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

The following report represents management’s discussion and analysis of the financial condition and results of operations of OAO LUKOIL as of September 30, 2010, and for the three and nine months ended September 30, 2010 and 2009, and significant trends 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 produced are translated into barrels using conversion rates characterizing the density of oil from each of our oilfields. 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 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.

Key financial and operational results

	9 months of		Change, %	3rd quarter of		Change, %
	2010	2009		2010	2009	
Sales (millions of US dollars)	76,272	56,802	34.3	26,517	21,941	20.9
Net income attributable to OAO LUKOIL (millions of US dollars)	6,820	5,285	29.0	2,818	2,056	37.1
EBITDA (millions of US dollars)	11,985	10,237	17.1	4,552	3,703	22.9
Taxes other than income taxes, excise and export tariffs (millions of US dollars)	(20,594)	(13,745)	49.8	(6,905)	(5,745)	20.2
Basic and diluted earning per share of common stock attributable to OAO LUKOIL (US dollars)	8.16	6.24	30.7	3.46	2.43	42.4
Hydrocarbon production by the Group including our share in equity affiliates (thousands of BOE)	614,036	604,378	1.6	204,663	202,648	1.0
Crude oil production by the Group including our share in equity affiliates (thousands of tonnes)	72,270	73,278	(1.4)	24,130	24,645	(2.1)
Gas available for sale produced by the Group including our share in equity affiliates (millions of cubic meters)	13,789	10,937	26.1	4,547	3,581	27.0
Refined products produced by the Group including our share in equity affiliates (thousands of tonnes)	47,792	44,409	7.6	16,695	15,641	6.7

During the nine months of 2010, our net income was $6,820 million, which is $1,535 million, or 29.0%, more than in the same period of 2009. Our net income for the third quarter of 2010 amounted to $2,818 million, which is $762 million, or 37.1%, more than in the third quarter of 2009.

Positive dynamic of our net income for the nine-month period of 2010 was mainly due to a sharp increase in hydrocarbon prices, compared to the respective period of 2009. Also, in the third quarter of 2010, we recognised a $438 million gain resulting from a successful completion of the legal dispute regarding one of our joint ventures in Kazakhstan. At the same time, our results were affected by increased extraction taxes and export tariff rates, appreciation of the Russian ruble and increase in operating and transportation expenses.

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.

The Group 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 37 countries on four continents.

LUKOIL is one of the world's largest energy companies in terms of hydrocarbon reserves. The Company's proved reserves as of January 1, 2010 amounted to 17.5 billion BOE and comprised of 13.7 billion BOE of crude oil and 22.9 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 natural gas. These activities are primarily located within Russia, with additional activities in Azerbaijan, Kazakhstan, Uzbekistan, the Middle East, South America, and Northern and Western Africa.
- **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.

Other businesses include banking, finance and other activities. 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 10, 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 19 "Segment information" to our interim consolidated financial statements.

Recent development and changes in the Group structure

On 28 July, 2010, the Group company signed a stock purchase agreement with ConocoPhillips' subsidiary to purchase 64.6 million of the Company's ordinary shares at $53.25 per share for the total amount of $3,442 million. This transaction was finalized in August 2010. Additionally, under this agreement the Group had a 60-day option to purchase any or all of the remaining 98.7 million of the Company's ordinary shares held by ConocoPhillips' subsidiary for the price of $56 per share. On September 26, 2010, the Group company exercised its option to acquire shares from ConocoPhillips by sending a notice of exercise in respect of 42,500,000 LUKOIL ADRs (each representing one ordinary share of the Company). The Group company sold these ADRs to UniCredit Bank AG. These transactions were completed on September 29, 2010 when 42,500,000 LUKOIL ADRs were directly transferred to UniCredit Bank AG, and UniCredit Bank AG paid the purchase price of $2.38 billion to ConocoPhillips' subsidiary. Simultaneously, UniCredit Bank AG issued a series of equity-linked notes to a Group company that are redeemable for 17,500,000 LUKOIL ADRs on or before September 29, 2011. These equity-linked notes have been classified within OAO LUKOIL stockholders' equity. UniCredit Bank AG also issued an option to the Group company to purchase from UniCredit Bank AG an additional 25,000,000 LUKOIL ADRs on or before September 29, 2011. The option provides for the purchase of LUKOIL ADRs at market price with a floor of $56 per ADR and is not valid if the market price per ADR is $50 or below.

In January 2010, the Company signed an agreement to develop the West Qurna-2 field located in the south of Iraq. The parties to the agreement are the Iraqi state-owned South Oil Company and the contracting consortium formed by the Iraqi state-owned North Oil Company, the Company and Norway's Statoil ASA. The Company's share in the project is 56.25%. The West Qurna-2 field has recoverable reserves of about 12.9 billion barrels.

In December 2009, the Group acquired the remaining 46.0% interest in its equity affiliate LUKARCO B.V. ("LUKARCO") for $1.6 billion, thereby increasing the ownership stake to 100%. LUKARCO is a holding company, which owns a 5.0% share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, and a 12.5% share in Caspian Pipeline Consortium ("CPC"), which carries Kazakhstani and Russian oil to Novorossiysk marine terminal. Therefore the Group increased the ownership in Tengizchevroil from 2.7% to 5.0% and the ownership in CPC from 6.75% to 12.5%. The first installment in amount of $300 million was paid in December 2009. $800 million should be paid no later than December 2010 and the remaining amount – no later than December 2011.

In June 2009, a Group company entered into an agreement with Total S.A. to acquire a 45.0% interest in TRN refinery in the Netherlands ("TRN"). The transaction was finalized in September 2009 in the amount of approximately $688 million (after completion adjustment). The Group provides crude oil and market refined products in line with its equity stake in the refinery. The refinery has the flexibility to process Urals blend crude oil as well as significant volumes of straight-run fuel oil and vacuum gasoil, which allowed us to integrate the plant into the Group's crude oil supply and refined products marketing operations. This plant with a Nelson complexity index of 9.8 has an annual topping capacity of 7.9 million tonnes and an annual capacity of a hydro-cracking unit of approximately 3.4 million tonnes. This acquisition was made in accordance with the Group's plans to develop its refining capacity in Europe.

In the first quarter of 2009, the Group acquired 100% interests in OOO Smolenskneftesnab, OOO IRT Investment, OOO PM Invest and OOO Retaier House for $238 million. These are holding companies, which between them own 96 petrol stations and plots of land in Moscow, the Moscow region and other regions of central European Russia. This acquisition was made in order to expand the Group's presence on the most advantageous retail market in the Russian Federation.

In the fourth quarter of 2008, the Group acquired 100% interests in ZAO Association Grand and OOO Mega Oil M for $493 million. ZAO Association Grand and OOO Mega Oil M are holding companies, owning 181 petrol stations in Moscow, the Moscow region and other regions of central European Russia. This acquisition was made in order to expand the Group's presence on the most advantageous retail markets in the Russian Federation.

In July 2008, a Group company signed an agreement to acquire a 100% interest in the Akpet group for $555 million. The transaction was finalized in November 2008. The amended agreement provided for three payments of purchase consideration: the first payment in amount of $250 million was made at the date of finalization, the second payment in amount of $150 million was made in April 2009, and the remaining amount was paid in October 2009. The Akpet group operated 689 petrol filling stations on the basis of dealer agreements and owned eight refined product terminals, five LNG storage tanks, three jet fuel terminals and a lubricant production plant in Turkey.

In June 2008, a Group company signed an agreement with ERG S.p.A. to establish a joint venture to operate the ISAB refinery complex (“ISAB”) in Priolo, Italy. In December 2008, the Group completed the acquisition of a 49.0% stake in the joint venture for €1.45 billion (approximately $1.83 billion) and paid €600 million (approximately $762 million) as a first installment. The remaining amount was paid in February 2009. The seller has a put option, the effect of which would be to increase the Group’s stake in the company operating ISAB up to 100%. The agreement states that each partner is responsible for procuring crude oil and marketing refined products in line with its equity stake in the joint venture. ISAB has the flexibility to process Urals blend crude oil, includes three jetties and storage tanks totaling 3,700 thousand cubic meters and has an annual refining capacity of 16 million tonnes.

In March 2008, a Group company entered into an agreement with a related party, whose management and directors include members of the Group’s management and Board of Directors, to acquire a 64.31% interest in OAO UGK TGK-8 (“TGK-8”) for approximately $2,117 million. The purchase consideration partly consisted of 23.55 million shares of common stock of the Company (at a market value of approximately $1,620 million). The transaction was finalized in May 2008. From May 2008 to June 2009, a Group company acquired the remaining interest in TGK-8 for a total of $1,202 million, increasing the Group’s ownership to 100%. TGK-8 is one of the major gas consumers in the Southern Federal District with an annual consumption of 6 billion cubic meters per year. Its power plants are located in Astrakhan, Volgograd and Rostov regions, Krasnodar and Stavropol Districts, and the Republic of Dagestan of the Russian Federation with total productive capacity of 3.6 GW. By purchasing TGK-8 LUKOIL expects significant synergies through natural gas supplies from the Company’s gas fields located in the Northern Caspian and in Astrakhan region, which will allow the Company to reach efficient gas price. This acquisition is made in accordance with the Company’s plans to develop its power generation business.

