Each \$1.00 per barrel increase in the Urals blend price over \$25.00 per barrel resulted in an increase in the crude oil export duty rate no more than by \$0.65 per barrel exported. From January 1, 2014 to December 31, 2014, the maximum increase in export duty rate was \$0.59 per barrel for each \$1.00 per barrel increase in the Urals blend price. From January 1, 2015, the maximum increase in export duty rate is \$0.42 per barrel for each \$1.00 per barrel increase in the Urals blend price.

The crude oil export duty rate is revised monthly on the basis of the preceding one-month period of crude oil price monitoring.

A special export duty regime is in place for certain greenfields. The list of the oilfields where the reduced rate is applied includes our Yu. Korchagin and V. Filanovsky oilfields located in the Caspian Sea and extra-heavy crude oil fields in Timan-Pechora.

Export duty rates on refined products are to be calculated by multiplying the current crude oil export duty rate by a coefficient according to the table below.

	From January 1, 2015 to December 31, 2015	From January 1, 2014 to December 31, 2014
Multiplier for:		
Light and middle distillates.....	0.48	0.66
Diesel fuel.....	0.48	0.65
Gasolines.....	0.78	0.90
Straight-run gasoline.....	0.85	0.90
Fuel oil.....	0.76	0.66

Crude oil and refined products exports from Russia are subject to two steps of customs declaration and duties payments: temporary and complete. Temporary declaration is submitted based on preliminary exports volumes and the duty is paid in rubles translated from US dollars as at the date of the temporary declaration. Complete declaration is submitted after receiving the actual data on the exported volumes, but not later than six months after the date of the temporary declaration. The final amount of the export duty is adjusted depending on the actual volumes, US dollar exchange rate as at the date of the complete declaration (except for pipeline deliveries when the exchange rate as at the temporary declaration date is used) and the export duty rate. If temporary and complete declarations are submitted in the different reporting periods, the final amount of the export duty is adjusted in the period of submission of the complete declaration. The high volatility of the ruble-dollar exchange rates may lead to significant value of such adjustments.

Crude oil and refined products exported to the member countries of the Custom Union – Belarus and Kazakhstan, are not subject to export duties.

Excise on refined products. The responsibility to pay excises on refined products in Russia is imposed on refined product producers (except for straight-run gasoline). Only domestic sales volumes are subject to excises.

In other countries where the Group operates, excises are paid either by producers or retailers depending on the local legislation.

Excise rates on refined products in Russia are tied to the ecological class of fuel. Excise tax rates for the periods considered are listed below. Translation to the US dollars was made using average exchange rate for the period.

		3 rd quarter of		Change,	9 months of		Change,
		2015	2014	%	2015	2014	%
Gasoline							
Below Euro-3.....	RUR/tonne	7,300.00	11,110.00	(34.3)	7,300.00	11,110.00	(34.3)
Euro-3	RUR/tonne	7,300.00	10,725.00	(31.9)	7,300.00	10,725.00	(31.9)
Euro-4	RUR/tonne	7,300.00	9,916.00	(26.4)	7,300.00	9,916.00	(26.4)
Euro-5	RUR/tonne	5,530.00	6,450.00	(14.3)	5,530.00	6,450.00	(14.3)
Diesel fuel							
Below Euro-3.....	RUR/tonne	3,450.00	6,446.00	(46.5)	3,450.00	6,446.00	(46.5)
Euro-3	RUR/tonne	3,450.00	6,446.00	(46.5)	3,450.00	6,446.00	(46.5)
Euro-4	RUR/tonne	3,450.00	5,427.00	(36.4)	3,450.00	5,427.00	(36.4)
Euro-5	RUR/tonne	3,450.00	4,767.00	(27.6)	3,450.00	4,767.00	(27.6)
Motor oils.....	RUR/tonne	6,500.00	8,260.00	(21.3)	6,500.00	8,260.00	(21.3)
Straight-run gasoline.....	RUR/tonne	11,300.00	11,252.00	0.4	11,300.00	11,252.00	0.4

		3 rd quarter of		Change,	9 months of		Change,
		2015	2014	%	2015	2014	%
Gasoline							
Below Euro-3.....	\$/tonne	115.91	306.98	(62.2)	123.15	313.95	(60.8)
Euro-3	\$/tonne	115.91	296.35	(60.9)	123.15	303.07	(59.4)
Euro-4	\$/tonne	115.91	273.99	(57.7)	123.15	280.21	(56.1)
Euro-5	\$/tonne	87.81	178.22	(50.7)	93.29	182.26	(48.8)
Diesel fuel							
Below Euro-3.....	\$/tonne	54.78	178.11	(69.2)	58.20	182.15	(68.0)
Euro-3	\$/tonne	54.78	178.11	(69.2)	58.20	182.15	(68.0)
Euro-4	\$/tonne	54.78	149.95	(63.5)	58.20	153.36	(62.0)
Euro-5	\$/tonne	54.78	131.72	(58.4)	58.20	134.71	(56.8)
Motor oils.....	\$/tonne	103.21	228.23	(54.8)	109.65	233.41	(53.0)
Straight-run gasoline.....	\$/tonne	179.43	310.91	(42.3)	190.63	317.96	(40.0)

