



LUKOIL

PJSC LUKOIL

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

**for the three and six-month periods ended
30 June 2016 and 2015**

The following report contains a discussion and analysis of the financial position of PJSC LUKOIL at 30 June 2016 and the results of its operations for the three and six month periods ended 30 June 2016 and 2015, as well as significant factors that may affect its future performance. It should be read in conjunction with our International Financial Reporting Standards (“IFRS”) condensed interim consolidated financial statements and notes thereto for the respective periods.

References to “LUKOIL,” “the Company,” “the Group,” “we” or “us” are references to PJSC LUKOIL and its subsidiaries and equity affiliates. All ruble amounts are in millions of Russian rubles (“RUB”), unless otherwise indicated. Income and expenses of our foreign subsidiaries were translated to rubles at rates which approximate actual rates at the date of the transaction. Tonnes of crude oil and natural gas liquids produced were translated into barrels using conversion rates characterizing the density of crude oil from each of our oilfields and the 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

	2 nd quarter of			1 st half of		
	2016	2015	Change, %	2016	2015	Change, %
	(millions of rubles)					
Sales.....	1,338,959	1,476,966	(9.3)	2,516,633	2,917,271	(13.7)
EBITDA (operating) ⁽¹⁾	189,571	206,679	(8.3)	381,563	417,387	(8.6)
EBITDA (operating) ⁽¹⁾ net of West Qurna-2 project... ..	182,681	171,085	6.8	353,179	354,553	(0.4)
Profit for the period attributable to LUKOIL shareholders	62,567	63,748	(1.9)	105,392	167,779	(37.2)
Capital expenditures, including non-cash transactions	118,886	150,773	(21.1)	241,447	304,844	(20.8)
Free cash flow ⁽²⁾	56,991	16,968	235.9	93,406	79,879	16.9
Production, including our share in equity affiliates:						
Hydrocarbons, thousand BOE per day.....	2,164	2,377	(9.0)	2,259	2,373	(4.8)
Hydrocarbons, thousand BOE.....	196,901	216,342	(9.0)	411,110	429,529	(4.3)
Crude oil and natural gas liquids, thousand barrels	167,046	187,041	(10.7)	349,629	370,009	(5.5)
Gas available for sale, million cubic meters.....	5,073	4,979	1.9	10,447	10,114	3.3
Production of refined products, thousand tonnes.....	15,460	14,713	5.1	30,327	28,793	5.3

⁽¹⁾ Profit from operating activities before depreciation, depletion and amortization.

⁽²⁾ Cash flow from operating activities less capital expenditures and acquisition of licenses.

Our results for the first half of 2016 were affected by a decrease in average hydrocarbon prices and fluctuations of ruble exchange rates to the US dollar and euro. This was partially offset by lower mineral extraction tax and export duty rates. As far as we compensated most of the costs incurred within the West Qurna-2 project, we were eligible for significantly lower volumes of compensation crude oil, compared to the respective periods of 2015 that affected our EBITDA (operating) and production volumes (see p. 6 for details). Timely upgrade of our Russian refineries allowed to enhance our product slate and supported our financial results in unfavorable macroeconomic environment.

In the first half of 2016, our profit amounted to 105 billion RUB and our EBITDA (operating) amounted to 382 billion RUB, representing a decrease of 37.2% and 8.6%, respectively, compared to the first half of 2015. Despite lower hydrocarbon prices, our net profit for the second quarter of 2016 remained practically unchanged compared to the second quarter of 2015. Net of the West Qurna-2 project, the Group’s EBITDA (operating) increased by 6.8% in the second quarter of 2016 and remained flat in the first half of 2016 compared to respective periods of 2015.

In the first half of 2016, we continued generating strong free cash flow that amounted to 93 billion RUB, compared to 80 billion RUB in the first half of 2015.

Business overview

LUKOIL is one of the world's largest publicly traded vertically integrated energy companies in terms of hydrocarbon reserves that amounted under SEC standards to 16.6 billion BOE at 1 January 2016 and comprised of 12.6 billion barrels of crude oil and 23.8 trillion cubic feet of gas. Most of our reserves are conventional. Our daily hydrocarbon production in the first half of 2016 amounted to 2.2 million BOE with liquid hydrocarbons representing approximately 85% of our overall production volumes.

The primary activities of LUKOIL and its subsidiaries are oil exploration, production, refining, marketing and distribution.

Our operations are divided into three main business segments:

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

Each of our 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 12, 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 analyze either of our main segments separately in the discussion that follows. However, we present the financial data for each in Note 28 “Segment information” to our condensed interim consolidated financial statements.

Changes in Group structure

In line with the Company's strategy of optimization its downstream operations in Europe, we sold petrol station networks in Poland, Latvia and Lithuania in the first quarter of 2016 and petrol stations networks in Ukraine and Estonia in the second quarter of 2015.

In August 2015, a Group company closed the transaction to sell its 50% interest in Caspian Investment Resources Ltd, an exploration and production company operating in Kazakhstan, to a Sinopec group company for \$1,067 million (70.1 billion RUB). Related structural decrease in the Group's crude oil production amounted to approximately 20 thousand barrels per day.

Sectorial sanctions against the Russian companies

In July-September 2014, the United States (“US”), the European Union (“EU”) and other countries imposed a set of economic sanctions on Russia, including certain sectoral sanctions which affect Russian oil and gas companies. Such sectoral sanctions prohibit US and the EU companies and individuals from providing, exporting, or re-exporting directly or indirectly, goods, services (except for financial services), or technology in support of exploration or production for deepwater, Arctic offshore, or shale projects on the territory of the Russian Federation.

The Company is not subject to any financial restrictions and is not currently involved in deepwater, Arctic offshore or shale projects in Russia. That is why we assess the impact of the sanctions on the Company's activities as immaterial.

Operational highlights

Hydrocarbon production

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

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
Crude oil and natural gas liquids production⁽¹⁾	(thousand BOE per day)			
Consolidated subsidiaries				
Western Siberia	845	926	855	934
Timan-Pechora	341	339	343	332
Ural region	323	320	323	316
Volga region.....	126	140	130	140
Other in Russia.....	36	37	36	37
Total in Russia.....	1,671	1,762	1,687	1,759
Iraq ⁽²⁾	69	177	132	167
Other outside Russia.....	37	41	43	41
Total outside Russia.....	106	218	175	208
Total consolidated subsidiaries	1,777	1,980	1,862	1,967
Our share in equity affiliates				
in Russia	21	15	20	15
outside Russia.....	38	60	39	62
Total share in equity affiliates.....	59	75	59	77
Total crude oil and natural gas liquids	1,836	2,055	1,921	2,044
Natural and petroleum gas available for sale production				
Consolidated subsidiaries				
Western Siberia	158	173	163	177
Timan-Pechora	15	13	15	12
Ural region	11	18	13	22
Volga region.....	24	6	22	6
Total in Russia.....	208	210	213	217
Total outside Russia.....	110	101	115	101
Total consolidated subsidiaries	318	311	328	318
Share in equity affiliates				
in Russia	1	1	1	1
outside Russia.....	9	10	9	10
Total share in production of equity affiliates.....	10	11	10	11
Total natural and petroleum gas available for sale ...	328	322	338	329
Total daily hydrocarbon production	2,164	2,377	2,259	2,373
		(millions of rubles)		
Hydrocarbon extraction expenses	53,594	52,144	107,671	103,978
- in Russia.....	41,107	37,934	80,818	74,015
- outside Russia ⁽³⁾	4,080	2,837	8,243	6,027
- in Iraq.....	8,407	11,373	18,610	23,936
Mineral extraction tax in Russia	105,073	128,720	174,811	245,369
		(ruble per BOE)		
Hydrocarbon extraction expenses⁽³⁾	246	213	238	209
- in Russia	241	212	234	207
- outside Russia ⁽³⁾	309	224	291	239
		(US dollar per BOE)		
Hydrocarbon extraction expenses⁽³⁾	3.73	4.04	3.41	3.68
- in Russia.....	3.65	4.02	3.35	3.64
- outside Russia ⁽³⁾	4.69	4.25	4.15	4.17

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

⁽²⁾ Compensation oil that represented approximately 32% of production from the West Qurna-2 field in the first half of 2016 and 52% in the first half of 2015.

⁽³⁾ Excluding expenses at the West Qurna-2 field.

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. Our international upstream segment includes stakes in PSA's and other projects in Kazakhstan, Azerbaijan, Uzbekistan, Romania, Iraq, Egypt, Ghana, Cote d'Ivoire, Norway, Cameroon, Nigeria and Mexico.