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. Also we have a consolidated joint venture with ConocoPhillips, OOO Narianmarneftegaz, in the Northern Timan-Pechora region. Exploration and production outside of Russia is performed by our 100% subsidiary LUKOIL-Overseas, that has stakes in PSA's and other projects in Kazakhstan, Azerbaijan, Uzbekistan, Iraq, Saudi Arabia, Columbia, Ghana and Cote d'Ivoire.

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

	9 months of		3rd quarter of	
	2010	**2009**	**2010**	**2009**
Daily production of hydrocarbons, including the Company's share in equity affiliates (thousand BOE per day), including:	2,249	2,214	2,225	2,203
- crude oil	1,952	1,978	1,934	1,974
- natural and petroleum gas[1]	297	236	291	229
Hydrocarbon extraction expenses (US dollar per BOE)	4.04	3.39	4.08	3.67
	(millions of US dollars)			
Hydrocarbon extraction expenses	2,388	1,989	804	722
- in Russia	2,238	1,850	747	671
- outside Russia	150	139	57	51
Exploration expenses	175	188	29	119
- in Russia	70	56	20	22
- outside Russia	105	132	9	97
Mineral extraction tax	5,664	3,790	1,907	1,720
- in Russia	5,611	3,751	1,888	1,704
- outside Russia	53	39	19	16

[1] Gas available for sale (excluding gas produced for our own consumption).

Crude oil production. In the nine months of 2010, we decreased our crude oil production by 1.4%, compared to the same period of 2009, and produced 532.9 million barrels, or 72.3 million tonnes (including the Company's share in equity affiliates).

The following table represents our crude oil production in the respective periods of 2010 and 2009 by major regions.

(thousands of tonnes)	**9 months of 2010**	**Change to 2009**			**9 months of 2009**
		Total, %	**Change in structure**	**Organic change**	
Western Siberia	38,273	(4.1)	–	(1,623)	39,896
Timan-Pechora	16,185	(0.2)	–	(31)	16,216
Ural region	9,233	3.7	–	333	8,900
Volga region	2,174	–	–	(1)	2,175
Other in Russia	1,536	(4.1)	–	(66)	1,602
Crude oil produced in Russia	67,401	(2.0)	–	(1,388)	68,789
Crude oil produced internationally	2,552	(2.8)	–	(73)	2,625
Total crude oil produced by consolidated subsidiaries	**69,953**	**(2.0)**	**–**	**(1,461)**	**71,414**
Our share in crude oil produced by equity affiliates:					
in Russia	249	9.7	–	22	227
outside Russia	2,068	26.3	437	(6)	1,637
Total crude oil produced	**72,270**	**(1.4)**	**437**	**(1,445)**	**73,278**

The main oil producing region of the Company is Western Siberia where we produced 54.7% of our crude oil in the nine months of 2010 (55.9% in the nine months of 2009). A significant impact on our production in Western Siberia was caused by increased field depletion rate as well as a reduced drilling footage. The reduction in drilling footage was due to implementation of the Company's strategy aiming at strengthening its financial position through focusing on high return projects and boosting cash flows.

In line with our strategy the Company is developing new oil fields in the Northern Timan-Pechora and Caspian regions in order to compensate for the decrease in crude oil production in the traditional regions. In August 2008, we began commercial production on the Yuzhnaya Khylchuya oil field, located in the Timan-Pechora region. We produced 5.4 million tonnes from this field in the nine months of 2010, compared to 5.1 million tonnes in the nine months of 2009. This oil field is developed by OOO Narianmarneftegaz, our joint venture with ConocoPhillips.

In December 2009, we started production drilling on the Yu. Korchagin field in the Caspian Sea. In April 2010, we began commercial production at the field. Maximum annual production from this field is expected to be 2.5 million tonnes of crude oil and gas condensate, and 1.0 billion cubic meters of gas. We expect that starting from December 2010, incentive export tariff rate will be applied to crude oil produced and exported from this field. According to the current legislation, mineral extraction tax rate for this field is zero.

The structural growth of our share in equity affiliates' production outside of Russia is explained by the increase of our effective share in Tengizchevroil, a joint venture which develops the Tengiz and Korolevskoe fields in Kazakhstan, to 5.0% as a result of acquiring the remaining 46.0% interest in LUKARCO.

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

	9 months of			
	2010		**2009**	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Crude oil purchases in Russia	1,437	196	1,840	251
Crude oil purchases internationally........	117,727	16,061	117,001	15,962
Total crude oil purchased....................	**119,164**	**16,257**	**118,841**	**16,213**

	3rd quarter of			
	2010		**2009**	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Crude oil purchases in Russia	1,056	144	1,349	184
Crude oil purchases internationally........	40,117	5,473	40,043	5,463
Total crude oil purchased....................	**41,173**	**5,617**	**41,392**	**5,647**

Significant part of our crude oil purchases is used for processing at our and at third party refineries. In the nine months of 2010, we purchased 8,629 thousand tonnes of crude for processing (including 3,279 thousand tonnes at ISAB and 1,542 thousand tonnes at TRN), compared to 8,520 thousand tonnes in the nine months of 2009 (including 4,029 thousand tonnes at the ISAB refinery complex and 169 thousand tonnes at the TRN refinery complex).

Gas production. In the nine months of 2010, we produced 13,789 million cubic meters of gas available for sale (including our share in equity affiliates), an increase of 26.1%, compared to the nine months of 2009.

Our major gas production field is the Nakhodkinskoe gas field, where we produced 6,072 million cubic meters of natural gas in the nine months of 2010, compared to 4,208 million cubic meters in the same period of 2009. This 44.3% increase in gas production from the field resulted from the increase of purchases of our gas by OAO Gazprom ("Gazprom") starting from the second half of 2009. Also, during the nine months of 2010, we increased utilization rates of petroleum gas in Western Siberia.

International gas production by our subsidiaries did not change significantly. Production from the Khauzak gas field in Uzbekistan was 1,966 million cubic meters of natural gas, compared to 1,936 million cubic meters in the same period of 2009. In the nine months of 2010, our share in production from the Shakh-Deniz field in Azerbaijan was 419 million cubic meters, compared to 377 million cubic meters in the nine months of 2009. As a result of acquisition of remaining share in LUKARCO we increased our share in production of petroleum gas from Tengiz field by 237 million cubic meters.

Refining, marketing and trading

Refining. We own and operate four refineries located in European Russia and three refineries located outside of Russia – in Bulgaria, Ukraine and Romania. Moreover, we have a 49% stake in the ISAB refinery complex in Italy and a 45% interest in TRN refinery in the Netherlands.

Compared to the nine months of 2009, production at our consolidated and affiliated refineries increased by 7.6%. Russian refineries increased their production by 1.3%. Production of our international refineries including our share of production at ISAB and TRN increased by 23.9%. The increase was a result of acquisition of TRN. The production at our Bulgarian and Ukrainian refineries was lower due to performed overhauls.

In the nine months of 2010, our share of refined products produced at ISAB amounted to 4,749 thousand tonnes (4,572 thousand tonnes in the nine months of 2009) and our share in production of TRN amounted to 3,469 thousand tonnes (371 thousand tonnes in the nine month of 2009).

In Russia, LUKOIL holds the leading position in production and sales of European standards motor fuel being ahead of the official terms of their obligatory implementation in the country. At our Russian refineries we produced 6,456 and 5,417 thousand tonnes of Euro 4 and Euro 5 diesel fuel, and 4,074 and 3,512 thousand tonnes of Euro 3 gasoline in the nine-month periods of 2010 and 2009, respectively.

Along with our own production of refined products we can refine crude oil at third party refineries depending on market conditions and other factors. Before 2010, we processed crude oil at third party refineries in Russia primarily to supply our network in the Ural region and for export sales. In 2010, we sell our crude oil to these refineries and purchase refined products from them. In order to supply our retail networks in Eastern Europe, we refined crude oil in Belarus and Serbia. Refined products processed in Belarus were used for supplying our local retail network and for wholesale export. In the end of 2009, we ceased refining of crude oil in Belarus due to decreased profitability of such operations as a result of certain amendments in the customs legislation. However, in the third quarter of 2010, we began refining our crude oil at third party refinery in Kazakhstan.

The following table summarizes key figures for our refining activities.

