MANAGEMENT'S DISCUSSION AND ANALYSIS

OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FOR THE THREE AND

NINE MONTHS ENDED 30 SEPTEMBER 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 statements" on page 22 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 30 September 2013 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		Change,	Nine months ended		Change,
	30 September 2013	30 September 2012	%	30 September 2013	30 September 2012	%
Financial results						
Sales, net (RR million)	123,389	127,247	*(3)*	334,639	334,390	*0.1*
Profit attributable to Group shareholders (RR million)	23,232	27,119	*(14.3)*	55,141	59,022	*(6.6)*
EBITDA [(1)] (RR million)	37,960	39,949	(5)	92,948	95,631	*(2.8)*
Additions to property, plant and equipment (RR million)	11,430	14,716	*(22.3)*	38,639	36,411	*6.1*
Free Cash Flow (RR million)	8,443	1,325	*537.2*	40,670	42,031	*(3.2)*
Basic and Diluted net profit per share of common stock (RR)						
Common	10.23	11.94	*(16.7)*	24.28	25.99	*(6.6)*
Preferred	10.20	11.92	*(16.7)*	24.25	25.97	*(6.6)*
Operational results						
Crude oil production by the Group (th. tonnes)	6,666	6,623	*0.6*	19,757	19,683	*0.4*
Crude oil production by the Group (th. barrels)	47,482	47,177	*0.6*	140,726	140,202	*0.4*
Crude oil daily production (th. barrels per day)	516.1	512.8	*0.6*	515.5	511.7	*0.7*
Gas production by the Group (million cubic meters)	236.3	233.9	*0.9*	699.7	694.9	*0.7*
Gas daily production (th. boe per day)	15.1	15.0	*0.0*	15.1	14.9	*1.3*
Refined products produced (th. tonnes)	2,345.8	1,906.4	*23.1*	6,057.6	5,282.1	*14.7*
Gas products produced (th. tonnes)	273.1	297.3	*(8.1)*	828.0	879.6	*(5.9)*
Refining throughput (th.barrels per day)	188.7	154.2	*22.7*	165.4	145.3	*13.8*
Production of tires (million tires)	3.2	3.3	*(3.0)*	9.6	9.7	*(1.0)*
Number of petrol (gas) stations in Russia[(2) (3)]	516	507		516	507	
Number of petrol (gas) stations outside of Russia[(2) (3)]	122	131		122	131	

(1) *As defined on page 13*
(2) *Including leased stations*
(3) *At the end of the period*

Our net profit in the third quarter of 2013 of RR 23,232 million was lower by RR 3,887 million than in the corresponding period of 2012 mostly due to lower sales and other operating revenues as well as total other expenses (vs income in the corresponding period of 2012), mainly decrease in foreign exchange gain, and higher profit attributable to non-controlling interest in the current period.

Our net profit in the nine months of 2013 was RR 55,141 million, which is RR 3,881 million, or 6.6%, less than in the corresponding period of 2012 mostly due to higher transportation expenses on refined products and total other expenses (mainly foreign exchange loss).

In the third quarter of 2013 the Group (including consolidated subsidiaries OAO Ilekneft, OOO Tatneft-Samara, OOO Tatneft-Severny) produced 6.7 million metric tonnes of crude oil which is 0.6% higher than in the third quarter of 2012. Our gas production in the third quarter of 2013 was 236.3 million cubic meters which is 0.9% higher than in the corresponding period of 2012.

In the nine months of 2013 the Group produced 19.8 million metric tonnes of crude oil which is 0.4% higher than in the nine months of 2012. Our gas production in the nine months of 2013 was 699.7 million cubic meters which is 0.7% higher than in the corresponding period of 2012. Increase of refining throughput by 13.8% in the nine months of 2013 compared to the corresponding period of 2012 was due to higher capacity utilization at the TANECO refinery.

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 and nine months ended 30 September 2013 compared to the three and nine months ended 30 September 2012