Income tax. The federal income tax rate is 2.0% and the regional income tax rate varies between 13.5% and 18.0%. The Group's foreign operations are subject to taxes at the tax rates applicable to the jurisdictions in which they operate.

The Company and its Russian subsidiaries file income tax returns in Russia. A number of Group companies in Russia are paying income tax as a consolidated taxpayers' group ("CTG"). This allows taxpayers to offset taxable losses generated by certain participants of a CTG against taxable profits of other participants of the CTG.

Transportation of crude oil and refined products in Russia

The main Russian crude oil production regions are remote from the main crude oil and refined products markets. Therefore, access by crude oil production companies to the markets is dependent on the extent of diversification of the transport infrastructure and access to it. As a result, transportation cost is an important macroeconomic factor affecting our net income.

Transportation of crude oil produced in Russia to refineries and export destinations is performed primarily through the trunk oil pipeline system of the state-owned company, Transneft, or by railway transport.

Transportation of refined products in Russia is performed by railway transport and the pipeline system of Transneftproduct. The Russian railway infrastructure is owned and operated by Russian Railways. Both these companies are state-owned. We transport the major part of our refined products by railway transport.

In Russia, gas is mostly sold at the wellhead and then transported through the Unified Gas Supply System ("UGSS"). The UGSS is responsible for gathering, transporting, dispatching and delivering substantially all natural gas supplies in Russia and is owned and operated by Gazprom. The Federal Service for Tariffs of the Russian Federation regulates natural gas transportation tariffs. We are not able to sell our gas other than through UGSS.

Three and nine months ended September 30, 2015, compared to three and nine months ended September 30, 2014

The table below sets forth data from our consolidated statements of comprehensive income for the periods indicated.

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
Revenues				
Sales (including excise and export tariffs)	23,418	39,021	74,712	112,907
Costs and other deductions				
Operating expenses	(1,887)	(2,726)	(5,758)	(7,593)
Cost of purchased crude oil, gas and products	(11,385)	(18,603)	(37,487)	(54,717)
Transportation expenses	(1,170)	(1,510)	(3,783)	(4,620)
Selling, general and administrative expenses	(640)	(994)	(2,075)	(2,865)
Depreciation, depletion and amortization	(2,287)	(2,788)	(6,292)	(6,785)
Taxes other than income taxes	(2,253)	(3,501)	(6,998)	(10,355)
Excise and export tariffs	(2,347)	(5,745)	(7,747)	(16,571)
Exploration expense	(164)	(207)	(552)	(476)
Loss on disposals and impairments of assets	(13)	(87)	(127)	(501)
Income from operating activities	1,272	2,860	3,893	8,424
Interest expense	(182)	(171)	(534)	(466)
Interest and dividend income	71	74	230	194
Equity share in income of affiliates	71	154	148	427
Currency translation loss	(2)	(347)	(222)	(615)
Other non-operating income (expense)	9	(108)	(77)	(227)
Income before income taxes	1,239	2,462	3,438	7,737
Current income taxes	(580)	(828)	(1,281)	(2,174)
Deferred income taxes	(45)	(5)	170	203
Total income tax expense	(625)	(833)	(1,111)	(1,971)
Net income	614	1,629	2,327	5,766
Net loss (income) attributable to non-controlling interests	9	(9)	(9)	(24)
Net income attributable to LUKOIL	623	1,620	2,318	5,742
Earning per share of common stock attributable to LUKOIL (in US dollars):				
Basic	0.84	2.15	3.08	7.61
Diluted	0.84	2.11	3.07	7.46

The analysis of the main financial indicators of the financial statements is provided below.

