MANAGEMENT'S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FOR THE THREE MONTHS ENDED 31 MARCH 2013

Content

The following discussion should be read in conjunction with the unaudited consolidated interim condensed financial statements prepared in accordance with IFRS and the related notes, published simultaneously with this Management's Discussion and Analysis of financial condition and results of operations (MD&A). This discussion includes forward-looking statements that involve risks and uncertainties. Actual results could differ materially from those anticipated in the forward looking statements as a result of numerous factors, including certain factors discussed later in this MD&A.

For financial reporting purposes, Tatneft converts metric tonnes of crude oil to barrels using a conversion factor of 7.123. This factor represents a blend of varying conversion factors specific to each of Tatneft's fields. Because the proportion of actual production by field varies from period to period, total reserves and production volumes for the Group in barrels converted from tonnes using the blended rate may differ from total reserves and production calculated on a field by field basis. 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 into BOE 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. Please see "Forward-looking statement" on page 21 for a discussion of some factors that could cause actual results to differ materially.

Background

OAO Tatneft (the "Company") and its subsidiaries (jointly referred to as the "Group" or "Tatneft") is one of the largest vertically integrated oil companies in Russia in terms of crude oil production and proved oil reserves. The Company is an open joint-stock company organized under the laws of the Russian Federation with the headquarters located in City of Almetyevsk, Tatarstan. The principal business of the Group is to explore for, develop, produce and market crude oil and refined products. The Group is also involved in petrochemicals', mainly tires, production and marketing.

As of 31 March 2013 and and 31 December 2012 OAO Svyazinvestneftekhim, a company wholly owned by the government of Tatarstan, together with its subsidiary, hold approximately 36% of the Company's voting stock. These shares were contributed to Svyazinvestneftekhim by the Ministry of Land and Property Relations of Tatarstan in 2003. Tatarstan also holds a "Golden Share", a special governmental right, in the Company. The exercise of its powers under the Golden Share enables the Tatarstan government to appoint one representative to the Board of Directors and one representative to the Revision Commission of the Company as well as to veto certain major decisions, including those relating to changes in the share capital, amendments to the Charter, liquidation or reorganization of the Company and "major" and "interested party" transactions as defined under Russian law. The Golden Share currently has an indefinite term.

The majority of the Group's crude oil and gas production, refining capacity and other operations are located in Tatarstan, a republic of the Russian Federation, situated between the Volga River and the Ural Mountains, approximately 750 kilometers southeast of Moscow.

The Group currently holds most of the exploration and production licenses and produces substantially all its crude oil in Tatarstan.

Key financial and operational results

	Three months ended 31 March 2013	Three months ended 31 March 2012	Change, %
Financial results			
Sales, net (RR million)	106,554	111,259	(4.2)
Profit attributable to Group shareholders (RR million)	16,974	27,365	(38.0)
EBITDA [(1)] (RR million)	28,978	37,392	(22.5)
Additions to property, plant and equipment (RR million)	12,433	8,874	40.1
Free Cash Flow (RR million)	16,385	28,186	(41.9)
Net debt (RR million)	41,980	57,004	(26.4)
Basic and Diluted net profit per share of common stock (RR)			
Common	7.47	12.05	(38.0)
Preferred	7.47	12.05	(38.0)
Operational results			
Crude oil production by the Group (thousand tonnes)	6,503	6,524	(0.3)
Crude oil production by the Group (thousand barrels)	46,319	46,472	(0.3)
Crude oil daily production (thousand bbl per day)	514.7	510.7	0.8
Gas production by the Group (million cubic meters)	230.0	233.5	(1.5)
Gas daily production (thousand boe per day)	15.0	15.1	(0.7)
Refined products produced (thousand tonnes)	1,913.4	1,448.4	32.1
Gas products produced (thousand tonnes)	278.4	288.5	(3.5)
Refining throughput (thousand bbl per day)	163.4	122.9	33.0
Production of tires (thousand tires)	3.1	3.0	3.3
Number of petrol (gas) stations in Russia[(2)]	505	511	(1.2)
Number of petrol (gas) stations outside of Russia[(2)]	135	130	3.8

(1) *As defined on page 12*
(2) *Including leased stations*

Our net profit in the first quarter of 2013 was RR 16,974 million, which is RR 10,391 million, or 38.0%, less than in the corresponding period of 2012. Our profit was affected by lower crude oil and refined products prices, while incurring higher export duties in the first quarter of 2013 compared to the corresponding period of 2012.

In the first quarter of 2013 the Group (including consolidated subsidiaries OAO Ilekneft, OOO Tatneft-Samara, OOO Tatneft-Severny) produced 6.5 million metric tonnes of crude oil, which is 0.3% lower than in the first quarter of 2012. Our gas production in the first quarter of 2013 was 230 million cubic meters, which is 1.5% lower than in the corresponding period of 2012. Increase of refining throughput in the first quarter of 2013 compared to the corresponding period of 2012 was due to achieving full operational capacity at the TANECO refinery (see Segment information section).

Segment information

Our operations are currently divided into the following main segments:

- **Exploration and production** – consists of the Company's oil and gas extraction and production divisions, as well as production subsidiaries, well repair and reservoir oil yield improvement subdivisions, pumping equipment repair centers, and other ancillary oilfield services' operations. Most oil and gas exploration and production activities are concentrated within the Company.

- **Refining and marketing** – consists of the Company's sales and marketing division (URNiN), a refining and petrochemical complex in Nizhnekamsk, Tatarstan, operated by OAO TANECO ("TANECO"), as well as the Company's combined hydrocracker facility construction division; our gas production, transportation and refining division Tatneftegaspererabotka; OOO Tatneft-AZS Center, OOO Tatneft-AZS-Zapad, OOO Tatneft-AZS-Sibir and OOO Tatneft-AZS-Yug, which manage the Tatneft branded gas stations network in Russia and carry out refined products wholesale sales; and certain other oil trading and ancillary companies.

- **Petrochemicals** - our petrochemicals segment has been consolidated under a management company, Tatneft-Neftekhim, which manages OAO Nizhnekamskshina, one of the largest tire manufacturers in Russia, and the companies technologically integrated with it, including OAO Nizhnekamsk Industrial Carbon Plant, ZAO Yarpolymermash-Tatneft, OAO Nizhnekamskiy Mekhanicheskiy Zavod, OOO Nizhnekamskiy Zavod Gruzovykh Shin and OOO Nizhnekamskiy Zavod Shin CMK. OOO Tatneft-Neftekhimsnab and OOO Trading House Kama are responsible for procuring supplies and marketing products produced by the companies within this segment, respectively.