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

(RR million)	Three months ended 30 September 2013 (unaudited)	Three months ended 30 September 2012 (unaudited)	Change, %	Nine months ended 30 September 2013 (unaudited)	Nine months ended 30 September 2012 (unaudited)	Change, %
Sales and other operating revenues, net	123,389	127,247	*(3)*	334,639	334,390	*0.1*
Costs and other deductions						
Operating	23,316	24,288	*(4)*	63,225	62,225	*1.6*
Purchased oil and refined products	12,572	14,826	*(15.2)*	37,623	39,970	*(5.9)*
Exploration	578	514	*12.5*	1,239	1,366	*(9.3)*
Transportation	7,920	7,691	*3*	23,366	21,686	*7.7*
Selling, general and administrative	11,247	10,974	*2.5*	31,816	28,838	*10.3*
Depreciation, depletion and amortization	3,679	4,383	*(16.1)*	12,894	13,175	*(2.1)*
(Gain)/ loss on disposals of property, plant and equipment, investments and impairments	(567)	417	*n/a*	(1,040)	1,123	*n/a*
Taxes other than income taxes	29,191	27,516	*6.1*	82,051	80,482	*1.9*
Maintenance of social infrastructure and transfer of social assets	1,172	1,072	*9.3*	3,411	3,069	*11.1*
Total costs and other deductions	89,108	91,681	*(2.8)*	254,585	251,934	*1.1*
Foreign exchange gain/ (loss)	117	1,941	*(94)*	(1,035)	1,255	*n/a*
Interest income	912	910	*0.2*	2,484	3,026	*(17.9)*
Interest expense, net of amounts capitalized	(1,476)	(1,866)	*(20.9)*	(4,614)	(5,807)	*(20.5)*
Earnings from equity investments	73	82	*(11)*	296	531	*(44.3)*
Other income, net	181	318	*(43.1)*	610	512	*19.1*
Total other (expenses)/ income	(193)	1,385	*n/a*	(2,259)	(483)	*367.7*
Profit before income taxes	34,088	36,951	*(7.7)*	77,795	81,973	*(5.1)*
Current income tax expense	(6,632)	(7,895)	*(16)*	(16,601)	(19,282)	*(13.9)*
Deferred income tax (expense)/ benefit	(1,461)	(244)	*498.8*	(1,285)	622	*n/a*
Total income tax expense	(8,093)	(8,139)	*(0.6)*	(17,886)	(18,660)	*(4.1)*
Profit for the period	25,995	28,812	*(9.8)*	59,909	63,313	*(5.4)*
Less: Profit attributable to non-controlling interest	(2,763)	(1,693)	*63.2*	(4,768)	(4,291)	*11.1*
Profit attributable to Group shareholders	23,232	27,119	*(14.3)*	55,141	59,022	*(6.6)*

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 30 September 2013	Three months ended 30 September 2012	Change, %	Nine months ended 30 September 2013	Nine months ended 30 September 2012	Change, %
Crude oil						
Sales	*93,099*	*104,312*	*(10.7)*	*270,755*	*290,164*	*(6.7)*
Less related export duties	*(36,366)*	*(39,479)*	*(7.9)*	*(107,219)*	*(114,238)*	*(6.1)*
	56,733	64,833	*(12.5)*	163,536	175,926	*(7)*
Refined products						
Sales	*64,907*	*56,399*	*15.1*	*164,457*	*136,599*	*20.4*
Less related export duties and excise taxes	*(13,507)*	*(10,570)*	*27.8*	*(35,936)*	*(22,990)*	*56.3*
	51,400	45,829	*12.2*	128,521	113,609	*13.1*
Petrochemicals	8,919	10,539	*(15.4)*	24,610	27,603	*(10.8)*
Corporate and other sales	6,337	6,046	*4.8*	17,972	17,252	*4.2*
Total Sales and other operating revenues, net	123,389	127,247	*(3)*	334,639	334,390	*0.1*

Decrease in sales and other operating revenues in the third quarter of 2013 in comparison to the corresponding period of 2012 and mostly unchanged sales and other operating revenues in the nine months of 2013 in comparison to the corresponding period of 2012 were due to changes in the balance of crude oil and refined products sold as well as the effect of related export duties and excise taxes paid in connection with such sales.

In the third quarter of 2013 export duties paid by the Group decreased by 0.9% to RR 49,444 million from RR 49,869 million in the corresponding period of 2012 and our expenses on excise taxes increased to RR 429 million from RR 180 million in the corresponding period of 2012.

In the nine months of 2013 export duties paid by the Group increased by 4.2% to RR 142,272 million from RR 136,542 million in the corresponding period of 2012 and our expenses in the nine months of 2013 on excise taxes increased to RR 883 million from RR 686 million in the corresponding period of 2012.

Export of crude oil and refined products from Russia

For 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.

Three months ended 30 September 2013

During the third quarter of 2013, the Group exported from Russia approximately 73% of all its crude oil sold which was the same level as in the corresponding period of 2012.

In the third quarter of 2013 the Company delivered 50% (27% in the third quarter of 2012) of its own crude oil for export through Transneft's Druzhba pipeline (mainly to Hungary, Poland and Slovakia); 18% (41% in the third quarter of 2012) of crude oil was shipped through Russian Black Sea ports (mainly Novorossiysk) and 32% (the same in the third quarter of 2012) of crude oil exported through Russian Baltic Sea ports (mainly Primorsk).

In the third quarter of 2013 the Group exported from Russia 1,510 thousand tonnes of refined products (including 17 thousand tonnes of purchased refined products) in comparison to 1,540 thousand tonnes in the third quarter of 2012 (including 21 thousand tonnes of purchased refined products).

Nine months ended 30 September 2013

During the nine months of 2013, the Group exported from Russia approximately 69% of all its crude oil sold compared to approximately 68% in the corresponding period of 2012.