	9 months of		3rd quarter of	
	2010	2009	2010	2009
	(millions of US dollars)			
Refining expenses at the Group refineries	778	670	263	235
- in Russia	570	484	189	175
- outside Russia	208	186	74	60
Refining expenses at ISAB and TRN	531	361	182	143
Refining expenses at third party refineries	3	132	1	22
- in Russia	1	104	–	12
- outside Russia	2	28	1	10
Capital expenditures	513	592	177	181
- in Russia	385	356	147	119
- outside Russia	128	236	30	62
	(thousand barrels per day)			
Refinery throughput at the Group refineries	1,103	1,113	1,138	1,138
- in Russia[1]	908	898	932	930
- outside Russia	195	215	206	208
Refinery throughput at ISAB and TRN[2] [3]	221	133	220	155
Refinery throughput at third party refineries	1	75	4	46
- in Russia	–	44	–	17
- outside Russia	1	31	4	29
Total refinery throughput	**1,325**	**1,321**	**1,362**	**1,339**
	(thousand of tonnes)			
Refined products produced at the Group refineries	39,574	39,466	13,923	13,706
- in Russia[1]	32,452	32,024	11,258	11,194
- outside Russia	7,122	7,442	2,665	2,512
Production of ISAB and TRN[2]	8,218	4,943	2,772	1,935
Refined products produced at third party refineries	51	2,500	47	528
- in Russia	–	1,426	–	183
- outside Russia	51	1,074	47	345
Total refined products produced	**47,843**	**46,909**	**16,742**	**16,169**

[1] Excluding mini refineries.
[2] Group's share.
[3] Including refined products 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 approximately 6 thousand petrol stations. Most of the stations operate under the LUKOIL brand. We continuously develop our retail business and LUKOIL brand by expanding our retail network. The table below summarizes figures for our trading activities.

	9 months of		3rd quarter of	
	2010	2009	2010	2009
	(thousand of tonnes)			
Retail sales	10,488	10,495	3,803	3,767
Wholesale sales	67,911	63,727	23,587	20,979
Total refined products sales	**78,399**	**74,222**	**27,390**	**24,746**
Refined products purchased in Russia	1,374	350	519	133
Refined products purchased internationally	33,826	29,482	10,811	9,099
Total refined products purchased	**35,200**	**29,832**	**11,330**	**9,232**

The increase in volumes of refined products purchased in Russia was due to termination of refining operations at domestic third party refineries in late 2009. In 2010, we commenced sales of crude oil to these third party refineries and started purchasing of refined products from them.

Exports of crude oil and refined products from Russia. In the nine months of 2010, our export of crude oil from Russia was 4.1% less than in the same period of 2009, and we exported 45.2% of our total domestic crude oil production (46.2% in the nine months of 2009).

The volumes of crude oil exported from Russia by our subsidiaries are summarized as follows:

	9 months of			
	2010		**2009**	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Exports of crude oil using Transneft export routes	172,196	23,492	182,671	24,921
Exports of crude oil bypassing Transneft	51,207	6,986	50,232	6,853
Total crude oil exports	**223,403**	**30,478**	**232,903**	**31,774**

	3rd quarter of			
	2010		**2009**	
	(thousand of barrels)	(thousand of tonnes)	(thousand of barrels)	(thousand of tonnes)
Exports of crude oil using Transneft export routes	55,546	7,578	53,890	7,352
Exports of crude oil bypassing Transneft	18,288	2,495	18,970	2,588
Total crude oil exports	**73,834**	**10,073**	**72,860**	**9,940**

The overall decrease of our export from Russia was a result of decreased crude oil production, termination of processing operations in Belarus and respective decrease of export to CIS. At the same time, export to far-abroad increased by 1,795 thousand tonnes, compared to the nine months of 2009.

In the nine months of 2010, the crude oil exported through our own export infrastructure was 6,767 thousand tonnes, or 2.4% more than in the nine months of 2009, due to increased export of crude oil produced from the Yuzhnaya Khylchuya oil field through our export terminal in Varandey.

In the nine months of 2010, we exported from Russia 19.5 million tonnes of refined products, a decrease of 8.3%, compared to the same period of 2009. This was mainly due to decreased export to CIS. Released volumes were sold on domestic market. We export from Russia primarily diesel fuel, fuel oil and gasoil. These products account for approximately 90% of our refined products export volumes.

In the nine months of 2010, our revenue from export of crude oil and refined products from Russia both to the Group companies and third parties amounted to $16,084 million and $10,445 million, respectively ($12,318 million for crude oil and $8,137 million for refined products in the nine months of 2009).

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 our revenues. During the nine months of 2010, the Brent crude oil price fluctuated between $67 and $86 per barrel and reached its peak of $86.79 in the end of April 2010.

During 2009, crude oil prices were in an upward trend and in the second half of the year crude oil price stabilized around $70 per barrel. In 2008, the crude oil prices were the highest ever in real terms. Starting from July 2008, crude oil prices began to descend and by the end of the year crude oil price dropped by more than $100 per barrel down to $37 per barrel driven by the world economic downturn.

Substantially all crude oil we export is Urals blend. The following table shows the average crude oil and refined product prices products in the respective periods of 2010 and 2009.

	9 months of		Change, %	3rd quarter of		Change, %
	2010	2009		2010	2009	
	(in US dollars per barrel, except for figures in percent)					
Brent crude	77.14	57.32	34.6	76.86	68.08	12.9
Urals crude (CIF Mediterranean) (1)	75.92	56.80	33.7	75.55	67.88	11.3
Urals crude (CIF Rotterdam) (1)	75.92	56.72	33.9	75.58	67.76	11.6
	(in US dollars per metric tonne, except for figures in percent)					
Fuel oil 3.5% (FOB Rotterdam)	434.12	316.13	37.3	425.47	395.29	7.6
Diesel fuel 10 ppm (FOB Rotterdam)	665.28	505.15	31.7	667.67	569.84	17.2
High-octane gasoline (FOB Rotterdam)	717.42	546.74	31.2	694.38	641.92	8.2

Source: Platts.

(1) The Company sells crude oil on foreign markets on various delivery terms. Thus, our average realized sales 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 respective periods of 2010 and 2009.

	9 months of		Change, %	3rd quarter of		Change, %
	2010	2009		2010	2009	
	(in US dollars per metric tonne, except for figures in percent)					
Fuel oil	230.71	144.44	59.7	244.71	172.00	42.3
Diesel fuel	534.03	438.97	21.7	508.83	456.27	11.5
High-octane gasoline (Regular)	705.97	552.11	27.9	732.28	747.07	(2.0)
High-octane gasoline (Premium)	732.11	596.17	22.8	775.18	771.87	0.4

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, the devaluation of the ruble against the US dollar generally causes our costs to decrease in US dollar terms, and vice versa. The devaluation 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 14.3% in the nine months of 2010, compared to the same period of 2009.

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

	9 months of		3rd quarter of	
	2010	**2009**	**2010**	**2009**
Ruble inflation (CPI), %	6.2	8.2	1.7	0.6
Change of the ruble-dollar exchange rate, %	(0.5)	(2.4)	2.5	3.8
Average exchange rate for the period (ruble to US dollar)	30.25	32.48	30.62	31.33
Exchange rate at the end of the period (ruble to US dollar)	30.40	30.09	–	–

Tax burden

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

		9 months of		Change, %
		2010(1)	**2009**(1)	
Export tariffs on crude oil	$/tonne	269.04	157.05	71.3
Export tariffs on refined products				
Light distillates (gasoline), middle distillates (jet fuel), diesel fuel and gasoils	$/tonne	193.57	118.12	63.9
Liquid fuels (fuel oil)	$/tonne	104.28	63.62	63.9
Excise on refined products				
Straight-run gasoline	RUR/tonne	4,290.00	3,900.00	10.0
High-octane gasoline	RUR/tonne	3,992.00	3,629.00	10.0
Low-octane gasoline	RUR/tonne	2,923.00	2,657.00	10.0
Diesel fuel	RUR/tonne	1,188.00	1,080.00	10.0
Motor oils	RUR/tonne	3,246.10	2,951.00	10.0
Mineral extraction tax				
Crude oil	RUR/tonne	2,948.68	2,139.57	37.8
Natural gas	RUR/1,000 m^3	147.00	147.00	–

(1) Average values.

		3rd quarter of		Change, %
		2010(1)	**2009**(1)	
Export tariffs on crude oil	$/tonne	261.91	224.25	16.8
Export tariffs on refined products				
Light distillates (gasoline), middle distillates (jet fuel), diesel fuel and gasoils	$/tonne	188.72	163.40	15.5
Liquid fuels (fuel oil)	$/tonne	101.69	88.01	15.5
Excise on refined products				
Straight-run gasoline	RUR/tonne	4,290.00	3,900.00	10.0
High-octane gasoline	RUR/tonne	3,992.00	3,629.00	10.0
Low-octane gasoline	RUR/tonne	2,923.00	2,657.00	10.0
Diesel fuel	RUR/tonne	1,188.00	1,080.00	10.0
Motor oils	RUR/tonne	3,246.10	2,951.00	10.0
Mineral extraction tax				
Crude oil	RUR/tonne	2,987.65	2,662.89	12.2
Natural gas	RUR/1,000 m^3	147.00	147.00	–

(1) Average values.

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

		9 months of 2010[1]	9 months of 2009[1]	Change, %
Excise on refined products				
Straight-run gasoline	$/tonne	141.80	120.07	18.1
High-octane gasoline	$/tonne	131.95	111.73	18.1
Low-octane gasoline	$/tonne	96.62	81.80	18.1
Diesel fuel	$/tonne	39.27	33.25	18.1
Motor oils	$/tonne	107.30	90.85	18.1
Mineral extraction tax				
Crude oil	$/tonne	97.46	65.87	48.0
Natural gas	$/1,000 m^3	4.86	4.53	7.2

[1] Average values.