Sales revenues

Sales breakdown	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
Crude oil				
Export and sales on international markets other than Customs Union	4,535	9,295	17,627	24,662
Export and sales to Customs Union	229	407	777	1,403
Domestic sales	619	819	1,931	2,756
	5,383	10,521	20,335	28,821
Refined products				
Export and sales on international markets				
Wholesale	10,908	17,141	33,997	53,129
Retail	2,848	4,438	8,132	12,087
Domestic sales				
Wholesale	1,159	2,270	3,250	5,743
Retail	1,606	2,625	4,501	7,054
	16,521	26,474	49,880	78,013
Petrochemicals				
Export and sales on international markets	152	188	453	677
Domestic sales	155	41	321	212
	307	229	774	889
Gas and gas products				
Export and sales on international markets	376	559	1,225	1,650
Domestic sales	150	305	478	888
	526	864	1,703	2,538
Sales of energy and related services				
Export and sales on international markets	68	117	141	138
Domestic sales	177	290	690	1,087
	245	407	831	1,225
Other				
Sales on international markets	256	280	681	763
Domestic sales	180	246	508	658
	436	526	1,189	1,421
Total sales	23,418	39,021	74,712	112,907

Sales volumes	3 rd quarter of		9 months of	
	2015	2014	2015	2014
Crude oil	(thousands of barrels)			
Export and sales on international markets other than Customs Union	99,725	94,220	343,572	239,046
Export and sales to Customs Union	6,597	8,694	21,726	27,891
Domestic sales	22,628	19,337	60,436	58,948
	128,950	122,251	425,734	325,885
Crude oil	(thousands of tonnes)			
Export and sales on international markets other than Customs Union	13,605	12,854	46,872	32,612
Export and sales to Customs Union	900	1,186	2,964	3,805
Domestic sales	3,087	2,638	8,245	8,042
	17,592	16,678	58,081	44,459
Refined products	(thousands of tonnes)			
Export and sales on international markets				
Wholesale	24,835	21,357	71,401	64,004
Retail	2,624	2,855	7,254	7,696
Domestic sales				
Wholesale	2,673	3,381	7,579	8,620
Retail	2,627	2,646	7,128	7,152
	32,759	30,239	93,362	87,472
Total sales volume of crude oil and refined products	50,351	46,917	151,443	131,931

Realized average sales prices	3 rd quarter of		9 months of		
	2015	2014	2015	2014	
Average realized price international					
Oil (beyond Customs Union)	(\$/barrel)	45.48	98.65	51.31	103.17
Oil (Customs Union)	(\$/barrel)	34.71	46.82	35.76	50.31
Refined products					
Wholesale	(\$/tonne)	439.22	802.62	476.14	830.08
Retail.....	(\$/tonne)	1,085.37	1,554.60	1,121.04	1,570.64
Average realized price within Russia					
Oil.....	(\$/barrel)	27.36	42.35	31.95	46.76
Refined products					
Wholesale	(\$/tonne)	433.60	671.49	428.82	666.24
Retail.....	(\$/tonne)	611.34	991.56	631.45	986.23

During the third quarter of 2015, our revenues decreased by \$15,603 million, or by 40.0%, compared to the third quarter of 2014. Our revenues from crude oil sales decreased by \$5,138 million, or by 48.8%, and our revenues from sales of refined products – by \$9,953 million, or by 37.6%.

During the nine months of 2015, our revenues decreased by \$38,195 million, or by 33.8%, compared to the same period of 2014. Our revenues from crude oil sales decreased by \$8,486 million, or by 29.4%. Our revenues from sales of refined products decreased by \$28,133 million, or by 36.1%.

Our revenue was severely affected by the sharp decrease in the international crude oil prices against the same periods of 2014. Moreover, the changes in ruble-nominated revenues against the nine months of 2014 were significantly affected by the nominal ruble devaluation by 40.3%.

Sales of crude oil

Compared to the third quarter of 2014, our international sales revenue decreased by 51.2%, or by \$4,760 million. International realized crude oil prices decreased by 53.9%, while sales volumes increased by 751 thousand tonnes, or by 5.8%, largely as a result of the increase in sales volumes of crude oil produced from the West Qurna-2 oilfield. Compared to the nine months of 2014, our crude oil sales volumes increased by 14,260 thousand tonnes, or by 43.7%, as a result of the increase in crude oil exports from Russia, increased volumes of crude oil trading and commencement of commercial production from the West Qurna-2 field in March 2014. Nevertheless, this was offset by the decrease in the international realized crude oil prices by 50.3%, thus, our international crude oil sales revenue decreased by 28.5%, or by \$7,035 million, compared to the nine months of 2014.

During the third quarter and the nine months of 2015, as a result of the ruble devaluation and the drop of international crude oil prices, our realized domestic crude oil prices decreased by 35.4% and 31.7%, respectively. In the third quarter of 2015, our domestic sales volumes increased by 449 thousand tonnes, or by 17.0%, mostly as a result of an increase in crude oil purchases and a decrease in throughput of our domestic refineries. During the nine months of 2015, the above mentioned factors were offset by the increase in crude oil export from Russia, so the sales volumes in Russia increased only by 202 thousand tonnes, or by 2.5%. As a consequence, in the third quarter and the nine months of 2015, our domestic sales revenue decreased by 24.4%, or by \$200 million, and by 29.9%, or by \$825 million, respectively.

