OPEN JOINT STOCK COMPANY “DOROGOBUZH”

International Financial Reporting Standards Consolidated Financial Statements and Auditor’s Report

31 December 2006

Contents

ZAO PricewaterhouseCoopers Audit
Kosmodamianskaya Nab. 52, Bld. 5
115054 Moscow
Russia
Telephone +7 (495) 967 6000
Facsimile +7 (495) 967 6001

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Open Joint Stock Company "Dorogobuzh"

1 We have audited the accompanying consolidated financial statements of Open Joint Stock Company "Dorogobuzh" and its subsidiaries (the "Group") which comprise the consolidated balance sheet as at 31 December 2006 and the consolidated income statement, consolidated statement of changes in equity and consolidated statement of cashflows for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

2 Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

3 Our responsibility is to express an opinion on these consolidated financial statements based on our audit. Except as discussed below, we conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

4 An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

5 We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

INDEPENDENT AUDITOR'S REPORT

Basis for Qualified Opinion

6 The ultimate controlling party of the Group is not disclosed in these consolidated financial statements which in our opinion is not in compliance with IAS 24 "Related party disclosures", (Revised).

Qualified Opinion

7 In our opinion, except for the omission of the information discussed in the Basis for Qualified Opinion paragraph 6, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group at 31 December 2006 and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

ZAO PricewaterhouseCoopers Audit

Moscow, Russian Federation

15 June 2007

(in thousands of Russian Roubles, except for per share amounts)

	Note	2006	2005
ASSETS			
Non-current assets			
Property, plant and equipment	13	3,085,532	2,453,823
Goodwill	14	52,068	-
Available-for-sale investments	15	2,790,118	2,548,887
Long-term loans receivable	11	5,500	57,500
Total non-current assets		**5,933,218**	**5,060,210**
Current assets			
Inventories	12	827,134	758,696
Other current assets		50,529	21,232
Short-term loans receivable	11	247,500	25,000
Accounts receivable	10	978,558	685,628
Dividends receivable		41,816	27,625
Cash and cash equivalents	9	458,855	347,032
Total current assets		**2,604,392**	**1,865,213**
Total assets		**8,537,610**	**6,925,423**
SHAREHOLDERS’ EQUITY			
Shareholders’ equity			
Share capital	19	1,735,359	1,735,359
Share premium	19	93,794	93,794
Retained earnings		860,320	623,942
Revaluation reserve		2,092,624	1,910,257
Total shareholders’ equity		**4,782,097**	**4,363,352**
LIABILITIES			
Non-current liabilities			
Long-term borrowings	18	1,343,617	100,739
Other long-term liabilities		44,805	59,160
Deferred tax liability	23	902,113	860,888
Total non-current liabilities		**2,290,535**	**1,020,787**
Current liabilities			
Accounts payable	16	411,083	259,554
Current income tax payable		9,928	9,057
Other taxes payable	17	72,954	100,963
Short-term borrowings	18	600,000	904,255
Advances received	16	371,013	267,455
Total current liabilities		**1,464,978**	**1,541,284**
Total liabilities		**3,755,513**	**2,562,071**
Total liabilities and shareholders’ equity		**8,537,610**	**6,925,423**

Approved for issue and signed on behalf of the Board of Directors on 15 June 2007.

I.N. Antonov
President

N. I. Sluzhenikina
Chief Accountant

(in thousands of Russian Roubles, except for per share amounts)

	Note	2006	2005
Revenue	7	5,572,353	5,823,920
Cost of sales	20	(3,782,330)	(3,482,382)
Gross profit		**1,790,023**	**2,341,538**
Transportation services		(387,152)	(461,905)
Selling, general and administrative expenses	21	(667,764)	(634,446)
Taxes other than income tax		(35,387)	(34,770)
Loss on disposal of property, plant and equipment, net		(50,906)	(20,272)
Bonds issuance costs		-	(7,111)
Other operating expenses		(49,911)	(47,175)
Other income		80,385	118,631
Finance expense	22	(117,837)	(112,573)
Profit before taxation		**561,451**	**1,141,917**
Income tax expense	23	(178,832)	(269,649)
Net profit for the year		**382,619**	**872,268**
Weighted average number of ordinary shares outstanding during the period		721,182,860	721,182,860
Weighted average number of preference shares outstanding during the period		154,256,400	154,256,400
Basic and diluted earnings per ordinary share (in Russian Roubles per share)	24	**0.43**	**0.97**
Basic and diluted earnings per preference share (in Russian Roubles per share)	24	**0.47**	**1.12**

(in thousands of Russian Roubles, except for per share amounts)

	Note	2006	2005
Cash flows from operating activities			
Profit before taxation		561,451	1,141,917
Adjustments for:			
Depreciation	13	186,348	181,308
Loss on / (reversal of) impairment of accounts receivable		(5,894)	34,719
Increase in (release of) / provision for write-down on inventory		2,614	(16,725)
Loss on disposal of property, plant and equipment		50,906	20,272
Finance expense, net		117,837	112,573
Other income		(80,385)	(118,631)
Foreign exchange effect on non-operating items		(25,089)	18,004
Operating cash flows before working capital changes		**807,788**	**1,373,437**
Increase in trade receivables		(212,065)	(64,297)
Increase in advances to suppliers		(82,080)	(81,392)
Increase in other receivables		(30,510)	(75,158)
Increase in inventories		(71,052)	(80,423)
Increase / (decrease) in trade payables		78,378	(7,349)
Increase / (decrease) in advances from customers		103,558	(137,405)
Increase / (decrease) in other payables		35,755	(9,876)
Increase in other current assets		(29,297)	(2,975)
(Decrease) / increase in employee benefits obligation		(14,355)	14,273
Cash provided from operations:		**586,120**	**928,835**
Income taxes paid		(204,232)	(290,504)
Interest paid		(126,729)	(95,828)
Net cash provided from operating activities:		**255,159**	**542,503**
Cash flows from investing activities:			
Purchase of property, plant and equipment		(795,409)	(193,648)
Loans provided	11	(252,500)	(44,324)
Proceeds from loans repaid	11	82,000	-
Interest received		12,015	22,521
Dividends received		68,370	79,436
Proceeds from sale of property, plant and equipment		-	252
Net cash used in investing activities:		**(885,524)**	**(135,763)**
Cash flows from financing activities:			
Dividends paid		(221,524)	(375,537)
Proceeds from borrowings	18	1,486,877	1,633,412
Repayment of borrowings	18	(523,165)	(1,572,784)
Net cash provided from (used in) financing activities		**742,188**	**(314,909)**
Net increase in cash and cash equivalents		**111,823**	**91,831**
Cash and cash equivalents at the beginning of the year	9	**347,032**	**255,201**
Cash and cash equivalents at the end of the year	9	**458,855**	**347,032**

(in thousands of Russian Roubles, except for per share amounts)

	Capital and reserves attributable to the Company equity holders				
	Share capital (Note 19)	**Share premium**	**Retained earnings**	**Revaluation reserve**	**Total**
Balance at 1 January 2005	**1,735,359**	**93,794**	**273,813**	**724,795**	**2,827,761**
Available-for-sale investments:					
- Fair value gains less losses (Note 15)	-	-	-	1,559,818	1,559,818
Income tax recorded in equity (Note 23)	-	-	-	(374,356)	(374,356)
Net income recognised directly in equity	-	-	-	1,185,462	1,185,462
Profit for the year	-	-	872,268	-	872,268
Total recognised income for 2005	-	-	872,268	1,185,462	2,057,730
Dividends	-	-	(522,139)	-	(522,139)
Balance at 31 December 2005	**1,735,359**	**93,794**	**623,942**	**1,910,257**	**4,363,352**
Balance at 1 January 2006	**1,735,359**	**93,794**	**623,942**	**1,910,257**	**4,363,352**
Available-for-sale investments:					
- Fair value gains less losses (Note 15)	-	-	-	239,956	239,956
Income tax recorded in equity (Note 23)	-	-	-	(57,589)	(57,589)
Net income recognised directly in equity	-	-	-	182,367	182,367
Profit for the year	-	-	382,619	-	382,619
Total recognised income for 2006	-	-	382,619	182,367	564,986
Dividends	-	-	(146,241)	-	(146,241)
Balance at 31 December 2006	**1,735,359**	**93,794**	**860,320**	**2,092,624**	**4,782,097**

1 Dorogobuzh Group and Its Operations

These financial statements have been prepared in accordance with International Financial Reporting Standards for the year ended 31 December 2006 for Open Joint Stock Company "Dorogobuzh" (the "Company" or "Dorogobuzh") and its subsidiaries (together referred to as the "Group" or "Dorogobuzh Group").

