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

The following report represents discussion and analysis of the financial condition of OAO LUKOIL as of March 31, 2014 and the results of it's operations for the first quarter of 2014, compared to the first quarter of 2013, as well as significant factors that may affect its future performance. It should be read in conjunction with our interim US GAAP consolidated financial statements and notes thereto.

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

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

Key financial and operational results

	3 months of 2014	3 months of 2013	Change, %
Sales (millions of US dollars)	35,681	33,770	5.7
Net income attributable to OAO LUKOIL (millions of US dollars)	1,733	2,581	(32.9)
Adjusted net income attributable to OAO LUKOIL (millions of US dollars)[(1)]	2,253	2,581	(12.7)
EBITDA (millions of US dollars)	3,995	4,775	(16.3)
Adjusted EBITDA (millions of US dollars)[(1)]	4,515	4,775	(5.4)
Taxes other than income taxes, excise and export tariffs (millions of US dollars)	(8,933)	(8,884)	0.6
Earning per share of common stock attributable to OAO LUKOIL (US dollars):			
Basic	2.30	3.42	(32.9)
Diluted	2.25	3.35	(32.7)
Hydrocarbon production by the Group including our share in equity affiliates (thousands of BOE)	199,296	197,614	0.9
Daily hydrocarbon production by the Group including our share in equity affiliates (thousands of BOE per day)	2,214	2,196	0.8
Crude oil and natural gas liquids produced by the Group including our share in equity affiliates (thousands of barrels)	169,674	166,615	1.8
Gas available for sale produced by the Group including our share in equity affiliates (millions of cubic meters)	5,034	5,267	(4.4)
Refined products produced by the Group including our share in equity affiliates (thousands of tonnes)	15,385	14,993	2.6

[(1)]Adjusted for loss on disposal of assets and dry whole related write-offs.

Our net income for the first quarter of 2014 was affected by a loss on the expected disposal of our share in Caspian Investment Resources Ltd. in amount of $358 million and write-offs related to our exploration projects in Africa in the total amount of $162 million. Our net income and EBITDA, adjusted for these non-recurring losses, decreased by $328 million, or by 12.7%, and by $260 million, or by 5.4%, respectively, as compared to the first quarter of 2013. Moreover, our results for the first quarter of 2014 were significantly affected by an increase in depreciation, depletion and amortization as a result of the growth of value of depreciable assets, a decrease in hydrocarbon prices and the ruble devaluation.

Business overview

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

OAO LUKOIL was established in accordance with Presidential Decree 1403, issued on November 17, 1992. Under this decree, on April 5, 1993, the Government of the Russian Federation transferred to the Company 51% of the voting shares of fifteen enterprises. Under Government Resolution 861 issued on September 1, 1995, a further nine enterprises were transferred to the Group during 1995. Since 1995, the Group has carried out a share exchange program to increase its shareholding in each of 24 founding subsidiaries to 100%. From formation, the Group has expanded substantially through consolidation of interests, acquisition of new companies and establishment of new businesses. Now LUKOIL is a global energy company operating through its subsidiaries in 39 countries on four continents.

LUKOIL is one of the world's largest energy companies in terms of hydrocarbon reserves that amounted to 17.4 billion BOE as of January 1, 2014 and comprised of 13.5 billion barrels of crude oil and 23.6 trillion cubic feet of gas.

Our operations are divided into four main business segments:

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

Each of our four main segments is dependent on the other, with a portion of the revenues of one segment being a part of the costs of the other. In particular, our Refining, Marketing and Distribution segment purchases crude oil from our Exploration and Production segment. As a result of certain factors considered in the "Domestic crude oil and refined products prices" section on page 9, benchmarking crude oil market prices in Russia cannot be determined with certainty. Therefore, the prices set for inter-segment purchases of crude oil reflect a combination of market factors, primarily international crude oil market prices, transportation costs, regional market conditions, the cost of crude oil refining and other factors. Accordingly, an analysis of either of these segments on a stand-alone basis could give a misleading impression of those segments' underlying financial position and results of operations. For this reason, we do not analyze either of our main segments separately in the discussion that follows. However, we present the financial data for each in Note 20 "Segment information" to our interim consolidated financial statements.

Recent developments

On April 15, 2014, a Group company entered into a contract with a Sinopec group company, to sell for $1.2 billion the Group's 50% interest in Caspian Investment Resources Ltd., an exploration and production company operating in Kazakhstan. The transaction's closing is subject to a number of conditions, including approval by the Kazakhstan state authorities, and is expected before the end of 2014.

In March 2014, the Group successfully launched the "Mishrif Early Oil" stage on the West Qurna-2 oilfield in Iraq and reached the planned daily production volume. The Group entered the project on December 12, 2009, when the Company, leading a consortium, was recognized as the winner in the bid to develop the West Qurna-2 project. On January 31, 2010, the service agreement for West Qurna-2 field development and production was signed. The agreement was ratified by the Ministry cabinet of the Iraq Republic. The parties of the project are Iraq's state-owned South Oil Company and a consortium of contractors, consisting of a Group company (75% interest) and state-owned North Oil Company (25% interest).

In December 2013, after approval by European regulatory authorities, the Group acquired the remaining 20% interest in the joint venture which operates the ISAB refinery complex (ISAB) for €446 million (approximately $613 million), increasing its stake in the joint venture from 80% to 100%. This transaction was exercised in line with the initial agreement on the establishment of the joint venture signed in 2008. This agreement gave the second investor, ERG S.p.A., a step-by-step put option to sell its share in the joint venture to the Group. The Group obtained control over ISAB in September 2012, when within this agreement, it acquired a 20% interest in the joint venture for €494 million (approximately $621 million) and increased its stake to 80%.