In the nine months of 2013 the Company delivered 45% (34% in the nine months of 2012) of its own crude oil for export through Transneft's Druzhba pipeline (mainly to Poland, Hungary and Slovakia); 19% (41% in the nine months of 2012) of crude oil was shipped through Russian Black Sea ports (mainly Novorossiysk) and 36% (25% in the nine months of 2012) of crude oil exported through Russian Baltic Sea ports (mainly Primorsk).

In the nine months of 2013 the Group exported from Russia 4,080 thousand tonnes of refined products (including 47 thousand tonnes of purchased refined products) in comparison to 4,096 thousand tonnes in the corresponding period of 2012 (including 30 thousand tonnes of purchased refined products).

Sales breakdown

Sales revenues

(RR million)	Three months ended 30 September 2013	Three months ended 30 September 2012	Change, %	Nine months ended 30 September 2013	Nine months ended 30 September 2012	Change, %
Crude oil						
Non-CIS						
Export sales	78,236	90,218	*(13.3)*	224,612	237,704	*(5.5)*
Less related export duties	(36,366)	(39,479)	*(7.9)*	(107,219)	(114,238)	*(6.1)*
CIS sales[1]	2,050	-	*n/a*	5,311	5,342	*(0.6)*
Domestic sales	12,813	14,094	*(9.1)*	40,832	47,118	*(13.3)*
	56,733	64,833	*(12.5)*	163,536	175,926	*(7)*
Refined products						
Non-CIS export sales						
Export sales	33,469	28,339	*18.1*	88,988	56,462	*57.6*
Less related export duties	(12,890)	(10,390)	*24.1*	(34,829)	(22,304)	*56.2*
CIS sales						
CIS sales	2,018	6,027	*(66.5)*	4,520	26,501	*(82.9)*
Less related export duties	(188)	-	*n/a*	(224)	-	-
Domestic sales						
Domestic sales	29,420	22,033	*33.5*	70,949	53,636	*32.3*
Less related excise taxes	(429)	(180)	*138.3*	(883)	(686)	*28.7*
	51,400	45,829	*12.2*	128,521	113,609	*13.1*
Petrochemical products						
Tires sales	8,540	10,294	*(17.0)*	23,649	26,744	*(11.6)*
Other petrochemicals sales	379	245	*54.7*	961	859	*11.9*
	8,919	10,539	*(15.4)*	24,610	27,603	*(10.8)*
Other sales	6,337	6,046	*4.8*	17,972	17,252	*4.2*

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

Sales volumes

(thousand tonnes)	Three months ended 30 September 2013	Three months ended 30 September 2012	Change, %	Nine months ended 30 September 2013	Nine months ended 30 September 2012	Change, %
Crude oil						
Non-CIS export sales	3,030	3,641	*(16.8)*	9,263	9,738	*(4.9)*
CIS sales	150	-	*n/a*	431	400	*7.7*
Domestic sales	1,203	1,336	*(10.0)*	4,286	4,806	*(10.8)*
	4,383	4,977	*(11.9)*	13,980	14,944	*(6.5)*
Refined products						
Non-CIS export sales	1,431	1,231	*16.2*	3,907	2,476	*57.8*
CIS sales	79	309	*(74.4)*	173	1,620	*(89.3)*
Domestic sales	1,382	1,127	*22.6*	3,450	2,766	*24.7*
	2,892	2,667	*8.4*	7,530	6,862	*9.7*

Realized average sales prices

(th. RR per tonne)	Three months ended 30 September 2013	Three months ended 30 September 2012	Change, %	Nine months ended 30 September 2013	Nine months ended 30 September 2012	Change, %
Crude oil						
Non-CIS export sales	25.82	24.78	4.2	24.25	24.41	(0.7)
CIS sales	13.67	-	n/a	12.32	13.36	(7.7)
Domestic sales	10.65	10.55	1.0	9.53	9.80	(2.8)
Refined products						
Non-CIS export sales	23.39	23.02	1.6	22.78	22.80	(0.1)
CIS sales	25.54	19.50	31.0	26.13	16.36	59.7
Domestic sales	21.29	19.55	8.9	20.56	19.39	6.1

Sales of crude oil

Sales of crude oil in the third quarter of 2013 and for the nine months of 2013 compared to the corresponding periods of 2012 decreased by 10.7% and 6.7%, respectively, and amounted to RR 93,099 million and RR 270,755 million, respectively, mainly due to increased volumes of own refining throughput resulting in decreased volumes of crude oil sales.

Sales of refined products

Increase in sales of refined products by 15.1% to RR 64,907 million in the third quarter of 2013 from RR 56,399 million in the corresponding period of 2012 was due to higher volumes of refined products sold in domestic market in the current period.

In the nine months of 2013 increase in sales of refined products by 20.4% to RR 164,457 million from RR 136,599 million in the corresponding period of 2012 was mostly due to increased throughput and sold volumes of TANECO's refined products and higher average prices of refined products sold in the current period.