In the third quarter and the nine months of 2015, our revenue from crude oil export from Russia both to the Group companies and third parties amounted to \$2,390 million and \$9,318 million, respectively.

Sales of refined products

Compared to the third quarter and the nine months of 2014, our revenue from the wholesale of refined products outside of Russia decreased by \$6,233 million, or by 36.4%, and by \$19,132 million, or by 36.0%, respectively. The decrease in sales prices by 45.3% in the third quarter of 2015 and by 42.6% in the nine months of 2015 was partially compensated by the increase in sales volumes by 16.3% and 11.6%, respectively, that resulted from the increase in refined products trading.

During the third quarter and the nine months of 2015, our realized retail prices outside of Russia decreased by 30.2% and 28.6%, and sales volumes decreased by 8.1% and 5.7%, that resulted in the decrease in retail revenue by \$1,590 million, or by 35.8%, and by \$3,955 million, or by 32.7%, compared to the third quarter and the nine months of 2014, respectively.

During the third quarter and the nine months of 2015, our revenue from the wholesale of refined products on the domestic market decreased by 48.9%, or by \$1,111 million, and by 43.4%, or by \$2,493 million, respectively. Our realized prices and sales volumes decreased by 35.4% and 20.9%, respectively, in the third quarter of 2015 and by 35.6% and 12.1%, respectively, in the nine months of 2015. The decrease in prices was a result of the ruble devaluation and the decrease in volumes was due to lower production at our domestic refineries.

During the third quarter and the nine months of 2015, our revenue from retail sales in Russia decreased by \$1,019 million, or by 38.8%, and by \$2,553 million, or by 36.2%, respectively. Our average domestic retail prices decreased by 38.3% and by 36.0%, respectively, as a result of the ruble devaluation while the retail volumes remained unchanged.

In the third quarter and the nine months of 2015, our revenue from export of refined products from Russia both to Group companies and third parties amounted to \$1,780 million and \$5,894 million, respectively.

Sales of petrochemical products

In the third quarter of 2015, our revenue from sales of petrochemical products increased by \$78 million, or by 34.1%, largely due to doubling of sales volumes against the background of low production as a consequence of the fire at our plant in Stavropol region of Russia in the end of the first quarter of 2014. In early April 2015, the production at the plant was resumed. During the nine months of 2015, the effect of the increased production volumes was outweighed by the effect of the ruble devaluation, and our revenue from sales of petrochemical products decreased by \$115 million, or by 12.9%.

Sales of gas and gas products

Sales of gas and gas refined products decreased by \$338 million, or by 39.1%, compared to the third quarter of 2014 and by \$835 million, or by 32.9%, compared to the nine months of 2014.

Our gas products wholesales revenue decreased by \$149 million, or by 53.0%, during the third quarter of 2015 and by \$360 million, or by 46.7%, in the nine months of 2015. Average realized wholesale prices decreased by 53.6% and sales volumes of gas products increased by 1.5% compared to the third quarter of 2014. Average realized wholesale prices decreased by 49.8% and sales volumes of gas products increased by 6.0% compared to the nine months of 2014. Retail gas products revenue decreased by \$89 million, or by 39.0%, in the third quarter of 2015 and by \$249 million, or by 38.2%, in the nine months of 2015, due to the decrease in realized prices.

Natural gas sales revenue decreased by \$100 million, or by 28.2%, in the third quarter of 2015 and by \$226 million, or by 20.3%, in the nine months of 2015, also as a result of the decrease in international hydrocarbon prices.

Sales of energy and related services

Our revenue from sales of electricity, heat and related services decreased by \$162 million, or by 39.8%, in the third quarter of 2015 and by \$394 million, or by 32.2%, in the nine months of 2015. The decrease was largely due to the ruble devaluation.

Sales of other products

Other sales include non-petroleum sales through our retail network, transportation services, rental revenue, crude oil extraction services, and other revenue of our production and marketing companies from sales of goods and services not related to our primary activities.

Revenue from other sales decreased by \$90 million, or by 17.1%, in the third quarter of 2015 and by \$232 million, or by 16.3%, in the nine months of 2015, largely as a result of the impact of the ruble devaluation on the revenue from sales of other products in Russia. At the same time, since the second quarter of 2014, we increased the volume of rendering crude oil extraction services.

Also, since the third quarter of 2014, other sales included revenue from sales of diamonds, in amount of \$41 million in the third quarter of 2015 and \$122 million in the nine months of 2015. In the third quarter of 2014, the volume of sales of diamonds was relatively insignificant.

