



**LUKOIL**



## **Business overview**

## **Operational highlights**

We undertake exploration for, and production of, crude oil and natural gas in Russia and internationally. In Russia, our major oil producing subsidiaries are LUKOIL-Western Siberia, LUKOIL-Komi and

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

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







The following table summarizes key figures for our refining activities.

	<b>2<sup>nd</sup> quarter of</b>		<b>1<sup>st</sup> half of</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
	(thousand barrels per day)			
Refinery throughput at the Group refineries .....	1,322	1,254	1,298	1,237
- in Russia .....	797	827	803	818
- outside Russia <sup>(1)</sup> .....	525	427	495	419
Refinery throughput at third party refineries .....	6	17	6	17
<b>Total refinery throughput .....</b>	<b>1,328</b>	<b>1,271</b>	<b>1,304</b>	<b>1,254</b>

(thousands of tonnes BT(u)-6.95711(g)6.383.....7P6(





## **Main macroeconomic factors affecting our results of operations**

### **Changes in the international price of crude oil and refined products**

The price at which we sell crude oil and refined products is the primary driver of the Group's revenues. During the first half of 2016, the price for Brent crude oil fluctuated between \$26 and \$50 per barrel, reached its maximum of \$50.7 in the middle of June and minimum of \$25.9 in the beginning of January, and averaged 31.2% less than in the first half of 2015. Nevertheless, as a result of ruble devaluation, the prices expressed in rubles decreased less significantly.

Substantially all the crude oil the Group exports is Urals blend. The following tables show the average





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

### **Transportation of crude oil, natural gas and refined products in Russia**

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

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

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



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

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

	2 <sup>nd</sup> quarter of		1 <sup>st</sup> half of	
	2016	2015	2016	2015
	(millions of rubles)			
<b>Revenues</b>				
Sales (including excise and export tariffs) .....	1,338,959	1,476,966	2,516,633	2,917,271
<b>Costs and other deductions</b>				
Operating expenses .....	(113,709)	(105,828)	(226,953)	(211,509)
Cost of purchased crude oil, gas and products .....	(677,297)	(777,640)	(1,215,030)	(1,477,705)
Transportation expenses .....	(77,665)	(68,377)	(164,364)	(147,162)
Selling, general and administrative expenses .....	(45,302)	(40,028)	(93,125)	(81,213)

## Sales revenues

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

Sales volumes	2 <sup>nd</sup> quarter of		1 <sup>st</sup> half of	
	2016	2015	2016	2015
	(thousands of barrels)			
Crude oil				
Export and sales on international markets other than Customs Union .....	118,805	125,966	247,967	243,033
Export and sales to Customs Union .....	7,030	6,245	13,478	13,376

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

During the second quarter of 2016, our revenues decreased by 138 billion RUB q-39.3338(08(b)-6.3339(i)0.721099(1)0.7210

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

During the second quarter and the first half of 2016, our revenue from the wholesale of refined products on the domestic market decreased by 9.0%, or by 5 b





## Transportation expenses

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

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

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

The increase in domestic expenses for transportation of refined products by 6.8% against the second quarter of 2015 and by 6.2% against the first half of 2015 was triggered mainly by the increase in tariffs.

**Equity share in income of affiliates**

The Group has investments in equity method affiliates and corporate joint ventures. These companies are primarily engaged in crude oil exploration, production, marketing and distribution operations in the Russian Federation, crude oil production and marketing in Kazakhstan. Currently, our largest affiliates are Tengizchevroil, exploration and production company operating in Kazakhstan, Bashneft-Polus, an exploration and production company that develops the Trebs and Titov oilfields in Timan-Pechora, Russia, Shakh-Deniz Midstream and Caspian Pipeline Consortium, midstream companies in Azerbaijan and



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

#### **Foreign exchange loss**

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

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

During the first half of 2016, US dollar exchange rate to ruble decreased from 72.88 rubles per dollar at 1 January to 64.26 rubles per dollar at 30 June that resulted in a 74 billion RUB foreign exchange loss. During the first half of 2015, US dollar exchange r

## Liquidity and capital resources

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

### Operating activities

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

### Investing activities

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

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

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

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

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

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

<b>2<sup>nd</sup> quarter of</b>		<b>1<sup>st</sup> half of</b>	
<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>