These segments are determined by the way management recognizes the segments within the Group for making operating decisions and how they are evident from the Group structure.

Results of operations for the three months ended 31 March 2013 compared to the three months ended 31 March 2012

The following table sets forth the consolidated statements of income both in absolute values and respective change over the analyzed periods:

(RR million)	Three months ended 31 March 2013 (unaudited)	Three months ended 31 March 2012 (unaudited)	Change, %
Sales and other operating revenues, net	106,554	111,259	(4.2)
Costs and other deductions			
Operating	18,841	17,172	9.7
Purchased oil and refined products	12,320	12,780	(3.6)
Exploration	326	369	(11.7)
Transportation	8,518	6,973	22.2
Selling, general and administrative	9,765	7,735	26.2
Depreciation, depletion and amortization	5,046	4,250	18.7
(Gain) /loss on disposals of property, plant and equipment, investments and impairments	(331)	454	n/a
Taxes other than income taxes	27,384	27,459	(0.3)
Maintenance of social infrastructure and transfer of social assets	753	925	(18.6)
Total costs and other deductions	82,622	78,117	5.8
Foreign exchange (loss) /gain	(204)	4,378	n/a
Interest income	732	929	(21.2)
Interest expense, net of amounts capitalized	(1,717)	(1,993)	(13.8)
Earnings from equity investments	227	466	(51.3)
Other income, net	693	8	n/a
Total other (expenses)/ income	(269)	3,788	n/a
Profit before income taxes	23,663	36,930	(35.9)
Current income tax expense	(6,304)	(8,376)	(24.7)
Deferred income tax benefit	601	44	n/a
Total income tax expense	(5,703)	(8,332)	(31.6)
Profit for the period	17,960	28,598	(37.2)
Less: Profit attributable to non-controlling interest	(986)	(1,233)	(20.0)
Profit attributable to Group shareholders	16,974	27,365	(38.0)

Sales and other operating revenues

A breakdown of sales and other operating revenues (by product type) is provided in the following table:

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012	Change, %
Crude oil			
Sales	*88,293*	*101,896*	*(13.3)*
Less related export duties	*(35,135)*	*(34,868)*	*0.8*
	53,158	67,028	*(20.7)*
Refined products			
Sales	*52,921*	*36,595*	*44.6*
Less related export duties and excise taxes	*(12,792)*	*(4,937)*	*159.1*
	40,129	31,658	*26.8*
Petrochemicals	6,924	7,214	*(4.0)*
Corporate and other sales	6,343	5,359	*18.4*
Total Sales and other operating revenues, net	106,554	111,259	*(4.2)*

Decrease in sales and other operating revenues in the first quarter of 2013 in comparison to the corresponding period of 2012 was mainly due to lower market prices for crude oil and refined products while incurring higher export duties.

In the first quarter of 2013 export duties, paid by the Group, increased by 20.5% to RR 47,664 million from RR 39,564 million in the corresponding period of 2012 due to higher volumes of refined products sold for export in the current period. Our expenses on excise taxes increased to RR 263 million from RR 241 million in the corresponding period of 2012 due to increase of the statutory excise tax rates.

Export of crude oil and refined products from Russia

For the crude oil export the Group is using transportation services of OAO AK Transneft ("Transneft"), the state-owned monopoly owner and operator of Russia's trunk crude oil pipelines. During the first quarter of 2013, the Group exported from Russia approximately 69% of all its crude oil sold compared to approximately 65% in the corresponding period of 2012.

In the first quarter of 2013 the Company delivered 40% (44% in the first quarter of 2012) of its own crude oil for export through Transneft's Druzhba pipeline (mainly to Poland, Hungary and Slovakia); 25% (42% in the first quarter of 2012) of crude oil was shipped through Russian Black Sea ports (mainly Novorossiysk) and 35% (14% in the first quarter of 2012) of crude oil exported through Russian Baltic Sea ports (mainly Primorsk).

In the first quarter of 2013 the Group exported from Russia 1,465 thousand tonnes of refined products (including 13 thousand tonnes of purchased refined products) in comparison to 1,114 thousand tonnes in the corresponding period of 2012 (including 4 thousand tonnes of purchased refined products).

Sales breakdown

Sales revenues

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012	Change, %
Crude oil			
Non-CIS			
Export sales	73,511	77,162	*(4.7)*
Less related export duties	(35,135)	(34,868)	*0.8*
CIS sales[1]	1,380	4,399	*(68.6)*
Domestic sales	13,402	20,335	*(34.1)*
	53,158	67,028	*(20.7)*
Refined products			
Non-CIS export sales			
Export sales	33,280	12 762	*160.8*
Less related export duties	(12,506)	(4,696)	*166.3*
CIS sales			
CIS sales	1,027	9,440	*(89.1)*
Less related export duties	(23)	-	*n/a*
Domestic sales			
Domestic sales	18,614	14,393	*29.3*
Less related excise taxes	(263)	(241)	*9.1*
	40,129	31,658	*26.8*
Petrochemical products			
Tires sales	6,629	6,914	*(4.1)*
Other petrochemicals sales	295	300	*(1.7)*
	6,924	7,214	*(4.0)*
Other sales	6,343	5,359	*18.4*

[1] *CIS is an abbreviation for Commonwealth of Independent States*

Sales volumes

(thousand tonnes)	Three months ended 31 March 2013	Three months ended 31 March 2012	Change, %
Crude oil			
Non-CIS export sales	3,052	3,065	*(0.4)*
CIS sales	115	332	*(65.4)*
Domestic sales	1,435	1,823	*(21.3)*
	4,602	5,220	*(11.8)*
Refined products			
Non-CIS export sales	1,429	538	*165.6*
CIS sales	36	576	*(93.8)*
Domestic sales	994	681	*46.0*
	2,459	1,795	*37.0*

Realized average sales prices

(th. RR per tonne)	Three months ended 31 March 2013	Three months ended 31 March 2012	Change, %
Crude oil			
Non-CIS export sales	*24.09*	*25.18*	*(4.3)*
CIS sales	*12.00*	*13.25*	*(9.4)*
Domestic sales	*9.34*	*11.15*	*(16.3)*
Refined products			
Non-CIS export sales	*23.29*	*23.72*	*(1.8)*
CIS sales	*28.53*	*16.39*	*74.1*
Domestic sales	*18.73*	*21.14*	*(11.4)*

Sales of crude oil

Sales of crude oil decreased by 13.3% to RR 88,293 million in the first quarter of 2013 from RR 101,896 million in the corresponding period of 2012, mainly due to increased volumes of own refining throughput.