The Group's principal activities include the manufacture, distribution and sales of chemical fertilisers and related by-products. The Group's manufacturing facilities are primarily based in the Smolenskaya oblast of Russia. Dorogobuzh was incorporated as a joint stock company on 27 July 1994. On that date the majority of assets and liabilities previously managed by the state were transferred to the Company. The transfer of assets and liabilities was made in accordance with Decree No. 721 on the privatisation of state companies approved on 1 July 1992.

The Group's immediate major shareholders at 31 December 2006 are Joint Stock Company "Acron" (further referred to as Parent company), ZAO "Nordic Rus Holding", and ZAO "Granit", holding 66.41%, 14.28% and 10.86% of voting share capital, respectively. The remaining 8.45% belong to shareholders each holding less than 5% of the Group's shares.

The Company's registered office is Verkhnedneprovsky, Smolenskaya oblast, 215753, Russia. In 2006 the Group had an average of 3,784 employees (2005: 3,661 employees).

2 Basis of Preparation of the Financial Statements

Basis of preparation. These consolidated financial statements have been prepared in accordance with, and comply with, International Financial Reporting Standards ("IFRS") under the historical cost convention except as modified by the fair value revaluation of available-for-sale investments. The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated (refer to Note 5, Adoption of New or Revised Standards and Interpretations).

Presentation currency. All amounts in these financial statements are presented in thousands of Russian Roubles ("RR thousands"), unless otherwise stated. The financial statements are based on the statutory records, with adjustments and reclassifications recorded for the purpose of fair presentation in accordance with IFRS.

Accounting for the effect of inflation. Prior to 1 January 2003 the adjustments and reclassifications made to the statutory records for the purpose of IFRS presentation included the restatement of balances and transactions for the changes in the general purchasing power of the RR in accordance with IAS 29, Financial Reporting in Hyperinflationary Economies. IAS 29 requires that the financial statements prepared in the currency of a hyperinflationary economy be stated in terms of the measuring unit current at the balance sheet date. As the characteristics of the economic environment of the Russian Federation indicate that hyperinflationary has ceased, effective from 1 January 2003 the Group no longer applies the provisions of IAS 29. Accordingly, the amounts expressed in the measuring unit current at 31 December 2002 are treated as the basis for the carrying amounts in these financial statements.

3 Summary of Significant Accounting Policies

3.1 Group accounting

Consolidated financial statements. Subsidiaries are those companies and other entities (including special purpose entities) in which the Group, directly or indirectly, has an interest of more than one half of the voting rights or otherwise has power to govern the financial and operating policies so as to obtain economic benefits. The existence and effect of potential voting rights that are presently exercisable or presently convertible are considered when assessing whether the Group controls another entity. Subsidiaries are consolidated from the date on which control is transferred to the Group (acquisition date) and are de-consolidated from the date that control ceases.

The purchase method of accounting is used to account for the acquisition of subsidiaries. The cost of an acquisition is measured at the fair value of the assets given up, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. The date of exchange is the acquisition date where a business combination is achieved in a single transaction, and is the date of each share purchase where a business combination is achieved in stages by successive share purchases.

3 Summary of Significant Accounting Policies (continued)

3.1 Group accounting (continued)

The excess of the cost of acquisition over the fair value of the net assets of the acquiree at each exchange transaction represents goodwill. The excess of the acquirer’s interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired over cost (”negative goodwill”) is recognised immediately in profit or loss. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured at their fair values at the acquisition date, irrespective of the extent of any minority interest.

Intercompany transactions, balances and unrealised gains on transactions between group companies are eliminated; unrealised losses are also eliminated unless the cost cannot be recovered. The Company and all of its subsidiaries use uniform accounting policies consistent with the Group’s policies.

Investments in associates. Associates are entities over which the Group has significant influence, but not control, generally accompanying a shareholding of between 20 and 50 percent of the voting rights. Investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The carrying amount of associates includes goodwill identified on acquisition less accumulated impairment losses, if any. The Group’s share of the post-acquisition profits or losses of associates is recorded in the consolidated income statement, and its share of post-acquisition movements in reserves is recognised in reserves. When the Group’s share of losses in an associate equals or exceeds its interest in the associate, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group’s interest in the associates; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

3.2 Cash and cash equivalents

Cash and cash equivalents includes cash in hand, deposits held at call with banks, and other short-term highly liquid investments with original maturities of three months or less. Cash and cash equivalents are carried at amortised cost using the effective interest method.

3.3 Trade and other receivables

Trade and other receivables are carried at amortised cost using the effective interest method. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the carrying amount and the recoverable amount, being the present value of estimated future cash flows, discounted at the original effective rate of interest. The amount of the provision is recognised in the income statement.

3.4 Value added tax

Output value added tax related to sales is payable to tax authorities upon delivery of the goods or services to customers. Input VAT is generally recoverable against output VAT upon receipt of the VAT invoice. The tax authorities permit the settlement of VAT on a net basis (except for export sales related input VAT which is reclaimable upon confirmation of export). VAT related to sales and purchases is recognized in the balance sheet on a gross basis and disclosed separately as an asset and liability. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT. The related VAT deferred liability is maintained until the debtor is written off for tax purposes.

3.5 Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost of inventory is determined on the weighted average basis. The cost of finished goods and work in progress comprises raw material, direct labour, other direct costs and related production overhead (based on normal operating capacity) but excludes borrowing costs. Net realisable value is the estimated selling price in the ordinary course of business, less the cost of completion and selling expenses.

(in thousands of Russian Roubles, except for per share amounts)

3 Summary of Significant Accounting Policies (continued)

3.6 Property, plant and equipment

Property, plant and equipment are recorded at cost, restated where applicable to the equivalent purchasing power of the Russian Rouble at 31 December 2002 for assets acquired prior to 1 January 2003, less accumulated depreciation and provision for impairment, where required.

At each reporting date the management assess whether there is any indication of impairment of property, plant and equipment. If any such indication exists, the management estimates the recoverable amount, which is determined as the higher of an asset's fair value less cost to sell and its value in use. The carrying amount is reduced to the recoverable amount and the difference is recognised as an expense (impairment loss) in the income statement. An impairment loss recognised for an asset in prior years is reversed if there has been a change in the estimates used to determine the assets recoverable amount. Gains and losses on disposals determined by comparing proceeds with carrying amount are recognised in the profit or loss.

Land is not depreciated. Depreciation is calculated to allocate cost of property, plant and equipment to their residual values on a straight-line basis. The depreciation periods, which approximate the estimated useful economic lives of the respective assets, are as follows:

	Number of years
Buildings	40 to 50
Plant and machinery	10 to 20
Other equipment and motor vehicles	5 to 20

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset were already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised and the assets replaced are retired. Gains and losses arising from the retirement or disposal of property, plant and equipment are included in the statement of income as incurred.

Borrowing costs on specific or general funds borrowed to finance the construction of qualifying asset are capitalised, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

3.7 Intangible assets

Goodwill. Goodwill represents the excess of the cost of an acquisition over the fair value of the acquirer's share of the net identifiable assets, liabilities and contingent liabilities of the acquired subsidiary or associate at the date of exchange.

Goodwill on acquisitions of subsidiaries is presented separately in the consolidated balance sheet. Goodwill on acquisitions of associates is included in the investment in associates. Goodwill is carried at cost less accumulated impairment losses, if any.

The Group tests goodwill for impairment at least annually and whenever there are indications that goodwill may be impaired. Goodwill is allocated to the acquirer's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the business combination. Such units or group of units represent the lowest level at which the Group monitors goodwill and are not larger than a segment. Gains or losses on disposal of an operation within a cash generating unit to which goodwill has been allocated include the carrying amount of goodwill associated with the operation disposed of, generally measured on the basis of the relative values of the operation disposed of and the portion of the cash-generating unit which is retained.