Crude oil and natural gas liquids production. In the first half of 2016, we produced (including the Company's share in equity affiliates) 46.8 million tonnes, or 342.8 million barrels, of crude oil, compared to 49.6 million tonnes, or 363.4 million barrels, of crude oil in the first half of 2015.

In the first half of 2016, the output of natural gas liquids at the Group gas processing plants in Western Siberia, Ural and Volgograd regions of Russia was 6.8 million BOE, compared to 6.6 million BOE in the first half of 2015.

The following table presents our crude oil production in the first half of 2016 and 2015 by major regions.

(thousands of tonnes)	Change to 2015				1 st half of 2015
	1 st half of 2016	Total, %	Change in structure	Organic change	
Western Siberia.....	20,629	(7.9)	–	(1,773)	22,402
Timan-Pechora.....	8,644	3.9	–	328	8,316
Ural region.....	7,548	1.7		123	7,425
Volga region.....	3,160	(6.6)		(223)	3,383
Other in Russia.....	922	(1.4)	–	(13)	935
Crude oil produced in Russia.....	40,903	(3.7)	–	(1,558)	42,461
Iraq ⁽¹⁾	3,510	(20.4)	–	(902)	4,412
Other outside Russia.....	1,000	5.3	–	50	950
Crude oil produced outside Russia.....	4,510	(15.9)	–	(852)	5,362
Total crude oil produced by consolidated subsidiaries.....	45,413	(5.0)	–	(2,410)	47,823
Our share in crude oil produced by equity affiliates:					
in Russia.....	468	33.7	–	118	350
outside Russia.....	893	(39.0)	(523)	(49)	1,465
Total crude oil produced.....	46,774	(5.8)	(523)	(2,341)	49,638

⁽¹⁾ Compensation oil that represented approximately 32% of production from the West Qurna-2 field in the first half of 2016 and 52% in the first half of 2015.

The main oil producing region for the Company is Western Siberia where we produced 45.4% of our crude oil in the first half of 2016 (46.8% in the first half of 2015).

Crude oil production in Western Siberia continued to decline due to natural depletion of reserves, increase in water cut and the Company's decision to reallocate capital to higher return projects in other regions of Russia, in particular those benefiting from tax incentives. We expect production decline rates in Western Siberia to decrease as a result of our recent decision to intensify production drilling in this region. Production growth in Timano-Pechora was primarily driven by ramp-up of production at the Yaregskoye and Usinskoye fields, as well as the fields in Denisovskaya depression. Production growth in Ural region was primarily driven by successful drilling on existing brownfields and launch of new small sized fields.

The decrease in our international production was a result of lower volumes of production from the West Qurna-2 oilfield in Iraq attributable to the Company. We compensated the major part of our initial costs incurred within the project and therefore were eligible for less volumes of compensation crude oil compared to the second quarter and the first half of 2015 (for details see p. 6).

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

The decrease in our share in crude oil produced by equity affiliates outside Russia resulted from the disposal of our 50% share in Caspian Investment Resources Ltd in the middle of 2015.

In the nearest future, we plan to start production at two new major fields, the V. Filanovskogo field in the Caspian Sea (Volga region) and the Pyakyakhinskoye field in the Bolshekhetskaya depression (Western Siberia). Launch of these fields will enable us to significantly increase our daily hydrocarbon production with a major positive impact on our financial results due to tax incentives and high quality reserve base.

Natural and petroleum gas production. In the first half of 2016, we produced 12,261 million cubic meters (72.2 million BOE) of gas (including our share in equity affiliates), that is 3.1% more than in the first half of 2015. Our available for sale gas production amounted to 10,447 million cubic meters (61.5 million BOE), compared to 10,114 million cubic meters (59.6 million BOE) in the first half of 2015.

The following table presents our available for sale gas production in the first half of 2016 and 2015 by major regions.

(millions of cubic meters)	<u>Change to 2015</u>				1 st half of 2015
	1 st half of 2016	Total, %	Change in structure	Organic change	
Western Siberia.....	5,024	(7.4)	–	(399)	5,423
Timan-Pechora.....	472	25.5	–	96	376
Ural region.....	395	(40.8)	–	(272)	667
Volga region.....	680	261.7	–	492	188
Other in Russia.....	11	–	–	–	11
Gas produced in Russia.....	6,582	(1.2)	–	(83)	6,665
Gas produced outside Russia.....	3,572	15.0	–	466	3,106
Total available for sale gas produced by consolidated subsidiaries.....	10,154	3.9	–	383	9,771
Our share in gas produced by equity affiliates:					
in Russia.....	28	21.7	–	5	23
outside Russia.....	265	(17.2)	(63)	8	320
Total available for sale gas produced.....	10,447	3.3	(63)	396	10,114

Our major gas production field is the Nakhodkinskoe field, which is in natural decline. Our production at the field was 3,423 million cubic meters of natural gas in the first half of 2016 (3,731 million cubic meters in the first half of 2015). This decrease was offset by commencement of gas production at the Yu. Korchagin field in the first half of 2016. Decrease in production in Ural region was largely a result of increase in own gas consumption following the launch of new power generation unit at the Perm refinery. We are planning to start gas production at the Pyakyakhinskoye field in the Bolshekhetskaya depression of Western Siberia by the end of 2016. This will enable us to substantially increase our gas production in the region.

Our international gas production (including our share in affiliates' production) increased by 12.0%, compared to the first half of 2015, which resulted from the increase in production in Uzbekistan and Azerbaijan. Growth of gas production in Uzbekistan was due to launching new wells and a compressor booster station at the Gissar field. We are currently involved in construction of a gas treatment plant in the region, which completion together with further upstream works will enable us to significantly increase gas production in that region.

West Qurna-2 project. The West Qurna-2 field in Iraq is 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). Service agreement for the West Qurna-2 field development and production was signed on 31 January 2010. Currently, 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 production of 120 thousand barrels per day in March 2014. According to the service agreement, costs compensation begins after this level of production is achieved and maintained during any 90 days within a 120-day period. In June 2014, we met this requirement and from the second quarter of 2014 started to receive cost compensation. The project's target production level is 1.2 million barrels per day and the total term of the contract is 25 years.

Accounting for the cost compensation within the West Qurna-2 project in our consolidated statement of financial position and consolidated statement of profit or loss and other comprehensive income is as follows.

Capital expenditures are recognized in *Property, plant and equipment*. Extraction expenses are recognized in *Operating expenses* in respect of all the volume of crude oil production at the field regardless of the volume of compensation crude oil the Group is eligible for. As the compensation revenue is recognized, capitalized costs are amortized.

There are two steps of revenue recognition:

- The Iraqi party, on a quarterly basis, approves invoice for cost recovery and remuneration fee for which the Group is eligible in the reporting period. Amount of the invoice depends on crude oil production volumes during the period and current crude oil market prices. Approved invoice amount and the remuneration fee for the reporting quarter are recognized in crude oil sales revenue.
- Based on the approved invoices, the Iraqi party arranges schedule of crude oil shipments against its debt for cost compensation and remuneration. As this crude oil is actually shipped, its cost is recognized at current market price in *Cost of purchased crude oil, gas and products*. Further, revenue from sales of this crude oil, or products from its refining, is recognized in *Sales (including excise and export tariffs)*. Unsold crude oil and refined products are recognized in *Inventories*.

The following table summarizes data on capital and operating cost incurred, compensation crude oil received, costs yet unrecovered and remuneration fee.

	Costs incurred ⁽¹⁾	Crude oil received	Unrecovered costs	Remuneration fee
		(millions of US dollars)		
Cumulative at 31 December 2015	6,801	5,169	1,632	198
Change during the first half of 2016.....	429	1,071	(642)	64
Income tax.....	–	–	–	(54)
Cumulative at 30 June 2016	7,230	6,240	990	208

⁽¹⁾ Including prepayments.

The West Qurna-2 project's summary is presented below:

	2 nd quarter			
	2016			2015
	(thousand barrels)	(thousand tonnes)	(thousand barrels)	(thousand tonnes)
Total production ⁽¹⁾	37,044	5,400	31,013	4,521
Production related to cost compensation and remuneration ⁽¹⁾	6,241	909	16,139	2,353
Shipment of compensation crude oil ^{(1) (2)}	17,755	2,588	17,127	2,497
	(millions of rubles)	(millions of US dollars)	(millions of rubles)	(millions of US dollars)
Cost compensation	13,381	203	45,440	863
Remuneration fee	2,097	32	1,580	30
Cost of compensation crude oil, received as debt settlement (included in <i>Cost of purchased crude oil, gas and products</i>) ⁽²⁾	44,518	676	53,023	1,007
Extraction expenses	8,407	127	11,373	216
Depreciation, depletion and amortization.....	4,968	73	34,173	649
EBITDA (operating)	6,890	105	35,594	676

⁽¹⁾ Translated into barrels using conversion rate characterizing the density of the field.