		3rd quarter of 2010[1]	3rd quarter of 2009[1]	Change, %
Excise on refined products				
Straight-run gasoline	$/tonne	140.10	124.49	12.5
High-octane gasoline	$/tonne	130.37	115.84	12.5
Low-octane gasoline	$/tonne	95.46	84.81	12.5
Diesel fuel	$/tonne	38.80	34.47	12.5
Motor oils	$/tonne	106.01	94.20	12.5
Mineral extraction tax				
Crude oil	$/tonne	97.57	85.00	14.8
Natural gas	$/1,000 m^3	4.80	4.69	2.2

[1] Average values.

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. The base rate is 419 rubles per metric tonne extracted and it 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 was 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) resulted in an increase of the tax rate by $1.61 per tonne extracted (or $0.22 per barrel extracted using a conversion factor of 7.33).

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, Caspian sea and the Nenetsky Autonomous District, depending on the period and volume of production. For crude oil produced in other regions the tax rate calculation described above should be multiplied by a coefficient characterizing the depletion of a particular oilfield. The coefficient is equal to 1.0 for oilfields with depletion below 80%. Each 1% increase of depletion of a particular oilfield above 80% results in a decrease of the coefficient by 0.035. The minimum value of the coefficient is 0.3. The depletion level assessment is based on crude oil production and reserves information reported to the Russian government.

The Group undertakes crude oil production from certain oilfields in Caspian Sea and the Nenetsky Autonomous District and can benefit from the application of zero tax rate.

Natural gas extraction tax rate. The mineral extraction tax on natural gas production is calculated using a flat rate. The current rate of 147 rubles per thousand cubic meters of natural gas extracted has been in effect since January 1, 2006.

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 by $0.65 per barrel exported.

Effective from December 2008, the crude oil export duty rate is revised monthly on the basis of the immediately preceding one-month period of crude oil price monitoring.

Starting from the end of 2009, zero export duty rate was set for crude oil produced at certain fields in Eastern Siberia. However, in July 2010, a zero rate for these fields was substituted for special reduced export duty rate. Effective from December 2010, the list of the oilfields where reduced rate applies will be extended by our Yu. Korchagin and V. Filanovsky oilfields. Both are located in the Caspian Sea.

Export duty rates on refined products are set by the Russian Government. The rate of export duty depends on internal demand for refined products and international crude oil market conditions.

Crude oil and refined products exported to CIS countries, other than Ukraine and Belarus, are not subject to export duties. In 2009, crude oil exported from Russia to Belarus was subject to export duties calculated with the application of a coefficient 0.356 to the regular export duty rate set by the Russian Government.

In 2010, under the agreement between the Russian Federation and Belarus, crude oil exported from Russia to Belarus up to total amount of 6.3 million tonnes is not subject to export duty. Volumes of crude oil export above this limit are taxed at a regular rate.

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

Starting from 2011, excise rates on refined products in Russia will be amended as follows taking into account ecological class of fuel. Excise tax rates for 2011 are below:

Gasoline		
Below Euro 3	RUR/tonne	4,624.60
Euro 3	RUR/tonne	4,302.20
Euro 4 and 5	RUR/tonne	3,773.00
Diesel fuel		
Below Euro 3	RUR/tonne	1,573.00
Euro 3	RUR/tonne	1,304.40
Euro 4 and 5	RUR/tonne	1,067.20
Motor oils	RUR/tonne	3,570.00
Straight-run gasoline	RUR/tonne	4,719.00

Income tax. Starting from January 1, 2009, 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.

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 of crude oil producing 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 state-owned OAO AK Transneft ("Transneft"). Access to the Transneft crude oil export pipeline network is allocated quarterly, based on recent volumes produced and delivered through the pipeline and proposed export destinations. The crude oil transported by Transneft is Urals blend – a mix of crude oils of various qualities. Therefore Russian companies that produce crude oil of a higher quality, cannot obtain benefits from selling it using Transneft's pipeline. Alternative access to international markets bypassing Transneft's export routes can be obtained through railroad transport, by tankers, and by the export infrastructure of oil producing companies. Our own export infrastructure includes the Vysotsk terminal in the Leningrad region, the Varandey terminal in the Nenetsky Autonomous District and the Svetly terminal in the Kaliningrad region. We use the offshore ice-resistant terminal in Varandey with annual capacity of 12 million tonnes to export crude oil produced by our joint venture with ConocoPhillips located in Northern Timan-Pechora. Through the Svetly terminal we export crude oil primarily produced by OOO LUKOIL-Kaliningradmorneft, our subsidiary operating in the Kaliningrad region, and refined products. Its annual capacity is 6 million tonnes. We use the Vysotsk terminal to export refined products. In the future we expect to use the terminal to export both crude oil and refined products, depending on market conditions. Currently it has a capacity of 12 million tonnes per year that can be expanded up to 15 million tonnes per year.

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. Besides transportation of refined products, OAO Russian Railways provides oil companies with crude oil transportation services. We transport the major part of our refined products by railway transport.

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"). The tariffs are dependent on transport destination, delivery volume, distance of transportation, and several other factors. Changes in the tariffs depend on inflation forecasts by the Ministry of Economic Development of the Russian Federation, the investment needs of owners of the transport infrastructure, other macroeconomic factors, and compensation of economically reasonable expense, incurred by entities of the natural monopolies. Tariffs are revised by the FST at least annually.

Nine months ended September 30, 2010, compared to nine months ended September 30, 2009

The table below represents our consolidated statements of income for the periods indicated.

	9 months of	
	2010	**2009**
	(millions of US dollars)	
Revenues		
Sales (including excise and export tariffs)	76,272	56,802
Costs and other deductions		
Operating expenses	(5,994)	(5,015)
Cost of purchased crude oil, gas and products	(31,173)	(21,475)
Transportation expenses	(4,169)	(3,594)
Selling, general and administrative expenses	(2,557)	(2,398)
Depreciation, depletion and amortization	(3,114)	(3,001)
Taxes other than income taxes	(6,522)	(4,569)
Excise and export tariffs	(14,072)	(9,176)
Exploration expense	(175)	(188)
Gain on disposals and impairments of assets	29	15
Income from operating activities	**8,525**	**7,401**
Interest expense	(535)	(503)
Interest and dividend income	144	105
Equity share in income of affiliates	335	270
Currency translation loss	(101)	(337)
Other non-operating income	225	37
Income before income taxes	**8,593**	**6,973**
Current income taxes	(1,678)	(1,430)
Deferred income taxes	18	(123)
Total income tax expense	**(1,660)**	**(1,553)**
Net income	**6,933**	**5,420**
Less: net income attributable to noncontrolling interests	(113)	(135)
Net income attributable to OAO LUKOIL	**6,820**	**5,285**
Basic and diluted earning per share of common stock attributable to OAO LUKOIL (in US dollars)	8.16	6.24

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

Sales revenues

Sales breakdown	9 months of 2010	9 months of 2009
	(millions of US dollars)	
Crude oil		
Export and sales on international markets other than CIS	18,628	13,199
Export and sales to CIS	723	1,189
Domestic sales	706	472
	20,057	**14,860**
Refined products		
Export and sales on international markets		
Wholesale	36,437	25,905
Retail	6,962	6,496
Domestic sales		
Wholesale	3,937	2,692
Retail	4,007	2,987
	51,343	**38,080**
Petrochemicals		
Export and sales on international markets	398	432
Domestic sales	520	338
	918	**770**
Gas and gas products		
Export and sales on international markets	1,137	792
Domestic sales	588	367
	1,725	**1,159**
Sales of energy and related services	**1,025**	**754**
Other		
Sales on international markets	701	764
Domestic sales	503	415
	1,204	**1,179**
Total sales	**76,272**	**56,802**

Sales volumes	9 months of 2010	9 months of 2009
Crude oil	(thousands of barrels)	
Export and sales on international markets other than CIS	248,186	236,774
Export and sales to CIS	17,174	29,056
Domestic sales	20,502	14,462
	285,862	**280,292**
Crude oil	(thousands of tonnes)	
Export and sales on international markets other than CIS	33,859	32,302
Export and sales to CIS	2,343	3,964
Domestic sales	2,797	1,973
	38,999	**38,239**
Refined products	(thousands of tonnes)	
Export and sales on international markets		
Wholesale	59,749	56,405
Retail	5,328	5,975
Domestic sales		
Wholesale	8,162	7,322
Retail	5,160	4,520
	78,399	**74,222**
Total sales volume of crude oil and refined products	**117,398**	**112,461**

Realized average sales prices

	9 months of 2010		9 months of 2009	
	($/barrel)	($/tonne)	($/barrel)	($/tonne)
Average realized price international				
Oil (excluding CIS)	75.06	550.18	55.74	408.60
Oil (CIS)	42.09	308.55	40.93	300.02
Refined products				
Wholesale		609.84		459.26
Retail		1,306.79		1,087.19
Average realized price within Russia				
Oil	34.43	252.34	32.66	239.41
Refined products				
Wholesale		482.22		367.65
Retail		776.59		660.85

During the nine months of 2010, our revenues increased by $19,470 million, or by 34.3%, compared to the same period of 2009. Our revenues from crude oil sales increased by $5,197 million, or by 35.0%. Our revenues from sales of refined products increased by $13,263 million, or by 34.8%. The increase in sales revenue was a result of a sharp increase in hydrocarbon prices, compared to the nine months of 2009. Moreover, the appreciation of the ruble against the US dollar also increased the US dollar value of our sales revenue denominated in Russian rubles.