3 Summary of Significant Accounting Policies (continued)

3.7 Intangible assets (continued)

Research and development. Research expenditure is recognised as an expense as incurred. Costs incurred on development projects (relating to the design and testing of new or improved products) are recognised as intangible assets when it is probable that the project will be a success considering its commercial and technological feasibility, and costs can be measured reliably. Other development expenditures are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period. Development costs with a finite useful life that have been capitalised are amortised from the commencement of the commercial production of the product on a straight-line basis over the period of its expected benefit, on average over a period not exceeding 5 years.

Other intangible assets. All of the Group's other intangible assets have definite useful lives and primarily include capitalised computer software, patents, trademarks and licences. Acquired computer software licenses, patents and trademarks are capitalised on the basis of the costs incurred to acquire and bring them to use. Intangible assets are amortised using the straight-line method over their useful lives, but not exceeding 20 years.

3.8 Borrowings

Borrowings are stated at amortised cost using the effective yield method; any difference between fair value of the proceeds (net of transaction costs) and the redemption amount is recognised as interest expense over the period of the borrowings. Borrowing costs on specific or general funds borrowed to finance the construction of qualifying asset are capitalised, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

3.9 Income taxes

Income taxes have been provided for in the consolidated financial statements in accordance with Russian legislation enacted or substantively enacted by the balance sheet date. The income tax charge/credit comprises current tax and deferred tax and is recognised in the consolidated income statement unless it relates to transactions that are recognised, in the same or a different period, directly in equity. Corporate profit tax rate is 24% (2005:24%) for Russia, where the most significant Group subsidiaries are registered.

Current tax is the amount expected to be paid to or recovered from the taxation authorities in respect of taxable profits or losses for the current and prior periods. Taxes, other than on income, are recorded within operating expenses.

Deferred income tax is provided using the balance sheet liability method for tax loss carry forwards and temporary differences arising between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. In accordance with the initial recognition exemption, deferred taxes are not recorded for temporary differences on initial recognition of an asset or a liability in a transaction other than a business combination if the transaction, when initially recorded, affects neither accounting nor taxable profit. Deferred tax liabilities are not recorded for temporary differences on initial recognition of goodwill and subsequently for goodwill which is not deductible for tax purposes. Deferred tax balances are measured at tax rates enacted or substantively enacted at the balance sheet date which are expected to apply to the period when the temporary differences will reverse or the tax loss carry forwards will be utilised. Deferred tax assets and liabilities are netted only within the individual companies of the Group. Deferred tax assets for deductible temporary differences and tax loss carry forwards are recorded only to the extent that it is probable that future taxable profit will be available against which the deductions can be utilised.

Deferred income tax is provided on post acquisition retained earnings of subsidiaries, except where the Group controls the subsidiary's dividend policy and it is probable that the difference will not reverse through dividends or otherwise in the foreseeable future.

3 Summary of Significant Accounting Policies (continued)

3.10 Foreign currency transactions

Foreign currency translation. Functional currency of each of the Group's consolidated entities is the currency of the primary economic environment in which the entity operates. The Group's functional currency is the national currency of the Russian Federation, Russian Roubles ("RR").

Monetary assets and liabilities are translated into each entity's functional currency at the official exchange rate of the CBRF at the respective balance sheet dates. Foreign exchange gains and losses resulting from the settlement of the transactions and from the translation of monetary assets and liabilities into each entity's functional currency at year-end official exchange rates of the CBRF are recognised in profit or loss. Translation at year-end rates does not apply to non-monetary items, including equity investments. Effects of exchange rate changes on the fair value of equity securities are recorded as part of the fair value gain or loss.

3.11 Provisions for liabilities and charges

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made. Where the Group expects a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain.

Provisions are evaluated and re-estimated annually, and are included in the financial statements at their expected net present values using discount rates appropriate to the Company in the economic environment in the Russian Federation at each balance sheet date.

3.12 Shareholders' equity

Share capital. Ordinary and non-cumulative no redeemable preference shares are classified as equity. External costs directly attributable to the issue of new shares, other than on a business combination, are shown as a deduction in equity from the proceeds, net of tax. Any excess of the fair value of consideration received over the par value of shares issued is recognised as a share premium.

Treasury shares. Where any Group company purchases the Company's equity share capital, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Company's equity holders until the shares are cancelled, reissued or disposed of. Where such shares are subsequently sold or reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Company's equity holders.

Dividends. Dividends are recognised as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the financial statements are authorised for issue.

3.13 Revenue recognition

Revenues from sales of chemical fertilisers and related by-products are recognised at the point of transfer of risks and rewards of ownership of the goods, normally when the goods are shipped. If the Group agrees to transport goods to a specified location, revenue is recognised when the goods are passed to the customer at the destination point.

Sales of services are recognised in the accounting period in which the services are rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided. Sales are shown net of VAT, custom duties and discounts, and after eliminating sales within the Group. Revenues are measured at the fair value of the consideration received or receivable. When the fair value of consideration received cannot be measured reliably, the revenue is measured at the fair value of the goods or service given up.

3 Summary of Significant Accounting Policies (continued)

3.14 Mutual cancellations

A portion of sales and purchases are settled by mutual settlements or non-cash settlements. These transactions are generally in the form of direct settlements through cancellation of mutual trade receivables and payables balances within the operational contracts. Non-cash settlements include 'veksels' or 'bills of exchange', which are negotiable debt obligations. Sales and purchases that are expected to be settled by mutual settlements or other non-cash settlements are recognised based on the estimate of the fair value to be received or given up in non-cash settlements. The fair value is determined with reference to various market information. Non-cash transactions have been excluded from the cash flow statement, so investing activities, financing activities and the total of operating activities represent actual cash transactions.

The Group also accepts bills of exchange from its customers (both issued by customers and third parties) as a settlement of receivables. Bills of exchange issued by customers or issued by third parties are carried at amortised cost using the effective interest method. A provision for impairment of bills of exchange is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

3.15 Employee benefits

Wages, salaries, contributions to the Russian Federation state pension and social insurance funds, paid annual leave and sick leave, bonuses, and non-monetary benefits (such as health services and kindergarten services) are accrued in the year in which the associated services are rendered by the employees of the Group.

Social costs. The Group incurs significant costs on social activities. These costs include the provision of health services, kindergartens, and the subsidy of worker holidays. These amounts represent an implicit cost of employing principally production workers and, accordingly, have been charged to cost of sales.

Pension costs. In the normal course of business the Group contributes to state pension schemes on behalf of its employees. Mandatory contributions to the governmental pension scheme are accrued in the year in which the associated services are rendered by the employees of the Group.

3.16 Financial assets and liabilities.

Classification of financial assets. The Group classifies its financial assets into the following measurement categories: available-for-sale, held to maturity and loans and receivables.

Loans and receivables are unquoted non-derivative financial assets with fixed or determinable payments other than those that the Group intends to sell in the near term.

Held to maturity classification includes quoted non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has both the intention and ability to hold to maturity. Management determines the classification of investment securities held to maturity at their initial recognition and reassesses the appropriateness of that classification at each balance sheet date.

Initial recognition of financial instruments. Financial assets and liabilities are initially recorded at fair value plus transaction costs. Fair value at initial recognition is best evidenced by the transaction price. A gain or loss on initial recognition is only recorded if there is a difference between fair value and transaction price which can be evidenced by other observable current market transactions in the same instrument or by a valuation technique whose inputs include only data from observable markets.

All purchases and sales of financial assets that require delivery within the time frame established by regulation or market convention ("regular way" purchases and sales) are recorded at trade date, which is the date that the Group commits to deliver a financial asset. All other purchases and sales are recognised on the settlement date with the change in value between the commitment date and settlement date not recognised for assets carried at cost or amortised cost; and recognised in equity for assets classified as available for sale.

3 Summary of Significant Accounting Policies (continued)

3.16 Financial assets and liabilities (continued)

Derecognition of financial assets. The Group derecognises financial assets when (i) the assets are redeemed or the rights to cash flows from the assets have otherwise expired or (ii) the Group has transferred substantially all the risks and rewards of ownership of the assets or (iii) the Group has neither transferred nor retained substantially all risks and rewards of ownership but has not retained control. Control is retained if the counterparty does not have the practical ability to sell the asset in its entirety to an unrelated third party without needing to impose additional restrictions on the sale.