Sales of refined products

Increase in sales of refined products by 44.6% from RR 36,595 million to RR 52,921 million was mostly due to increased volumes of TANECO's refined products sold in the first quarter of 2013.

Non-CIS export sales	Three months ended 31 March 2013		Three months ended 31 March 2012		Change*, %	
	RR million	million tonnes	RR million	million tonnes	Sales	Volumes
Vacuum gasoil	11,946	0.50	2,748	0.11	*334.7*	*344.6*
Fuel oil	7,300	0.43	4,792	0.25	*52.3*	*68.6*
Naphtha	6,855	0.24	4,362	0.15	*57.2*	*60.6*
Gas products	1,896	0.07	847	0.03	*123.8*	*122.4*
Heating oil	4,538	0.16	-	-	*n/a*	*n/a*
Other	745	0.03	13	0.00	*n/a*	*n/a*
Total	33,280	1.43	12,762	0.54	*160.8*	*164.8*

CIS export sales	Three months ended 31 March 2013		Three months ended 31 March 2012		Change*, %	
	RR million	million tonnes	RR million	million tonnes	Sales	Volumes
Heating oil	-	-	3,210	0.15	*n/a*	*n/a*
Fuel oil	-	-	3,501	0.28	*n/a*	*n/a*
Vacuum gasoil	-	-	1,539	0.09	*n/a*	*n/a*
Gas products	312	0.01	680	0.04	*(54.1)*	*(60.3)*
Naphtha	-	-	406	0.02	*n/a*	*n/a*
Other	715	0.02	104	0.00	*587.5*	*513.8*
Total	1,027	0.03	9,440	0.58	*(89.1)*	*(94.8)*

Domestic sales	Three months ended 31 March 2013		Three months ended 31 March 2012		Change*, %	
	RR million	million tonnes	RR million	million tonnes	Sales	Volumes
Heating oil	7,507	0.41	3,453	0.19	*117.4*	*114.2*
Petrol fuel	5,409	0.18	5,446	0.20	*(0.7)*	*(8.0)*
Diesel fuel	3,082	0.11	3,170	0.12	*(2.8)*	*(8.1)*
Gas products	1,798	0.19	1,891	0.15	*(4.9)*	*28.8*
Other	818	0.10	433	0.02	*88.9*	*450.6*
Total	18,614	0.99	14,393	0.68	*29.3*	*45.6*

** The difference between percents presented here and in the sections is a result of rounding*

Sales of petrochemical products

Sales of petrochemical products decreased slightly mainly due to lower average prices of tires sold. The Group's production of tires in the first quarter of 2013 increased by 3.3% to 3.1 million tires.

Other sales

Other sales increased by 18.4% to RR 6,343 million in the first quarter of 2013 from RR 5,359 million in the corresponding period of 2012. Other sales primarily represent sales of materials and equipment, various oilfield services (such as drilling, well construction and repairs, and geophysical works) and sales of energy, water and steam provided by the Group entities to third parties.

Costs and other deductions

Operating expenses. Operating expenses include the following costs:

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012
Crude oil extraction expenses	10,018	8,606
Refining expenses	1,093	525
Petrochemical production expenses	5,664	6,253
Other operating expenses	2,067	1,457
Operating expenses not attributed to the revenue in the current period[1]	(1)	331
Total operating expenses	**18,841**	**17,172**

[1] This change includes extraction expenses related to crude oil produced by the Group in one period but sold to third parties in the different reporting period.

Crude oil extraction expenses. The Group's extraction ("lifting") expenses related to crude oil production are incurred by the Company's oil and gas producing divisions and subsidiaries. They include expenditures related to maintenance services, repairs and insurance of extraction equipment, labour costs, expenses on artificial stimulation of reservoirs, fuel and electricity costs, materials and goods consumed in crude oil production, and other similar costs.

Expenses of the Company's crude oil production units and subsidiaries consisting of the purchase of services and goods that are unrelated to their core activities and the change in crude oil and refined products inventory, have been excluded from extraction expenses and are included in other operating costs.

Lifting expenses averaged to RR 216.3 per barrel in the first quarter of 2013 compared to RR 185.2 per barrel in the corresponding period of 2012. Higher equipment services, other overhead and injection costs were the primary reason for the increase in lifting expenses in the first quarter of 2013 compared to the corresponding period of 2012.

Refining expenses. Refining expenses mostly consist of expenses related to the production of refined products at our TANECO refinery and primarily include expenditures of raw materials and supplies, maintenance and repairs of productive equipment, labour and electricity costs, and other similar costs. The refining expenses incurred in the first quarter of 2013 were RR 599.7 per tonne of crude oil throughput (RR 604.0 per tonne of products output).

Petrochemical production expenses. Petrochemical production expenses primarily include the costs of raw materials, labour, maintenance and electricity consumed in the production of petrochemical products. Cost of petrochemical products decreased to RR 5,664 million by 9.4% in the first quarter of 2013 compared to the corresponding period of 2012.

Other operating expenses include costs of other services, goods and materials not related to the core production activities of the Group. Other operating expenses slightly increased compared to the corresponding period of 2012 due to increase in sales volumes.

Cost of purchased crude oil and refined products. A summary of purchased oil and refined products in the first quarter of 2013 and 2012, respectively, are as follows:

	Three months ended 31 March 2013	Three months ended 31 March 2012
Purchased crude oil (RR million)	4,688	4,798
Volume (thousand tonnes)	*194*	*240*
Average price (th. RR per tonne)	*24.17*	*19.99*
Purchased refined products (RR million)	7,632	7,982
Volume (thousand tonnes)	*303*	*346*
Average price (th. RR per tonne)	*25.19*	*23.07*
Total purchased oil and refined products	**12,320**	**12,780**

Cost of purchases of crude oil decreased in the first quarter of 2013 compared to the corresponding period of 2012 due to lower volumes of crude oil purchased for resale.

Purchases of refined products in the first quarter of 2013 decreased by 4% and amounted to RR 7,632 million in the first quarter of 2013 compared to RR 7,982 million in the corresponding period of 2012 mainly due to a decrease in volumes of purchased refined products for trading by 12% partly offset by an increase in average purchase price per tonne by 9%.

Exploration expenses. Exploration expenses consist primarily of exploratory drilling, geological and geophysical costs, and the costs of carrying and retaining undeveloped properties. Exploration expenses decreased to RR 326 million in the first quarter of 2013 from RR 369 million in the corresponding period of 2012.