Sales of crude oil

Our total crude oil sales revenues increased by 35.0%, mainly due to growth of crude oil prices.

Cease in crude oil refining at third party refineries in Russia and Belarus released crude oil volumes for sales on domestic market, as a result, our crude oil sales raised by 2.0% in terms of volumes.

Sales of refined products

In the nine months of 2010, our revenue from the wholesale of refined products outside of Russia increased by $10,532 million, or by 40.7%, compared to the same period of 2009, due to increased average realized price by 32.8%. Despite the decrease in output at our refineries in Bulgaria and Ukraine due to overhaul, commencement of crude oil refining at TRN and expansion of trading activities led to an increase in wholesales volumes by 5.9%.

In the nine months of 2010, our revenue from international retail sales increased by $466 million, or by 7.2%, compared to the nine months of 2009. Positive effect from average retail prices increase by 20.2% was offset by 10.8% sales volumes decrease, that reflects restructuring of our retail network in the USA.

In the nine months of 2010, our revenue from the wholesale of refined products on the domestic market increased by $1,245 million, or by 46.2%, compared to the nine months of 2009, mainly due to an increase in the average realized price by 31.2%. Sales volumes increased by 840 thousand tonnes, or by 11.5%. This was primarily due to a decrease in refined products export from Russia. Decrease in refining volumes at third parties refineries in Russia was partially compensated by purchases from these refineries.

In the nine months of 2010, our revenue from retail sales in Russia increased by $1,020 million, or by 34.1%, compared to the nine months of 2009, due to an increase both in volumes, being a result of higher average daily sales per petrol station, and in prices. In the nine months of 2010, our retail sales revenue was 50.4% of total refined products sales in Russia (in the nine months of 2009 – 52.6%).

Sales of petrochemical products

In the nine months of 2010, our revenue from sales of petrochemical products increased by $148 million, or by 19.2%, compared to the nine months of 2009. Outside of Russia, decrease in sales volumes due to decreased refining and trading was partially compensated by price growth. The growth of domestic sales revenue was largely a result of increase in realized prices and the effect of the real ruble appreciation against the US dollar.

Sales of gas and gas products

In the nine months of 2010, sales of gas and gas refined products increased by $566 million, or by 48.8%, compared to the nine months of 2009. Gas products sales revenue increased by $352 million, or by 50.4%, primarily as a result of an increase in sales prices. Retail gas product revenue increased up to $360 million, or by 21.5%, due to price growth. Retail revenue represented 37.6% and 46.9% of our total gas product revenue in the nine months of 2010 and 2009, respectively.

Natural gas sales revenue amounted to $636 million – an increase of 43.6%, compared to the same period of 2009. Our domestic natural gas sales revenue significantly increased as a result of increased gas production. Natural gas sales revenue outside of Russia increased in the nine month of 2010 as a result of a revision of sale prices related to the Shakh-Deniz field for 2008-2010 which led to additional revenue of $101 million, recognized in the third quarter of 2010.

The major purchaser of our natural gas produced in the Russian Federation is Gazprom. In the nine months of 2010, we sold 6,072 million cubic meters of natural gas to Gazprom (4,208 million cubic meters in the nine months of 2009). The average realized price increased by 7.4% to $35.00 per 1,000 cubic meters as a result of the ruble appreciation.

Sales of energy and related services

We have been developing our power generation business since the acquisition of TGK-8 in 2008. As a result, in the nine months of 2010, our revenue from sales of electricity, heat and related services increased by $271 million, or by 35.9%. The ruble appreciation also contributed to the increase of this revenue. Substantially we sell energy and related services domestically. International sales are relatively insignificant.

Sales of other products

Other sales include non-petroleum sales through our retail network, and revenue of our production and marketing companies from sales of other services and goods not related to our primary activities (such as transportation, etc.).

In the nine months of 2010, our other sales increased by $25 million, or by 2.1%. A decrease of transportation services provided abroad was compensated by higher non-petroleum retail revenue. During the nine months of 2010, sales of goods and other products from our retail stations amounted to $467 million, an increase of $48 million from the level of the nine months of 2009.

Operating expenses

Operating expenses include the following:

	9 months of	
	2010	**2009**
	(millions of US dollars)	
Hydrocarbon extraction expenses	2,388	1,989
Own refining expenses	778	670
Refining expenses at third party and affiliated refineries	534	493
Expenses for crude oil transportation to refineries	802	709
Power generation and distribution expenses	452	313
Petrochemical expenses	138	90
Other operating expenses	1,073	1,016
	6,165	**5,280**
Change in operating expenses in crude oil and refined products inventory originating within the Group(1)	(171)	(265)
Total operating expenses	**5,994**	**5,015**

(1) The change in operating expenses in crude oil and refined products inventory originating within the Group includes extraction and refining expenses related to crude oil and refined products produced by the Group during the reporting period, but not sold to third party.

Compared to the nine months of 2009, our operating expenses increased by $979 million, or by 19.5%, which is mainly explained by general increase in operating expenses in Russia due to the real ruble appreciation against the US dollar by 14.3%, increase in hydrocarbon extraction expenses, refining expenses and power generation and distribution expenses.

Hydrocarbon extraction expenses

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

In the nine months of 2010, our extraction expenses increased by $399 million, or by 20.1%, compared to the nine months of 2009. This was mainly a result of the real ruble appreciation against the US dollar, increased expenses for power supply, artificial stimulation of reservoirs, labor costs and an increase in other expenses. Our average hydrocarbon extraction cost increased from $3.39 to $4.04 per BOE, or by 19.2%, compared to the nine months of 2009.

Own refining expenses

In the nine months of 2010, our own refining expenses increased by $108 million, or by 16.1%, compared to the nine months of 2009.

Refining expenses at our domestic refineries increased by 17.8%, or by $86 million, mainly as a result of the real ruble appreciation against the US dollar, increase in power supply costs and higher consumption of additives.

Refining expenses at our international refineries increased by 11.8%, or by $22 million, mainly as a result of increased power supply costs.

Refining expenses at third party and affiliated refineries

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

As opposed to 2009, we did not process crude oil on third party refineries during the nine months of 2010 in Russia and Belarus. Nevertheless, as a result of commencement of crude oil refining at TRN we increased our throughput at third party and affiliated refineries by 6.7%, compared to the nine months of 2009 (including refined products processed). Thus, in the nine months of 2010, refining expenses at third party and affiliated refineries increased by 8.3%, compared to the nine months of 2009. Processing cost at our refineries in Western Europe is higher than at the refineries in Russia or Belarus.

Petrochemical expenses

In the nine months of 2010, operating expenses of our petrochemical plants increased by $48 million, or by 53.3%, compared to the nine months of 2009. Expenses in Russia were impacted by increased production, increased cost of raw materials and ruble appreciation to the US dollar. Despite petrochemical capacity downtime in Bulgaria and Ukraine in the nine months of 2010, the decrease of our international petrochemical operating expenses compared to the nine months of 2009 was insignificant due to sizeable share of fixed costs.

In the fourth quarter of 2010, we commenced production in our petrochemical plant Karpatnaftochim Ltd. in Ukraine after modernization and construction of a chlorine and caustic production line. Some operating expenses related to undertaken pre-start works were recognized in the third quarter of 2010.

Expenses for crude oil transportation to refineries

Expenses for crude oil transportation to refineries increased in the nine months of 2010 by $93 million, or by 13.1%, compared to the nine months of 2009, due to an increase in transportation tariff rates and as a result of the real ruble appreciation in Russia (see Transportation expenses below). Moreover, in 2010, we commenced supplying our crude oil to the TRN refinery.

Power generation and distribution expenses

Power generation and distribution expenses increased by $139 million, or by 44.4%, reflecting expansion of our power generating business and as a result of the real ruble appreciation in Russia.

Other operating expenses

Other operating expenses include expenses of the Group's upstream and downstream enterprises that do not relate to their core activities, namely sales of transportation services, other goods, etc., operating expenses of our gas processing plants, costs of other services provided and goods sold by our marketing companies, and of non-core businesses of the Group.

In the nine months of 2010, our other operating expenses increased by $57 million, or by 5.6%, compared to the nine months of 2009.

Cost of purchased crude oil, gas and products

Cost of purchased crude oil, gas and products increased by $9,698 million in the nine months of 2010, or by 45.2%, compared to the same period of 2009, due to an increase in crude oil and refined products prices and increase in volumes of refined products purchases.