⁽²⁾ This crude oil is sold to third party customers or delivered to our refineries. After realization of these products, respective sales revenues are recognized.

	1 st half of			
	2016	2016	2015	2015
	(thousand barrels)	(thousand tonnes)	(thousand barrels)	(thousand tonnes)
Total production ⁽¹⁾	75,062	10,942	57,686	8,410
Production related to cost compensation and remuneration ⁽¹⁾	24,081	3,510	30,260	4,412
Shipment of compensation crude oil ⁽¹⁾⁽²⁾	35,282	5,143	32,708	4,769
	(millions of rubles)	(millions of US dollars)	(millions of rubles)	(millions of US dollars)
Cost compensation	42,860	598	83,501	1,475
Remuneration fee	4,536	65	3,446	60
Cost of compensation crude oil, received as debt settlement (included in <i>Cost of purchased crude oil, gas and products</i>) ⁽²⁾	73,994	1,071	95,065	1,683
Extraction expenses	18,610	264	23,936	418
Depreciation, depletion and amortization.....	24,345	330	57,060	1,017
EBITDA (operating)	28,384	393	62,834	1,114

⁽¹⁾ Translated into barrels using conversion rate characterizing the density of the field.

⁽²⁾ This crude oil is sold to third party customers or delivered to our refineries. After realization of these products, respective sales revenues are recognized.

The Group is exposed to various 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.

Refining, marketing and trading

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

We own two petrochemical plants in Russia, one in Ukraine and petrochemical capacity at our refinery in Bulgaria. Currently, production at our petrochemical plant in Ukraine is suspended due to adverse economic and political environment in this country.

Compared to the first half of 2015, the total volume of refined products produced by the Group increased by 5.3%.

In Russia, our production volumes decreased by 2.0% due to throughput optimization as a result of general weakening of refining margins in Russia driven by excise tax increases in January and April 2016. Due to completed upgrade program and throughput optimization, our Russian refineries remained profitable in the first half of 2016 despite unfavorable macroeconomic environment. Timely launch of new secondary processing units in 2015 and 2016 enabled us to substantially enhance our refined product slate by reducing production of fuel oil and vacuum gasoil in favor of light products. In order to optimize dark products yield, in the first half of 2016, we also decreased throughput volumes and redirected vacuum gas oil produced at our Perm and Ukhta refineries from export deliveries to supply catalytic cracking unit at our refinery in Nizhny Novgorod. We expect our refined product slate to further enhance via achieving full utilization of the hydrocracking unit at our Volgograd refinery launched in the second quarter of 2016. Maintenance works at our refineries in Nizhny Novgorod and Ukhta also affected our refining volumes in the second quarter and the first half of 2016.

Internationally, the production increase amounted to 19.9% against the background of low output in the first quarter of 2015 due to overhauls at our Italian refinery as well as strong refining margins.

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.

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(thousand barrels per day)			
Refinery throughput at the Group refineries	1,322	1,254	1,298	1,237
- in Russia	797	827	803	818
- outside Russia ⁽¹⁾	525	427	495	419
Refinery throughput at third party refineries	6	17	6	17
Total refinery throughput	1,328	1,271	1,304	1,254
	(thousands of tonnes)			
Production of the Group refineries in Russia	9,365	9,758	18,818	19,194
- diesel fuel	3,142	2,993	6,389	6,135
- gasoline	1,837	1,589	3,643	3,219
- fuel oil	1,116	1,993	2,672	4,080
- jet fuel	469	639	910	1,076
- motor oils	263	250	502	447
- other products	2,538	2,294	4,702	4,237
Production of the Group refineries outside Russia	6,095	4,955	11,509	9,599
- diesel fuel	2,601	1,961	4,895	3,903
- gasoline	1,301	1,109	2,468	2,214
- fuel oil	925	821	1,786	1,472
- jet fuel	236	221	420	409
- motor oils	52	42	100	98
- other products	980	801	1,840	1,503
Refined products produced by the Group	15,460	14,713	30,327	28,793
Refined products produced at third party refineries	71	206	159	406
Total refined products produced	15,531	14,919	30,486	29,199
Products produced at petrochemical plants	322	264	646	433
- in Russia	225	178	458	255
- outside Russia	97	86	188	178
	(millions of RUB)			
Refining expenses at the Group refineries	22,804	21,004	45,254	43,172
- in Russia	11,076	10,403	21,211	18,925
- outside Russia	11,728	10,601	24,043	24,247
	(ruble per tonne)			
Refining expenses	190	184	192	193
- in Russia	153	138	145	128
- outside Russia	245	273	267	320
	(US dollar per tonne)			
Refining expenses	2.88	3.50	2.74	3.37
- in Russia	2.32	2.63	2.08	2.26
- outside Russia	3.73	5.18	3.81	5.55
	(millions of RUB)			
Capital expenditures	10,255	18,247	22,539	42,783
- in Russia	8,506	12,685	18,447	30,131
- outside Russia	1,749	5,562	4,092	12,652

⁽¹⁾ Including refined product processed.

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

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.

The following tables show the volumes of crude oil purchases by the Group during the periods considered.

	2 nd quarter of			
	2016		2015	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Purchases in Russia.....	1,510	206	4,618	630
Purchases for trading internationally.....	42,690	5,824	41,253	5,628
Purchases for refining internationally	28,961	3,951	20,897	2,851
Shipment of the West Qurna-2 compensation crude oil ⁽¹⁾	17,754	2,588	17,125	2,497
Total crude oil purchased	90,915	12,569	83,893	11,606

	1 st half of			
	2016		2015	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Purchases in Russia.....	3,035	414	6,854	935
Purchases for trading internationally.....	88,832	12,119	79,655	10,867
Purchases for refining internationally	53,458	7,293	37,947	5,177
Shipment of the West Qurna-2 compensation crude oil ⁽¹⁾	35,281	5,143	32,706	4,769
Total crude oil purchased	180,606	24,969	157,162	21,748

⁽¹⁾ Translated into barrels using conversion rate characterizing the density of the field.

Compared to the second quarter and the first half of 2015, our purchases for refining at international refineries increased by 38.6% and 40.9%, respectively, and our purchases for trading increased by 3.5% and 11.5%, respectively. Moreover, in the second quarter and the first half of 2016, the Group received 2.6 million tonnes and 5.1 million tonnes, respectively, of compensation crude from Iraq's state-owned South Oil Company as cost compensation within the West Qurna-2 project (in the respective periods of 2015, the Group received 2.5 million tonnes and 4.8 million tonnes of compensation crude oil).

The table below summarizes figures for our refined products marketing and trading activities.

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(thousands of tonnes)			
Retail sales	3,338	3,472	6,507	6,676
Wholesale sales	27,750	27,546	53,390	53,809
Total refined products sales	31,088	31,018	59,897	60,485
Refined products purchased in Russia.....	421	433	791	777
Refined products purchased internationally	16,992	18,165	32,089	33,771
Total refined products purchased	17,413	18,598	32,880	34,548

In the first half of 2016, in line with the strategy to optimize our downstream operations, a Group company sold 100% of its interest in LUKOIL Poland, LUKOIL Baltija and LUKOIL Baltija R, distribution companies operating over 270 petrol stations in Poland, Lithuania and Latvia. In July 2015, we sold 100% of interest in LUKOIL Eesti, and in April 2015 – 100% of interest in LUKOIL Ukraine.

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:

	2 nd quarter of			
	2016		2015	
	(thousands of barrels)	(thousands of tonnes)	(thousands of barrels)	(thousands of tonnes)
Exports of crude oil to Customs Union	7,125	972	7,029	959
Exports of crude oil beyond Customs Union	58,669	8,004	59,292	8,089
Total crude oil exports	65,794	8,976	66,321	9,048
Exports of refined products		4,439		5,144

	1 st half of			
	2016		2015	
	(thousands of barrels)	(thousands of tonnes)	(thousands of barrels)	(thousands of tonnes)
Exports of crude oil to Customs Union	14,323	1,954	14,183	1,935
Exports of crude oil beyond Customs Union	116,378	15,877	119,926	16,361
Total crude oil exports	130,701	17,831	134,109	18,296
Exports of refined products.....		9,370		10,403

In the first half of 2016, the volume of our crude oil exports from Russia decreased by 2.5%, and we exported 43.6% of our domestic crude oil production (43.1% in the first half of 2015) and 216 thousand tonnes of crude oil purchased from our affiliates and third parties (794 thousand tonnes in the first half of 2015). The decrease in crude oil exports was a result of lower domestic production. The volume of our refined products exports decreased by 9.9% compared to the first half of 2015 due to higher domestic sales volumes driven by favorable netbacks and decreased refining volumes.