In April 2013, after approval by the Federal Anti-monopoly Service, in line with the strategy to increase crude oil production in Russia the Company purchased 100% of the shares of ZAO Samara-Nafta for $2.1 billion after final adjustments. ZAO Samara-Nafta is an exploration and production company operating in the Samara and Uljanovsk regions of the Russian Federation.

In April-May 2013, Group companies acquired the remaining 50% of the shares of ZAO Kama-oil, an exploration and production company operating in the Perm region of the Russian Federation, for $400 million increasing the Group's ownership to 100%. As a result of this acquisition, the Group obtained control over ZAO Kama-oil and consolidated it.

Operational highlights

Hydrocarbon production

We undertake exploration for, and production of, crude oil and natural gas in Russia and internationally. In Russia, our major oil producing subsidiaries are OOO LUKOIL-Western Siberia, OOO LUKOIL-Komi and OOO LUKOIL-PERM. Exploration and production outside of Russia is performed by our 100% subsidiary LUKOIL-Overseas Holding GmbH. This has stakes in PSA's and other projects in Kazakhstan, Azerbaijan, Uzbekistan, Romania, Iraq, Saudi Arabia, Egypt, Ghana, Cote d'Ivoire, Vietnam, Venezuela, and Norway.

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

	3 months of	
	2014	**2013**
Crude oil and natural gas liquids production[(1)]	(thousand BOE per day)	
Consolidated subsidiaries		
Western Siberia	980	1,009
Timan-Pechora	310	304
Ural region	309	291
Volga region	134	85
Other in Russia	37	37
Total in Russia	1,770	1,726
Total outside Russia	63	68
Total consolidated subsidiaries	**1,833**	**1,794**
Our share in equity affiliates		
in Russia	8	8
outside Russia	44	50
Total share in equity affiliates	**52**	**58**
Total crude oil and natural gas liquids	**1,885**	**1,852**
Natural gas production available for sale[(2)]		
Consolidated subsidiaries		
Western Siberia	189	194
Timan-Pechora	12	13
Ural region	20	18
Volga region	6	7
Other in Russia	0	0
Total in Russia	227	232
Total outside Russia	93	103
Total consolidated subsidiaries	**320**	**335**
Share in equity affiliates		
in Russia	1	1
outside Russia	8	8
Total share in production of equity affiliates	**9**	**9**
Total natural gas available for sale	**329**	**344**
Total daily hydrocarbon production	**2,214**	**2,196**
	(US dollar per BOE)	
Hydrocarbon extraction expenses	5.23	5.29
- in Russia	5.26	5.35
- outside Russia	4.97	4.67
	(millions of US dollars)	
Hydrocarbon extraction expenses	1,011	1,009
- in Russia	942	938
- outside Russia	69	71
Exploration expenses	205	63
- in Russia	85	43
- outside Russia	120	20
Mineral extraction tax	3,099	3,013
- in Russia	3,081	2,996
- outside Russia	18	17

(1) Natural gas liquids produced at the Group gas processing plants.
(2) Including petroleum gas sold to third parties.

Crude oil production. In the first quarter of 2014, our crude oil production (including the Company's share in equity affiliates) increased by 1.9%, compared to the first quarter of 2013, and amounted to 22.5 million tonnes, or 166.0 million barrels, of crude oil. The main oil producing region for the Company is Western Siberia where we produced 53.3% of our crude oil in the first quarter of 2014 (56.1% in the first quarter of 2013).

The following table represents our crude oil production in the first quarter of 2014 and 2013 by major regions.

(thousands of tonnes)	3 months of 2014	Change from 2013 Total, %	Change in structure	Organic change	3 months of 2013
Western Siberia	11,675	(2.8)	–	(339)	12,014
Timan-Pechora	3,850	1.9	–	72	3,778
Ural region	3,568	5.4	34	148	3,386
Volga region	1,618	65.4	657	(17)	978
Other in Russia	457	(1.1)	–	(5)	462
Crude oil produced in Russia	21,168	2.7	691	(141)	20,618
Crude oil produced internationally	743	(7.1)		(57)	800
Total crude oil produced by consolidated subsidiaries	**21,911**	**2.3**	**691**	**(198)**	**21,418**
Our share in crude oil produced by equity affiliates:					
in Russia	93	(2.1)	(17)	15	95
outside Russia	509	(11.8)	–	(68)	577
Total crude oil produced	**22,513**	**1.9**	**674**	**(251)**	**22,090**

The decrease in oil production in Western Siberia was due to natural depletion of reserves and an increase in water cut. Nevertheless, this was compensated for by the acquisitions of new upstream properties, development of greenfields, successful employment of new technologies and an increase in drilling footage. As a result, our daily domestic crude oil and natural gas liquids production volumes increased by 2.5%, compared to the first quarter of 2013.

The structural increase in our domestic production was a result of the acquisition of a 100.0% share of ZAO Samara-Nafta and an increase in the Group's ownership in ZAO Kama-oil from 50.0% to 100.0% during the second quarter of 2013. At the same time, the transfer of ZAO Kama-oil from affiliates to subsidiaries led to some structural decrease in the affiliates' production in Russia.

On March 28, 2014, the Group commenced crude oil production on the West Qurna-2 oil field in Iraq and achieved a level of 120 thousand barrels per day. According to the Service contract for development and production on this oilfield, costs are compensated if this level of production is achieved during any 90 days within a 120-day period. Therefore the recognition of revenue and the compensation of costs will start only after the fulfillment of this term, which will be no earlier than in the second quarter of 2014. Accordingly, in the first quarter of 2014, the Group neither recognized revenue from the sale of the crude oil produced from the oilfield, nor included the volume of this crude oil in the total amount of production by the Group.