	Three months ended				Change*, %		Nine months ended				Change*, %	
	30 September 2013		30 September 2012				30 September 2013		30 September 2012			
Non-CIS export sales	RR mln	mln tonnes	RR mln	mln tonnes	Sales	Volumes	RR mln	mln tonnes	RR mln	mln tonnes	Sales	Volumes
Vacuum gasoil	10,870	0.43	11,268	0.45	(3.5)	(4.4)	29,731	1.23	18,912	0.77	57.2	59.7
Fuel oil	9,766	0.55	8,965	0.47	8.9	17.0	24,126	1.39	17,881	0.94	34.9	47.9
Naphtha	3,845	0.13	6,620	0.25	(41.9)	(48.0)	16,341	0.59	16,275	0.62	0.4	(4.8)
Gas products	7,494	0.26	1,055	0.04	610.3	550.0	11,139	0.40	2,500	0.10	345.6	300.0
Heating oil	2	-	-	-	n/a	n/a	4,938	0.18	-	-	n/a	n/a
Other	1,492	0.06	431	0.03	246.2	100.0	2,713	0.12	894	0.05	203.5	140.0
Total	33,469	1.43	28,339	1.24	18.1	15.3	88,988	3.91	56,462	2.48	57.6	57.7

	Three months ended				Change*, %		Nine months ended				Change*, %	
	30 September 2013		30 September 2012				30 September 2013		30 September 2012			
CIS export sales	RR mln	mln tonnes	RR mln	mln tonnes	Sales	Volumes	RR mln	mln tonnes	RR mln	mln tonnes	Sales	Volumes
Heating oil	-	-	3,386	0.15	n/a	n/a	-	-	12,287	0.61	n/a	n/a
Fuel oil	8	0.00	465	0.05	(98.3)	n/a	18	0.00	5,741	0.52	(99.7)	n/a
Vacuum gasoil	475	0.02	998	0.05	(52.4)	(60.0)	475	0.02	4,626	0.28	n/a	(92.9)
Gas products	242	0.01	321	0.02	(24.6)	(50.0)	787	0.03	1,815	0.11	(56.6)	(72.7)
Naphtha	2	0.00	165	0.01	(98.8)	n/a	2	0.00	1,068	0.07	n/a	n/a
Other	1,291	0.05	692	0.02	86.6	150.0	3,238	0.12	964	0.02	235.9	n/a
Total	2,018	0.08	6,027	0.30	(66.5)	(73.3)	4,520	0.17	26,501	1.61	(82.9)	(89.4)

Domestic sales	Three months ended 30 September 2013 RR mln	Three months ended 30 September 2013 mln tonnes	Three months ended 30 September 2012 RR mln	Three months ended 30 September 2012 mln tonnes	Change*, % Sales	Change*, % Volumes	Nine months ended 30 September 2013 RR mln	Nine months ended 30 September 2013 mln tonnes	Nine months ended 30 September 2012 RR mln	Nine months ended 30 September 2012 mln tonnes	Change*, % Sales	Change*, % Volumes
Heating oil	1,220	0.07	9,637	0.52	*(87.3)*	*(86.5)*	18,589	0.95	17,964	1.04	*3.5*	*(8.7)*
Petrol fuel	7,223	0.25	6,356	0.22	*13.6*	*13.6*	19,298	0.65	18,397	0.65	*4.9*	*0.0*
Diesel fuel	3,838	0.17	3,784	0.17	*1.4*	*0.0*	11,243	0.43	9,657	0.40	*16.4*	*7.5*
Gas products	2,187	0.20	2,021	0.21	*8.2*	*(4.8)*	5,872	0.60	6,286	0.60	*(6.6)*	*0.0*
Other	14,952	0.70	235	0.01	*n/a*	*n/a*	15,947	0.82	1,332	0.08	*n/a*	*n/a*
Total	29,420	1.39	22,033	1.13	*33.5*	*23.0*	70,949	3.45	53,636	2.77	*32.3*	*24.5*

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

Sales of petrochemical products

Sales of petrochemical products decreased in the third quarter of 2013 and in the nine months of 2013 compared to the corresponding periods of 2012 mainly due to lower volumes of tires sold. The Group's production of tires in the third quarter of 2013 and in the nine months of 2013 decreased by 3% and 1% and amounted to 3.2 million and 9.6 million tires, respectively.

Other sales

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 by the Group entities to third parties.

In the third quarter of 2013 other sales increased by 4.8% to RR 6,337 million from RR 6,046 million in the corresponding period of 2012.

In the nine months of 2013 other sales increased by 4.2% to RR 17,972 million from RR 17,252 million in the corresponding period of 2012.