Substantially, we use the Transneft infrastructure to export our crude oil. Nevertheless, during the second quarter and first half of 2016, we exported 2,178 thousand tonnes and 4,091 thousand tonnes, respectively, through our own infrastructure (1,865 thousand tonnes and 3,689 thousand tonnes during the second quarter and first half of 2015). All the volume of crude oil exported that bypassed Transneft was routed beyond the Customs Union.

In the first half of 2016, the Company exported 600 thousand tonnes of light crude oil through the Eastern Siberia – Pacific Ocean pipeline compared to 795 thousand tonnes in the first half of 2015. This allowed us to preserve the premium quality of crude oil and thus enabled us to achieve higher netbacks compared to exports to traditional Western markets.

During the second quarter of 2016, our revenue from export of crude oil and refined products from Russia both to Group companies and third parties amounted to 172 billion RUB and 98 billion RUB, respectively (196 billion RUB for crude oil and 118 billion RUB for refined products in the second quarter of 2015). During the first half of 2016, our revenue from export of crude oil and refined products from Russia both to Group companies and third parties amounted to 307 billion RUB and 186 billion RUB, respectively (395 billion RUB for crude oil and 239 billion RUB for refined products in the first half of 2015).

Power generation. In the first half of 2016, we continued to develop the power generation sector of our business as part of our strategic development program. This sector encompasses all aspects of the power generation business, from generation to transmission and sale of heat and electrical power. Our power generation business sector now includes OOO LUKOIL-Volgogradenergo, OOO LUKOIL-Kubanenergo, OOO LUKOIL-Astrakhanenergo, OOO LUKOIL-Rostovenergo, OOO LUKOIL-Stavropolenergo, OOO Rostovskie Teplovyie Seti, OOO LUKOIL-Ecoenergo, our own power generating facilities at our oil and gas fields in Russia and at our refineries in Bulgaria, Romania, Italy and Perm region of Russia.

Main macroeconomic factors affecting our results of operations

Changes in the international 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. During the first half of 2016, the price for Brent crude oil fluctuated between \$26 and \$50 per barrel, reached its maximum of \$50.7 in the middle of June and minimum of \$25.9 in the beginning of January, and averaged 31.2% less than in the first half of 2015. Nevertheless, as a result of ruble devaluation, the prices expressed in rubles decreased less significantly.

Substantially all the crude oil the Group exports is Urals blend. The following tables show the average crude oil and refined product prices in the respective periods of 2016 and 2015.

	2 nd quarter of		Change,	1 st half of		Change,
	2016	2015	%	2016	2015	%
	(in US dollars per barrel, except for figures in percent)					
Brent crude.....	45.59	61.88	(26.3)	39.81	57.84	(31.2)
Urals crude (CIF Mediterranean) ⁽¹⁾	44.30	62.25	(28.8)	38.55	57.68	(33.2)
Urals crude (CIF Rotterdam) ⁽¹⁾	43.37	61.21	(29.1)	37.56	56.83	(33.9)
	(in US dollars per metric tonne, except for figures in percent)					
Fuel oil 3.5% (FOB Rotterdam).....	199.75	323.50	(38.3)	167.77	299.51	(44.0)
Diesel fuel 10 ppm (FOB Rotterdam).....	411.25	579.97	(29.1)	362.30	554.66	(34.7)
High-octane gasoline (FOB Rotterdam).....	503.24	671.00	(25.0)	445.11	608.90	(26.9)

Source: Platts.

	2 nd quarter of		Change,	1 st half of		Change,
	2016	2015	%	2016	2015	%
	(in rubles per barrel, except for figures in percent)					
Brent crude.....	3,004	3,258	(7.8)	2,797	3,320	(15.8)
Urals crude (CIF Mediterranean) ⁽¹⁾	2,919	3,278	(11.0)	2,708	3,311	(18.2)
Urals crude (CIF Rotterdam) ⁽¹⁾	2,858	3,223	(11.3)	2,639	3,262	(19.1)
	(in rubles per metric tonne, except for figures in percent)					
Fuel oil 3.5% (FOB Rotterdam).....	13,161	17,034	(22.7)	11,787	17,191	(31.4)
Diesel fuel 10 ppm (FOB Rotterdam).....	27,097	30,538	(11.3)	25,455	31,836	(20.0)
High-octane gasoline (FOB Rotterdam).....	33,158	35,331	(6.2)	31,273	34,949	(10.5)

Translated into rubles using average exchange rate for the period.

⁽¹⁾ The Company sells various crude oil blends 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 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 respective periods of 2016 and 2015.

	2 nd quarter of		Change,	1 st half of		Change,
	2016	2015	%	2016	2015	%
	(in rubles per metric tonne, except for figures in percent)					
Fuel oil.....	6,794	7,415	(8.4)	5,674	6,900	(17.8)
Diesel fuel	28,835	28,901	(0.2)	28,011	28,619	(2.1)
High-octane gasoline (Regular)	34,524	31,963	8.0	33,081	30,159	9.7
High-octane gasoline (Premium)	35,777	33,016	8.4	34,637	31,391	10.3

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, a devaluation of the ruble against the US dollar generally causes our revenues to increase in ruble terms, and vice versa. Ruble inflation also affects the results of our operations.

The following table provides data on inflation in Russia and change in the ruble-dollar and ruble-euro exchange rates.

	2 nd quarter		1 st half of	
	2016	2015	2016	2015
Ruble inflation (CPI), %	1.2	1.0	3.3	8.5
Average exchange rate for the period (ruble to US dollar)	65.9	52.7	70.3	57.4
Exchange rate at the beginning of the period (ruble to US dollar) ..	67.6	58.5	72.9	56.3
Exchange rate at the end of the period (ruble to US dollar)	64.3	55.5	64.3	55.5
Average exchange rate for the period (ruble to euro).....	74.4	58.2	78.4	64.3
Exchange rate at the beginning of the period (ruble to euro)	76.5	63.4	79.7	68.3
Exchange rate at the end of the period (ruble to euro)	71.2	61.5	71.2	61.5

Taxation

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 changed monthly and is calculated by multiplying the base rate by a coefficient reflecting average international Urals price and ruble-dollar exchange rate during the month. The base rate for 2016 is set at 857 rubles per metric tonne extracted (766 rubles for 2015).

The tax rate is zero when the average international Urals price is less than, or equal to, \$15.00 per barrel. In 2016, each \$1.00 per barrel increase in the international Urals price above \$15.00 per barrel results in an increase in the tax rate by \$0.45 per barrel (\$0.40 per barrel in 2015).

The mineral extraction tax on crude oil is payable in rubles per tonne of crude oil extracted.

There are different types of tax incentives on the mineral extraction tax on crude oil applied to our fields and deposits:

- A special coefficient is applied to the standard tax rate depending on location, depletion, type of reserves, size and complexity of a particular field, as well as on the average international Urals price and the ruble-dollar exchange rate. This type of incentive with different coefficients is applied to our highly depleted fields (more than 80% depletion), our Yu. Korchagin field located in the Caspian offshore, the Permian layers of our Usinskoye field in Timan-Pechora producing high-viscous crude oil, our Pyakyakhinskoye field located in the Yamal-Nenets region of Western Siberia, a number of fields in the Nenets Autonomous region, as well as to our new small-sized fields (recoverable reserves less than 5 million tonnes) and fields and deposits with low permeability like V. N. Vinogradov field and Tyumen deposits;
- A fixed tax rate of 15% of the international Urals price is applied to our V. Filanovsky field, located in the Caspian offshore;
- A zero tax rate is applied to our Yaregskoye field producing extra-viscous crude oil, as well as to unconventional deposits (Bazhenov and others).

Some of the mineral extraction tax incentives are limited in time or by cumulative oil production volumes.

The table on the page 14 illustrates the impact of mineral extraction tax incentives on the tax rate at \$50 Urals price.

Natural gas extraction tax rate. 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, regional location and complexity of particular gas field.

In the first half of 2016, actual average natural gas extraction tax rate for our major gas field – Nakhodkinskoe in Western Siberia amounted to 208 rubles per thousand cubic meters (150 rubles in the first half of 2015). The rate to this field is subject to a special regional reducing coefficient.

Crude oil export duty rate is denominated in US dollars per tonne of crude oil exported and is calculated on a progressive scale according to the bellow table.