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

	3 months of			
	2014		2013	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Purchases in Russia	2,133	291	205	28
Purchases for trading internationally	23,390	3,191	3,452	471
Purchases for refining internationally	16,778	2,289	15,394	2,100
Total crude oil purchased	**42,301**	**5,771**	**19,051**	**2,599**

A significant part of our crude oil purchases is for processing. Compared to the first quarter of 2013, our purchases for processing at international refineries increased by 9.0%. Moreover, in the first quarter of 2014, our purchases for trading increased almost seven-fold against the background of abnormally low level of purchases in the first quarter of 2013.

Production of gas and natural gas liquids. During the first quarter of 2014, we produced 5,034 million cubic meters (29.6 million BOE) of gas available for sale (including our share in equity affiliates), that is 4.4% less than in the first quarter of 2013.

Our major gas production field is the Nakhodkinskoe field, where we produced 2,055 million cubic meters of natural gas in the first quarter of 2014 (2,056 million cubic meters in the first quarter of 2013). Our international gas production decreased by 9.5%, compared to the first quarter of 2013.

In the first quarter of 2014, the output of natural gas liquids at the Group gas processing plants in Western Siberia, Ural and Volgograd regions of Russia was 3.7 million BOE, compared to 3.5 million BOE in the first quarter of 2013.

Refining, marketing and trading

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

In December 2013, the Group obtained full control over ISAB after acquisition of the remaining 20% share. Initially, in December 2008, the Group acquired a 49% interest in ISAB, then increased its interest to 60% in April 2011 and to 80% in September 2012, when control over the refinery was obtained and ISAB became our consolidated subsidiary, rather than an equity affiliate.

Compared to the first quarter of 2013, the total volume of refined products produced by the Group (including our share in production at the Zeeland refinery) increased by 2.6%. Production volumes at our Russian refineries increased by 1.8%, largely due to an increase of production volumes at our refinery in Perm region against the background of relatively low production volumes in the first quarter of 2013. Production at our international refineries increased by 9.0% as a result of the acquisition of the full stake in ISAB in December 2013 and low production volumes in the first quarter of 2013 due to the overhauls. At the same time, our share of production at Zeeland refinery decreased by 7.7% due to lower refining margins.

Along with our own production of refined products we can refine crude oil at third party refineries depending on market conditions and other factors. In the periods considered, we processed our crude oil at third party refineries in Belarus and Kazakhstan. At the same time, the volume of processing of our crude oil at the third party refineries in Belarus in the first quarter of 2014 was significantly lower compared to the first quarter of 2013.

During the first quarter of 2014, political and economic uncertainty in Ukraine has been increasing. The Group owns downstream assets in Ukraine, consisting of a network of 238 gas stations, a petrochemical plant, lubricants distributors, and a jet fuel supplier. Though the Group's assets and operations in Ukraine are not material (in the first quarter of 2014, revenues that were derived from our operations in Ukraine comprised less than 1% of our total revenues), the Group monitors the situation and assesses the risks associated with its operations in Ukraine. Management believes that there are no potential losses that can be identified and reasonably estimated with respect to situation in Ukraine at present.

The following table summarizes key figures for our refining activities.

	3 months of	
	2014	**2013**
	(thousand barrels per day)	
Refinery throughput at the Group refineries	1,224	1,172
- in Russia	921	903
- outside Russia[1]	303	269
Refinery throughput at Zeeland refinery[1]	87	94
Refinery throughput at third party refineries	16	43
Total refinery throughput	**1,327**	**1,309**
	(thousands of tonnes)	
Refined products produced at the Group refineries in Russia	10,804	10,612
Production of the Group refineries outside Russia	3,516	3,227
Production of Zeeland refinery	1,065	1,154
Refined products produced by the Group including our share in Zeeland refinery	**15,385**	**14,993**
Refined products produced at third party refineries	185	494
Total refined products produced	**15,570**	**15,487**
	(millions of US dollars)	
Refining expenses at the Group refineries	480	508
- in Russia	230	259
- outside Russia	250	249
Refining expenses at Zeeland refinery	57	57
Refining expenses at third party refineries	7	20
Capital expenditures	399	579
- in Russia	201	434
- outside Russia	198	145

[1] Including refined product processed.

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

The Group retails its refined products in 27 countries through nearly 5.6 thousand petrol stations (including franchisees). Most of the stations operate under the LUKOIL brand.

The table below summarizes figures for our trading activities.

	3 months of	
	2014	**2013**
	(thousands of tonnes)	
Retail sales	3,638	3,546
Wholesale sales	24,535	23,872
Total refined products sales	**28,173**	**27,418**
Refined products purchased in Russia	437	630
Refined products purchased internationally	14,678	13,540
Total refined products purchased	**15,115**	**14,170**

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

	3 months of			
	2014		**2013**	
	(thousands of barrels)	(thousands of tonnes)	(thousands of barrels)	(thousands of tonnes)
Exports of crude oil using Transneft export routes	41,539	5,667	46,678	6,368
Exports of crude oil bypassing Transneft	12,080	1,648	9,813	1,339
Total crude oil exports	**53,619**	**7,315**	**56,491**	**7,707**
Exports of refined products		**6,324**		**5,967**

During the first quarter of 2014, the volume of our crude oil export from Russia decreased by 5.1%, compared to the first quarter of 2013, and we exported 34.6% of our total domestic crude oil production (37.4% – during the first quarter of 2013). The decrease of crude oil export was a result of higher sales in Russia and increased throughput at our domestic refineries.

All the volume of crude oil exported that bypassed Transneft in the periods considered was routed through our own export infrastructure.