Available-for-sale investments. Available-for-sale investments are carried at fair value. Interest income on available for sale debt securities is calculated using the effective interest method and recognised in profit or loss. Dividends on available-for-sale equity instruments are recognised in profit or loss when the Group's right to receive payment is established. All other elements of changes in the fair value are deferred in equity until the investment is derecognised or impaired at which time the cumulative gain or loss is removed from equity to profit or loss.

Impairment losses are recognised in profit or loss when incurred as a result of one or more events ("loss events") that occurred after the initial recognition of available-for-sale investments. A significant or prolonged decline in the fair value of an equity security below its cost is an indicator that it is impaired. The cumulative impairment loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that asset previously recognised in profit or loss – is removed from equity and recognised in profit or loss. Impairment losses on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through current period's profit or loss.

Held to maturity investments. Held to maturity investments are carried at amortised costs using the effective interest method, net of a provision for incurred impairment losses.

3.17 Earnings per share

An earnings per share is determined by dividing the net profit attributable to shareholders by the weighted average number of shares outstanding during the reporting year. Preference shares are not redeemable and are considered to be participating shares. Earnings per share is determined by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of participating shares outstanding during the period. Preference shares participate in the calculation because dividends attributable to preference shares cannot be less then dividends on ordinary shares.

3.18 Reclassifications

Certain amounts in previously issued financial statements have been reclassified to conform to the current year presentation.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Management also makes certain judgements, apart from those involving estimations, in the process of applying the accounting policies. Judgements that have the most significant effect on the amounts recognised in the financial statements and estimates that can cause a significant adjustment to the carrying amount of assets and liabilities within the next financial year include:

Tax legislation. Russian tax, currency and customs legislation is subject to varying interpretations. Refer to Note 25.

4 Critical Accounting Estimates, and Judgements in Applying Accounting Policies (continued)

Related party transactions. In the normal course of business the Group enters into transactions with its related parties. These transactions are priced predominantly at market rates. Judgement is applied in determining if transactions are priced at market or non-market interest rates, where there is no active market for such transactions. The basis for judgement is pricing for similar types of transactions with unrelated parties and effective interest rate analyses. Refer to Note 8.

Useful lives of property, plants and equipment. Management assesses the remaining useful life of property, plant and equipment in accordance with current technical condition of assets and estimated period during which these assets will bring economic value of the Group.

Valuation of available-for-sale investments. Management uses information available from market analysts on fertiliser industry in applying valuation techniques to estimate fair value of respective investments (for further details refer to Note 15). It is reasonably possible based on existing knowledge that outcomes within the next financial year that are different from assumptions could require a material adjustment to the carrying amount of the available-for-sale investments.

5 Adoption of New or Revised Standards and Interpretations

Certain new IFRSs became effective for the Group from 1 January 2006. Listed below are those new or amended standards or interpretations which are or in the future could be relevant to the Group's operations and the nature of their impact on the Group's accounting policies. All changes in accounting policies were applied retrospectively with adjustments made to retained earnings at 1 January 2005, unless otherwise described below.

IFRIC 4, Determining whether an Arrangement contains a Lease (effective from 1 January 2006). IFRIC 4 requires that determining whether an arrangement is, or contains, a lease be based on the substance of the arrangement. It requires an assessment of whether (a) fulfilment of the arrangement is dependent on the use of a specific asset or assets (the asset); and (b) the arrangement conveys a right to use the asset. The Group reassessed its arrangements and concluded that no adjustments are required as a result of adoption of IFRIC 4.

IAS 39 (Amendment) – The Fair Value Option (effective from 1 January 2006). IAS 39 (as revised in 2003) permitted entities to designate irrevocably on initial recognition practically any financial instrument as one to be measured at fair value with gains and losses recognised in profit or loss ('fair value through profit or loss'). The amendment changes the definition of financial instruments 'at fair value through profit or loss' and restricts the ability to designate financial instruments as part of this category. The Group may now designate financial instruments as part of this category only if (a) such classification eliminates or significantly reduces an accounting mismatch that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or (b) a group of financial assets, financial liabilities or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information on that basis is regularly provided to and reviewed by the Company's Board of Directors; or (c) a contract contains one or more embedded derivatives unless: (i) the embedded derivative(s) does not significantly modify the cash flows that otherwise would be required by the contract; or (ii) it is clear with little or no analysis when the embedded derivative is first considered that separation of the embedded derivative(s) is prohibited. The Group applies the amendment retrospectively in accordance with the transitional provisions of the Fair Value Option amendment to IAS 39. As a result of adoption of this amendment the Group has reclassified investments at fair value through profit or loss to available-for-sale investments totalling RR 2,548,887.

IAS 39 (Amendment) - Cash Flow Hedge Accounting of Forecast Intragroup Transactions (effective from 1 January 2006). The amendment allows the foreign currency risk of a highly probable forecast intragroup transaction to qualify as a hedged item in the consolidated financial statements provided that the transaction is denominated in a currency other than the functional currency of the entity entering into that transaction and the foreign currency risk will affect consolidated profit or loss. The Group does not apply hedge accounting and therefore the amendment did not have an impact on these financial statements.

(in thousands of Russian Roubles, except for per share amounts)

5 Adoption of New or Revised Standards and Interpretations (continued)

IAS 39 (Amendment) – Financial Guarantee Contracts (effective from 1 January 2006). As a result of this amendment, the Group measures issued financial guarantees initially at their fair value, which is normally evidenced by the amount of fees received. This amount is then amortised on a straight line basis over the life of the guarantee. At each balance sheet date, the guarantees are measured at the higher of (i) the unamortised balance of the amount at initial recognition and (ii) the best estimate of expenditure required to settle the commitment at the balance sheet date. This amendment did not have a significant impact on these financial statements.

IAS 21 (Amendment) - Net Investment in a Foreign Operation (effective from 1 January 2006). This amendment requires foreign exchange gains and losses on monetary items that form part of net investment in a foreign operation (eg quasi-equity intercompany loans) to be reported in consolidated equity even if the loans are not in the functional currency of either the lender or the borrower. Previously, such exchange differences were required to be recognised in consolidated profit or loss. It also extended the definition of 'net investment in a foreign operation' to include loans between sister companies. This amendment did not have a significant impact on these financial statements.

IAS 19 (Amendment) - Employee Benefits (effective from 1 January 2006). The amendment introduced an additional option to recognise actuarial gains and losses arising in post-employment defined benefit plans in full directly in retained earnings in equity. It also requires new disclosures about defined benefit plans and clarifies accounting for a contractual agreement between a multi-employer plan and participating employers. This amendment did not have a significant impact on these financial statements.

IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds (effective from 1 January 2006). Subject to certain exceptions, this interpretation prohibits offsetting a liability for decommissioning costs with an asset representing an interest in a decommissioning or similar fund and clarifies measurement of the reimbursement asset. This interpretation did not have a significant impact on these financial statements.

IFRIC 6, Liabilities arising from Participating in a Specific Market - Waste Electrical and Electronic Equipment (effective for periods beginning on or after 1 December 2006, that is from 1 January 2006). The Interpretation states that a liability shared among market participants in proportion to their respective market share, in particular the liability for the decommissioning of historical waste electrical and electronic equipment in the European Union, should not be recognised until the measurement period because participation in the market during the measurement period is the obligating event in accordance with IAS 37. This interpretation did not have a significant impact on these financial statements.

IFRS 6, Exploration for and Evaluation of Mineral Resources (effective from 1 January 2006). IFRS 6 allows an entity to continue using the accounting policies for exploration and evaluation assets applied immediately before adopting the IFRS, subject to certain impairment test requirements. This standard did not have a significant impact on these financial statements.