International Urals price	Export duty rate
Less than, or equal to, \$109.50 per tonne (\$15.00 per barrel)	\$0.00 per tonne
Above \$109.50 but less than, or equal to, \$146.00 per tonne (\$20.00 per barrel)	35% of the difference between the actual price and \$109.50 per tonne (or \$0.35 per barrel per each \$1.00 increase in the Urals price over \$15.00)
Above \$146.00 but less than, or equal to, \$182.50 per metric tonne (\$25.00 per barrel)	\$12.78 per tonne plus 45% of the difference between the actual price and \$146.00 per tonne (or \$0.45 per barrel per each \$1.00 increase in the Urals price over \$20.00)
Above \$182.50 per metric tonne (\$25.00 per barrel)	\$29.20 per tonne plus 42% of the difference between the actual price and \$182.50 per tonne (or \$0.42 per barrel per each \$1.00 increase in the Urals price over \$25.00)

The export duty rate changes every month with the rate for the next month being based on average Urals price for the period from the 15th day of the previous month to the 14th day of the current month.

Crude oil produced at some of our fields is subject to special export duty rates calculated according to special formulas, which are lower than standard rates. A reduced rate is applied to crude oil produced at our Yaregskoye field producing extra-viscous crude oil and our Yu. Korchagin field in the Caspian offshore. A zero rate applies to crude oil of our V. Filanovskogo field also located in the Caspian offshore.

The table below illustrates the impact of tax incentives for different fields and deposits in our portfolio at \$50 per barrel Urals price under 2016 tax formulas.

	Mineral extraction tax	Export duty	Total	As % of oil price
	(in US dollars per barrel, except for figures in percent)			
Standard	15.7	14.5	30.2	60.5
Yaregskoye field	0.0	1.8	1.8	3.6
Yu. Korchagin field.....	5.5	0.0	5.5	10.9
V. Filanovskogo field.....	7.5	0.0	7.5	15.0
Usinskoye (Permian layers)	5.5	14.5	20.0	39.9
Pyakakhinskoye field	5.5	14.5	20.0	39.9
V. Vinogradova field.....	7.5	14.5	22.0	44.1
Highly depleted fields	8.6-15.7	14.5	23.1-30.2	46.1-60.5
Small sized fields	9.3-15.7	14.5	23.8-30.2	47.6-60.5
Tyumen deposits	13.7	14.5	28.2	56.4

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

	From 1 January 2016 to 31 December 2016	From 1 January 2015 to 31 December 2015
Multiplier for:		
Light and middle distillates	0.40	0.48
Diesel fuel	0.40	0.48
Gasolines.....	0.61	0.78
Straight-run gasoline	0.71	0.85
Fuel oil	0.82	0.76

Crude oil and refined products exports from Russia are subject to two steps of customs declaration and duty payments: temporary and complete. A temporary declaration is submitted based on preliminary exports volumes and the duty is paid in rubles translated from US dollars at the date of the temporary declaration. A complete declaration is submitted after receiving the actual data on the exported volumes, but no 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, the US dollar exchange rate at the date of the complete declaration (except for pipeline deliveries when the exchange rate at the temporary declaration date is used) and the export duty rate. If temporary and complete declarations are submitted in 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 adjustments. For the purposes of the IFRS consolidated financial statements, temporary declarations at the reporting period end are translated to rubles from US dollars using the period-end exchange rate.

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

The following tables represent average enacted rates for taxes specific to the oil industry in Russia for the respective periods.

		2 nd quarter of			1 st half of		
		2016	2015	Change, %	2016	2015	Change, %
Export duties on crude oil	\$/tonne	67.15	130.41	(48.5)	61.08	130.30	(53.1)
Export duties on refined products							
Light and middle distillates	\$/tonne	26.83	62.56	(57.1)	24.41	62.48	(60.9)
Fuel oil	\$/tonne	55.02	99.08	(44.5)	50.04	99.00	(49.5)
Gasoline	\$/tonne	40.89	101.68	(59.8)	37.20	101.59	(63.4)
Straight-run gasoline	\$/tonne	47.62	110.80	(57.0)	43.32	110.71	(60.9)
Diesel fuel	\$/tonne	26.83	62.56	(57.1)	24.41	62.48	(60.9)

		2 nd quarter of			1 st half of		
		2016	2015	Change, %	2016	2015	Change, %
Export duties on crude oil ⁽¹⁾	RUB/tonne	4,425	6,867	(35.6)	4,291	7,479	(42.6)
Export duties on refined products ⁽¹⁾							
Light and middle distillates	RUB/tonne	1,768	3,294	(46.3)	1,715	3,586	(52.2)
Fuel oil	RUB/tonne	3,625	5,217	(30.5)	3,516	5,682	(38.1)
Gasoline	RUB/tonne	2,694	5,354	(49.7)	2,614	5,831	(55.2)
Straight-run gasoline	RUB/tonne	3,138	5,834	(46.2)	3,043	6,354	(52.1)
Diesel fuel	RUB/tonne	1,768	3,294	(46.3)	1,715	3,586	(52.2)
Mineral extraction tax							
Crude oil	RUB/tonne	6,139	7,073	(13.2)	5,109	6,954	(26.5)

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

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 respective periods of 2016 and 2015 are listed below.

		2 nd quarter of			1 st half of		
		2016	2015	Change, %	2016	2015	Change, %
Gasoline							
Euro-4 and below	RUR/tonne	13,100	7,300	79.5	11,800	7,300	61.6
Euro-5	RUR/tonne	10,130	5,530	83.2	8,830	5,530	59.7
Diesel fuel							
All ecological classes	RUR/tonne	5,293	3,450	53.4	4,722	3,450	36.9
Motor oils	RUR/tonne	6,000	6,500	(7.7)	6,000	6,500	(7.7)
Straight-run gasoline	RUR/tonne	13,100	11,300	15.9	11,800	11,300	4.4

During the first half of 2016, excise rates in Russia were increased twice, on 1 January and 1 April.

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, natural gas 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 profit.

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

Transportation of refined products in Russia is by railway transport and the pipeline system of Transnefteproduct. 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.

Three and six months ended 30 June 2016 compared to three and six months ended 30 June 2015

The table below sets forth data from our consolidated statements of profit or loss and other comprehensive income for the periods indicated.

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(millions of rubles)			
Revenues				
Sales (including excise and export tariffs)	1,338,959	1,476,966	2,516,633	2,917,271
Costs and other deductions				
Operating expenses	(113,709)	(105,828)	(226,953)	(211,509)
Cost of purchased crude oil, gas and products	(677,297)	(777,640)	(1,215,030)	(1,477,705)
Transportation expenses	(77,665)	(68,377)	(164,364)	(147,162)
Selling, general and administrative expenses	(45,302)	(40,028)	(93,125)	(81,213)
Depreciation, depletion and amortization	(71,608)	(87,058)	(155,956)	(165,521)
Taxes other than income taxes	(118,724)	(141,219)	(202,277)	(271,054)
Excise and export tariffs	(113,820)	(123,609)	(228,769)	(296,458)
Exploration expenses	(2,871)	(13,586)	(4,552)	(14,783)
Profit from operating activities.....	117,963	119,621	225,607	251,866
Finance income	3,511	4,036	7,342	8,567
Finance costs.....	(11,098)	(11,026)	(21,469)	(22,486)
Equity share in income of affiliates	3,425	2,382	5,778	6,475
Foreign exchange loss.....	(28,945)	(29,154)	(74,323)	(23,479)
Other expenses.....	(4,205)	(2,784)	(7,548)	(8,556)
Profit before income taxes.....	80,651	83,075	135,387	212,387
Current income taxes	(17,183)	(19,394)	(27,659)	(42,334)
Deferred income taxes	(774)	575	(2,064)	(1,358)
Total income tax expense	(17,957)	(18,819)	(29,723)	(43,692)
Profit for the period.....	62,694	64,256	105,664	168,695
Profit for the period attributable to non-controlling interests.....	(127)	(508)	(272)	(916)
Profit for the period attributable to PJSC LUKOIL shareholders	62,567	63,748	105,392	167,779
Earning per share of common stock attributable to PJSC LUKOIL shareholders (in Russian rubles):				
Basic	87.76	89.42	147.83	235.34
Diluted	87.76	88.13	147.83	231.28