Operating expenses

Operating expenses include the following:

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
Hydrocarbon extraction expenses	883	1,288	2,767	3,558
Own refining expenses	364	545	1,081	1,543
Refining expenses at third parties and affiliated refineries.....	56	69	154	185
Expenses for crude oil transportation to refineries	181	258	531	801
Power generation and distribution expenses	139	282	473	643
Petrochemical expenses	49	24	133	135
Other operating expenses	215	260	619	728
Total operating expenses	1,887	2,726	5,758	7,593

The method of allocation of operating expenses above differs from the approach used in preparing the data for Note 19 “Segment information” to our interim consolidated financial statements. Expenditures in the segment reporting are grouped depending on the segment to which a particular company belongs. Operating expenses for the purposes of this analysis are grouped based on the nature of the costs incurred.

Compared to the respective periods of 2014, our operating expenses decreased by \$839 million, or by 30.8%, in the third quarter of 2015, and by \$1,835 million, or by 24.2%, in the nine months of 2015.

The changes in ruble-nominated operating expenses against the nine months of 2014 were significantly affected by the nominal ruble devaluation by 40.3%.

Hydrocarbon extraction expenses

Our extraction expenses include expenditures related to repairs of extraction equipment, labor costs, expenses on artificial stimulation of reservoirs, fuel and electricity costs, cost of extraction of natural gas liquids, property insurance of extraction equipment and other similar costs.

Our extraction expenses decreased by \$405 million, or by 31.4%, in the third quarter of 2015 and by \$791 million, or by 22.2%, in the nine months of 2015. Our extraction expenses included start-up costs and production expenses related to the West Qurna-2 project in the amount of \$640 million in the nine months of 2015 and \$362 million in the nine months of 2014. In Russia, the increase in costs was offset by the ruble devaluation.

Our average hydrocarbon extraction expenses decreased from \$6.12 per BOE in the third quarter of 2014 to \$4.12 per BOE in the third quarter of 2015, or by 32.7%, and from \$5.84 per BOE in the nine months of 2014 to \$4.37 per BOE in the nine months of 2015, or by 25.2%. In Russia, average hydrocarbon extraction expenses decreased by 36.9% to \$3.51 per BOE in the third quarter of 2015 and by 35.0% to \$3.57 per BOE in the nine months of 2015 as a result of the ruble devaluation.

Own refining expense

Our own refining expenses decreased by \$181 million, or by 33.2%, in the third quarter of 2015, and by \$462 million, or by 29.9%, in the nine months of 2015.

Refining expenses at our domestic refineries decreased by 34.4%, or by \$105 million, in the third quarter of 2015, and by 34.3%, or by \$277 million, in the nine months of 2015, as a result of the ruble devaluation and the decrease in production volumes that was partially offset by increased consumption of additives and overhaul costs.

Refining expenses at our refineries outside of Russia decreased by \$76 million, or by 31.7%, in the third quarter of 2015, and by \$185 million, or by 25.1%, in the nine months of 2015, largely as a result of depreciation of the euro against the US dollar.

Refining expenses at third party and affiliated refineries

Along with our own production of refined products we refine crude oil at third party and affiliated refineries both in Russia and abroad.

In the third quarter and the nine months of 2015, refining expenses at third party and affiliated refineries decreased by 18.8%, or by \$13 million, and by 16.8%, or by \$31 million, respectively, due to the euro depreciation against the US dollar.

Expenses for crude oil transportation to refineries

Expenses for crude oil transportation to refineries include pipeline, railway, freight and other costs related to delivery of the Group's own crude oil to refineries for further processing.

Our expenses for crude oil transportation to refineries decreased by \$77 million, or by 29.8%, in the third quarter of 2015 and by \$270 million, or by 33.7%, in the nine months of 2015, largely due to the ruble devaluation and the decrease in crude oil refining in Russia.

Petrochemical expenses

During the third quarter of 2015, operating expenses of our petrochemical plants more than doubled due to the increase in domestic production volumes after commencement of production at our petrochemical plant in Stavropol region of Russia in April 2015 (the plant's operation was limited since a fire in February 2014). During the nine months of 2015, the effect of the increased production volumes was offset by the effect of the ruble devaluation, and our petrochemical expenses didn't change significantly.

Power generation and distribution expenses

Our power generation and distribution expenses decreased by \$143 million, or by 50.7%, during the third quarter of 2015, and by \$170 million, or by 26.4%, during the nine months of 2015. The decrease in expenses in Russia due to the ruble devaluation was partially offset by the cost of maintenance works at one of our Russian power plants in June 2015.

Other operating expenses

Other operating expenses include expenses of the Group's upstream and downstream entities that do not relate to their core activities, namely rendering of transportation and extraction services, costs of other services provided and goods sold by our production and marketing companies, and of non-core businesses of the Group.