In the first quarter of 2014, the Company exported 300 thousand tonnes of light crude oil through the Eastern Siberia – Pacific Ocean pipeline. This allowed us to preserve the premium quality of crude oil and thus increased the efficiency of export, compared to export to traditional Western markets.

During the first quarter of 2014, the volume of our exported refined products from Russia increased by 6.0%, compared to the first quarter of 2013. Primarily, we export from Russia diesel fuel, fuel oil and gasoil. These products accounted for approximately 88% of our exported refined products volumes.

During the first quarter of 2014, our revenue from export of crude oil and refined products from Russia both to Group companies and third parties amounted to $5,253 million and $4,720 million, respectively ($5,592 million for crude oil and $4,598 million for refined products in the first quarter of 2013).

Main macroeconomic factors affecting our results of operations

Changes in the price of crude oil and refined products

The price at which we sell crude oil and refined products is the primary driver of the Group's revenues. During the first quarter of 2014, the Brent crude oil price fluctuated between $105 and $111 per barrel and reached its peak of $111.31 in early March.

Substantially all the crude oil the Group exports is Urals blend. The following table shows the average crude oil and refined product prices in the first quarter of 2014 and 2013.

	3 months of		**Change, %**
	2014	**2013**	
	(in US dollars per barrel, except for figures in percent)		
Brent crude	108.21	112.51	(3.8)
Urals crude (CIF Mediterranean) [(1)]	106.81	111.06	(3.8)
Urals crude (CIF Rotterdam) [(1)]	106.24	110.53	(3.9)
	(in US dollars per metric tonne, except for figures in percent)		
Fuel oil 3.5% (FOB Rotterdam)	571.37	613.02	(6.8)
Diesel fuel 10 ppm (FOB Rotterdam)	924.69	974.06	(5.1)
High-octane gasoline (FOB Rotterdam)	959.20	1,040.53	(7.8)

Source: Platts.

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

Domestic crude oil and refined products prices

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

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

The table below represents average domestic wholesale prices of refined products in the first quarter of 2014 and 2013.

	3 months of		**Change, %**
	2014	**2013**	
	(in US dollars per metric tonne, except for figures in percent)		
Fuel oil	257.56	363.62	(29.2)
Diesel fuel	806.79	907.10	(11.1)
High-octane gasoline (Regular)	809.35	822.26	(1.6)
High-octane gasoline (Premium)	842.52	865.94	(2.7)

Source: InfoTEK (excluding VAT).

Changes in the US dollar-ruble exchange rate and inflation

A substantial part of our revenue is either denominated in US dollars or is correlated to some extent with US dollar crude oil prices, while most of our costs in the Russian Federation are settled in Russian rubles. Therefore, ruble inflation and movements of exchange rates can significantly affect the results of our operations. In particular, an appreciation of the ruble against the US dollar generally causes our costs to increase in US dollar terms, and vice versa. The appreciation of the purchasing power of the US dollar in the Russian Federation calculated on the basis of the ruble-dollar exchange rates and the level of inflation in Russia was 7.4% in the first quarter of 2014, compared to the first quarter of 2013.

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

	3 months of	
	2014	**2013**
Ruble inflation (CPI), %	2.3	1.9
Average exchange rate for the period (ruble to US dollar)	34.96	30.41
Exchange rate at the end of the period (ruble to US dollar)	35.69	31.08

Tax burden

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

		3 months of		Change, %
		2014	**2013**	
Export tariffs on crude oil	\$/tonne	390.71	406.61	(3.9)
Export tariffs on refined products				
Middle distillates (jet fuel), liquid fuels (fuel oil) and gasoils	\$/tonne	257.83	268.37	(3.9)
Light distillates	\$/tonne	351.60	365.96	(3.9)
Diesel fuel	\$/tonne	255.27	268.37	(4.9)
Mineral extraction tax				
Crude oil	RUR/tonne	6,078.49	5,255.83	15.7
Natural gas	RUR/1,000 m^3	471.00	265.00	77.7

Average tax rates set in rubles and translated at the average exchange rates are as follows:

		3 months of		Change, %
		2014	**2013**	
Mineral extraction tax				
Crude oil	\$/tonne	173.87	172.81	0.6
Natural gas	\$/1,000 m^3	13.47	8.71	54.6

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

Crude oil extraction tax rate is determined by adjusting the base rate depending on the international market price of Urals blend and the ruble 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 (or $0.25 per barrel extracted using a conversion factor of 7.33) above the base rate.

During the first quarter of 2014, the base rate was 493 rubles per metric tonne extracted (470 rubles in the first quarter of 2013).

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

The Group produces crude oil in the Caspian Sea and benefits from the application of a zero extraction tax rate. We also produce extra-heavy oil in Timan-Pechora.

Natural gas extraction tax rate. The mineral extraction tax on natural gas produced by independent producers in Russia is calculated using a flat rate. For the first quarter of 2014, the rate was set at 471 rubles per thousand cubic meters (265 rubles per thousand cubic meters in the first quarter of 2013).

Crude oil export duty rate is calculated on a progressive scale. The rate is zero when the average Urals blend international market price is less than or equal to approximately $15.00 per barrel ($109.50 per metric tonne). If the Urals blend price is between $15.00 and $20.00 per barrel ($146.00 per metric tonne), each $1.00 per barrel increase in the Urals blend price over $15.00 results in an increase of the crude oil export duty rate by $0.35 per barrel exported. If the Urals blend price is between $20.00 and $25.00 per barrel ($182.50 per metric tonne), each $1.00 per barrel increase in the Urals blend price over $20.00 results in an increase of the crude oil export duty rate by $0.45 per barrel exported. Each $1.00 per barrel increase in the Urals blend price over $25.00 per barrel results in an increase of the crude oil export duty rate no more than by $0.65 per barrel exported. Starting from October 1, 2011 to December 31, 2013, the maximum increase of export duty rate was $0.60 per barrel for each $1.00 per barrel increase in the Urals blend price. Starting from January 1, 2014 to December 31, 2014, the maximum increase of export duty rate is $0.59 per barrel for each $1.00 per barrel increase in the Urals blend price.