Transportation expenses. Transportation of the Group's crude oil and refined products, including purchased crude oil and refined products, are mostly carried out using the Transneft trunk pipeline system and railway. Transportation expenses in the first quarter of 2013 mostly represent expenses related to refined products transportation. Therefore, increase of transportation costs by 22.2% to RR 8,518 million in the first quarter of 2013 from RR 6,973 million in the corresponding period of 2012 was due to increased volumes of refined products transported by railway in the first quarter of 2013 as well as increase in transportation tariffs.

Selling, general and administrative expenses. Certain selling, general and administrative expenses by nature are fixed costs, which are not directly related to production, such as payroll, general business costs, insurance, advertising, share based compensation, legal fees, consulting and audit services, charity and other expenses, including bad debt provisions. Increase in selling, general and administrative expenses by RR 2,030 million to RR 9,765 million in the first quarter of 2013 compared to the corresponding period of 2012 was attributed, among other factors, to an increase in bad debt provisions as well as certain accounting adjustments.

(Gain)/ loss on disposals of property, plant and equipment and impairment of investments. In the first quarter of 2013 we recorded a gain on disposals of property, plant and equipment and impairment of investments amounted to RR 331 million, mainly resulting from disposal of some non-core subsidiaries, compared to a RR 454 million loss in the corresponding period of 2012.

Taxes other than income taxes. Taxes other than income taxes include the following:

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012
Mineral extraction tax	25,859	26,598
Property tax	1,155	557
Penalties and interest	20	5
Other	350	299
Total taxes other than income taxes	**27,384**	**27,459**

Taxes other than income taxes decreased by 0.3% to RR 27,384 million in the first quarter of 2013 from RR 27,459 million in the corresponding period of 2012 due to decrease in Group's mineral extraction tax expense by 2.8%. Other taxes include land tax and non-recoverable VAT.

Effective 1 January 2007, the tax rate formula for mineral extraction tax was modified to provide for fields whose depletion rate is 80% or above as determined under Russian reserves classification. Under these rules, the Group receives a benefit of 3.5% per field for each percent of depletion within the limits of 80% to 100%. As Romashkinskoye field, the Group's largest, along with certain other fields is more than 80% depleted, the Group received a benefit in the first quarter of 2013 of RR 6.0 billion in comparison to RR 5.4 billion in the corresponding period of 2012.

Since April 2007, a zero mineral extraction tax rate is applied to the production of highly viscous crude oil from the Group's Ashalchinskoye, Mordovo-Karmalskoye, and since 2010 and 2011 – also from some other fields, resulting in the first quarter of 2013 in a tax benefit of RR 0.4 billion in comparison to RR 0.2 billion in the corresponding period of 2012.

Maintenance of social infrastructure and transfer of social assets. Maintenance of social infrastructure expenses and transfer of social assets decreased to RR 753 million in the first quarter of 2013 from RR 925 million in the corresponding period of 2012. These social infrastructure expenses relate primarily to housing, schools and cultural buildings in Tatarstan.

Foreign exchange (loss)/ gain. The Group recorded a foreign exchange loss amounted to RR 204 million in the first quarter of 2013 compared to a foreign exchange gain of RR 4,378 million in the corresponding period of 2012, which was due to volatility of Ruble to US Dollar exchange rate in the reporting periods, resulting in the corresponding revaluation of US Dollars denominated debt under the long-term credit facilities of the Group on the back of overall decrease of amounts outstanding in accordance with the scheduled repayment.

Interest income decreased by 21.2% to RR 732 million in the first quarter of 2013 compared to the corresponding period of 2012 due to decrease in interest income received from our certificates of deposit.

Interest expense includes among other things a provision for the future costs of decommissioning of oil and gas assets. Interest expense, net of amounts capitalized, decreased by 14% RR 1,717 million in the first quarter of 2013, which was mainly due to the decrease in the current period's amount of total debt outstanding.

Earnings from equity investments. The Group recorded a gain from equity investments amounted to RR 227 million in the first quarter of 2013 compared to RR 466 million gain in the corresponding period of 2012.

Other income, net, in the first quarter of 2013 amounted to RR 693 million compared to RR 8 million of other income, net, in the corresponding period of 2012.

Income taxes

The effective income tax rate in the first quarter of 2013 was 24.1%, compared to the statutory tax rate of 20% in the Russian Federation. This difference was due to non-deductible or partially deductible expenses incurred during the reporting period.

EBITDA reconciliation

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012
Sales and other operating revenues, net	106,554	111,259
Costs and other deductions	(82,622)	(78,117)
Depreciation, depletion and amortization	5,046	4,250
EBITDA	28,978	37,392

EBITDA is a non-IFRS financial measure, defined as earnings before interest, taxes, 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 operating costs under IFRS, these expenses primarily represent the non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods. Our EBITDA calculation is commonly used as a basis by 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 profit, operating income or any other measure of performance under IFRS. EBITDA does not consider our need to replace our capital equipment over time.

Financial Condition Summary Information

The following table shows certain key financial indicators:

(RR million)	At 31 March 2013	At 31 December 2012
Current assets	146,003	140,332
Long-term assets	495,633	490,275
Total assets	641,636	630,607
Current liabilities	70,998	76,550
Long-term liabilities	106,450	107,824
Total liabilities	177,448	184,374
Shareholders' equity	464,188	446,233
Working capital	75,005	63,782

Working capital position

As of 31 March 2013 working capital of the Group amounted to RR 75,005 million compared to RR 63,782 million as of 31 December 2012. The increase in the working capital in the current period compared to previous period was attributable to an increase in current assets (mainly cash and cash equivalents) and a decrease of current liabilities (mainly in current portion of long-term debt).

Liquidity and Capital Resources

The following table shows a summary from the Consolidated Statements of Cash Flows:

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012
Net cash provided by operating activities	28,818	37,060
Net cash used in investment activities	(12,693)	(18,139)
Net cash used in financing activities	(8,870)	(7,585)
Net change in cash and cash equivalents	7,255	11,336

Net cash provided by operating activities

Our primary source of cash flow is funds generated from our operations. Net cash provided by operating activities decreased by 22.2% to RR 28,818 million in the first quarter of 2013 from RR 37,060 million in the corresponding period of 2012 which is explained primarily through lower profit attributable to Group shareholders earned in the first quarter of 2013.

Net cash used in investing activities

Net cash used in investing activities decreased by 30.0% to RR 12,693 million in the first quarter of 2013 from RR 18,139 million in the corresponding period of 2012, which was primarily due to decrease in cash used to purchase certificates of deposit.