Other operating expenses decreased by \$45 million, or by 17.3%, in the third quarter of 2015, and by \$109 million, or by 15.0%, in the nine months of 2015, largely as a result of the ruble devaluation. At the same time, other operating expenses in the nine months of 2015 included expenses related to the production of diamonds that commenced in the third quarter of 2014.

Cost of purchased crude oil, gas and products

Cost of purchased crude oil, gas and products includes the cost of crude oil and refined products purchased for trading or refining, gas and fuel oil to supply our power generation entities and the result of hedging of crude oil and refined products sales.

Cost of purchased crude oil, gas and products decreased by \$7,218 million, or by 38.8%, in the third quarter of 2015 and by \$17,230 million, or by 31.5%, in the nine months of 2015, following the sharp decrease in hydrocarbon prices, that was partially offset by the increase in crude oil and refined products trading volumes. Crude oil purchases in the nine months of 2015 also included \$2,267 million related to 7,009 thousand tonnes of compensation crude oil received from Iraq's state-owned South Oil Company within the West Qurna-2 project (in the nine months of 2014, we received 856 thousand tonnes of compensation crude oil at cost of \$534 million).

In the third quarter of 2015, we recognized an \$883 million net gain from hedging, compared to a \$594 million net gain in the third quarter of 2014. In the nine months of 2015, we recognized a \$421 million net gain from hedging, compared to a net gain of \$485 million in the nine months of 2014.

Transportation expenses

Our transportation expenses decreased by \$340 million, or by 22.5%, compared to the third quarter of 2014 and by \$837 million, or by 18.1%, compared to the nine months of 2014. The decrease in expenses as a result of the decrease in tariffs largely due to the ruble devaluation and decreased volume of refined products exports from Russia was partially offset by increased volumes of crude oil exports from Russia and crude oil trading.

Our actual transportation tariffs related to crude oil and refined products deliveries to various exports destinations, weighted by volumes transported, changed to the nine months of 2014 as follows: crude oil pipeline tariffs decreased by 33.1%, railway tariffs for refined products transportation decreased by 35.4%.

Selling, general and administrative expenses

Selling, general and administrative expenses include payroll costs (excluding extraction entities', refineries' and power generation entities' production staff costs), insurance costs (except for property insurance related to extraction and refinery equipment), costs of maintenance of social infrastructure, movement in bad debt provision and other expenses.

Our selling, general and administrative expenses decreased by \$354 million, or by 35.6%, in the third quarter of 2015 and by \$790 million, or by 27.6%, in the nine months of 2015. Largely, this was due to the devaluation of the ruble and the euro against the US dollar.

Depreciation, depletion and amortization

Our depreciation, depletion and amortization expenses decreased by \$501 million, or by 18.0%, compared to the third quarter of 2014, and by \$493 million, or by 7.3%, compared to the nine months of 2014. Our depreciation, depletion and amortization expenses for the third quarter and the nine months of 2015 included \$674 million and \$1,691 million, respectively, related to the West Qurna-2 field, where we commenced commercial production in the second quarter of 2014. In the nine months of 2014, our depreciation, depletion and amortization included \$2,230 million of such expenses, of which \$1,225 million were recognized in the third quarter.

Equity share in income of affiliates

The Group has investments in equity method affiliates and corporate joint ventures. These companies are primarily engaged in crude oil exploration, production, marketing and distribution operations in the Russian Federation, crude oil production and marketing in Kazakhstan and refining operations in the Netherlands. Currently, our largest affiliates are Turgai Petroleum and Tengizchevroil, exploration and production companies operating in Kazakhstan, the Zeeland refinery in the Netherlands and Bashneft-Polus, an exploration and production company that develops the Trebs and Titov oilfields in Timan-Pechora, Russia.

Our share in income of affiliates decreased by \$83 million, or by 53.9%, compared to the third quarter of 2014, and by \$279 million, or by 65.3%, compared to the nine months of 2014, largely as a result of the decrease in income of our upstream affiliates in Kazakhstan.

Taxes other than income taxes

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
In Russia				
Mineral extraction taxes	2,031	3,187	6,307	9,323
Social security taxes and contributions	86	101	275	379
Property tax	75	119	230	368
Other taxes	11	22	33	66
Total in Russia	2,203	3,429	6,845	10,136
International				
Mineral extraction taxes	3	13	12	46
Social security taxes and contributions	24	30	73	93
Property tax	12	12	28	29
Other taxes	11	17	40	51
Total internationally	50	72	153	219
Total	2,253	3,501	6,998	10,355

In the third quarter and the nine months of 2015, our taxes other than income taxes decreased by \$1,248 million, or by 35.6%, and by \$3,357 million, or by 32.4%, respectively, which was driven largely by the decrease in the international crude oil prices and the ruble devaluation. At the same time, the ruble-nominated mineral extraction tax rate increased as a result of the amendments in tax legislation. The decrease in social security taxes and contributions, property and other taxes in Russia against the third quarter and the nine months of 2014 was also mainly due to the ruble devaluation.