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

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

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

	From January 1, 2014 to December 31, 2014	**Prior to January 1, 2014**
Multiplier for:		
Light distillates (except for gasolines), middle distillates (jet fuel), gasoils, liquid fuels (fuel oil), motor and other oils, other products	0.660	0.660
Diesel fuel	0.650	0.660
Gasolines	0.900	0.900

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

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

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

Excise rates on refined products in Russia are tied to the ecological class of fuel. Excise tax rates for the first quarter of 2014 and 2013 are listed below:

		3 months of		**Change, %**
		2014	**2013**	
Gasoline				
Below Euro-3	RUR/tonne	11,110.00	10,100.00	10.0
Euro-3	RUR/tonne	10,725.00	9,750.00	10.0
Euro-4	RUR/tonne	9,916.00	8,560.00	15.8
Euro-5	RUR/tonne	6,450.00	5,143.00	25.4
Diesel fuel				
Below Euro-3	RUR/tonne	6,446.00	5,860.00	10.0
Euro-3	RUR/tonne	6,446.00	5,860.00	10.0
Euro-4	RUR/tonne	5,427.00	4,934.00	10.0
Euro-5	RUR/tonne	4,767.00	4,334.00	10.0
Motor oils	RUR/tonne	8,260.00	7,509.00	10.0
Straight-run gasoline	RUR/tonne	11,252.00	10,229.00	10.0

		3 months of 2014	2013	Change, %
Gasoline				
Below Euro-3	$/tonne	317.79	332.08	(4.3)
Euro-3	$/tonne	306.78	320.57	(4.3)
Euro-4	$/tonne	283.64	281.45	0.8
Euro-5	$/tonne	184.50	169.10	9.1
Diesel fuel				
Below Euro-3	$/tonne	184.38	192.67	(4.3)
Euro-3	$/tonne	184.38	192.67	(4.3)
Euro-4	$/tonne	155.24	162.23	(4.3)
Euro-5	$/tonne	136.36	142.50	(4.3)
Motor oils	$/tonne	236.27	246.89	(4.3)
Straight-run gasoline	$/tonne	321.86	336.32	(4.3)

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

Until January 1, 2012, there were no provisions in the taxation legislation of the Russian Federation to permit the Group to reduce taxable profits of a Group company by offsetting tax losses of another Group company against such profits. Tax losses could be fully or partially used to offset taxable profits in the same company in any of the ten years following the year of loss.

Starting from January 1, 2012, if certain conditions are met, taxpayers are able to pay income tax as a consolidated taxpayers' group ("CTG"). This allows taxpayers to offset taxable losses generated by certain participants of a CTG against taxable profits of other participants of the CTG. Certain Group companies met the legislative requirements and pay income tax as a CTG starting from the first quarter of 2012.

Losses generated by a taxpayer before joining a CTG are not available for offset against taxable profits of other participants of the CTG. However, if a taxpayer leaves a CTG, such losses again become available for offset against future profits generated by the same taxpayer. The expiration period of the losses is extended for any time spent within a CTG when the losses were unavailable for use.

Transportation of crude oil and refined products in Russia

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

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

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

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

Three months ended March 31, 2014, compared to three months ended March 31, 2013

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

	3 months of	
	2014	**2013**
	(millions of US dollars)	
Revenues		
Sales (including excise and export tariffs)	35,681	33,770
Costs and other deductions		
Operating expenses	(2,309)	(2,450)
Cost of purchased crude oil, gas and products	(17,243)	(15,103)
Transportation expenses	(1,553)	(1,650)
Selling, general and administrative expenses	(856)	(866)
Depreciation, depletion and amortization	(1,512)	(1,369)
Taxes other than income taxes	(3,446)	(3,383)
Excise and export tariffs	(5,487)	(5,501)
Exploration expense	(205)	(63)
Loss on disposals and impairments of assets	(415)	(7)
Income from operating activities	**2,655**	**3,378**
Interest expense	(140)	(97)
Interest and dividend income	57	61
Equity share in income of affiliates	182	158
Currency translation loss	(270)	(139)
Other non-operating (expense) income	(80)	13
Income before income taxes	**2,404**	**3,374**
Current income taxes	(805)	(646)
Deferred income taxes	138	(143)
Total income tax expense	**(667)**	**(789)**
Net income	**1,737**	**2,585**
Net income attributable to non-controlling interests	(4)	(4)
Net income attributable to OAO LUKOIL	**1,733**	**2,581**
Earning per share of common stock attributable to OAO LUKOIL (in US dollars):		
Basic	2.30	3.42
Diluted	2.25	3.35

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

Sales revenues

Sales breakdown	3 months of	
	2014	2013
	(millions of US dollars)	
Crude oil		
Export and sales on international markets other than Custom Union countries	6,958	5,099
Export and sales to Custom Union countries	536	385
Domestic sales	984	538
	8,478	**6,022**
Refined products		
Export and sales on international markets		
Wholesale	18,853	18,936
Retail	2,466	2,443
Domestic sales		
Wholesale	1,612	1,921
Retail	2,092	2,196
	25,023	**25,496**
Petrochemicals		
Export and sales on international markets	255	223
Domestic sales	132	246
	387	**469**
Gas and gas products		
Export and sales on international markets	553	557
Domestic sales	298	286
	851	**843**
Sales of energy and related services	**501**	**489**
Other		
Sales on international markets	236	260
Domestic sales	205	191
	441	**451**
Total sales	**35,681**	**33,770**