Net cash used in financing activities

Cash flow used in financing activities were RR 8,870 million in the first quarter of 2013 in comparison to RR 7,585 million used for financing activities in the corresponding period of 2012. It was in line with net debt repayments of RR 8,785 million in the first quarter of 2013 compared with net debt repayments of RR 7,582 million in the corresponding period of 2012.

Additions to property, plant and equipment

The following additions to property, plant and equipment (by segment, excluding non-cash additions) were made in the first quarter of 2013 compared to the corresponding period of 2012:

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012
Exploration and production	5,921	4,643
Refining and marketing	5,480	3,389
Petrochemicals	74	14
Corporate and other	958	828
Total additions to property, plant and equipment	12,433	8,874

Calculation of Free Cash Flow

(RR million)	Three months ended 31 March 2013	Three months ended 31 March 2012
Net cash provided by operating activities	28,818	37,060
Additions to property, plant and equipment	(12,433)	(8,874)
Free Cash Flow	16,385	28,186

Analysis of Debt

At 31 March 2013, long-term debt, net of current portion, amounted to RR 36,094 million as compared to RR 37,991 million at 31 December 2012.

The decrease in total debt outstanding balances in the current period was mainly attributed to scheduled repayments under a dual (3 and 5 year) tranches secured syndicated pre-export credit facility for up to US$ 1.5 billion arranged in October 2009 and a triple (3, 5 and 7 year) tranches secured credit facility for up to USD 2 billion arranged in June 2010.

Under the US$ 1.5 billion facility the undiscounted amounts outstanding, including the current portion, as of 31 March 2013 and 31 December 2012 were RR 4,279 million (US$ 138 million) and RR 4,808 million (US$ 158 million), respectively.

Under the USD 2 billion facility the undiscounted amounts outstanding, including the current portion, as of 31 March 2013 and 31 December 2012 were RR 24,455 million (US$ 787 million) and RR 28,921 million (US $952 million), respectively.

In February 2011 the Company reached an agreement with the lenders under the US$ 2 billion 2010 Facility to decrease the margins. The margins were decreased to LIBOR plus 2.40% and 3.40% for the 3 and 5 year's tranches, respectively.

In February 2011 the Company also reached an agreement with the lenders under the US$ 1.5 billion 2009 Facility to substantially decrease the amount of crude oil volumes used as collateral for this facility. The crude oil volumes used as collateral decreased from 480,000 to 360,000 metric tons of oil in a calendar quarter.

In June 2011, the Company entered into a US $550 million unsecured credit facility with a fixed rate of 3.50% per annum with bullet repayment in three years, arranged by BNP Paribas (Suisse) SA, The Bank Of Tokyo Mitsubishi UFJ, Ltd., Commerzbank Aktiengesellschaft, ING Bank N.V., Natixis, Open Joint Stock Company Nordea Bank, Sumitomo Mitsui Banking Corporation and WestLB AG, London Branch. The undiscounted amounts outstanding under this credit facility as of 31 March 2013 and 31 December 2012 were RR 17,096 million (US $550 million) and RR 16,705 million (US $550 million), respectively.

In November 2011, TANECO entered into a US $75 million credit facility with equal semi-annual repayments during ten years. The loan was arranged by Nordea Bank AB (Publ), Société Générale and Sumitomo Mitsui Banking Corporation Europe Limited. The loan bears interest at LIBOR plus 1.1% per annum. The loan agreement requires compliance with certain financial covenants including, but not limited to, minimum levels of consolidated tangible net worth, and interest coverage ratios. The undiscounted amounts outstanding under this credit facility as of 31 March 2013 and 31 December 2012 were RR 2,098 million (US $68 million) and RR 2,050 million (US $68 million), including the current portion, respectively.

Also in November 2011, TANECO entered into a US $144.48 million credit facility with equal semi-annual repayments during ten years with first repayment date on 15 May 2014. The loan was arranged by Société Générale, Sumitomo Mitsui Banking Corporation Europe Limited and the Bank of Tokyo-Mitsubishi UFJ, LTD. The loan bears interest at LIBOR plus 1.25% per annum. The loan agreement requires compliance with certain financial covenants including, but not limited to, minimum levels of consolidated tangible net worth, and interest coverage ratios. The undiscounted amount outstanding under this credit facility as of 31 March 2013 and 31 December 2012 were RR 2,378 million (US $77 million) and RR 2,165 million (US $71 million), including the current portion, respectively.

In October 2009, P-D Tatneft-Alabuga Steklovolokno entered into a EUR 44 million credit facility with fourteen equal semi-annual repayments with the first repayment date on 28 February 2012. The loan was arranged by Landesbank Baden-Wurttemberg. The loan bears interest at EURIBOR plus 1.5% per annum. The undiscounted amount outstanding under this credit facility as of 31 March 2013 and 31 December 2012 were RR 1,330 million (EUR 33 million) and RR 1,468 million (EUR 36.5 million), including the current portion, respectively.

Calculation of Net Debt

(RR million)	At 31 March 2013	At 31 December 2012
Short term debt	26,308	32,096
Long term debt, net of current portion	36,094	37,991
Total debt	62,402	70,087
Cash and cash equivalents	20,422	13,083
Net Debt	41,980	57,004

Contractual obligations, other contingencies and off balance sheet arrangements

Guarantees

The Group has no outstanding guarantees at 31 March 2013 and 31 December 2012.

Commitments and Contingent Liabilities

The Group is subject to various lawsuits and claims arising in the ordinary course of business. The outcomes of such contingencies, lawsuits or other proceedings cannot be determined at present. In the case of all known contingencies the Group accrues a liability when the loss is probable and the amount is reasonably estimable. Based on currently available information, management believes that it is remote that future costs related to known contingent liability exposures would have a material adverse impact on the Group's consolidated financial statements.

Ukrtatnafta

The Group holds 49.6% investment in AmRUZ Trading AG ("AmRUZ") and 100% investment in Seagroup International Inc. ("Seagroup"). These entities primary activities are ownership interests in Closed Joint Stock Company Ukrtatnafta ("Ukrtatnafta"), the owner of the Kremenchug refinery, which constitute 8.34% and 9.96% of the outstanding common shares in Ukrtatnafta, respectively.

Historically, and in particular during the course of 2007, there have been a number of attempts by Ukraine to challenge AmRUZ and Seagroup's acquisition of shares in Ukrtatnafta, and in particular, by the State Property Fund and NJSC Naftogaz of Ukraine ("Naftogaz"). Naftogaz is 100% owned by the Ukrainian Government and also owner of record of 43% Ukrtatnafta's common shares.