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

Sales revenues

Sales breakdown	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(millions of rubles)			
Crude oil				
Export and sales on international markets other than Customs Union	325,492	376,988	605,638	742,902
Export and sales to Customs Union	15,366	13,776	27,768	28,099
Domestic sales	23,404	37,859	44,744	75,232
	364,262	428,623	678,150	846,233
Refined products				
Export and sales on international markets				
Wholesale	669,088	743,051	1,215,661	1,465,805
Retail	71,660	74,593	149,974	154,625
Domestic sales				
Wholesale	55,569	61,045	104,366	114,019
Retail	90,541	88,172	171,920	166,177
	886,858	966,861	1,641,921	1,900,626
Petrochemicals				
Export and sales on international markets	8,804	8,875	18,962	17,089
Domestic sales	8,915	6,296	18,094	9,394
	17,719	15,171	37,056	26,483
Gas and gas products				
Export and sales on international markets	19,877	21,187	44,285	48,859
Domestic sales	8,582	9,533	17,820	18,831
	28,459	30,720	62,105	67,690
Sales of energy and related services				
Sales on international markets	2,797	1,719	6,525	4,209
Domestic sales	11,642	11,523	30,678	29,420
	14,439	13,242	37,203	33,629
Other				
Sales on international markets	14,545	12,552	37,302	23,982
Domestic sales	12,677	9,797	22,896	18,628
	27,222	22,349	60,198	42,610
Total sales	1,338,959	1,476,966	2,516,633	2,917,271

Sales volumes	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(thousands of barrels)			
Crude oil				
Export and sales on international markets other than Customs Union	118,805	125,966	247,967	243,033
Export and sales to Customs Union	7,030	6,245	14,162	13,018
Domestic sales	11,618	18,831	25,413	37,808
	137,453	151,042	287,542	293,859
	(thousands of tonnes)			
Crude oil				
Export and sales on international markets other than Customs Union	16,208	17,185	33,829	33,156
Export and sales to Customs Union	959	852	1,932	1,776
Domestic sales	1,585	2,569	3,467	5,158
	18,752	20,606	39,228	40,090
	(thousands of tonnes)			
Refined products				
Export and sales on international markets				
Wholesale	25,140	24,964	48,221	49,019
Retail	986	1,119	2,021	2,175
Domestic sales				
Wholesale	2,610	2,582	5,169	4,790
Retail	2,352	2,353	4,486	4,501
	31,088	31,018	59,897	60,485
Total sales volume of crude oil and refined products	49,840	51,624	99,125	100,575

Realized average sales prices	2 nd quarter of		1 st half of		
	2016	2015	2016	2015	
Average realized price international					
Oil (beyond Customs Union)	(RUB/barrel)	2,740	2,993	2,442	3,057
Oil (Customs Union)	(RUB/barrel)	2,186	2,204	1,961	2,158
Refined products					
Wholesale	(RUB/tonne)	26,614	29,764	25,210	29,902
Retail.....	(RUB/tonne)	72,677	66,660	74,208	71,092
Oil (beyond Customs Union)	(\$/barrel)	41.58	56.84	34.76	53.26
Oil (Customs Union)	(\$/barrel)	33.18	41.86	27.91	37.60
Refined products					
Wholesale	(\$/tonne)	403.93	565.27	358.82	520.97
Retail.....	(\$/tonne)	1,103.04	1,266.00	1,056.22	1,238.60
Average realized price within Russia					
Oil.....	(RUB/barrel)	2,014	2,010	1,761	1,990
Refined products					
Wholesale	(RUB/tonne)	21,291	23,648	20,191	23,804
Retail.....	(RUB/tonne)	38,495	37,481	38,324	36,923

During the second quarter of 2016, our revenues decreased by 138 billion RUB, or by 9.3%, compared to the second quarter of 2015. Our revenues from crude oil sales decreased by 64 billion RUB, or by 15.0%, and our revenues from sales of refined products decreased by 80 billion RUB, or by 8.3%.

During the first half of 2016, our revenues decreased by 401 billion RUB, or by 13.7%, compared to the first half of 2015. Our revenues from crude oil sales decreased by 168 billion RUB, or by 19.9%, and our revenues from sales of refined products decreased by 259 billion RUB, or by 13.6%.

The main reason for the decrease in revenue was the decrease in international hydrocarbon prices. That was partially compensated for by the effect of ruble devaluation on our revenues denominated in other currencies.

Sales of crude oil

Our international crude oil sales revenue decreased by 13.7%, or by 51 billion RUB, and by 18.5%, or by 137 billion RUB, compared to the second quarter and the first half of 2015, respectively. Our international sales volumes (beyond the Customs Union) decreased by 977 thousand tonnes, or by 5.7%, in the second quarter of 2016 driven by decrease in the Company's share in production from the West Qurna-2 field, and increased by 673 thousand tonnes, or by 2.0%, in the first half of 2016, due to higher volumes of crude oil trading. Our average international ruble realized prices decreased by 8.5% and 20.1% compared to the second quarter and the first half of 2015, respectively.

Our realized domestic crude oil sales price did not change compared to the second quarter of 2015 and decreased by 11.5% compared to the first half of 2015, while our domestic sales volumes decreased by 984 thousand tonnes, or by 38.3%, and by 1,691 thousand tonnes, or by 32.8%, respectively, following the decrease in production in Russia. As a consequence, in the second quarter and the first half of 2016, our domestic sales revenue decreased by 38.2%, or by 14 billion RUB, and by 40.5%, or by 30 billion RUB, respectively.

In the second quarter and the first half of 2016, our revenue from crude oil export from Russia both to Group companies and third parties amounted to 172 billion RUB and 307 billion RUB, respectively (196 billion RUB and 395 billion RUB in the second quarter and the first half of 2015).

Sales of refined products

Compared to the second quarter and the first half of 2015, our revenue from the wholesale of refined products outside Russia decreased by 74 billion RUB, or by 10.0%, and by 250 billion RUB, or by 17.1%, respectively, that was largely price driven. During the second quarter of 2016, our dollar and ruble realized prices decreased by 28.5% and 10.6%, respectively, and during the first half of 2016 they decreased by 31.1% and 15.7%, respectively. At the same time, compared to the second quarter and the first half of 2015, our sales volumes didn't change significantly.

During the second quarter and the first half of 2016, our dollar realized retail prices outside Russia decreased by 12.9% and 14.7%, respectively, while our ruble realized prices increased by 9.0% and 4.4%, respectively, due to the ruble devaluation. Our sales volumes decreased by 11.9% and 7.1% as a consequence of sale of our retail networks in Eastern Europe. As a result, our international retail revenue decreased by 3 billion RUB, or by 3.9%, and by 5 billion RUB, or by 3.0%, compared to the second quarter and the first half of 2015, respectively.

During the second quarter and the first half of 2016, our revenue from the wholesale of refined products on the domestic market decreased by 9.0%, or by 5 billion RUB, and by 8.5%, or by 10 billion RUB, respectively. Our realized prices decreased by 10.0% and 15.2%, but our sales volumes increased by 1.1% and 7.9% in the second quarter and the first half of 2016.

During the second quarter and the first half of 2016, our revenue from refined products retail sales in Russia increased by 2 billion RUB, or by 2.7%, and by 6 billion RUB, or by 3.5%, respectively. Our average domestic retail prices increased by 2.7% and 3.8%, while our retail volumes did not change significantly.

In the second quarter and the first half of 2016, our revenue from export of refined products from Russia both to Group companies and third parties amounted to 98 billion RUB and 186 billion RUB, respectively (118 billion RUB and 239 billion RUB in the second quarter and the first half of 2015).

Sales of petrochemical products

In the second quarter and the first half of 2016, our revenue from sales of petrochemical products increased by 3 billion RUB, or by 16.8%, and by 11 billion RUB, or by 39.9%, respectively, largely due to the increase in domestic output against the background of low production as a consequence of a fire at our plant in the Stavropol region of Russia at the end of the first quarter of 2014. Production at the plant was resumed in early April 2015.

Sales of gas and gas products

Compared to the second quarter and the first half of 2015, sales of gas and gas refined products decreased by 2 billion RUB, or by 7.4%, and by 6 billion RUB, or by 8.3%, respectively, mainly as a result of the decrease in sales prices.

Natural gas sales revenue decreased by 1 billion RUB, or by 5.0%, in the second quarter of 2016 and by 3 billion RUB, or by 8.1%, in the first half of 2016.

Gas products revenue decreased by 1 billion RUB, or by 9.9%, and by 3 billion RUB, or by 8.4%, compared to the second quarter and the first half of 2015, respectively.

Sales of energy and related services

During the second quarter and the first half of 2016, our revenue from sales of electricity, heat and related services increased by 1 billion RUB, or by 9.0%, and by 4 billion RUB, or by 10.6%, respectively. In Russia, the increase was largely due to putting in operation a combined cycle gas turbine with a capacity of 135 MW at the Group's power plant in the Stavropol region of Russia in March 2015. Our international revenue increased as a result of the significant increase in volumes of electricity sales in Sicily, Italy.

Other sales

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.