Cost of purchased crude oil, gas and products includes the result of hedging of international crude oil and refined products sales. In the nine months of 2010, we recognized a $60 million gain from hedging, compared to a $525 million expense in the nine months of 2009.

Cost of purchased crude oil, gas and products includes purchases of natural gas and fuel oil to supply our power generation segment entities.

Transportation expenses

In the nine months of 2010, our transportation expenses increased by $575 million, or by 16.0%, compared to the nine months of 2009. This was primarily due to increase of ruble denominated pipeline and railway transportation tariffs in Russia, which was emphasized by the ruble appreciation.

Our actual transportation expenses related to crude oil and refined products deliveries to various export destinations, weighted by volumes transported, changed in the nine months of 2010, compared to the nine months of 2009, as follows: crude oil pipeline tariffs increased by 24.2%, railway tariffs for refined products transportation increased by 25.7%, crude oil freight rates decreased by 13.4% and refined products freight rates increased by 7.5%.

Selling, general and administrative expenses

Selling, general and administrative expenses include general business expenses, 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.

In the nine months of 2010, our selling, general and administrative expenses increased by $159 million, or by 6.6%, compared to the nine months of 2009, substantially due to the effect of ruble appreciation on selling, general and administrative expenses in Russia. Besides, our selling, general and administrative expenses were affected by an increase in expenses for personnel compensation.

Depreciation, depletion and amortization

Depreciation, depletion and amortization expenses include depletion of assets fundamental to production, depreciation of other productive and non-productive assets and certain intangible assets.

Our depreciation, depletion and amortization expenses increased by $113 million, or by 3.8%, compared to the nine months of 2009.

Exploration expenses

During the nine months of 2010, exploration expense decreased by $13 million, or 6.9%, compared to the nine months of 2009. Dry hole costs decreased by $17 million to $97 million.

Interest expense

In the nine months of 2010, interest expense increased by $32 million, which is 6.4% more than in the respective period of the previous year. This increase mainly relates to discounting of the VAT recoverable of our refinery in Ukraine as a result of the restructuring of this receivable.

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 Europe. Our largest affiliates are Turgai Petroleum, an exploration and production company operating in Kazakhstan, and ISAB and TRN refineries.

At the end of 2009, we increased our share in LUKARCO from 54% to 100%, thus increasing our stake in Tengizchevroil, an exploration and production joint-venture in Kazakhstan, to 5%. As a result, our share in income of affiliates increased by $65 million, or by 24.1%.

Other non-operating income

In the nine months of 2010, other non-operating income included a $438 million gain related to successful settlement of a corporate dispute between a Group company and a CNPC group company regarding Turgai Petroleum, and an $111 million expense related to provisions accrued in respect of claims to the Group companies by Federal Anti-monopoly Service of the Russian Federation (FAS of Russia). All these amounts were recognized by the Group in the third quarter of 2010.

Taxes other than income taxes

	9 months of	
	2010	**2009**
	(millions of US dollars)	
In Russia		
Mineral extraction taxes	5,611	3,751
Social security taxes and contributions	286	277
Property tax	359	311
Other taxes	69	63
Total in Russia	**6,325**	**4,402**
International		
Mineral extraction taxes	53	39
Social security taxes and contributions	75	48
Property tax	31	24
Other taxes	38	56
Total internationally	**197**	**167**
Total	**6,522**	**4,569**

In the nine months of 2010, taxes other than income taxes increased by 42.7%, or by $1,953 million, compared to the nine months of 2009, mainly due to an increase in mineral extraction taxes in Russia. This is explained by an increase in the tax rate following the increase of international crude oil prices. Application of zero tax rate for crude oil produced in Timan-Pechora and decreased rate for depleted oilfields led to approximately $1,010 million tax reduction (in the nine months of 2009 – about $630 million).

Excise and export tariffs

	9 months of	
	2010	**2009**
	(millions of US dollars)	
In Russia		
Excise tax on refined products	685	559
Crude oil export tariffs	7,896	4,268
Refined products export tariffs	2,680	1,623
Total in Russia	**11,261**	**6,450**
International		
Excise tax and sales taxes on refined products	2,722	2,603
Crude oil export tariffs	85	64
Refined products export tariffs	4	59
Total internationally	**2,811**	**2,726**
Total	**14,072**	**9,176**

In spite of a decrease in crude oil and refined products export volumes, export tariffs increased by $4,651 million, or by 77.3%, compared to the nine months of 2009, due to an increase in tariff rates in Russia as a result of international crude oil prices growth. The increase in excises in Russia resulted from the ruble appreciation, increase of excise rate and increase in sales volumes.

Starting from the end of 2009, for crude oil produced at certain fields in Eastern Siberia a reduced export duty rate was set. Currently this benefit does not apply to crude oil production at our new oilfields in Caspian Sea and the Nenetsky Autonomous District. We expect that starting from December, 2010 the Group will apply reduced export duty rate for the crude oil produced from the Yu. Korchagin field.

Income taxes

In the nine months of 2010, our total income tax expense increased by $107 million, or by 6.9%, compared to the nine months of 2009. Income before income tax increased by $1,620 million, or by 23.2%.

In the nine months of 2010, our effective income tax rate was 19.3%, compared to 22.3% in the nine months of 2009, while the maximum statutory rate for the Russian Federation is 20%. Relatively low level of the effective income tax rate in the nine months of 2009 was attributable mostly to a $438 million non-taxable gain related to successful settlement of a corporate dispute between a Group company and a CNPC group company regarding Turgai Petroleum.

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

	9 months of	
	2010	**2009**
	(millions of US dollars)	
Net income attributable to OAO LUKOIL	**6,820**	**5,285**
Add back:		
Income tax expense	1,660	1,553
Depreciation and amortization	3,114	3,001
Interest expense	535	503
Interest and dividend income	(144)	(105)
EBITDA	**11,985**	**10,237**

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.

Three months ended September 30, 2010, compared to three months ended September 30, 2009

The table below represents our consolidated statements of income for the periods indicated.

	3rd quarter of 2010	3rd quarter of 2009
	(millions of US dollars)	
Revenues		
Sales (including excise and export tariffs)	26,517	21,941
Costs and other deductions		
Operating expenses	(2,192)	(1,907)
Cost of purchased crude oil, gas and products	(10,898)	(8,203)
Transportation expenses	(1,389)	(1,238)
Selling, general and administrative expenses	(902)	(878)
Depreciation, depletion and amortization	(1,054)	(998)
Taxes other than income taxes	(2,173)	(1,976)
Excise and export tariffs	(4,732)	(3,769)
Exploration expense	(29)	(119)
Gain on disposals and impairments of assets	19	3
Income from operating activities	**3,167**	**2,856**
Interest expense	(162)	(169)
Interest and dividend income	46	40
Equity share in income of affiliates	99	88
Currency translation loss	(59)	(213)
Other non-operating income (expense)	300	(24)
Income before income taxes	**3,391**	**2,578**
Current income taxes	(538)	(593)
Deferred income taxes	(26)	73
Total income tax expense	**(564)**	**(520)**
Net income	**2,827**	**2,058**
Less: net income attributable to noncontrolling interests	(9)	(2)
Net income attributable to OAO LUKOIL	**2,818**	**2,056**
Basic and diluted earning per share of common stock attributable to OAO LUKOIL (in US dollars)	3.46	2.43

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

Sales revenues

Sales breakdown	**3rd quarter of 2010**	**3rd quarter of 2009**
	(millions of US dollars)	
Crude oil		
Export and sales on international markets other than CIS	6,453	4,924
Export and sales to CIS	210	408
Domestic sales	225	429
	6,888	**5,761**
Refined products		
Export and sales on international markets		
Wholesale	12,487	9,997
Retail	2,498	2,506
Domestic sales		
Wholesale	1,463	1,047
Retail	1,508	1,232
	17,956	**14,782**
Petrochemicals		
Export and sales on international markets	128	158
Domestic sales	170	162
	298	**320**
Gas and gas products		
Export and sales on international markets	492	298
Domestic sales	202	148
	694	**446**
Sales of energy and related services	**295**	**229**
Other		
Sales on international markets	218	254
Domestic sales	168	149
	386	**403**
Total sales	**26,517**	**21,941**

Sales volumes	**3rd quarter of 2010**	**3rd quarter of 2009**
Crude oil	(thousands of barrels)	
Export and sales on international markets other than CIS	85,394	72,553
Export and sales to CIS	5,101	8,891
Domestic sales	6,223	13,231
	96,718	**94,675**
Crude oil	(thousands of tonnes)	
Export and sales on international markets other than CIS	11,650	9,898
Export and sales to CIS	696	1,213
Domestic sales	849	1,805
	13,195	**12,916**
Refined products	(thousands of tonnes)	
Export and sales on international markets		
Wholesale	20,554	18,517
Retail	1,908	2,051
Domestic sales		
Wholesale	3,033	2,462
Retail	1,895	1,716
	27,390	**24,746**
Total sales volume of crude oil and refined products	**40,585**	**37,662**

Realized average sales prices

	3rd quarter of			
	2010		2009	
	($/barrel)	($/tonne)	($/barrel)	($/tonne)
Average realized price international				
Oil (excluding CIS)	75.57	553.91	67.87	497.46
Oil (CIS)	41.21	302.08	45.91	336.49
Refined products				
Wholesale		607.56		539.86
Retail		1,309.77		1,222.21
Average realized price within Russia				
Oil	36.11	264.68	32.46	237.92
Refined products				
Wholesale		481.69		425.28
Retail		796.48		718.16

During the third quarter of 2010, our revenues increased by $4,576 million, or by 20.9%, compared to the same period of 2009. Our revenues from crude oil sales increased by $1,127 million, or by 19.6%. Our revenues from sales of refined products increased by $3,174 million, or by 21.5%. The increase in sales revenue was a result of an increase in hydrocarbon prices and volumes, compared to the third quarter of 2009. Moreover, the appreciation of the ruble against the US dollar also increased the US dollar value of our sales revenue denominated in Russian rubles.