The challenges were suspended in April 2006 when the Supreme Court of Ukraine ruled the payment for Ukrtatnafta shares made with promissory notes issued by AmRUZ and Seagroup was lawful. However, in May 2007 the Ministry of Fuel and Energy of Ukraine ("MFEU") resumed its attempts and, as a result, succeeded in obtaining alleged and doubtful court decisions, after which it announced the transfer into Naftogaz's custody the 18.3% of Ukrtatnafta's shares, representing the entire holdings of AmRUZ and Seagroup in Ukrtatnafta. Subsequent to these actions, MFEU effectively began to exclude the Group from exercising their shareholder rights related to Ukrtatnafta.

In October 2007 the existing management of Ukrtatnafta, as appointed by its shareholders, was forcibly removed based on an alleged court order. Subsequently, individuals who obtained the ability to manage Ukrtatnafta took certain actions effectively assisting MFEU in taking control over the shares in Ukrtatnafta owned by SeaGroup and

AmRUZ. In addition, Ukrtatnafta subsequently refused to settle its payables to ChMPKP Avto (Note 3), a Ukrainian intermediary that previously purchased crude from the Group for deliveries to Ukrtatnafta. Following this forced change of control of Ukrtatnafta, the Company (originally the key crude supplier to the Kremenchug refinery) suspended its crude oil deliveries to Ukrtatnafta.

Subsequently, the Ukrainian courts also invalided direct purchase of the shares in Ukrtatnafta by Tatneft.

In May 2008, Tatneft commenced international arbitration against Ukraine on the basis of the agreement between the Government of the Russian Federation and the Cabinet of Ministries of Ukraine on the Encouragement and Mutual Protection of Investments of 27 November 1998 ("Russia-Ukraine BIT"). The arbitration concerns losses suffered by Tatneft as a consequence of the forcible takeover of Ukrtatnafta and seizure of shares of the Group in Ukrtatnafta. Tatneft requested the arbitral tribunal declare Ukraine has breached the Russian-Ukraine BIT and to order Ukraine to pay compensation in excess of US$ 2.4 billion. In March 2013 the arbitral tribunal held the hearing on the merits with the award expected by the end of 2013.

As a result of the ongoing legal dispute over shareholding interests, the Company has fully provided for its investments in Ukrtatnafta.

Libya

As a result of the political situation in Libya, in February 2011 the Group had to entirely suspend its operations there and evacuate all its personnel. From February 2013 the Group has started the process of resuming its operations in Libya, including the return of some of its personnel to a branch in Tripoli. However, as of the date of this report the Group is not certain when it would be able to return to full operational activity in Libya.

Social commitments

The Group contributes significantly to the maintenance of local infrastructure and the welfare of its employees within Tatarstan, which includes contributions towards the construction, development and maintenance of housing, hospitals and transport services, recreation and other social needs. Such funding is periodically determined by the Board of Directors after consultation with governmental authorities and recorded as expenditures when incurred.

Certain Macroeconomic and Other Factors Affecting the Group's Results of Operations

The Group's results of operations and the period-to-period changes therein have been and will continue to be impacted by various factors outlined below.

Crude oil and refined products prices

The primary driver of our revenue is the selling price of crude oil and refined products. During the first quarter of 2013, Brent crude oil price fluctuated between $106 and $119 per barrel and averaged $112.6 per barrel in comparison to average $118.5 per barrel in the corresponding period of 2012.

Substantially all the crude oil we sell is Urals blend. The table below shows average and the end of the period crude oil and refined products prices for the respective periods, in US Dollars and RUB. The prices nominated in US$ are translated into RUB at average US$/RUB exchange rate for the respective period.

	Average for the three months ended		Change,	At March 31		Change,
	2013	2012	%	2013	2012	%
World market [1]	(in US Dollars per barrel, except for figures in percent)					
Brent crude	112.6	118.5	*(5.0)*	107.4	123.5	*(13.0)*
Urals crude *(CIF Mediterranean)*	111.0	116.9	*(5.0)*	107.0	120.5	*(11.2)*
Urals crude *(CIF Rotterdam)*	110.5	116.8	*(5.4)*	106.0	119.5	*(11.3)*
	(in US Dollars per tonne, except for figures in percent)					
Gasoil 0.1 1/2 *(CIF NWE/Basis ARA + FOB Rotterdam)*	957.9	993.1	*(3.5)*	914.1	1,013.5	*(9.8)*
Fuel oil 3.5% 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	610.9	684.2	*(10.7)*	600.3	695.8	*(13.7)*
Fuel oil 3.5% *(FOB Med (Italy))*	608.0	674.1	*(9.8)*	598.3	693.0	*(13.7)*
Naphtha Phy 1/2 *(CIF NEW/Basis ARA+ FOB Rotterdam)*	943.0	1,013.4	*(6.9)*	879.0	1,062.5	*(17.3)*
HS VGO(2) 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	801.9	851.9	*(5.9)*	767.8	888.3	*(13.6)*
	(in th. RR per tonne, except for figures in percent)					
Brent crude	24.39	25.54	*(4.5)*	23.26	26.61	*(12.6)*
Urals crude *(CIF Mediterranean)*	24.04	25.20	*(4.6)*	23.18	25.98	*(10.8)*
Urals crude *(CIF Rotterdam)*	23.94	25.17	*(4.9)*	22.95	25.76	*(10.9)*
	(in th. RR per tonne, except for figures in percent)					
Gasoil 0.1 1/2 *(CIF NWE/Basis ARA + FOB Rotterdam)*	29.13	30.05	*(3.1)*	27.80	30.67	*(9.4)*
Fuel oil 3.5% 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	18.58	20.70	*(10.2)*	18.26	21.05	*(13.3)*
Fuel oil 3.5% *(FOB Med (Italy))*	18.49	20.40	*(9.4)*	18.19	20.97	*(13.3)*
Naphtha Phy 1/2 *(CIF NEW/Basis ARA+ FOB Rotterdam)*	28.68	30.67	*(6.5)*	26.73	32.15	*(16.9)*
HS VGO(2) 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	24.39	25.78	*(5.4)*	23.35	26.88	*(13.1)*
Russian market [1]	(in th. RR per tonne (incl.excise tax and VAT), except for figures in percent)					
Crude oil	12,56	12,98	*(3.2)*	12,55	13,96	*(10.1)*
Fuel oil	7,43	8,95	*(17.0)*	7,78	9,28	*(16.2)*

Source: Platts (world market), Kortes (Russian market)

[1] The Company sells crude oil for export and in the domestic market on various delivery terms. Therefore, our average realized sales prices differ from average reported prices.