Sales volumes	3 months of	
	2014	2013
Crude oil	(thousands of barrels)	
Export and sales on international markets other than Custom Union countries	65,061	46,194
Export and sales to Custom Union countries	10,511	7,528
Domestic sales	20,568	11,076
	96,140	**64,798**
Crude oil	(thousands of tonnes)	
Export and sales on international markets other than Custom Union countries	8,876	6,302
Export and sales to Custom Union countries	1,434	1,027
Domestic sales	2,806	1,511
	13,116	**8,840**
Refined products	(thousands of tonnes)	
Export and sales on international markets		
Wholesale	22,138	21,243
Retail	1,485	1,469
Domestic sales		
Wholesale	2,397	2,629
Retail	2,153	2,077
	28,173	**27,418**
Total sales volume of crude oil and refined products	**41,289**	**36,258**

Realized average sales prices		**3 months of**	
		2014	**2013**
Average realized price international			
Oil (excluding Custom Union)	($/barrel)	106.94	110.37
Oil (Custom Union)	($/barrel)	51.00	51.20
Refined products			
Wholesale	($/tonne)	851.59	891.35
Retail	($/tonne)	1,659.93	1,663.53
Average realized price within Russia			
Oil	($/barrel)	47.83	48.56
Refined products			
Wholesale	($/tonne)	672.75	730.55
Retail	($/tonne)	971.77	1,057.54

During the first quarter of 2014, our revenues increased by $1,911 million, or by 5.7%, compared to the first quarter of 2013. Our revenues from crude oil sales increased by $2,456 million, or by 40.8%. Our revenues from sales of refined products decreased by $473 million, or by 1.9%.

The changes in ruble-nominated revenues against the first quarter of 2013 were significantly affected by the nominal ruble devaluation by 15.0%.

Sales of crude oil

Compared to the first quarter of 2013, our international sales volumes increased by 2,981 thousand tonnes, or by 40.7%, due to significantly increased volumes of trading, while our realized crude oil prices decreased by 3.1%. As a result, our international sales revenue increased by 36.7%, or by $2,010 million. Moreover, domestic sales volumes nearly doubled, compared to the first quarter of 2013, due to continuing increase of domestic demand and increase of crude oil production in Russia. As a result, in the first quarter of 2014, our domestic sales revenue increased by 82.9%, or by $446 million.

During the first quarter of 2014, our revenue from crude oil export from Russia both to the Group companies and third parties amounted to $5,253 million.

Sales of refined products

Compared to the first quarter of 2013, our revenue from the wholesale of refined products outside of Russia decreased by $83 million, or by 0.4%. The 4.2% increase in sales volumes was outweighed by the 4.5% decrease in sales prices.

Compared to the first quarter of 2013, neither our retail volumes nor retail prices outside of Russia changed significantly, therefore, our international retail sales revenue remained on the level of the first quarter of 2013.

In the first quarter of 2014, our revenue from the wholesale of refined products on the domestic market decreased by $309 million, or by 16.1%. The effect of the decrease in sales volumes by 232 thousand tonnes, or by 8.8%, was amplified by the decrease in sales price by 7.9% caused largely by the ruble devaluation.

Our revenue from retail sales in Russia decreased by $104 million, or by 4.7%, in the first quarter of 2014. Although retail sales volumes increased by 3.7%, our average retail prices in Russia decreased by 8.1% due to the ruble devaluation.

In the first quarter of 2014, our revenue from export of refined products from Russia both to Group companies and third parties amounted to $4,720 million.

Sales of petrochemical products

Our revenue from sales of petrochemical products decreased by $82 million, or by 17.5%, in the first quarter of 2014. Domestic sales volumes decreased by 69 thousand tonnes, or by 36.5%, as a result of cease of production at our plant in Stavropol region of Russia as a consequence of a fire at the plant in the end of February 2014. At the same time, in the first quarter of 2014, our international sales volumes increased by 10.6%.

Sales of gas and gas products

Sales of gas and gas refined products increased by $8 million, or by 0.9%, in the first quarter of 2014, compared to the first quarter of 2013.

Gas products wholesales revenue increased by $10 million, or by 3.5%, in the first quarter of 2014. Average realized wholesale prices increased by 2.7% and gas products wholesale volumes increased by 0.6%.

In the first quarter of 2014, retail gas products revenue increased by $8 million, or by 5.8%, compared to the first quarter of 2013.

Natural gas sales revenue decreased by $10 million, or by 3.1%, in the first quarter of 2014. Domestic sales volumes and prices did not change compared to the first quarter of 2013. Outside of Russia, the decreased sales volumes were partially compensated by the increase in average realized prices.

Sales of energy and related services

Our revenue from sales of electricity, heat and related services increased by $12 million, or by 2.5%, in the first quarter of 2014. The increase of sales volumes that resulted from commissioning of two combined cycle gas turbines with a combined capacity of 235 MW in Astrakhan, Russia in mid-2013 and consequent increase in volumes of power generation, compared to the first quarter of 2013, was partially offset by the effect of ruble devaluation.

Sales of other products

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

In the first quarter of 2014, other sales decreased by $10 million, or by 2.2%.

Operating expenses

Operating expenses include the following:

	3 months of	
	2014	**2013**
	(millions of US dollars)	
Hydrocarbon extraction expenses	1,011	1,009
Own refining expenses	480	508
Refining expenses at third parties and affiliated refineries	64	77
Cost of processing operations at ISAB	–	44
Expenses for crude oil transportation to refineries	273	338
Power generation and distribution expenses	190	192
Petrochemical expenses	66	79
Other operating expenses	225	203
Total operating expenses	**2,309**	**2,450**

The method of allocation of operating expenses above differs from the approach used in preparing the data for Note 20 “Segment information” to our interim consolidated financial statements. Expenditures in the segment reporting are grouped depending on the segment to which a particular company belongs. Operating expenses for the purposes of this analysis are grouped based on the nature of the costs incurred.