Sales of crude oil

Our total crude oil sales revenues increased by 19.6% due to growth of crude oil prices. Sales volumes were 2.2% higher, compared to the respective period of 2009. The increase of international sales volumes resulted from a decrease of crude oil stock in the third quarter of 2010, whereas in the third quarter of 2009 crude oil stock increased. The decrease of sales volumes in Russia is explained by relatively high sale volumes in the third quarter of 2009 when we doubled our domestic sales in order to benefit from current market conditions.

Sales of refined products

In the third quarter of 2010, our revenue from the wholesale of refined products outside of Russia increased by $2,490 million, or by 24.9%, compared to the same period of 2009, primarily due to increased sales volumes and prices. The volumes increased by 11.0% as a result of a commencement of crude oil refining at TRN, an increase in output at our refineries in Bulgaria and Ukraine and increased trading activities. The sales prices increased by 12.5%.

In the third quarter of 2010, our revenue from international retail sales remained on the level of the third quarter of 2009. Average retail prices increased by 7.2%. However, sales volumes decreased by 7.0% mainly due to restructuring of our retail network in the USA.

In the third quarter of 2010, our revenue from the wholesale of refined products on the domestic market increased by $416 million, or by 39.7%, compared to the third quarter of 2009, due to an increase in the average realized price by 13.3% and in sales volumes by 571 thousand tonnes, or by 23.2%, as a result of lower volumes of refined products export from Russia and increased production of domestic refineries.

In the third quarter of 2010, our revenue from retail sales in Russia increased by $276 million, or by 22.4%, compared to the third quarter of 2009, due to an increase both in volumes, being a result of higher average daily sales per petrol station, and an increase in prices. In the third quarter of 2010, our retail sales revenue was 50.8% of total refined products sales in Russia (in the third quarter of 2009 – 54.1%).

Sales of petrochemical products

In the third quarter of 2010, our revenue from sales of petrochemical products decreased by $22 million, or by 6.9%, compared to the third quarter of 2009. This resulted from a decrease in sales volumes due to lower level of trading activities that outweighed the effect of price growth.

Sales of gas and gas products

In the third quarter of 2010, sales of gas and gas refined products increased by $248 million, or by 55.6%, compared to the third quarter of 2009. Gas products sales revenue increased by $94 million, or by 30.9%, as a result of increase in sales prices and volumes. Retail gas product revenue increased up to $138 million, or by 11.7%, due to price growth. Retail revenue represented 37.9% and 44.8% of our total gas product revenue in the third quarters of 2010 and 2009, respectively.

Natural gas sales revenue amounted to $282 million – an increase of 108.9%, compared to the same period of 2009. Our domestic natural gas sales revenue significantly increased as a result of increased gas production. Natural gas sales revenue outside of Russia increased in the third quarter of 2010 as a result of a revision of sale prices related to the Shakh-Deniz field for 2008-2010 which led to additional revenue of $101 million.

In the third quarter of 2010, we sold 1,962 million cubic meters of natural gas to Gazprom (1,258 million cubic meters in the third quarter of 2009). The average realized price increased by 1.7% to $34.55 per 1,000 cubic meters.

Sales of energy and related services

In the third quarter of 2010, our revenue from sales of electricity, heat and related services increased by $66 million, or by 28.8%, as a result of expansion of our power generation and distribution segment. The ruble appreciation also contributed to an increase of this revenue. Substantially we sell energy and related services domestically. International sales are relatively insignificant.

Operating expenses

Operating expenses include the following:

	3rd quarter of	
	2010	**2009**
	(millions of US dollars)	
Hydrocarbon extraction expenses	804	722
Own refining expenses	263	235
Refining expenses at third party and affiliated refineries	183	165
Expenses for crude oil transportation to refineries	261	244
Power generation and distribution expenses	159	113
Petrochemical expenses	58	36
Other operating expenses	403	365
	2,131	**1,880**
Change in operating expenses in crude oil and refined products inventory originating within the Group[(1)]	61	27
Total operating expenses	**2,192**	**1,907**

[(1)] The change in operating expenses in crude oil and refined products inventory originating within the Group includes extraction and refining expenses related to crude oil and refined products produced by the Group during the reporting period, but not sold to third party.

Compared to the third quarter of 2009, our operating expenses increased by $285 million, or by 14.9%, as a result of general increase in operating expenses in Russia due to the ruble appreciation against the US dollar, increase in hydrocarbon extraction expenses and power generation and distribution expenses.

Hydrocarbon extraction expenses

In the third quarter of 2010, our extraction expenses increased by $82 million, or by 11.4%, compared to the third quarter of 2009. The increase was mainly a result of the real ruble appreciation against the US dollar, increased expenses for power supply, artificial stimulation of reservoirs, labor costs, and an increase in other expenses. Our average hydrocarbon extraction cost increased from $3.67 to $4.08 per BOE, or by 11.1%, compared to the third quarter of 2009.

Own refining expenses

In the third quarter of 2010, our own refining expenses increased by $28 million, or by 11.9%, compared to the third quarter of 2009.

Refining expenses at our domestic refineries increased by 8.0%, or by $14 million, mainly as a result of the real ruble appreciation against the US dollar, increased expenses for power supply and higher consumption of additives.

Refining expenses at our international refineries increased by 23.3%, or by $14 million, as a result of increased production in the third quarter of 2010.

Refining expenses at third party and affiliated refineries

As opposed to 2009, we did not process crude oil on third party refineries in Russia and Belarus in the third quarter of 2010. However, we commenced crude oil refining at TRN that compensated decrease in processing volumes at third party refineries. In the third quarter of 2010, we also started crude oil refining at third party refinery in Kazakhstan, though processed volumes and associated cost were not significant.

As a result of commencement of crude oil refining at TRN refining expenses at third party and affiliated refineries increased by 10.9%, compared to the third quarter of 2009.

Petrochemical expenses

In the third quarter of 2010, operating expenses of our petrochemical plants increased by $22 million, or by 61.1%, compared to the third quarter of 2009 as a result of increased cost of raw materials and ruble appreciation to the US dollar.

In the fourth quarter of 2010, we commenced production in our petrochemical plant Karpatnaftochim Ltd. in Ukraine after modernization and construction of a chlorine and caustic production line. Some operating expenses related to undertaken pre-start works were recognized in the third quarter of 2010.

Expenses for crude oil transportation to refineries

Expenses for crude oil transportation to refineries increased in the third quarter of 2010 by $17 million, or by 7.0%, compared to the third quarter of 2009, due to an increase in transportation tariff rates and as a result of the real ruble appreciation in Russia (see Transportation expenses below). Besides, expenses for crude oil transportation to refineries in the third quarter of 2010 included expenses for supplying our crude oil to TRN.

Power generation and distribution expenses

Power generation and distribution expenses increased by $46 million, or by 40.7%, reflecting expansion of our power generation business emphasized by the real ruble appreciation in Russia.

Other operating expenses

In the third quarter of 2010, our other operating expenses increased by $38 million, or by 10.4%, compared to the third quarter of 2009.

Cost of purchased crude oil, gas and products

Cost of purchased crude oil, gas and products increased by $2,695 million in the third quarter of 2010, or by 32.9%, compared to the same period of 2009, due to an increase in crude oil and refined products prices and increase in volumes of purchased refined products.

Cost of purchased crude oil, gas and products includes the result of hedging of international crude oil and refined products sales. In the third quarter of 2010, we recognized a $187 million loss from hedging, compared to a $17 million gain in the third quarter of 2009.

Cost of purchased crude oil, gas and products includes purchases of natural gas and fuel oil to supply our power generation segment entities.

Transportation expenses

In the third quarter of 2010, our transportation expenses increased by $151 million, or by 12.2%, compared to the third quarter of 2009. This was primarily due to an increase in volumes of crude oil and products transported outside of Russia and an increase in ruble denominated pipeline and railway transportation tariffs in Russia, which was emphasized by the ruble appreciation.

Selling, general and administrative expenses

Despite the adverse effect of ruble appreciation, our selling, general and administrative expenses did not change significantly. The increase to the third quarter of 2009 amounted to $24 million, or 2.7%, and was largely due to higher expenses for personnel compensation.