Effect of Adoption. The effect of adoption of the above new or revised standards and interpretations on the Group's financial position at 31 December 2006 and 31 December 2005 and on the results of its operations for the years then ended can be summarised as follows:

	2006	**2005**
Increase in		
Available-for-sale investments	-	2,548,887
Revaluation reserve for investment securities available for sale	-	1,910,257
Decrease in		
Investments designated at Fair Value Through Profit or Loss	-	(2,548,887)
Retained earnings	-	(1,910,257)

(in thousands of Russian Roubles, except for per share amounts)

6 New Accounting Pronouncements

Certain new standards and interpretations have been published that are mandatory for the Group's accounting periods beginning on or after 1 January 2007 or later periods and which the entity has not early adopted:

IFRS 7 Financial Instruments: Disclosures and a complementary Amendment to IAS 1 Presentation of Financial Statements - Capital Disclosures (effective from 1 January 2007). The IFRS introduces new disclosures to improve the information about financial instruments. The volume of disclosures will increase significantly with an emphasis on quantitative aspects of risk exposures and the methods of risk management. The quantitative disclosures will provide information about the extent to which the entity is exposed to risk, based on information provided internally to the entity's key management personnel. Qualitative and quantitative disclosures will cover exposure to credit risk, liquidity risk and market risk including sensitivity analysis to market risk. IFRS 7 replaces IAS 30, Disclosures in the Financial Statements of Banks and Similar Financial Institutions, and some of the requirements in IAS 32, Financial Instruments: Disclosure and Presentation. The Amendment to IAS 1 introduces disclosures about level of an entity's capital and how it manages capital. The Group is currently assessing what impact the new IFRS and the amendment to IAS 1 will have on disclosures in its financial statements.

IFRS 8, Operating Segments (effective for annual periods beginning on or after 1 January 2009). The Standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information. Management is currently assessing what impact the Standard will have on segment disclosures in the Group's financial statements.

Other new standards or interpretations. The Group has not early adopted the following other new standards or interpretations:

- IFRIC 7, Applying the Restatement Approach under IAS 29 (effective for periods beginning on or after 1 March 2006, that is from 1 January 2007).
- IFRIC 8, Scope of IFRS 2 (effective for periods beginning on or after 1 May 2006, that is from 1 January 2007).
- IFRIC 9, Reassessment of Embedded Derivatives (effective for annual periods beginning on or after 1 June 2006);
- IFRIC 10, Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006);
- IFRIC 11, IFRS 2—Group and Treasury Share Transactions (effective for annual periods beginning on or after 1 March 2007);
- IFRIC 12, Service Concession Arrangements (effective for annual periods beginning on or after 1 January 2008).

Unless otherwise described above, these new standards and interpretations are not expected to significantly affect the Group's financial statements.

7 Segment Information

The Group has one reportable segment, which is manufacturing and sale of chemical fertilizers which have similar risks and rewards. The Group evaluates performance and makes investment and strategic decisions based upon review of profitability for the Group as a whole. Its secondary reporting format is determined to be the geographical segments: Russia and CIS countries, and other counties.

Sales are based on the geographical area in which the customer is located. There are no sales or other transactions between the segments. Production and all assets and liabilities of the Group are located in the Russian Federation.

Revenue	**2006**	**2005**
Overseas	1,993,937	3,672,324
Russia and CIS countries	3,578,416	2,151,596
	5,572,353	**5,823,920**

(in thousands of Russian Roubles, except for per share amounts)

7 Segment Information (continued)

The Group sells to two international trading entities that account for the majority of its sales outside of Russia. In 2006, AgroNitrogen Logistics Ltd. and NPKhemical Trading Inc. purchased 44% and 30% of the Group’s sales outside Russia, respectively (2005: 34% and 25%). The sales to them are included in the overseas segment as risks and returns on them are similar to other overseas sales.

8 Balances and Transactions with Related Parties

For the purposes of these financial statements, parties are considered to be related if one party has the ability to control the other party, is under common control or exercise significant influence over the other party in making financial or operational decisions as defined by IAS 24 “Related Party Disclosures”. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions, which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The nature of the related party relationships for those related parties with whom the Group entered into significant transactions or had significant balances outstanding at 31 December 2006 and 2005 are detailed below. Transactions were entered into with related parties during the ordinary course of business on normal commercial terms.

i Balances with related parties

Balance sheet caption	Notes	Relationship	2006	2005
Trade receivables, gross:	10	Parent company	5,542	2,040
		Parties under common control	140,714	137,581
Provision for impairment of trade receivables:	10	Parties under common control	(60,378)	(92,136)
Prepayments, gross:		Parties under common control	42,811	50,057
Provision for impairment of prepayments:		Parties under common control	(1,000)	-
Dividends receivable:		Parent company	41,816	27,625
Loans provided:	11	Parties under common control	103,000	67,500
		Parent company	150,000	-
Trade payables:	16	Parties under common control	5,618	5,692
		Parent company	13,904	109
Dividends payable to shareholders:		Parties under common control	-	12,687
		Parent company	-	53,180
Advances from customers:		Party under common control	44,319	2,702

ii Transactions with related parties

Statement of income caption	Notes	Relationship	2006	2005
Sales:	7	Parent company	37,054	28,980
		Parties under common control	1,263,193	936,818
Purchases:	20	Parent company	(50,463)	(18,807)
		Parties under common control	(21,090)	(17,780)
Transportation expenses:		Parties under common control	(390,134)	(377,909)
Security services:		Parties under common control	(65,882)	(76,385)
Dividends accrued:		Parent company	(69,049)	(245,990)
		Parties under common control	(32,309)	(58,688)

(in thousands of Russian Roubles, except for per share amounts)

8 Balances and Transactions with Related Parties (continued)

iii Loans issued to related parties

At 31 December 2006 and 2005 short-term loans denominated in RR totalled RR 247,500 and RR 10,000, respectively, at interest rates in the range of 8.5% to 10.5%. The loans are unsecured.

In 2006 the Group accrued interest income of RR 11,534 (2005: RR 11,570).

At 31 December 2006 long-term loan denominated in RR totalled RR 5,500 (2005: RR 57,500). Interest rate was fixed at 8.5% The loan is unsecured.

9 Cash and Cash Equivalents

Cash and cash equivalents comprise the following:

	2006	2005
RR denominated cash on hand and balances with banks	180,088	131,278
Foreign currency denominated balances with banks	278,767	215,754
	458,855	**347,032**

10 Accounts Receivable

	2006	2005
Trade accounts receivable (refer to Note 8)	445,594	233,528
Value-added tax recoverable	259,891	302,665
Notes receivable	31,962	1,452
Income tax prepayments	13,637	3,715
Advances given	332,964	250,884
Other taxes receivable	2,203	1,223
Receivables for securities	-	11,021
Less impairment provision for trade and other receivables	(107,693)	(118,860)
	978,558	**685,628**

RR 247,509 and RR 39,866 of trade receivables are denominated in USD at 31 December 2006 and 2005 respectively.

RR 11,829 and RR 88,778 of advances paid to suppliers are denominated in euro as at 31 December 2006 and 2005 respectively.

RR 23,811 and RR 1,452 of notes receivable are promissory notes issued by Sberbank as at 31 December 2006 and 2005 respectively.

11 Loans Receivable

	2006	2005
Current loans receivable		
Loans issued to third-parties	-	15,000
Loans issued to related parties (Note 8)	97,500	10,000
Loans issued to parent company	150,000	-
	247,500	**25,000**
Non-current loans receivable		
Loans issued to related parties (Note 8)	5,500	57,500
	5,500	**57,500**

At 31 December 2006 and 2005 all short-term loans were denominated in RR totalled RR 247,500 and RR 25,000, respectively, at interest rates in the range of 8.5% to 10.5%. The loans are unsecured.

In 2006 the Group accrued interest income of RR 11,782 (2005: RR 11,570).

At 31 December 2006 long-term loan denominated in RR totalled RR 5,500 (2005: RR 57,500). Interest rate was fixed at 8.5% The loan is unsecured.

(in thousands of Russian Roubles, except for per share amounts)

12 Inventories

	2006	**2005**
Raw materials and spare parts	675,177	590,510
Work in progress	28,117	18,670
Finished products	123,840	149,516
	827,134	**758,696**

Included in raw materials and spare parts are catalysers of RR 216,552 (2005: RR 168,478), which are used in the production process over more than one year. Raw materials and spare parts inventories are recorded net of obsolescence provision of RR 39,880 at the year ended 31 December 2006 (2005: RR 37,266). No inventories have been pledged as security for borrowings at 31 December 2006 and 2005.