The changes in ruble-nominated operating expenses against the first quarter of 2013 were significantly affected by the nominal ruble devaluation by 15.0%.

Our operating expenses decreased by $141 million, or by 5.8%, compared to the first quarter of 2013.

Hydrocarbon extraction expenses

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

In the first quarter of 2014, our extraction expenses remained on the level of the first quarter of 2013. The increase in energy costs triggered by the tariffs growth, repairs, artificial stimulation of reservoirs and maintenance costs was compensated by the ruble devaluation. In the first quarter of 2014, approximately $24 million of the extraction expenses refer to ZAO Samara-Nafta, acquired in April 2013. Our average hydrocarbon extraction cost decreased from $5.29 per BOE to $5.23 per BOE, or by 1.1%, in the first quarter of 2014.

Own refining expense

Our own refining expenses decreased by $28 million, or by 5.5%, compared to the first quarter of 2013.

In the first quarter of 2014, refining expenses at our domestic refineries decreased by 11.2%, or by $29 million. The effect of ruble devaluation, lower consumption and cost of additives and lower expenses for overhauls were partly outweighed by the effect of increased production volumes.

Refining expenses at our international refineries did not change significantly compared to the first quarter of 2013. Despite sizeable increase in production volumes at ISAB against the background of low volumes of refining in the first quarter of 2013 due to overhauls, operating expenses at our Italian refinery decreased in the first quarter of 2014 as a result of the drop in electricity tariffs in Sicily.

Refining expenses at third party and affiliated refineries

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

In the first quarter of 2014, refining expenses at third party and affiliated refineries decreased by 16.9%, or by $13 million, as a result of significantly lower volumes of crude oil processing at third party refineries in Belarus.

Expenses for crude oil transportation to refineries

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

In the first quarter of 2014, our expenses for crude oil transportation to refineries decreased by $65 million, or by 19.2%, due to significantly lower volumes of crude oil processing at third party refineries in Belarus, compared to the first quarter of 2013, and the effect of ruble devaluation.

Petrochemical expenses

In the first quarter of 2014, our petrochemical operating expenses decreased by $13 million, or by 16.5%, compared to the first quarter of 2013. This was mainly due to the cease of production at our petrochemical plant in Stavropol region of Russia since the end of February 2014 as a consequence of a fire and dormant time at our petrochemical plant in Ukraine since February 2014 due to unfavorable economic and political environment.

Power generation and distribution expenses

In the first quarter of 2014, power generation and distribution remained flat compared to the respective period of 2013. The effect of ruble devaluation outweighed the increase of expenses that resulted from the commissioning of new combined cycle gas turbines with a combined capacity of 235 MW in Astrakhan, Russia in the middle of 2013.

Other operating expenses

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

In the first quarter of 2014, other operating expenses increased by $22 million, or by 10.8%.

Cost of purchased crude oil, gas and products

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

Cost of purchased crude oil, gas and products increased by $2,140 million, or by 14.2%, in the first quarter of 2014. The increase in crude oil trading volumes was partially offset by the decrease in international crude oil and refined products prices.

In the first quarter of 2014, we recognized a $73 million net gain from hedging, compared to a $65 million net loss in the first quarter of 2013.

Transportation expenses

Our transportation expenses decreased by $97 million, or by 5.9%, compared to the first quarter of 2013, largely due to the ruble devaluation.

Our actual transportation expenses related to crude oil and refined products deliveries to various export destinations, weighted by volumes transported, changed to the first quarter of 2013 as follows: crude oil pipeline tariffs decreased by 8.6%, railway tariffs for refined products transportation decreased by 15.3%, crude oil freight rates increased by 14.0%, and refined products freight rates decreased by 10.0%.

Selling, general and administrative expenses

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

Our selling, general and administrative expenses decreased by $10 million, or by 1.2%, in the first quarter of 2014.

Depreciation, depletion and amortization

Our depreciation, depletion and amortization expenses increased by $143 million, or by 10.4%, compared to the first quarter of 2013. This was a result of the Company's capital expenditures and the corresponding increase in value of depreciable assets. Moreover, the acquisition of ZAO Samara-Nafta contributed to this increase.

Equity share in income of affiliates

The Group has investments in equity method affiliates and corporate joint ventures. These companies are primarily engaged in crude oil exploration, production, marketing and distribution operations in the Russian Federation, crude oil production and marketing in Kazakhstan and refining operations in the Netherlands. Our largest affiliates are Turgai Petroleum and Tengizchevroil, exploration and production companies operating in Kazakhstan, and Zeeland Refinery in the Netherlands.

Our share in income of affiliates increased by $24 million, or by 15.2%, compared to the first quarter of 2013.

Taxes other than income taxes

	3 months of	
	2014	**2013**
	(millions of US dollars)	
In Russia		
Mineral extraction taxes	3,081	2,996
Social security taxes and contributions	145	166
Property tax	124	128
Other taxes	21	19
Total in Russia	**3,371**	**3,309**
International		
Mineral extraction taxes	18	17
Social security taxes and contributions	31	30
Property tax	9	8
Other taxes	17	19
Total internationally	**75**	**74**
Total	**3,446**	**3,383**

In the first quarter of 2014, taxes other than income taxes increased by 1.9%, or by $63 million, following the increase in mineral extraction tax expenses, compared to the first quarter of 2013. The effects of growth of mineral extraction tax rate and the increase in domestic crude oil production were partially offset by the increase in the amount of mineral extraction tax incentive.