Costs and other deductions

Operating expenses. Operating expenses include the following costs:

(RR million)	Three months ended 30 September 2013	Three months ended 30 September 2012	Nine months ended 30 September 2013	Nine months ended 30 September 2012
Crude oil extraction expenses	11,902	10,901	32,734	29,127
Refining expenses	1,464	765	3,460	1,833
Petrochemical production expenses	7,361	9,257	19,872	23,529
Other operating expenses	2,677	3,248	7,084	7,172
Operating expenses not attributed to the revenue in the current period[(1)]	(88)	117	75	564
Total operating expenses	23,316	24,288	63,225	62,225

[(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.

In the third quarter of 2013 lifting expenses averaged to RR 250.7 per barrel compared to RR 231.1 per barrel in the corresponding period of 2012.

In the nine months of 2013 lifting expenses averaged to RR 232.6 per barrel compared to RR 207.7 per barrel in the corresponding period of 2012.

Higher equipment services, energy costs for oil extraction and injection costs were the primary reason for the increase in lifting expenses in the three and the nine months ended 30 September 2013 compared to the corresponding periods 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 third quarter of 2013 were RR 674.2 per tonne of crude oil throughput (RR 678.2 per tonne of products output) compared to RR 406.1 per tonne of crude oil throughput (RR 409.3 per tonne of products output) in the corresponding period of 2012.

The refining expenses incurred in the nine months of 2013 were RR 619.7 per tonne of crude oil throughput (RR 623.9 per tonne of products output) compared to RR 351.3 per tonne of crude oil throughput (RR 356.1 per tonne of products output) in the corresponding period of 2012.

Petrochemical production expenses. Petrochemical production expenses primarily include the costs of raw materials, labour, maintenance and electricity consumed in the production of petrochemical products.

Compared to the prior periods, in the third quarter of 2013 and for the nine months of 2013 cost of petrochemical products decreased to RR 7,361 million and to RR 19,872 million, respectively. The decrease by 20.5% and 15.5%, respectively, compared to the corresponding periods of 2012 were due to lower cost of raw materials.

Other operating expenses include costs of other services, goods and materials not related to the core production activities of the Group. In the third quarter of 2013 in comparison to the corresponding period of 2012 other operating expenses decreased by 17.6% due to decrease in sales volumes of other services, goods and materials.

In the nine months of 2013 in comparison to the corresponding period of 2012 other operating expenses decreased by 1.2%.

Cost of purchased crude oil and refined products. A summary of purchased oil and refined products in the respective periods of 2013 and 2012 were as follows:

	Three months ended		Nine months ended	
	30 September 2013	30 September 2012	30 September 2013	30 September 2012
Purchased crude oil (RR million)	3,557	5,285	12,548	14,250
Volume (thousand tonnes)	*137*	*227*	*519*	*668*
Average price (th. RR per tonne)	*25.96*	*23.28*	*24.18*	*21.33*
Purchased refined products (RR million)	9,015	9,541	25,075	25,720
Volume (thousand tonnes)	*347*	*384*	*974*	*1,076*
Average price (th. RR per tonne)	*25.98*	*24.85*	*25.74*	*23.91*
Total purchased oil and refined products	12,572	14,826	37,623	39,970

Exploration expenses. Exploration expenses consist primarily of exploratory drilling, geological and geophysical costs, and the costs of carrying and retaining undeveloped properties.

In the third quarter of 2013 and for the nine months of 2013 exploration expenses decreased to RR 578 million and RR 1,239 million, respectively, from RR 514 million and RR 1,366 million in the corresponding periods 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.

In the third quarter of 2013 increase of transportation expense by 3% to RR 7,920 million from RR 7,691 million in the corresponding period of 2012 was mainly due to increased volumes of refined products sold in the current period.

Increase of transportation expense by 7.7% to RR 23,366 million in the nine months of 2013 from RR 21,686 million in the corresponding period of 2012 was due to increased volumes of refined products sold and transported by the railway in the current period as well as an 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 2,978 million to RR 31,816 million in the nine months of 2013 and by RR 273 million to RR 11,247 million in the third quarter of 2013 compared to the corresponding periods 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 third quarter of 2013 we recorded a gain from disposals of some non-core assets, which resulted to the gain recorded in the three and nine months ended 30 September 2013 compared to the corresponding periods of 2012.

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

	Three months ended		Nine months ended	
(RR million)	30 September 2013	30 September 2012	30 September 2013	30 September 2012
Mineral extraction tax	27,640	26,955	77,451	78,061
Property tax	1,150	571	3,466	1,660
Penalties and interest	(9)	(329)	20	(265)
Other	410	319	1,114	1,026
Total taxes other than income taxes	29,191	27,516	82,051	80,482

Taxes other than income taxes increased in the three months ended 30 September 2013 in comparison to the corresponding periods of 2012 by 6.1%.

Taxes other than income taxes increased in the nine months ended 30 September 2013 in comparison to the corresponding periods of 2012 by 1.9%, due to higher Group's property tax.