During the second quarter and the first half of 2016, revenue from other sales increased by 5 billion RUB, or by 21.8%, and by 18 billion RUB, or by 41.3%, respectively. The non-petrol revenue of our retail network increased by 2 billion RUB, or by 23.4%, and by 3 billion RUB, or by 21.1%. In the second quarter and the first half of 2016, revenue from transportation services abroad increased by 2 billion RUB, or by 63.4%, and by 5 billion RUB, or by 78.5%, respectively. In the second quarter and the first half of 2016, our other sales also included revenue from sales of diamonds in the amount of 3 billion RUB and 11 billion RUB, respectively (3 billion RUB and 5 billion RUB in the second quarter and the first half of 2015).

Operating expenses

Operating expenses include the following:

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(millions of rubles)			
Hydrocarbon extraction expenses ⁽¹⁾	45,187	40,771	89,061	80,042
Extraction expenses at the West Qurna-2 field	8,407	11,373	18,610	23,936
Own refining expenses	22,804	21,004	45,254	43,172
Refining expenses at third parties refineries	173	525	421	1,078
Expenses for crude oil transportation to refineries	10,917	9,612	23,228	20,120
Power generation and distribution expenses	8,618	9,566	18,889	18,633
Petrochemical expenses	3,289	2,410	6,602	4,793
Other operating expenses	14,314	10,567	24,888	19,735
Total operating expenses	113,709	105,828	226,953	211,509

⁽¹⁾ Excluding extraction expenses at the West Qurna-2 field.

The method of allocation of operating expenses above differs from the approach used in preparing the data for Note 28 “Segment information” to our condensed 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 2015, our operating expenses increased by 8 billion RUB, or by 7.4%, in the second quarter of 2016, and by 15 billion RUB, or by 7.3%, in the first half of 2016, largely as a result of inflation in Russia and the effect of the ruble devaluation on the ruble value of foreign subsidiaries’ expenses.

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.

In the second quarter and the first half of 2016, our extraction expenses increased by 4 billion RUB, or by 10.8%, and by 9 billion RUB, or by 11.3%.

Our average hydrocarbon extraction expenses increased from 213 RUB per BOE in the second quarter of 2015 to 246 RUB per BOE in the second quarter of 2016, or by 15.5%. In the first half of 2016, our average hydrocarbon extraction expenses increased from 209 RUB per BOE in the first half of 2015 to 238 RUB per BOE, or by 13.9%. In Russia, average hydrocarbon extraction expenses increased by 13.7% to 241 RUB per BOE in the second quarter of 2016 and by 13.0% to 234 RUB per BOE in the first half of 2016. Our domestic expenses increased driven by higher costs of materials and services and shift towards more cost-intensive projects benefiting from tax exemptions.

At the same time, our average hydrocarbon extraction expenses decreased from \$4.04 per BOE in the second quarter of 2015 to \$3.73 per BOE in the second quarter of 2016, or by 7.7%, and from \$3.68 per BOE in the first half of 2015 to \$3.41 per BOE in the first half of 2016, or by 7.3%. In Russia, average hydrocarbon extraction expenses decreased by 9.2% to \$3.65 per BOE in the second quarter of 2016 and by 8.0% to \$3.35 per BOE in the first half of 2016.

Crude oil extraction expenses at the West Qurna-2 field

Crude oil extraction expenses at the West Qurna-2 field represent expenses related to 100% production from the West Qurna-2 field, while we are only eligible for a share of production that compensates our historically incurred costs and expenses. For details see p. 6.

In the second quarter and the first half of 2016, our expenses related to the West Qurna-2 project amounted to 8 billion RUB and 19 billion RUB, respectively (11 billion RUB and 24 billion RUB in the second quarter and the first half of 2015). The decrease in expenses was a result of completion of commissioning stage of the field development and consecutive decrease in personnel involved and associated transportation, security and other related services provided.

Own refining expense

During the second quarter and the first half of 2016, our own refining expenses increased by 2 billion, or by 8.6%, and by 2 billion, or by 4.8%, respectively.

Despite lower production volumes, refining expenses at our domestic refineries increased by 6.5%, or by 1 billion RUB, in the second quarter of 2016, and by 12.1%, or by 2 billion RUB, in the first half of 2016, as a result of increase in consumption and costs of additives and commissioning of new units at our refineries in Nizhny Novgorod and Volgograd.

Refining expenses at our refineries outside Russia increased by 1 billion RUB, or by 10.6%, compared to the second quarter of 2015 and did not change significantly compared to the first half of 2015. The increase was a result of the ruble devaluation and commissioning of heavy residue processing complex at our Bulgarian refinery, but in the first half of 2016, it was offset by lower overhaul expenses at our Italian refinery compared to first quarter of 2015.

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 crude oil and refined products to refineries for further processing.

During the second quarter and the first half of 2016, our expenses for crude oil transportation to refineries increased by 1 billion RUB, or by 13.6%, and by 3 billion RUB, or by 15.4%, largely as a result of the increase in transportation tariffs, international refining volumes and the effect of the ruble devaluation.

Petrochemical expenses

In the second quarter and the first half of 2016, operating expenses of our petrochemical plants increased by 1 billion RUB, or by 36.5%, and by 2 billion RUB, or by 37.7%, respectively, due to the increase in domestic production volumes after commencement of production at our petrochemical plant in the Stavropol region of Russia in April 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.

In the second quarter and the first half of 2016, other operating expenses increased by 4 billion RUB, or by 35.5%, and by 5 billion RUB, or by 26.1%, respectively, largely as a result of the increased cost of transportation services provided to third parties, non-petrol sales of our retail network and the increase in the ruble value of other operating expenses of our foreign subsidiaries.

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.

In the second quarter and the first half of 2016, the cost of purchased crude oil, gas and products decreased by 100 billion RUB, or by 12.9%, and by 263 billion RUB, or by 17.8%, respectively, following the decrease in hydrocarbon prices. Crude oil purchases in the second quarter and the first half of 2016 also included 45 billion RUB and 74 billion RUB related to 2,588 thousand tonnes and 5,143 thousand tonnes of compensation crude oil received from Iraq's state-owned South Oil Company within the West Qurna-2 project (53 billion RUB and 95 billion RUB related to 2,497 thousand tonnes and 4,769 thousand tonnes of compensation crude oil in the second quarter and the first half of 2015).

In the second quarter of 2016, we recognized a 36 billion RUB net loss from hedging, compared to a 16 billion RUB net loss in the second quarter of 2015. In the first half of 2016 we recognized a 34 billion RUB net loss from hedging, compared to a 26 billion RUB net loss in the first half of 2015.

Transportation expenses

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(millions of rubles)			
Crude oil transportation expenses.....	25,070	21,575	49,617	46,082
- in Russia.....	13,737	13,796	26,939	27,068
- outside Russia.....	11,333	7,779	22,678	19,014
Refined products transportation expenses	45,047	41,968	101,192	92,085
- in Russia.....	20,102	18,829	42,241	39,778
- outside Russia.....	24,945	23,139	58,951	52,307
Other transportation expenses.....	7,548	4,834	13,555	8,995
- in Russia.....	3,868	2,743	7,199	4,931
- outside Russia.....	3,680	2,091	6,356	4,064
Total transportation expenses.....	77,665	68,377	164,364	147,162

Our transportation expenses increased by 9 billion RUB, or by 13.6%, in the second quarter of 2016 and by 17 billion RUB, or by 11.7%, in the first half of 2016.

Our expenses for transportation of crude oil in Russia were flat both to the second quarter and the first half of 2015 as inflation of tariffs was offset by decrease in exports volumes. Outside of Russia, increase in crude oil transportation expenses was driven primarily by the effect of the ruble devaluation.

The increase in domestic expenses for transportation of refined products by 6.8% against the second quarter of 2015 and by 6.2% against the first half of 2015 was triggered mainly by the increase in tariffs. Outside of Russia, the increase was again mostly a result of the ruble devaluation.

Other transportation expenses were mostly represented by the expenses for transportation of gas. In Russia, the increase to the respective periods of 2015 was mainly due to higher volumes of transportation of gas from the Yu. Korchagin field in the Caspian Sea. Internationally, the increase that resulted from higher transportation volumes as a result of the increase in gas production was amplified by the ruble devaluation.

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 are roughly equally split between domestic and international operations.

Our selling, general and administrative expenses increased by 5 billion RUB, or by 13.2%, in the second quarter of 2016, and by 12 billion RUB, or by 14.7%, in the first half of 2016. In Russia, expenses increased by 6 billion RUB, or by 23.2%, in the second quarter of 2016 and by 7 billion RUB, or by 16.2%, in the first half of 2016 as a result of inflation and higher accruals within share-based compensation program. Internationally, decrease in selling expenses denominated in local currencies as a result of the sale of our retail networks in Eastern Europe was offset by the effect of the ruble devaluation on the expenses of our foreign subsidiaries and our expenses outside of Russia decreased by 1 billion RUB, or by 5.6%, compared to the second quarter of 2015 and increased by 5 billion RUB, or by 13.0%, compared to the first half of 2015.