In the third quarter and the nine months of 2015, application of the reduced rate for crude oil produced from depleted oilfields and the zero rate for crude oil produced from oilfields with extra heavy crude oil and from greenfields led to \$315 million and \$966 million mineral extraction tax reduction, respectively (\$599 million and \$1,790 million reduction in the third quarter and the nine months of 2014, respectively).

Excise and export tariffs

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
In Russia				
Excise tax on refined products	231	543	678	1,460
Crude oil export tariffs	786	2,507	2,901	7,272
Refined products export tariffs	470	1,481	1,762	4,634
Total in Russia	1,487	4,531	5,341	13,366
International				
Excise tax and sales taxes on refined products	845	1,107	2,340	2,907
Crude oil export tariffs	3	42	37	145
Refined products export tariffs	12	65	29	153
Total internationally	860	1,214	2,406	3,205
Total	2,347	5,745	7,747	16,571

Export tariffs decreased by \$2,824 million, or by 69.0%, in the third quarter of 2015 and by \$7,475 million, or by 61.3%, in the nine months of 2015, largely, due to nearly three-fold decrease in export duty rates for crude oil and refined products.

The decrease in the excise expenses in Russia both to the third quarter and the nine months of 2014 was a result of the ruble devaluation and the decrease in the excise rates. Internationally, the decrease in excise expenses was a result of a decrease in sales volumes subject to excises and depreciation of euro to the US dollar.

Exploration expenses

In the third quarter of 2015, our exploration expenses decreased by \$43 million mostly as a result of the decrease in the amount of dry hole write-offs, compared to the same quarter of the previous year. In the third quarter of 2015, we charged to expense the cost of an exploratory well in Romania in the amount of \$127 million, compared to the cost of a dry well in Ghana in the amount of \$140 million in the third quarter of 2014. During the nine months of 2015, our exploration expenses increased by \$76 million. Dry hole write-offs totaled \$385 million that mostly represented the costs of two dry exploratory wells in Romania, compared to \$243 million in the nine months of 2014 that mostly represented the cost of dry wells in West Africa. This increase in dry hole costs was partially offset by the impact of the ruble devaluation on our geological and geophysical exploration expenses in Russia.

Loss on disposals and impairments of assets

In April 2014, a Group company entered into a contract with a Sinopec group company, to sell the Group's 50% interest in Caspian Investment Resources Ltd. Subsequently, on June 3, 2015, a substitute transaction was made in regard of this sale. In the first quarter of 2014, the Group recognized the loss on this expected disposal in the amount of \$358 million. In the first quarter of 2015, the Group recognized an additional impairment loss related to this transaction amounting to \$80 million.

Also, in the third and the first quarters of 2014, the Group wrote off signing bonuses related to projects in Ghana in the amount of \$45 million and in Sierra Leone and Cote d'Ivoire in the total amount of \$67 million, respectively.

Income taxes

The maximum statutory income tax rate in Russia is 20%. Nevertheless, the actual effective income tax rate may be higher due to non-deductible expenses or lower due to certain non-taxable gains. Moreover, quarterly deviations of the effective income tax rates from the maximum statutory rate may happen due to currency translation losses and gains reported by Russian Group companies, that decrease or increase taxable income in the respective periods.

In the third quarter of 2015, our total income tax expense decreased by \$208 million, or by 25.0%, compared to the third quarter of 2014. At the same time, our income before income tax decreased by \$1,223 million, or by 49.7%.

In the nine months of 2015, our total income tax expense decreased by \$860 million, or by 43.6%, compared to the nine months of 2014, while our income before income tax decreased by \$4,299 million, or by 55.6%.

In the third quarter of 2015, our effective income tax rate was 50.4%, compared to 33.8% in the third quarter of 2014. In the nine months of 2015, our effective income tax rate was 32.3%, compared to 25.5% in the nine months of 2014. The high level of the effective income tax rate was due to non-deductible dry hole write-offs and losses on assets disposals, as well as taxable translation gains reported by our Russian subsidiaries.