There is no independent or uniform market price for crude oil in Russia primarily because a significant portion of crude oil destined for sale in Russia is produced by vertically integrated Russian oil companies and is refined by the same vertically integrated companies. Crude oil that is not exported from Russia, refined by the producer or sold on previously agreed terms, offered for sale in the domestic market at prices determined on a transaction-by-transaction basis. However, there may be significant price differences between regions for similar quality crude oil as a result of the competition and economic conditions in those regions.

Inflation and foreign currency exchange rate fluctuations

A significant part of the Group's revenues are derived from export sales of crude oil and refined products which are denominated in US Dollars. The Group's operating costs are primarily denominated in Rubles. Accordingly, the relative movements of Ruble inflation and Ruble/US Dollar exchange rates can significantly affect the results of operations of the Group. For instance, operating margins are generally adversely affected by an appreciation of the

Ruble against the US Dollar, because in the inflatory economy this will generally cause costs to increase relative to revenues. The Group has not historically used financial instruments to hedge against foreign currency exchange rate fluctuations.

The following table shows the rates of inflation in Russia, the period-end and average Ruble/US Dollar exchange rates for the periods indicated.

	Three months ended 31 March 2013	Three months ended 31 March 2012
Ruble inflation, %	1.9	1.5
Period-end exchange rate (Ruble to US$)	31.08	29.33
Average exchange rate (Ruble to US$)	30.41	30.26

Sources: Federal Service of State Statistics and the Central Bank of Russia

At present, the Ruble is not a freely convertible currency outside the Commonwealth of Independent States. Certain exchange restrictions and controls still exist related to converting Rubles into other currencies.

Taxation

The tables below present a summary of statutory tax rates that the Company and the majority of its subsidiaries were subject to in the respective periods:

Tax	Three months ended 31 March 2013	Three months ended 31 March 2012	Change, %	Taxable base
Income tax – maximum rate	20%	20%	-	Taxable income
Value Added Tax (VAT)	18%	18%	-	Sales from goods/services
Property tax – maximum rate	2.2%	2.2%	-	Taxable property
	(in RR per tonne, except for figures in percent)			
Mineral extraction tax, average rates[1]	5,261	5,284	*(0.4)*	Tonne produced (crude oil)
	(in US $ per tonne, except for figures in percent)			
Crude oil export duty, average rates	406.5	400.8	*1.4*	Tonne exported
Refined products export duty average rates:				
Gasoline, straight-run gasoline	365.9	360.7	*1.4*	
Light and middle distillates, gasoils, fuel oil *(mazut)*	268.3	264.5	*1.4*	Tonne exported

[1] *Without taking into account differentiated taxation*

Starting from 1 May 2011 the Russian Government ("the Government") introduced a special export duty on gasoline equivalent to 90% of the export duty on crude oil. Starting from 1 June 2011 the Government introduced a special export duty on straight-run gasoline equivalent to 90% of the export duty on crude oil. The Group's results of operation are not materially affected by these special export duties.

In the first quarter of 2013 mineral extraction tax rate decreased by 0.4%. Average refined products export duty rate increased by 1%, mainly due to the fact that rates of the export customs duty on refined products are linked to the crude oil export duty, average value of which increased also by 1%.

The rates of mineral extraction tax and export duties for crude oil and refined products are linked to international crude oil prices and are changed in line with them. Below are presented tax rates calculation approach.

Mineral extraction tax (MET) rate. The base tax rate for the production of oil in the first quarter of 2013 is set at RR 470 per tonne (an increase from RUR 446 base tax rate applied in the corresponding period of 2012) and is adjusted depending on the international market price of Urals blend and the Ruble 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 of the tax rate by $1.80 per tonne extracted.

The MET rate is applied with a discount based on the level of depletion of the related oil fields as determined under Russian reserves classification guidelines. Such formula benefits producers with oil fields having a depletion level 80% and above as determined by the Russian reserves classification. The Group receives a benefit of 3.5% per field for each percent of depletion within the limits of 80% to 100%. As Romashkinskoye field, the Group's largest, along with certain other fields, is more than 80% depleted, the Group received a benefit related to crude oil production from these fields in the first quarter of 2013 of RR 6.0 billion (RR 5.4 billion in the first quarter of 2012).

Also a zero MET rate applies to the production of highly viscous crude oil (defined as crude oil of more than 200 Megapascal second in reservoir conditions). Since April 2007, the Group's production of highly viscous crude oil from the Ashalchinskoye and Mordovo-Karmalskoye fields, and since 2010 and 2011 - also from some other fields is subject to a zero MET rate, resulting in a tax benefit in the first quarter of 2013 attributed to that production of RR 0.4 billion (RR 0.2 billion in the first quarter of 2012).

At the end of November 2011 new amendments to the Tax Code of the Russian Federation were signed into law, which provide for a possibility to decrease the mineral extraction tax payable on production of crude oil from certain fields located entirely or partially in Tatarstan until 2016.

Crude oil export duties. The Government determines the export duty rate, which is dependent on the average Urals price for the monitoring period and cannot exceed the following levels:

Quoted Urals price (P), US$ per tonne	Maximum Export Duty Rate
0 – 109.50	0%
109.50 – 146.00	35.0% * (P - 109.50)
146.00 – 182.50	US$ 12.78 + 45.0% * (P - 146.00)
>182.50	US$ 29.20 + 60.0% * (P - 182.50)

The crude oil export duty rate is revised monthly on the basis of monitoring of crude oil prices for preceding one-month period between the 15th day of each calendar month and the 14th day of the following calendar month (inclusive).

Effective from 1 October 2011 the Government sets the export duty for crude oil at a marginal rate of 60% of the Urals crude oil price during the monitoring period.

In accordance with the amendments to the Russian Federation law on customs tariffs, with effect from 1 April 2013 the Government established formulas for calculation of the export customs duties on crude oil based on international oil prices (reflecting the levels described above and providing for special formulas with respect to extra-viscous oil and oil with special physical and chemical characteristics). With effect from 1 April 2013 specific crude oil export customs duties are calculated and published by the Russian Ministry of Economic Development in accordance with the established formulas.

The export duty rate on crude oil increased by 1% in the first quarter of 2013 to US$ 406.5 per tonne (US$ 55.7 per barrel) from US$ 400.8 per tonne (US$ 54.9 per barrel) in the first quarter of 2012.

Refined products export duties. Export customs duty on refined products is set every month by the Government simultaneously with the export customs duty on crude oil and is denominated in US$ per tonne. The rate of the export customs duty on refined products is linked to the crude oil export duty rate. At the moment, the rate of the export customs duty is the same for all types of refined products with the exception of gasoline and straight-run gasoline.