13 Property, Plant and Equipment

Property, plant and equipment and related accumulated depreciation consist of the following:

	Buildings and constructions	**Plant and equipment**	**Other**	**Assets under construction**	**Total**
Cost					
Balance at 1 January 2005	**5,693,404**	**4,170,553**	**62,893**	**105,434**	**10,032,284**
Additions	-	-	-	200,335	**200,335**
Transfers	34,144	78,749	13,284	(126,177)	**-**
Disposals	(48,271)	(21,324)	(12,910)	-	**(82,505)**
Balance at 31 December 2005	**5,679,277**	**4,227,978**	**63,267**	**179,592**	**10,150,114**
Accumulated Depreciation					
Balance at 1 January 2005	3,495,746	4,036,461	38,072	-	**7,570,279**
Depreciation charge	109,247	57,809	14,252	-	**181,308**
Disposals	(24,236)	(20,487)	(10,573)	-	**(55,296)**
Balance at 31 December 2005	**3,580,757**	**4,073,783**	**41,751**	**-**	**7,696,291**
Net Book Value					
Balance at 1 January 2005	**2,197,658**	**134,092**	**24,821**	**105,434**	**2,462,005**
Balance at 31 December 2005	**2,098,520**	**154,195**	**21,516**	**179,592**	**2,453,823**

(in thousands of Russian Roubles, except for per share amounts)

13 Property, Plant and Equipment (continued)

	Buildings and constructions	Plant and equipment	Other	Assets under construction	Total
Cost					
Balance at 1 January 2006	**5,679,277**	**4,227,978**	**63,267**	**179,592**	**10,150,114**
Additions	-	-	-	797,239	**797,239**
Acquisitions through business combinations (Note 26)	292,442	60,743	-	405	**353,590**
Transfers	14,329	141,852	38,931	(195,112)	**-**
Disposals	(123,013)	(88,271)	(19,487)	-	**(230,771)**
Balance at 31 December 2006	**5,863,035**	**4,342,302**	**82,711**	**782,124**	**11,070,172**
Accumulated Depreciation					
Balance at 1 January 2006	3,580,757	4,073,783	41,751	-	**7,696,291**
Acquisitions through business combinations (Note 26)	239,364	34,646	-	-	**274,010**
Depreciation charge	103,790	65,700	16,858	-	**186,348**
Disposals	(69,002)	(86,965)	(16,042)	-	**(172,009)**
Balance at 31 December 2006	**3,854,909**	**4,087,164**	**42,567**	**-**	**7,984,640**
Net Book Value					
Balance at 1 January 2006	**2,098,520**	**154,195**	**21,516**	**179,592**	**2,453,823**
Balance at 31 December 2006	**2,008,126**	**255,138**	**40,144**	**782,124**	**3,085,532**

At 31 December 2006 and 31 December 2005 the gross carrying value of fully depreciated property, plant and equipment was RR 3,290,414 and RR 2,983,896 respectively.

In 2004 the Group adjusted the gross book values and accumulated depreciation of property, plant and equipment which were purchased and/or constructed over a long period of time (up to 8 years) for the amount of inflation. The inflation was calculated in accordance with IAS 29, Financial Reporting in Hyperinflationary Economies, for each respective part of cost of the property, plant and equipment items from the dates of their origination. The adjustment did not affect the net book values of property, plant and equipment.

14 Goodwill

Movements in goodwill arising on the acquisition of new subsidiaries are:

	Note	2006	2005
Carrying amount at 1 January		**-**	**-**
Acquisition of subsidiary	26	52,068	-
Carrying amount at 31 December		**52,068**	**-**
Gross book value at 31 December		52,068	-
Carrying amount at 31 December		**52,068**	**-**

In December 2006 the Group acquired 100% of the share capital of LLC "Andrex" from the third party for a cash consideration of RR 131,683. Management believes that no separately identifiable intangible assets exist in acquired company, which could qualify for separate accounting in accordance with IFRS 3. The goodwill for RR 52,068 is primarily attributable to the profitability of the acquired business, cost of new market entry and the significant synergies and combined costs savings expected to arise due to unique geographical location of assets of the acquired company for the Group.

(in thousands of Russian Roubles, except for per share amounts)

14 Goodwill (continued)

Goodwill Impairment Test. Goodwill is allocated to cash-generating units (CGUs) which represent the lowest level within the Group at which the goodwill is monitored by management and which are not larger than a segment as follows:

	2006	2005
LLC "Andrex"	52,068	-
Total carrying amount of goodwill	**52,068**	**-**

Group management believes there is no indication of goodwill impairment at the end of the reporting period.

15 Available-for-sale investments

	2006	2005
Balance at 1 January	2,548,887	989,277
Additions	17,901	107
Fair value gain	239,956	1,559,818
Disposals	(16,626)	(315)
Balance at 31 December	**2,790,118**	**2,548,887**

Investments previously classified as at fair value through profit of loss were designated by the Group as available-for-sale in line with requirements of IAS 39 (revised) effective from 01 January 2006. These investments comprise principally equity securities, which are listed on the RTS but which are not actively traded and hence are not considered to be quoted in an active market in line with requirements of IAS 39. For these investments, fair value is estimated by using valuation techniques based on application guidance of IAS 39 (revised). Applied multiples of enterprise value to sales and EBIT were 1.30 and 4.96 respectively. Applied discounts for lack of control and lack of marketability were 15% and 35% respectively. For other investments traded in active markets, fair value is determined by reference to the current market value at the close of business on 31 December.

The Group has investments in the following companies:

Name	Activity	Country of registration	2006	2005
OAO "Acron"	Fertilizers manufacture	Russia	2,538,591	2,432,487
OAO "Sberbank"	Banking	Russia	227,213	93,360
Other			24,314	23,040
			2,790,118	**2,548,887**

16 Accounts Payable and Advances Received

Accounts payable

	2006	2005
Trade accounts payable (refer to Note 8)	143,877	65,499
Payables to employees	111,426	87,619
Dividends payable	2,076	97,744
Deferred purchase consideration for acquisition of new subsidiaries (refer to Notes 14 and 26)	137,656	-
Accrued liabilities and other creditors	16,048	8,692
	411,083	**259,554**

RR 136,055 and RR 970 of trade payables are denominated in foreign currency, mainly US dollars, at 31 December 2006 and 31 December 2005, respectively.

Advances received

RR 245,165 and RR 204,174 of advances received are denominated in foreign currency, mainly US dollars, at 31 December 2006 and 31 December 2005, respectively.

(in thousands of Russian Roubles, except for per share amounts)

17 Other Taxes Payable

	2006	2005
Value-added tax payable	42,308	76,103
Payroll taxes	24,154	22,788
Property and other taxes	6,492	2,072
	72,954	**100,963**

18 Borrowings

Borrowings consist of the following:

	2006	2005
Bonds issued	882,823	904,255
Term loans	1,060,794	100,739
	1,943,617	**1,004,994**

In June 2005 the Group issued 900 thousand non-convertible three year Russian rouble denominated bonds (at par value 1,000 roubles each) totalling RR 900,000 with quarterly coupon payments of 9.9% per annum with an early redemption option subject to approval of Board of directors. In June 2005 Board of Directors approved the decision to grant to the holders of the bonds an option to redeem the bonds starting from December 2006. Bonds for amount of RR 17,177 were redeemed and not placed as at 31 December 2006. In present financial statements these bonds were classified as long-term. The whole amount of issue was guaranteed by the Parent company.

The Group's borrowings mature as follows:

	2006	2005
Borrowings due:		
- within 1 year	600,000	904,255
- between 1 and 5 years	1,343,617	100,739
	1,943,617	**1,004,994**

The Group's borrowings are denominated in currencies as follows:

	2006	2005
Borrowings denominated in:		
- Russian Roubles	1,482,823	904,255
- US Dollars	460,794	100,739
	1,943,617	**1,004,994**

The effective interest rates at the balance sheet date were as follows:

	31 December 2006		**31 December 2005**	
In % per annum	Russian Roubles	US Dollars	Russian Roubles	US Dollars
Bonds issued	9.9%	-	9.9%	-
Term loans	-	7.0%	-	7.5%

The details of the significant short-term loan balances are summarized below (amounts denominated in US$ are presented in US$ dollars):

Short-term loan from Sberbank-Moscow denominated in Russian roubles totalled RR 600,000 as at 31 December 2006 (2005: RR Nil) at interest rate 7.0%. Loan is not secured, but there are covenants concerning level of export revenue credited to the account of the Company, opened in Sberbank.

The details of the significant long-term loan balances are summarized below (amounts denominated in US$ are presented in US$ dollars):

There was long-term loan from Moscow International Bank denominated in foreign currency totalled US$ 3,500,000 as at 31 December 2005 at interest rate LIBOR+4%. Loan was not secured. It was repaid in the year 2006.