In the first quarter of 2014, application of the reduced rate for crude oil produced from depleted oilfields and the zero rate for crude oil produced from oilfields with extra heavy crude oil and from greenfields led to $584 million mineral extraction tax reduction ($468 million in the first quarter of 2013). Of this amount, $61 million refer to the production from the Yu. Korchagin field in the Caspian Sea ($57 million in the first quarter of 2013).

Excise and export tariffs

	3 months of	
	2014	**2013**
	(millions of US dollars)	
In Russia		
Excise tax on refined products	417	436
Crude oil export tariffs	2,548	2,484
Refined products export tariffs	1,626	1,615
Total in Russia	**4,591**	**4,535**
International		
Excise tax on refined products	821	822
Crude oil export tariffs	52	62
Refined products export tariffs	23	82
Total internationally	**896**	**966**
Total	**5,487**	**5,501**

In the first quarter of 2014, our export tariffs didn’t change compared to the first quarter of the previous year. Compared to the first quarter of 2013, the volumes of crude oil export beyond the Customs Union didn’t change significantly, while refined products export volumes increased by 6.0%. At the same time, this was outweighed by the decrease of export tariffs rates. Export tariff savings on crude oil produced from the Yu. Korchagin field in the Caspian Sea did not change compared to the respective period of 2013 and amounted to $70 million.

Exploration expenses

In the first quarter of 2014, our exploration expenses increased by $142 million. Dry hole costs amounted to $95 million, compared to $1 million in the first quarter of 2013.

In the first quarter of 2014, we charged to expense the costs of dry exploratory well in Cote d’Ivoire in the amount of $95 million.

Loss on disposals and impairments of assets

In April 2014, the Group entered into an agreement to sell its 50% share in Caspian Investment Resources Ltd. The loss on expected disposal of this share was estimated at $358 million. For more details on this agreement, refer to page 2.

Moreover, in the first quarter of 2014, the Group wrote off signing bonuses related to projects in Sierra Leone and Cote d’Ivoire in the total amount of $67 million.

Income taxes

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

Our total income tax expense decreased by $122 million, or by 15.5%, compared to the first quarter of 2013. At the same time, our income before income tax decreased by $970 million, or by 28.7%.

In the first quarter of 2014, our effective income tax rate was 27.7%, compared to 23.4% in the first quarter of 2013. The higher level of the effective income tax rate in the first quarter of 2014 was mostly due to non-deductible loss on disposal and dry whole and signing bonuses write-offs.

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

	3 months of	
	2014	**2013**
	(millions of US dollars)	
Net income	**1,733**	**2,581**
Add back:		
Income tax expense	667	789
Depreciation and amortization	1,512	1,369
Interest expense	140	97
Interest and dividend income	(57)	(61)
EBITDA	**3,995**	**4,775**
Loss on disposal of assets and dry hole related write-offs	520	–
Adjusted EBITDA	**4,515**	**4,775**

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

Liquidity and capital resources

	3 months of 2014	2013
	(millions of US dollars)	
Net cash provided by operating activities	3,292	3,842
Net cash used in investing activities	(3,200)	(4,007)
Net cash provided by (used in) financing activities	970	(41)

Operating activities

Our primary source of cash flow is funds generated from our operations. In the first quarter of 2014, cash generated from operations decreased by 14.3%, compared to the respective period of the prior year, and amounted to $3,292 million.

Investing activities

In the first quarter of 2014, the amount of cash used in investing activities decreased by 20.1% largely against the background of significant spending on the acquisition of licenses in the first quarter of 2013.

Our capital expenditures, including non-cash transactions, amounted to $3,232 million, which was 3.4% lower than in the first quarter of 2013.

	3 months of 2014	2013
	(millions of US dollars)	
Capital expenditures, including non-cash transactions and prepayments		
Exploration and production		
Russia	1,973	1,874
International	752	663
Total exploration and production	2,725	2,537
Refining, marketing and distribution		
Russia	227	471
International	220	159
Total refining, marketing and distribution	447	630
Chemicals		
Russia	32	3
International	–	–
Total chemicals	32	3
Power generation and distribution	8	21
Other	20	155
Total capital expenditures	**3,232**	**3,346**

Capital expenditures in the exploration and production segment increased by $188 million, or by 7.4%, compared to the first quarter of 2013. In Russia, the increase related to higher volumes and the cost of production drilling in the Ural region, the Komi Republic and Western Siberia was partially outweighed by the effect of ruble devaluation. Outside of Russia, we decreased investments in the development of the West Qurna-2 field due to completion of preparation of “Mishrif early oil” project.

Other capital expenditures mostly refer to investments of OAO Arkhangelskgeoldobycha, a Group company, involved in diamond deposits development in the Arkhangelsk region of Russia. The decrease of the respective capital expenditures was due to fulfillment of the most stages of the capital investment program at the deposits.

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

	3 months of 2014	2013
	(millions of US dollars)	
Yamal	76	113
Caspian region(1)	235	444
Ghana	2	7
Cote d’Ivoire	80	7
Iraq	376	457
Uzbekistan	133	96
Total	**902**	**1,124**

(1) Russian and international projects.

In the first quarter of 2014 we did not make any significant acquisitions of licenses, while in the first quarter of 2013, a Group company paid $835 million as a second 50% installment for the acquisition of the subsoil rights for the site that includes the Imilorskoye, West Imilorskoye and Istochnoye fields in Western Siberia. The first 50% payment was made in December 2012.

Financing activities

In the first quarter of 2014, net movements of short-term and long-term debt generated an inflow of $989 million, compared to an outflow of $7 million in the first quarter of 2013.