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 three and nine months ended 30 September 2013 of RR 6.5 billion and RR 18.1 billion, respectively (in comparison to RR 5.5 billion and RR 16.1 billion, respectively, in the corresponding periods 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 a tax benefit in the three and nine months ended 30 September 2013 of RR 0.7 billion and RR 1.9 billion, respectively (in comparison to RR 0.3 billion and RR 0.8 billion, respectively, in the corresponding periods of 2012).

Maintenance of social infrastructure and transfer of social assets. In the three and nine months ended 30 September 2013 maintenance of social infrastructure expenses and transfer of social assets increased to RR 1,172 million and RR 3,411 million, respectively, from RR 1,072 million and RR 3,069 million, respectively, in the three and nine months ended 30 September 2012. These social infrastructure expenses relate primarily to housing, schools and cultural buildings in Tatarstan.

Foreign exchange gain/ (loss). In the three and nine months ended 30 September 2013 the Group recorded a foreign exchange gain amounted to RR 117 million and a foreign exchange loss of RR 1,035 million, respectively, compared to a foreign exchange gain of RR 1,941 million and RR 1,255 million, respectively, in the three and nine months ended 30 September 2012. Volatility of Ruble to US Dollar exchange rates in the reporting periods, resulting in the corresponding revaluations of US Dollars denominated debt under the long-term credit facilities of the Group was the main reason of such movements in foreign exchange losses in the reporting periods.

Interest income in the three months ended 30 September 2013 increased by 0.2% to RR 912 million compared to RR 910 million in the corresponding period of 2012.

In the nine months ended 30 September 2013 interest income decreased by 17.9% to RR 2,484 million compared to the corresponding period of 2012 due to decrease in interest income received from the certificates of deposit.

Interest expense includes among other things an unwinding of the discount on the provision for the future costs of decommissioning of oil and gas assets.

In the three and nine months ended 30 September 2013 interest expense, net of amounts capitalized, decreased by 20.9% and 20.5% to RR 1,476 million and RR 4,614 million, respectively, compared to the corresponding periods of 2012 due to the decrease in the current period's amount of total debt outstanding.

Earnings from equity investments. In the three and the nine monthes of 2013 the Group recorded a gain from equity investments amounted to RR 73 million and RR 296 million, respectively, compared to a gain of RR 82 million and RR 531 million, respectively, in the corresponding periods of 2012.

Other income, net, in the third quarter of 2013 amounted to RR 181 million compared to RR 318 million of other income, net, in the corresponding period of 2012.

In the nine months of 2013 the Group recorded other income, net, amounted to RR 610 million compared to RR 512 million of other income, net, in the corresponding period of 2012.

Income taxes

The effective income tax rate in the nine months of 2013 was 23%, 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

	Three months ended		Nine months ended	
(RR million)	30 September 2013	30 September 2012	30 September 2013	30 September 2012
Sales and other operating revenues, net	123,389	127,247	334,639	334,390
Costs and other deductions	(89,108)	(91,681)	(254,585)	(251,934)
Depreciation, depletion and amortization	3,679	4,383	12,894	13,175
EBITDA	37,960	39,949	92,948	95,631

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 30 September 2013	At 31 December 2012
Current assets	147,327	140,332
Long-term assets	512,306	490,275
Total assets	659,633	630,607
Current liabilities	85,670	76,550
Long-term liabilities	87,937	107,824
Total liabilities	173,607	184,374
Shareholders' equity	486,026	446,233
Working capital	61,657	63,782

Working capital position

As of 30 September 2013 working capital of the Group amounted to RR 61,657 million compared to RR 63,782 million as of 31 December 2012. The decrease in the working capital in the current period compared to previous period was attributable to an increase in current liabilities.

Liquidity and Capital Resources

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

(RR million)	Nine months ended 30 September 2013	Nine months ended 30 September 2012
Net cash provided by operating activities	79,309	78,442
Net cash used in investment activities	(34,502)	(36,683)
Net cash used in financing activities	(40,889)	(41,673)
Net change in cash and cash equivalents	3,918	86

Net cash provided by operating activities

Our primary source of cash flow is funds generated from our operations. Net cash provided by operating activities increased by 1.1% to RR 79,309 million in the nine months of 2013 from RR 78,442 million in the corresponding period of 2012.