Long-term loan from Moscow International Bank denominated in foreign currency totalled US$ 17,500,000 as at 31 December 2006 (2005: RR Nil) at interest rate LIBOR + 2.75%. The significant covenants relate to the level of revenue and the level of encumbrance over assets. The contract contains covenants, including requirement about advanced repayment of credit in case of breach of obligations to other creditors in amount more than settled limit.

(in thousands of Russian Roubles, except for per share amounts)

19 Shareholders' Equity

Total number of outstanding shares comprises:

	Ordinary shares			Preferred shares	
	Number of shares authorised issued and paid	Share Capital	Share premium	Number of shares authorised issued and paid	Share Capital
Balance at 31 December 2004	721,182,860	1,379,569	93,794	154,256,400	355,790
Balance at 31 December 2005	721,182,860	1,379,569	93,794	154,256,400	355,790
Balance at 31 December 2006	**721,182,860**	**1,379,569**	**93,794**	**154,256,400**	**355,790**

The Company has two classes of shares, Class A preferred and ordinary. The nominal value for both classes of share capital is RR 0.25 per share. The Company's Board of Directors is authorised to issue both classes of share capital at their discretion.

Class A preferred shares carry no voting rights and are entitled to a minimum annual dividend of 10% of the Company's net statutory profit after taxes. Preferred shares have priority over ordinary shares in the event of liquidation but carry no voting rights except on resolutions regarding liquidation or reorganisation of the Company, changes to dividend levels of preferred shares, or the issuance of additional preferred shares. Such resolutions require approval by two thirds of preferred shareholders. The preferred shares have no rights of redemption or conversion. The share capital is shown in the amount of the historical contribution adjusted for inflation since the date of privatisation until 31 December 2002.

Russian legislation identifies the basis of distribution as the current year net profit. For 2006, the Company recorded a statutory profit as reported in the published annual statutory reporting forms of RR 2,962,865 (2005: profit of RR 1,050,718).

However, the legislation and other statutory laws and regulations dealing with the distribution rights are open to legal interpretation and accordingly management believes at present it would not be appropriate to disclose an amount for the distributable reserves in these financial statements.

A dividend was declared in 2006 in respect of 2005 to holders of ordinary and preferred shares of RR 0.55 per ordinary share and RR 0.69 per preferred share (2005: RR 0.18 per ordinary share and RR 0.23 per preferred share in respect of 2004). During 2006 no interim dividends were declared.

20 Cost of Sales

The components of cost of sales were as follows:

	2006	2005
Change in inventories of finished goods and work in progress	10,725	(36,701)
Staff costs	481,357	474,918
Materials and components used	1,106,527	1,104,962
Fuel and energy	484,708	418,261
Natural gas	986,690	927,538
Depreciation	186,348	181,308
Production overheads	25,172	38,545
Overhaul costs	420,039	298,131
Social expenditure	80,764	75,420
	3,782,330	**3,482,382**

(in thousands of Russian Roubles, except for per share amounts)

21 Selling, General and Administrative Expenses

	2006	2005
Staff costs	381,474	384,369
Bad debts expense / (reversal)	(1,314)	33,871
Business trips expenses	20,338	13,038
Audit, legal and consulting services	76,818	50,082
Bank services	19,164	12,505
Insurance	4,394	4,159
Buildings maintenance and rent	58,326	39,400
Security	80,640	73,617
Telecommunication costs	9,441	8,851
Representation expenses	4,918	7,285
Other expenses	13,565	7,269
	667,764	**634,446**

22 Finance Expense

	2006	2005
Interest expense	128,706	100,629
Foreign exchange (gains) / losses	(10,869)	11,944
	117,837	**112,573**

23 Income Taxes

	2006	2005
Income tax expense – current	195,196	324,675
Deferred tax charge/(credit) – origination and reversal of temporary differences	(16,364)	(55,026)
Income tax charge	**178,832**	**269,649**

Profit before taxation for financial reporting purposes is reconciled to tax expense/(credit) as follows:

	2006	2005
Profit before taxation	561,451	1,141,917
Theoretical tax charge at statutory rate of 24% thereon (2005: 24%)	134,748	274,060
Tax effect of items which are not deductible or assessable for taxation purposes:		
Income not taxable	(20,276)	(25,695)
Other non-deductible expenses	64,360	21,284
Income tax charge	**178,832**	**269,649**

(in thousands of Russian Roubles, except for per share amounts)

23 Income Taxes (continued)

Most companies of the Group were subject to tax rates of 24% on taxable profits for 2006. Deferred tax assets / liabilities are measured at the rate of 24% as at 31 December 2006 (24% as at 31 December 2005). The net effect of the change on deferred tax balances recognised as at 31 December 2006 is reflected in the statement of income for the year ended 31 December 2006.

	31 December 2004	Differences recognition and reversal in income statement	Differences recognition and reversal directly in equity	31 December 2005
Tax effects of taxable temporary differences:				
Property, plant and equipment	361,497	(29,575)	-	331,922
Investments	220,429	-	374,356	594,785
Inventories	(12,958)	19,824	-	6,866
Other temporary differences	(2,729)	5,206	-	2,477
Tax effects of deductible temporary differences:				
Accounts receivable	(9,504)	(34,877)	-	(44,381)
Accounts payable	(4,404)	(12,180)	-	(16,584)
Employee benefit obligation	(10,773)	(3,424)	-	(14,197)
Total net deferred tax liability	**541,558**	**(55,026)**	**374,356**	**860,888**
Including:				
Deferred tax liability, long-term	**571,153**			**912,510**
Deferred tax asset, short-term	**(29,595)**			**(51,622)**

	31 December 2005	Differences recognition and reversal in income statement	Differences recognition and reversal directly in equity	31 December 2006
Tax effects of taxable temporary differences:				
Property, plant and equipment	331,922	(22,761)	-	309,161
Investments	594,786	6,836	57,589	659,211
Inventories	6,866	(2,471)	-	4,395
Other temporary differences	2,477	(360)	-	2,117
Tax effects of deductible temporary differences:				
Accounts receivable	(44,381)	2,680	-	(41,701)
Accounts payable	(16,584)	(3,733)	-	(20,317)
Employee benefit obligation	(14,198)	3,445	-	(10,753)
Total net deferred tax liability	**860,888**	**(16,364)**	**57,589**	**902,113**
Including:				
Deferred tax liability, long-term	**912,510**			**957,618**
Deferred tax asset, short-term	**(51,622)**			**(55,505)**

Substantially all deferred tax liabilities presented in the balance sheet are expected to be realised within a period exceeding 12 months from the balance sheet date.

(in thousands of Russian Roubles, except for per share amounts)

24 Earnings Per Share

Earnings per share is calculated by dividing the net income attributable to participating shareholders by the weighted average number of ordinary and preference shares in issue during the period, excluding the average number of ordinary shares purchased by the Company or its subsidiary and held as treasury shares (see Note 19).

	2006	2005
Weighted average number of ordinary shares outstanding	721,182,860	721,182,860
Weighted average number of preference shares outstanding	154,256,400	154,256,400
Dividends to ordinary shareholders	115,390	411,074
Dividends to preference shareholders	30,851	111,065
Total dividends for the year	**146,241**	**522,139**
Profit attributable to ordinary shareholders	310,117	699,509
Profit attributable to preference shareholders	72,502	172,759
Profit for the year	**382,619**	**872,268**
Basic and diluted earnings per ordinary share (in Russian roubles)	**0.43**	**0.97**
Basic and diluted earnings per preference share (in Russian roubles)	**0.47**	**1.12**

25 Contingencies, Commitments and Operating Risks

i Contractual commitments and guarantees

As at 31 December 2006 the Group had outstanding capital commitments in relation to property, plant and equipment for amount of RR 27,852 (2005: RR 372,617).

As at December 31, 2006 and 2005, the Group has not issued any financial guarantees to third parties in respect of borrowings from non-group companies.

ii Taxation

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently.

Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments, and it is possible that transactions and activities that have not been challenged in the past may be challenged. As a result, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

Russian transfer pricing legislation introduced 1 January 1999 provides the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of all controllable transactions, provided that the transaction price differs from the market price by more than 20%.