Depreciation, depletion and amortization

Our depreciation, depletion and amortization expenses decreased by 15 billion RUB, or by 17.7%, compared to the second quarter of 2015, and by 10 billion RUB, or by 5.8%, compared to the first half of 2015. The effect of the increase in the depreciation rate of upstream assets following the decrease in hydrocarbon proved reserves was offset by the decrease of expenses related to the West Qurna-2 project. Our depreciation, depletion and amortization expenses for the second quarter of 2016 and 2015 included 5 billion RUB and 34 billion RUB, respectively, related to the West Qurna-2 field. In the first half of 2016 and 2015, those expenses amounted to 24 billion RUB and 57 billion RUB, respectively. Other international subsidiaries' depreciation, depletion and amortization increased as a result of the effect of the ruble devaluation.

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. Currently, our largest affiliates are Tengizchevroil, exploration and production company operating in Kazakhstan, Bashneft-Polus, an exploration and production company that develops the Trebs and Titov oilfields in Timan-Pechora, Russia, Shakh-Deniz Midstream and Caspian Pipeline Consortium, midstream companies in Azerbaijan and Kazakhstan. One of our major affiliates was Caspian Investments Resources Ltd, which was sold in August 2015.

Our share in income of affiliates increased by 1 billion RUB, or by 43.8%, compared to the second quarter of 2015 and decreased by 1 billion RUB, or by 10.8%, compared to the first half of 2015.

Taxes other than income taxes

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
(millions of rubles)				
In Russia				
Mineral extraction taxes	105,073	128,720	174,811	245,369
Social security taxes and contributions	5,808	5,506	11,835	10,850
Property tax	4,728	4,398	9,266	8,732
Other taxes	642	398	1,097	1,102
Total in Russia	116,251	139,022	197,009	266,053
International				
Social security taxes and contributions	1,586	1,319	3,159	2,794
Property tax	38	258	564	749
Other taxes	849	620	1,545	1,458
Total internationally	2,473	2,197	5,268	5,001
Total	118,724	141,219	202,277	271,054

In the second quarter of 2016, our taxes other than income taxes decreased by 22 billion RUB, or by 15.9%, compared to the second quarter of 2015. In the first half of 2016, our taxes other than income taxes decreased by 69 billion RUB, or by 25.4%, compared to the first half of 2015. This was largely driven by the decrease in the mineral extraction tax rate in Russia.

In the second quarter and the first half of 2016, 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 a 15 billion RUB and 26 billion RUB mineral extraction tax reduction, respectively (19 billion RUB and 37 billion RUB in the second quarter and the first half of 2015).

Excise and export tariffs

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
(millions of rubles)				
In Russia				
Excise tax on refined products	23,591	13,373	40,182	25,673
Crude oil export tariffs	30,872	50,566	62,364	119,823
Refined products export tariffs	9,160	19,112	24,686	64,174
Total in Russia	63,623	83,051	127,232	209,670
International				
Excise tax and sales taxes on refined products	50,100	40,219	101,317	85,757
Crude oil export tariffs	12	15	21	28
Refined products export tariffs	85	324	199	1,003
Total internationally	50,197	40,558	101,537	86,788
Total	113,820	123,609	228,769	296,458

In the second quarter and the first half of 2016, export tariffs decreased by 30 billion RUB, or by 42.7%, and by 98 billion RUB, or by 52.8%, respectively, due to the sharp decrease in export duty rates for crude oil and refined products in Russia amplified by the decrease in export volumes. Compared to the second quarter and the first half of 2015, the volumes of crude oil export beyond the Customs Union decreased by 1.0% and 3.0% and the volumes of the refined products exports decreased by 13.7% and 9.9%, respectively. The increase in excise tax expenses in Russia was driven by increase in rates, while international excise expenses increased due to the ruble devaluation.

Foreign exchange loss

Foreign exchange loss mostly related to revaluation of US dollar and euro net monetary position of Russian subsidiaries that mostly consists of accounts receivables and loans to our foreign subsidiaries.

During the second quarter of 2016 and 2015, US dollar exchange rate showed similar decline that, along with comparable net monetary position, resulted in 29 billion RUB foreign exchange loss in both periods.

During the first half of 2016, US dollar exchange rate to ruble decreased from 72.88 rubles per dollar at 1 January to 64.26 rubles per dollar at 30 June that resulted in a 74 billion RUB foreign exchange loss. During the first half of 2015, US dollar exchange rate changed less significantly (decreased from 56.26 rubles per dollar at 1 January to 55.52 rubles per dollar at 30 June) that resulted in a 23 billion RUB foreign exchange loss.

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.

In the second quarter of 2016, our total income tax expense decreased by 1 billion RUB, or by 4.6%, compared to the second quarter of 2015. At the same time, our profit before income tax decreased by 2 billion RUB, or by 2.9%.

In the first half of 2016, our total income tax expense decreased by 14 billion RUB, or by 32.0%, compared to the first half of 2015. At the same time, our profit before income tax decreased by 77 billion RUB, or by 36.3%.

In the second quarter of 2016, our effective income tax rate was 22.3%, compared to 22.7% in the second quarter of 2015. In the first half of 2016, our effective income tax rate was 22.0%, compared to 20.6% in the first half of 2015.

Liquidity and capital resources

	1 st half of	
	2016	2015
(millions of rubles)		
Net cash provided by operating activities	344,478	383,103
Net cash used in investing activities	(258,515)	(290,868)
Net cash provided by (used in) financing activities	37,267	(89,562)

Operating activities

Our primary source of cash flow is funds generated from our operations. In the first half of 2016, cash generated from operations decreased by 39 billion RUB, or by 10.1%, compared to the first half of 2015, mainly as a result of the decrease in profit.

Investing activities

In the first half of 2016, the amount of cash used in investing activities decreased by 32 billion RUB, or by 11.1%, mostly due to a decrease in capital expenditures.

In the first half of 2016, our capital expenditures, including non-cash transactions, decreased by 63 billion RUB, or by 20.8%.

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
(millions of rubles)				
Capital expenditures, including non-cash transactions and prepayments				
Exploration and production				
Western Siberia	28,172	27,919	60,176	61,775
Timan-Pechora	20,980	19,592	45,535	38,942
Ural region	6,173	8,204	11,989	14,792
Volga region	11,979	10,201	20,543	20,109
Other in Russia	1,068	4,156	3,038	8,507
Total in Russia	68,372	70,072	141,281	144,125
Iraq	2,400	7,575	11,696	21,422
Other outside Russia	32,486	42,408	55,167	77,060
Total outside Russia	34,886	49,983	66,863	98,482
Total exploration and production	103,258	120,055	208,144	242,607
Refining, marketing and distribution				
Russia	11,852	22,366	24,639	43,533
International	3,144	7,033	7,535	15,964
Total refining, marketing and distribution	14,996	29,399	32,174	59,497
Corporate and other				
Russia	442	846	692	1,497
International	190	473	437	1,243
Total corporate and other	632	1,319	1,129	2,740
Total capital expenditures	118,886	150,773	241,447	304,844

In the first half of 2016, our capital expenditures in the exploration and production segment decreased by 34 billion RUB, or by 14.2%. The decrease was largely in our international segment and related to completion of current stage of the West Qurna-2 project and of exploratory drilling in Cameroon and Romania.

The decrease in capital expenditures in the domestic refining, marketing and distribution segment in Russia was due to completion of upgrades at our Russian refineries. The decrease in the international segment was a result of completion of the construction of a heavy residue processing complex at our Bulgarian refinery.

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

	2 nd quarter of		1 st half of	
	2016	2015	2016	2015
	(millions of rubles)			
Western Siberia (Pyakyakhinskoye field)	4,076	7,636	13,333	17,084
Caspian region (Projects in Russia).....	9,546	7,606	16,324	14,949
Timan-Pechora (Yaregkoye field)	6,448	3,539	12,072	5,873
Iraq.....	2,400	7,575	11,696	21,422
Uzbekistan	20,320	17,604	26,276	27,560
Nigeria	554	10,077	5,050	10,077
Romania.....	246	5,603	660	11,721
Cameroon.....	95	250	259	8,034
Total	43,685	59,890	85,670	116,720

Financing activities

In the first half of 2016, net movements of short-term and long-term debt generated an inflow of 110 billion RUB, compared to an outflow of 30 billion RUB in the first half of 2015.