Net cash used in investing activities

Net cash used in investing activities decreased by 5.9% to RR 34,502 million in the nine months of 2013 from RR 36,683 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 was to RR 40,889 million in the nine months of 2013 in comparison to RR 41,673 million used in the corresponding period of 2012. It was in line with net debt repayments of RR 20,633 million in the nine months of 2013 compared to net debt repayments of RR 25,481 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 three and nine months ended 30 September 2013 compared to the corresponding periods of 2012:

(RR million)	Three months ended 30 September 2013	Three months ended 30 September 2012	Nine months ended 30 September 2013	Nine months ended 30 September 2012
Exploration and production	5,467	7,312	18,691	18,522
Refining and marketing	3,432	6,377	13,487	15,353
Petrochemicals	86	56	258	263
Corporate and other	2,445	971	6,203	2,273
Total additions to property, plant and equipment	11,430	14,716	38,639	36,411

Calculation of Free Cash Flow

(RR million)	Three months ended 30 September 2013	Three months ended 30 September 2012	Nine months ended 30 September 2013	Nine months ended 30 September 2012
Net cash provided by operating activities	19,873	16,041	79,309	78,442
Additions to property, plant and equipment	(11,430)	(14,716)	(38,639)	(36,411)
Free Cash Flow	8,443	1,325	40,670	42,031

Analysis of Debt

At 30 September 2013, long-term debt, net of current portion, amounted to RR 14,427 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 US$ 2 billion arranged in June 2010.

Under the US$ 1.5 billion facility the undiscounted amounts outstanding, including the current portion, as of 30 September 2013 and 31 December 2012 were RR 3,117 million (US$ 96 million) and RR 4,808 million (US$ 158 million), respectively.

Under the US$ 2 billion facility the undiscounted amounts outstanding, including the current portion, as of 30 September 2013 and 31 December 2012 were RR 17,850 million (US$ 552 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. 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.

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. 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.

In June 2011, the Company entered into a US $550 million unsecured credit facility with a fixed rate of 3.50% per annum with bullet repayment in three years, arranged by BNP Paribas (Suisse) SA, The Bank Of Tokyo Mitsubishi UFJ, Ltd., Commerzbank Aktiengesellschaft, ING Bank N.V., Natixis, Open Joint Stock Company Nordea Bank, Sumitomo Mitsui Banking Corporation and WestLB AG, London Branch. The loan agreement requires compliance with certain financial covenants including, but not limited to, minimum levels of consolidated tangible net worth, and interest coverage ratios. The undiscounted amounts outstanding under this credit facility as of 30 September 2013 and 31 December 2012 were RR 17,790 million (US$ 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 30 September 2013 and 31 December 2012 were RR 2,062 million (US$ 64 million) and RR 2,050 million (US$ 68 million), including the current portion, respectively.

Also in November 2011, TANECO entered into a US$ 144.5 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 30 September 2013 and 31 December 2012 were RR 2,655 million (US$ 82 million) and RR 2,165 million (US$ 71 million), including the current portion, respectively.

In May 2013, TANECO entered into a EUR 55 million credit facility with equal semi-annual repayment during ten years. The loan was arranged by The Royal Bank of Scotland plc and Sumitomo Mitsui Banking Corporation Europe Limited. The loan bears interest at LIBOR plus 1.5% 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 30 September 2013 were RR 1,133 million (EUR 26 million), including the current portion.

Calculation of Net Debt

(RR million)	At 30 September 2013	At 31 December 2012
Short term debt	37,135	32,096
Long term debt, net of current portion	14,427	37,991
Total debt	51,562	70,087
Cash and cash equivalents	17,234	13,083
Net Debt	34,328	57,004

Contractual obligations, other contingencies and off balance sheet arrangements

Guarantees

The Group has no outstanding guarantees at 30 September 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 5), 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 and is currently discussing with all relevant parties arrangements relating to its exploration activities. 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 third quarter of 2013, Brent crude oil price fluctuated between $103 and $117 per barrel and averaged $110.4 per barrel in comparison to average $109.6 per barrel in the corresponding period of 2012.

During the nine months of 2013, Brent crude oil price fluctuated between $97 and $119 per barrel and averaged $108.5 per barrel in comparison to average $112.1 per barrel in the corresponding period of 2012.