Controllable transactions include transactions with interdependent parties, as determined under the Russian Tax Code, and all cross-border transactions (irrespective whether performed between related or unrelated parties), transactions where the price applied by a taxpayer differs by more than 20% from the price applied in similar transactions by the same taxpayer within a short period of time, and barter transactions. There is no formal guidance as to how these rules should be applied in practice. The arbitration court practice with this respect is contradictory.

Tax liabilities arising from intercompany transactions are determined using actual transaction prices. It is possible with the evolution of the interpretation of the transfer pricing rules in the Russian Federation and the changes in the approach of the Russian tax authorities, that such transfer prices could potentially be challenged in the future. Given the brief nature of the current Russian transfer pricing rules, the impact of any such challenge cannot be reliably estimated; however, it may be significant.

The Group’s Management believes that its interpretation of the relevant legislation is appropriate and the Group’s tax, currency legislation and customs positions will be sustained. Accordingly, at 31 December 2006 no provision for potential tax liabilities had been recorded (2005: no provision).

25 Contingencies, Commitments and Operating Risks (continued)

iii Environmental matters

The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental regulations. As obligations are determined, they are recognised immediately. Potential liabilities, which might arise as a result of changes in existing regulations, civil litigation or legislation, cannot be estimated but could be material. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental damage.

iv Legal proceedings

From time to time and in the normal course of business, claims against the Group are received. On the basis of its own estimates and both internal and external professional advice the management is of the opinion that no material losses will be incurred in respect of claims. No provisions for such losses have been made in these consolidated financial statements.

v Operating environment

Whilst there have been improvements in economic trends in the country, the Russian Federation continues to display certain characteristics of an emerging market. These characteristics include, but are not limited to, the existence of a currency that is not freely convertible in most countries outside of the Russian Federation, restrictive currency controls, and relatively high inflation. The tax, currency and customs legislation within the Russian Federation is subject to varying interpretations, and changes, which can occur frequently. The future economic direction of the Russian Federation is largely dependent upon the effectiveness of economic, financial and monetary measures undertaken by the Government, together with tax, legal, regulatory, and political developments.

26 Business combinations

Acquisition of subsidiaries

On 27 December 2006 the Group acquired 100% of the share capital of LLC "Andrex" from the third party for a cash consideration of RR 131,683. The acquired company holds title for facilities for transhipment, mixing, packaging and storing of bulk fertilizers located in Kaliningrad seaport. This acquisition was made consistent with Group's strategy, aiming for optimization of fertilizer exports logistics. The acquired company is consolidated by the Group for the first time as at the effective date of obtaining control which management considers to be December 2006.

The acquired company contributed revenue of RR 0 and profit of RR 0 to the Group for the period from the date of acquisition to 31 December 2006. If the acquisition had occurred on 1 January 2006, effect on Group revenue for 2006 would have been RR 0, and effect on profit for 2006 would have been RR 0. Prior to acquisition LLC "Andrex" leased out its primary assets to OAO "Kaliningrad Seaport" on a free of charge basis. Starting from date of acquisition the Group terminated these lease contracts and concluded new lease contracts at current market rates.

The Group has completed the process of the purchase price allocation and the following table summarizes the fair values of the assets acquired and liabilities assumed in this business combination, determined in accordance with IFRS 3 "Business combinations". The fair values of property, plant and equipment were based on estimates of independent professional appraiser.

(in thousands of Russian Roubles, except for per share amounts)

26 Business combinations (continued)

Details of the assets and liabilities acquired and goodwill arising are as follows:

	Note	IFRS carrying amount immediately before business combination	Attributed fair value
Cash and cash equivalents		11	11
Property, plant and equipment		12,826	79,581
Other assets		274	274
Other liabilities		(251)	(251)
Fair value of net assets of subsidiary			**79,615**
Goodwill arising from the acquisition	14		52,068
Total purchase consideration			**131,683**
Less: deferred purchase consideration	16		(131,683)
Less: cash and cash equivalents of subsidiary acquired			(11)
Inflow of cash and cash equivalents on acquisition			**11**

27 Significant Non-Cash Transactions

Included in sales are non-cash transactions amounting to RR 100,235 (2005: RR 43,146) were settled via non-cash transactions during the years ended 31 December 2006 and 2005, respectively. The transactions primarily represent cancellation of mutual balances with customers and suppliers within the operating cycle.

28 Financial Risk Management

i Credit risk

Financial assets, which potentially subject Group entities to credit risk, consist principally of trade receivables. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. The carrying amount of accounts receivable, net of provision for impairment of receivables, represents the maximum amount exposed to credit risk. The Group has no other significant concentrations of credit risk. Although collection of receivables could be influenced by economic factors, management believes that there is no significant risk of loss to the Group beyond the provision already recorded.

Cash is placed in financial institutions, which are considered at time of deposit to have minimal risk of default.

ii Market risk

The Group takes on exposure to market risks. Market risks arise from commodity prices and open positions in interest rate, currency and equity financial instruments, all of which are exposed to general and specific market movements. The Board of Directors sets limits on the value of risk that may be accepted, which is monitored on a daily basis. However, the use of this approach does not prevent losses outside of these limits in the event of more significant market movements.

28 Financial Risk Management (continued)

iii Foreign exchange risk

The Group exports 36% (2005: 63%) of its production to overseas and attracts substantial amount of foreign currency denominated long-term borrowings and is thus exposed to foreign exchange risk. Foreign currency denominated assets and liabilities give rise to foreign exchange exposure. Foreign currency denominated assets (see Note 9 and 10) and liabilities (see Note 16 and 18) are disclosed in respective notes. The Group does not have formal arrangements to mitigate foreign exchange risks of the Group's operations.

iv Cash flow and fair value interest rate risk

The Group's income and operating cash flows are exposed to changes in market interest rates. The Group is exposed to fair value interest rate risk through market value fluctuations of interest bearing short-term and long-term borrowings majority of which are at fixed interest rates. The Group has no significant interest-bearing assets.

29 Fair Value of Financial Instruments

Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties, other than in a forced sale or liquidation, and is best evidenced by an active quoted market price.

The estimated fair values of financial instruments have been determined by the Group using available market information, where it exists, and appropriate valuation methodologies. However, judgement is necessarily required to interpret market data to determine the estimated fair value. The Russian Federation continues to display some characteristics of an emerging market and economic conditions continue to limit the volume of activity in the financial markets. Market quotations may be outdated or reflect distress sale transactions and therefore not represent fair values of financial instruments. Management has used all available market information in estimating the fair value of financial instruments.

Financial instruments carried at fair value. Available-for-sale investments are carried on the consolidated balance sheet at their fair value. Cash and cash equivalents are carried at amortised cost, which approximates current fair value.

Fair values for available-for-sale investments carried at fair value were determined by using valuation techniques based on application guidance of IAS 39 (revised) on the basis of financial data of the investees and application of other valuation methodologies. It is reasonably possible based on existing knowledge that outcomes within the next financial year that are different from assumptions could require a material adjustment to the carrying amount of the available-for-sale investments (refer to Note 15).

Financial assets carried at amortised cost. The fair value of floating rate instruments is normally their carrying amount. The estimated fair value of fixed interest rate instruments is based on estimated future cash flows expected to be received discounted at current interest rates for new instruments with similar credit risk and remaining maturity. Discount rates used depend on credit risk of the counterparty. Carrying amounts of trade receivables approximate fair values.

Liabilities carried at amortised cost. The fair value is based on quoted market prices, if available. The estimated fair value of fixed interest rate instruments with stated maturity, for which a quoted market price is not available, was estimated based on expected cash flows discounted at current interest rates for new instruments with similar credit risk and remaining maturity. At 31 December 2006 and 2005 the fair value of the current and non-current borrowings is not materially different from their carrying amounts.

30 Subsequent Events

Dividends. Shareholders decided not to pay any dividends out of net profit earned in the year ended 31 December 2006 on Annual shareholders meeting in May 2007.

Short-term loans and borrowings. The Group has repaid borrowings from banks totalling RR 364,689 in the period from 31 December 2006 to the date these financial statements were signed.

Long-term loans and borrowings. The Group has received new and repaid existed long-term bank borrowings from banks totalling RR 136,200 and RR 316,071 respectively in the period from 31 December 2006 to the date these financial statements were signed.