Reconciliation of net income to EBITDA (earnings before interest, income taxes, depreciation and amortization)

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
Net income	623	1,620	2,318	5,742
Add back:				
Income tax expense.....	625	833	1,111	1,971
Depreciation and amortization	2,287	2,788	6,292	6,785
Interest expense.....	182	171	534	466
Interest and dividend income	(71)	(74)	(230)	(194)
EBITDA	3,646	5,338	10,025	14,770
Add back loss on disposal of assets and dry hole related write-offs.....	127	185	451	705
EBITDA adjusted for one-off items	3,773	5,523	10,476	15,475
Including impact of West Qurna-2 project.....	707	1,247	1,779	2,264

EBITDA is a non-US GAAP financial measure. EBITDA is defined as net income before interest, taxes and depreciation and amortization. The Company believes that EBITDA provides useful information to investors because it is an indicator of the strength and performance of our business operations, including our ability to finance capital expenditures, acquisitions and other investments and our ability to incur and service debt. While depreciation and amortization are considered as operating costs under US GAAP, these expenses primarily represent the non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods. The EBITDA calculation is commonly used as a basis for some investors, analysts and credit rating agencies to evaluate and compare the periodic and future operating performance and value of companies within the oil and gas industry. EBITDA should not be considered in isolation as an alternative to net income, operating income or any other measure of performance under US GAAP. EBITDA does not include our need to replace our capital equipment over time.

Liquidity and capital resources

	9 months of	
	2015	2014
	(millions of US dollars)	
Net cash provided by operating activities	9,708	12,198
Net cash used in investing activities	(6,364)	(10,978)
Net cash (used in) provided by financing activities	(2,223)	434

Operating activities

Our primary source of cash flow is funds generated from our operations. During the nine months of 2015, cash generated from operations decreased by \$2,490 million, or by 20.4%, compared to the nine months of 2014, largely, as a result of the decrease in net income. In the nine months of 2014, our cash flows from operating activities were negatively affected by an increase in receivables for cost recovery related to commencement of cost compensation within the West Qurna-2 project. Subsequently, after commencement of shipments of compensation crude oil, changes of this receivable do not affect significantly our cash flow from operating activity.

Investing activities

In the nine months of 2015, the amount of cash used in investing activities decreased by 42.0% mostly due to the decrease in capital expenditures that resulted from the ruble devaluation. Moreover, cash from investing activities included proceeds from the sale of our share in Caspian Investment Resources Ltd. and other subsidiaries in the total amount of \$1,260 million.

Our capital expenditures, including non-cash transactions, decreased by 36.1% and amounted to \$7,460 million.

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
Capital expenditures, including non-cash transactions and prepayments				
Exploration and production				
Russia	949	2,094	3,472	6,534
International	840	906	2,623	2,636
Total exploration and production	1,789	3,000	6,095	9,170
Refining, marketing and distribution				
Russia	231	551	882	1,459
International	66	193	290	624
Total refining, marketing and distribution	297	744	1,172	2,083
Chemicals				
Russia	15	88	71	168
International	1	1	1	1
Total chemicals	16	89	72	169
Power generation and distribution	20	62	69	140
Other	18	63	52	118
Total capital expenditures	2,140	3,958	7,460	11,680

In the nine months of 2015, our capital expenditures in the exploration and production segment decreased by \$3,075 million, or by 33.5%. In Russia, capital expenditures decreased mostly due to the effect of ruble devaluation. Outside of Russia, our capital expenditures didn't change significantly compared to the nine months of 2014.

The decrease in capital expenditures in domestic refining, marketing and distribution segment in Russia was due to approaching completion of construction of a catalytic cracking unit at our refinery in Nizhny Novgorod, as well as to the ruble depreciation. The decrease in the international segment was a result of the completion of the construction of heavy residue processing complex at our Bulgarian refinery.

The table below shows our exploration and production capital expenditures in promising new production regions.

	3 rd quarter of		9 months of	
	2015	2014	2015	2014
	(millions of US dollars)			
Yamal.....	72	76	310	370
Caspian region ⁽¹⁾	195	349	738	1,057
Ghana.....	7	145	19	296
Cote d'Ivoire.....	3	6	25	88
Iraq.....	191	300	574	1,101
Uzbekistan	263	248	759	549
Romania.....	88	39	292	95
Cameroon.....	1	–	131	–
Nigeria	97	–	272	–
Total	917	1,163	3,120	3,556

⁽¹⁾ Russian and international projects.

Financing activities

In the nine months of 2015, net movements of short-term and long-term debt generated an outflow of \$352 million, compared to an inflow of \$1,787 million in the nine months of 2014.

In the first quarter of 2014, the Company received the loans from Sberbank in the amount of \$500 million maturing in 2021 and bearing interest at twelve month LIBOR plus 2.75% per annum and from Promsvyazbank in the amount of \$300 million maturing in 2019 and bearing interest at three month LIBOR plus 2.75% per annum.