Substantially all the crude oil we sell is Urals blend. The table below shows for average and at 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 30 September 2013	Average for the three months ended 30 September 2012	Change, %	Average for the nine months ended 30 September 2013	Average for the nine months ended 30 September 2012	Change, %
World market [1]	(in US Dollars per barrel, except for figures in percent)					
Brent crude	110.4	109.6	*0.7*	108.5	112.1	*(3.2)*
Urals crude *(CIF Mediterranean)*	109.9	109.2	*0.6*	107.8	111.0	*(2.9)*
Urals crude *(CIF Rotterdam)*	109.4	108.8	*0.6*	107.3	110.6	*(3.0)*
	(in US Dollars per tonne, except for figures in percent)					
Gasoil 0.1 1/2 *(CIF NWE/Basis ARA + FOB Rotterdam)*	929.7	983.7	*(5.5)*	918.8	967.7	*(5.1)*
Fuel oil 3.5% 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	592.7	620.0	*(4.4)*	593.8	642.5	*(7.6)*
Fuel oil 3.5% *(FOB Med (Italy))*	592.8	618.0	*(4.1)*	591.6	638.7	*(7.4)*
Naphtha Phy 1/2 *(CIF NEW/Basis ARA+ FOB Rotterdam)*	904.8	906.9	*(0.2)*	892.2	932.3	*(4.3)*
HS VGO(2) 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	774.8	790.8	*(2.0)*	768.2	805.4	*(4.6)*
	(in th. RR per tonne, except for figures in percent)					
Brent crude	25.79	24.99	*3.2*	24.44	24.83	*(1.6)*
Urals crude *(CIF Mediterranean)*	25.68	24.90	*3.1*	24.28	24.58	*(1.2)*
Urals crude *(CIF Rotterdam)*	25.56	24.81	*3.0*	24.17	24.49	*(1.3)*
	(in th. RR per tonne, except for figures in percent)					
Gasoil 0.1 1/2 *(CIF NWE/Basis ARA + FOB Rotterdam)*	30.49	31.49	*(3.2)*	29.05	30.09	*(3.5)*
Fuel oil 3.5% 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	19.44	19.85	*(2.1)*	18.78	19.98	*(6.0)*
Fuel oil 3.5% *(FOB Med (Italy))*	19.44	19.78	*(1.7)*	18.71	19.86	*(5.8)*
Naphtha Phy 1/2 *(CIF NEW/Basis ARA+ FOB Rotterdam)*	29.68	29.03	*2.2*	28.21	28.99	*(2.7)*
HS VGO(2) 1/2 *(CIF NWE/Basis ARA+ FOB Rotterdam)*	25.41	25.31	*0.4*	24.29	25.04	*(3.0)*
Russian market [1]	(in th. RR per tonne (incl.excise tax and VAT), except for figures in percent)					
Crude oil	13.23	12.33	*7.3*	12.54	12.34	*1.6*
Fuel oil	9.67	9.92	*(2.5)*	8.43	9.34	*(9.7)*

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 nor 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		Nine months ended	
	30 September 2013	30 September 2012	30 September 2013	30 September 2012
Ruble inflation, %	1.2	2.0	4.7	5.2
Period-end exchange rate (Ruble to US$)	32.35	30.92	32.35	30.92
Average exchange rate (Ruble to US$)	32.80	32.01	31.62	31.09

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:

	Three months ended		Change,	Nine months ended		Change,	Taxable
Tax	30 September 2013	30 September 2012	%	30 September 2013	30 September 2012	%	base
Income tax – maximum rate	20%	20%	-	20%	20%	-	Taxable income
Value Added Tax (VAT)	18%	18%	-	18%	18%	-	Sales from goods/services
Property tax – maximum rate	2.2%	2.2%	-	2.2%	2.2%	-	Taxable property
	(in RR per tonne, except for figures in percent)						
Mineral extraction tax, average rates[(1)]	5,631	5,147	*9.4*	5,282	5,086	*3.9*	Tonne produced (crude oil)
	(in US $ per tonne, except for figures in percent)						
Crude oil export duty, average rates	383.2	366.6	*4.5*	389.8	403.5	*(3.5)*	Tonne exported
Refined products export duty average rates:							Tonne exported
Gasoline, straight-run gasoline	344.9	329.9	*4.5*	350.8	363.1	*(3.3)*	
Light and middle distillates, gasoils, fuel oil *(mazut)*	252.9	241.9	*4.5*	257.3	266.2	*(3.4)*	

[(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.

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 nine months 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 three and nine months ended 30 September 2013 of RR 6.5 billion and RR 18.1 billion, respectively (in comparison to RR 5.5 billion and RR 16.1 billion, respectively, in the corresponding periods 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 three and nine months ended 30 September 2013 attributed to that production of RR 0.7 billion and RR 1.9 billion, respectively (in comparison to RR 0.3 billion and RR 0.8 billion, respectively, in the corresponding periods 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.

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

With effect from 1 April 2013 specific rates are calculated 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.

	Three months ended		Nine months ended	
(RR per tonne)	30 September 2013	30 September 2012	30 September 2013	30 September 2012
Gasoline:				
High octane gasoline below Euro-3,4,5	10,100	8,225	10,100	7,892
High octane gasoline Euro-3	9,750	7,882	9,750	7,549
High octane gasoline Euro-4	8,560	6,822	8,560	6,822
High octane gasoline Euro-5	5,143	5,143	5,143	6,822
Straight-run gasoline	10,229	7,824	10,229	7,824
Diesel fuel:				
Diesel below Euro- 3,4,5	5,860	4,300	5,860	4,165
Diesel Euro-3	5,860	4,300	5,860	3,976
Diesel Euro-4	4,934	3,562	4,934	3,562
Diesel Euro-5	4,334	2,962	4,334	3,362
Motor oils	7,509	6,072	7,509	6,072
Heating oil	5,860	-	5,860	-

Excise tax rates on refined products increased in the three and nine months ended 30 September 2013 by 36% and 37%, respectively, on average in comparison to corresponding periods of 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 unaudited consolidated interim condensed financial statements for the three and nine months ended 30 September 2013.

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.