Depreciation, depletion and amortization

Our depreciation, depletion and amortization expenses increased by $56 million, or by 5.6%, compared to the third quarter of 2009.

Interest expense

In the third quarter of 2010, interest expense decreased by $7 million, or by 4.1% compared to respective period of the previous year.

Equity share in income of affiliates

Compared to the third quarter of 2009, our share in income of affiliates increased by $11 million, or by 12.5%. This was primarily due to the changes in affiliates structure.

Other non-operating income

In the third quarter of 2010, other non-operating income included a $438 million gain related to successful settlement of a corporate dispute between a Group company and a CNPC group company regarding Turgai Petroleum and a $111 million expense related to provisions accrued in respect of claims to the Group companies by FAS of Russia.

Taxes other than income taxes

	3rd quarter of	
	2010	**2009**
	(millions of US dollars)	
In Russia		
Mineral extraction taxes	1,888	1,704
Social security taxes and contributions	83	76
Property tax	121	114
Other taxes	11	25
Total in Russia	**2,103**	**1,919**
International		
Mineral extraction taxes	19	16
Social security taxes and contributions	27	17
Property tax	13	9
Other taxes	11	15
Total internationally	**70**	**57**
Total	**2,173**	**1,976**

In the third quarter of 2010, taxes other than income taxes increased by 10.0%, or by $197 million, compared to the third quarter of 2009, mainly due to an increase in mineral extraction taxes in Russia. This is explained by an increase in the tax rate following the increase of international crude oil prices. Application of zero tax rate for crude oil produced in Timan-Pechora and decreased rate for depleted oilfields led to approximately $332 million tax reduction (in the third quarter of 2009 – about $280 million).

Excise and export tariffs

	3rd quarter of	
	2010	**2009**
	(millions of US dollars)	
In Russia		
Excise tax on refined products	250	207
Crude oil export tariffs	2,533	1,898
Refined products export tariffs	928	696
Total in Russia	**3,711**	**2,801**
International		
Excise tax and sales taxes on refined products	990	923
Crude oil export tariffs	31	24
Refined products export tariffs	–	21
Total internationally	**1,021**	**968**
Total	**4,732**	**3,769**

In spite of a decrease in crude oil and refined products export volumes, export tariffs increased by $853 million, or by 32.3%, compared to the third quarter of 2009, due to an increase in tariff rates in Russia as a result of international crude oil prices growth. The increase in excises in Russia was due to the ruble appreciation, increase of excise rate and increase in sales volumes.

Starting from the end of 2009, for crude oil produced at certain fields in Eastern Siberia a reduced export duty rate was set. Currently this benefit does not apply to crude oil production at our new oilfields in Caspian Sea and the Nenetsky Autonomous District. We expect that starting from December, 2010 the Group will apply reduced export duty rate for the crude oil produced from the Yu. Korchagin field.

Income taxes

In the third quarter of 2010, our total income tax expense increased by $44 million, or by 8.5%, compared to the third quarter of 2009. Income before income tax increased by $813 million, or by 31.5%.

In the third quarter of 2010, our effective income tax rate was 16.6%, compared to 20.2% in the third quarter of 2009. Maximum statutory rate for the Russian Federation is 20%. Relatively low level of the effective income tax rate in the nine months of 2009 was attributable mostly to a $438 million non-taxable gain related to successful settlement of a corporate dispute between a Group company and a CNPC group company regarding Turgai Petroleum, and effect of currency translation differences taxable according to Russian legislation.

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

	3rd quarter of	
	2010	**2009**
	(millions of US dollars)	
Net income attributable to OAO LUKOIL	**2,818**	**2,056**
Add back:		
Income tax expense	564	520
Depreciation and amortization	1,054	998
Interest expense	162	169
Interest and dividend income	(46)	(40)
EBITDA	**4,552**	**3,703**

Liquidity and capital resources

	9 months of 2010	2009
	(millions of US dollars)	
Net cash provided by operating activities	11,632	6,073
Net cash used in investing activities	(4,625)	(6,367)
Net cash used in financing activities	(6,158)	(468)

Operating activities

Our primary source of cash flow is funds generated from our operations. During the nine months of 2010, cash generated by operating activities was $11,632 million, which is nearly twice as much as in the same period of 2009, mainly due to a decrease in working capital by $1,023 million, compared to January 1, 2010 (as opposed to the nine months of 2009, when our working capital increased by $2,255 million). Besides, our cash provided by operating activities was impacted by increase in revenue.

The decrease of working capital was mainly caused by:

- a $440 million net decrease in tax accounts receivable;
- a $628 million net decrease in VAT accounts receivable;
- a $112 million net decrease in trade accounts receivable and payable.
- a $151 million net decrease in other assets and liabilities

At the same time, the effect from the above mentioned factors was partly offset by an increase in inventory of $308 million.

Investing activities

The decrease in cash used in investing activities resulted from a decrease in payments for acquisitions by $1,975 million.

In the nine months of 2009, we paid the remaining amount of $1,066 million for the acquisition of a 49% stake in the ISAB refinery complex, approximately $600 million within the acquisition of 45% interest in the TRN refinery, and settled a $150 million liability within the acquisition of Akpet. Other acquisitions refer to advances for downstream assets in Russia.

Financing activities

In the nine months of 2010, net movements of short-term and long-term debt generated an outflow of $657 million, compared to an inflow of $582 million in the nine months of 2009.

In August 2010, we raised a $1.5 billion loan facility from a group of banks. The facility was partially prepaid in November 2010 in amount of $1.0 billion.

In August 2010, we purchased approximately 7.599% of our shares at $53.25 per share for approximately $3.44 billion from ConocoPhillips.

As a part of Company's shares purchase option from ConocoPhillips, in September 2010 a Group company purchased a series of equity-linked notes exchangeable for 17,500,000 LUKOIL ADRs issued by UniCredit Bank AG for approximately $980 million.

In November 2010, we completed the issuance of a dual-tranche offering of 6.125% notes due 2020 in aggregate principal amount of $1 billion. The notes were issued in two tranches at the same time and form part of the same series. $800 million of the notes were issued at a price of 99.081% of their face value, resulting in a yield to maturity of 6.25%, and $200 million of the notes were issued at a price of 102.44% of their face value, resulting in a yield to maturity of 5.80%.

In June 2009, we completed offering of three series of stock exchange bonds on MICEX, altogether worth 15 billion rubles. Coupon rate for each of the issues was set at 13.5%. The bonds had maturity period of 364 days and were repaid in June 2010.

In February 2009, we received short-term loans of $500 million and 17 billion rubles from Sberbank to finance our working capital. Also, in the first quarter of 2009, we received a long-term loan of €1,000 million from Gazprombank. All these loans were repaid in 2009.

Analysis of capital expenditures

	9 months of		3rd quarter of	
	2010	2009	2010	2009
	(millions of US dollars)			
Capital expenditures(1)				
Exploration and production				
Russia	2,712	2,939	874	1,040
International	762	529	210	187
Total exploration and production	3,474	3,468	1,084	1,227
Refining, marketing and distribution				
Russia	617	558	238	215
International	226	345	73	81
Total refining, marketing and distribution	843	903	311	296
Chemicals				
Russia	17	9	5	3
International	42	80	11	25
Total chemicals	59	89	16	28
Power generation and distribution	298	177	98	66
Other	45	46	20	26
Total capital expenditures	**4,719**	**4,683**	**1,529**	**1,643**
Acquisitions of subsidiaries (2)				
Exploration and production				
Russia	3	–	–	–
International	–	–	–	–
Total exploration and production	3	–	–	–
Refining, marketing and distribution				
Russia	50	210	–	2
International	3	1,820	3	256
Total refining, marketing and distribution	53	2,030	3	258
Power generation and distribution	–	10	–	–
Less cash acquired	–	(9)	–	–
Total acquisitions	**56**	**2,031**	**3**	**258**

(1) Including non-cash transactions and prepayments.
(2) Including prepayments related to acquisitions of subsidiaries and non-cash transactions.

During the nine months of 2010, our capital expenditures, including non-cash transactions, remained on the level of the respective period of the previous year. Our capital expenditures in exploration and production also did no change, compared to the respective period of 2009. The decrease in capital expenditures in exploration and production segment in new regions was compensated by the increase in such capital expenditures in European Russia and abroad. Our capital expenditures in Iraq for the nine months of 2010 included payment of $112 million non-recoverable signature bonus for entering West Qurnah-2 project.

Capital expenses of our power generation and distribution entities related to fulfillment of their investment program.

The table below shows our exploration and production capital expenditures in promising new production regions. In April 2010, we started commercial production on the Yu. Korchagin field in the Caspian Sea. Maximum annual production from this field is expected to be 2.5 million tonnes of oil and gas condensate, and 1.0 billion cubic meters of gas.

	9 months of		3rd quarter of	
	2010	2009	2010	2009
	(millions of US dollars)			
Northern Timan-Pechora	185	307	56	74
Yamal	126	106	35	24
Caspian region(1)	252	438	87	230
Total	**563**	**851**	**178**	**328**

(1) Russian and international projects.