Prior to February 2011, export customs duty on light refined products (gasoline, diesel, jet fuel, etc.) was calculated using the following formula: 0.438 * (Price * 7.3 – 109.5), where Price is the average Urals price in the US Dollar per barrel. Export customs duty on heavy refined products (fuel oil, etc.) was calculated using the following formula: 0.236 * (Price * 7.3 – 109.5).

Starting from February 2011, the export duty rate on refined products was determined by the Government by applying coefficients of 0.67 of the export duty for crude oil for light refined products and 0.467 for heavy refined products.

The Government introduced special export duties starting from May 2011 for gasoline and starting from June 2011 for straight-run gasoline, which are underlined in the table below.

Starting from October 2011, the export duty for light refined products was lowered from 0.67 to 0.66 of export duty for crude oil; the export duty for heavy refined products was raised from 0.467 to 0.66 of export duty for crude oil.

	Maximum coefficients (effective until 1 October 2011)	Maximum coefficients effective from 1 October 2011 (per Decree No. 716 of 26 August 2011)
Diesel and jet fuel	0.670	0.660
Fuel oil	0.467	0.660
Oil lubricants	0.467	0.660
Gasoline	0.900	0.900
Straight-run gasoline	0.900	0.900

With effect from 1 April 2013 specific rates are calculcated and published by the Russian Ministry of Economic Development.

Excise tax on refined products. According to the legislation introduced in December 2010 the excise tax rates on the refined products were increased and linked to the environmental characteristics of the products. The responsibility to pay excise taxes on refined products in Russia is imposed on refined product producers (except for straight-run gasoline). The excise tax is paid per metric tonne produced and sold domestically.

(RR per tonne)	Three months ended 31 March 2013	Three months ended 31 March 2012
Gasoline:		
High octane gasoline below Euro-3,4,5	10,100	7,725
High octane gasoline Euro-3	9,750	7,382
High octane gasoline Euro-4	8,560	6,822
High octane gasoline Euro-5	5,143	6,822
Straight-run gasoline	10,229	7,824
Diesel fuel:		
Diesel below Euro- 3,4,5	5,860	4,098
Diesel Euro-3	5,860	3,814
Diesel Euro-4	4,934	3,562
Diesel Euro-5	4,334	3,562
Motor oils	7,509	6,072

Excise tax rates on refined products increased in the first quarter of 2013 by 25% on average in comparison to 2012.

Property tax. The maximum property tax rate in Russia is 2.2%. Exact tax rates are set by the regional authorities.

Value added tax (VAT). The Group is subject to value added tax (or VAT) of 18% on most sales. The Group's results of operations exclude the impact of VAT.

Income tax. The total income tax rate of 20% includes federal part of 2.0%, and the regional part, which varies between 13.5% and 18.0%.

Transportation of crude oil and refined products

Due to the fact that majority of Russian crude oil production regions are remote from the main crude oil and refined products markets oil companies are dependent on the extent of diversification of transport infrastructure and access to it. Thus, transportation cost is an important factor affecting our operations and financial results.

The Group transports substantially all of the crude oil that it sells in export and local markets through trunk pipelines in Russia that are controlled by Transneft.

Transportation of crude oil is based on contracts with Transneft and its subsidiaries, which set forth the basic obligations of the contracting parties, including the right of Transneft to blend or substitute a company's oil with oil of other producers. The Group's crude oil is blended in the Transneft pipeline system with other crude oil of varying qualities to produce an export blend commonly referred to as Urals. The Group benefits from this blending since the quality of its crude oil is generally lower than that produced by some other oil companies due to the relatively high sulfur content.

A significant portion of crude oil transported by pipeline is delivered to marine terminals for onward transportation. There are constraints present in Russia's oil shipment terminals due to geographic location, weather conditions, and port capacity limitations. However, government sponsored and private programs are seeking to improve port facilities.

Transneft collects on prepayment terms a Ruble tariff on domestic shipments and an additional US Dollar tariff on exports.

Transportation of refined products in Russia is mostly performed by railway transport. The Russian railway infrastructure is owned and operated by OAO Russian Railways.

Transneft and OAO Russian Railways are state-owned companies. As the activities of the above mentioned companies fall under the scope of natural monopolies, the fundamentals of their tariff policies are defined by the state authorities to ensure the balance of interests of the state and all participants in the transportation process. Transportation tariffs of natural monopolies are set by the Federal Service for Tariffs of the Russian Federation ("FST") and are dependent on transport destination, delivery volume, distance of transportation, and several other factors. Tariffs are revised by the FST at least annually.

Critical accounting policies

The preparation of consolidated financial statements in conformity with IFRS requires management to select appropriate accounting policies and to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. For a full description of our significant accounting policies, please refer to Note 2 of our consolidated financial statements.

Forward-looking statements

Certain statements in this document are not historical facts and are ''forward-looking'' (as such term is defined in the US Private Securities Litigation Reform Act of 1995). We may from time to time make written or oral forward-looking statements in reports to shareholders and in other communications. Examples of such forward-looking statements include, but are not limited to:

- projections of revenues, income (or loss), earnings (or loss) per share, dividends, capital structure or other financial items or ratios;
- statements of our plans, objectives or goals, including those related to products or services;
- statements of future economic performance; and
- statements of assumptions underlying such statements.

Words such as ''believes,'' ''anticipates,'' ''expects,'' ''intends'' and ''plans'' and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that the predictions, forecasts, projections and other forward-looking statements will not be achieved. We caution readers that a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements.

These factors include:

- inflation, interest rate, and exchange rate fluctuations;
- the price of oil;
- the effect of, and changes in, Russian or Tatarstan government policy;
- the effect of terrorist attack or other geopolitical instability, either within Russia or elsewhere;
- the effects of competition in the geographic and business areas in which we conduct operations;
- the effects of changes in laws, regulations, taxation or accounting standards or practices;
- our ability to increase market share and control expenses;
- acquisitions or divestitures;
- technological changes.

This list of important factors is not exhaustive; when relying on forward-looking statements to make decisions with respect to our shares, American Depositary Shares (ADSs) or other securities, investors and others should carefully consider the foregoing factors and other uncertainties and events, especially in light of the difficult political, economic, social and legal environment in which we operate. Such forward-looking statements speak only at the date on which they are made, and we do not undertake any obligation to update or revise any of them, whether as a result of new information, future events or otherwise. We do not make any representation, warranty or prediction that the results anticipated by such forward-looking statements will be achieved, and such forward-looking statements represent, in each case, only one of many possible scenarios and should not be viewed as the most likely or standard scenario.