JOINT STOCK COMPANY POLYMETAL

Consolidated Financial Statements
For The Years Ended 31 December 2007 and 2006

JOINT STOCK COMPANY POLYMETAL

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STATEMENT OF MANAGEMENT'S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2007

The following statement, which should be read in conjunction with the independent auditors' responsibilities stated in the independent auditors' report, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the consolidated financial statements of Open Joint Stock Company Polymetal ("JSC Polymetal") and its subsidiaries (the "Group"). Management is responsible for the preparation of the consolidated financial statements that present fairly the financial position of the Group as at December 31, 2007, and the results of its operations, cash flows and changes in shareholders' equity for the year then ended, in compliance with Accounting Principles Generally Accepted in the United States of America ("U.S. GAAP").

In preparing the consolidated financial statements, management is responsible for:

- Selecting suitable accounting policies and applying them consistently;
- Making judgments and estimates that are reasonable and prudent;
- Stating whether U.S. GAAP has been followed, subject to any material departures disclosed and explained in the consolidated financial statements;
- Preparing the consolidated financial statements on a going concern basis, unless it is inappropriate to presume that the Group will continue in business for the foreseeable future.

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls, throughout the Group;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Group, and which enable them to ensure that the consolidated financial statements of the Group comply with U.S. GAAP;
- Maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The consolidated financial statements for the year ended December 31, 2007 were approved by management on June 30, 2008:

On behalf of the Board of Directors:

Nesis V.N.	**Cherkashin S.A.**
Chief Executive Officer	Chief Financial Officer

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Open Joint Stock Company "Polymetal":

We have audited the accompanying consolidated balance sheet of Open Joint Stock Company "Polymetal" and its subsidiaries (the "Group") as at December 31, 2007, and the related consolidated statements of operations, changes in shareholders' equity, and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The consolidated financial statements of the Group for the year ended December 31, 2006 were audited by other auditors whose report, dated June 21, 2007, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Group as at December 31, 2007, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

June 30, 2008

JOINT STOCK COMPANY POLYMETAL

CONSOLIDATED BALANCE SHEETS
(In thousands of U.S. Dollars, except share and per share data)

	Note	December 31, 2007	December 31, 2006
Assets			
Cash and cash equivalents		5,019	6,532
Accounts receivable		-	3,218
Prepayments to suppliers		12,540	13,872
Inventories	5	213,141	155,629
Short-term VAT receivable	6	52,078	45,335
Short-term deferred tax asset	7	3,806	816
Other current assets	8	18,057	13,904
Total current assets		**304,641**	**239,306**
Property, plant and equipment	9	502,470	406,418
Goodwill	10	30,141	31,896
Investments and long-term loans to third parties		269	615
Long-term loans to related parties	11	6,119	6,138
Long-term VAT receivable	6	10,288	9,019
Long-term deferred tax asset	7	3,926	3,962
Total non-current assets		**553,213**	**458,048**
Total assets		**857,854**	**697,354**
Liabilities and shareholders' equity			
Accounts payable and accrued liabilities		32,253	29,216
Accounts payable to related parties		-	302
Short-term debt and current portion of long-term debt	12	152,006	229,770
Taxes payable		9,453	7,292
Short-term deferred tax liability	7	11,437	14,902
Current portion of capital lease liabilities	13	2,417	4,210
Total current liabilities		**207,565**	**285,692**
Long-term portion of capital lease liabilities	13	147	2,445
Long-term debt	14	71,200	169,895
Long-term debt from related parties		2	4,574
Deferred tax liability	7	37,628	35,284
Reclamation and mine closure obligation	15	8,035	7,230
Deferred payments	16	7,438	-
Total non-current liabilities		**124,450**	**219,428**
Total liabilities		**332,015**	**505,120**
Commitments and contingencies	26	-	-
Shareholders' equity			
Share capital (2,444,000,000 shares authorized with par value of Rubles 0.2 per share; 315,000,000 and 275,000,000 shares issued at December 31, 2007 and 2006, respectively; 309,459,677 and 275,000,000 shares outstanding at December 31, 2007 and 2006, respectively	17	6,698	6,397
Additional paid-in capital		367,129	56,710
Treasury shares, at cost (5,540,323 ordinary shares at December 31, 2007)	17	(50)	-
Accumulated other comprehensive income		• 56208	10,447
Retained earnings		95,854	118,680
Total shareholders' equity		**525,839**	**192,234**
Total liabilities and shareholders' equity		**857,854**	**697,354**

The accompanying consolidated notes are integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED
(In thousands of U.S. Dollars, except share and per share data)

	Note	December 31, 2007	December 31, 2006
Revenues	19	308,747	315,596
Cost of sales	20	254,638	171,283
Gross profit		**54,109**	**144,313**
General, administrative and selling expenses		42,275	28,351
Other operating expenses	21	27,423	21,207
Operating (loss)/income		**(15,589)**	**94,755**
Interest expense		10,519	25,267
Capital lease finance costs		2,088	2,569
Exchange gain, net		(11,433)	(26,784)
(Loss)/income before income tax and minority interest		**(16,763)**	**93,703**
Income tax expense	22	6,063	25,755
(Loss)/income before minority interest		**(22,826)**	**67,948**
Minority interest		**-**	**6,261**
Net (loss)/income		**(22,826)**	**61,687**
Basic and diluted (loss)/earnings per share (expressed in U.S. Dollars)	17	(0.074)	0.224
Weighted average number of shares outstanding		307,581,330	275,000,000

The accompanying consolidated notes are integral part of these consolidated financial statements.

JOINT STOCK COMPANY POLYMETAL

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED
(In thousands of U.S. Dollars)

	December 31, 2007	December 31, 2006
Cash flows from operating activities		
Net (loss)/income	(22,826)	61,687
Adjustments to reconcile net (loss) income to cash provided by operations:		
Depreciation and depletion	47,329	39,366
Capital lease finance costs	2,088	2,569
Deferred income tax expense	(6,379)	3,801
Loss on disposal of property, plant and equipment	343	1,339
Minority interest	-	6,261
Share based compensation	10,584	-
Exchange loss/(gain), net	(11,433)	(26,784)
Loss on impairment of asset	6,676	-
Other non-cash expense	8,489	228
Changes in working capital, excluding cash:		
Accounts receivable	3,587	-
Prepayments to suppliers	1,813	(127)
Inventories	(36,174)	(46,427)
VAT receivable	(4,060)	(6,615)
Other current assets	(11,074)	(5,166)
Accounts payable and accrued liabilities	8,655	231
Taxes payable	1,631	(1,261)
Net cash provided by operating activities	**(2,805)**	**29,102**
Cash flows from investing activities		
Additions to property, plant and equipment	(115,654)	(60,311)
Proceeds from the sale of property, plant and equipment	4,211	2,845
Acquisition of subsidiaries and minority interest, net of cash acquired	(18,250)	(93,705)
Equity investment	-	(250)
Loans provided to third parties	-	(764)
Repayment of loans provided to third parties	392	501
Loans provided to related parties	-	(6,138)
Repayment of loans provided to related parties	465	15,088
Net cash used in by investing activities	**(128,836)**	**(142,734)**
Cash flows from financing activities		
Proceeds from short-term loans and borrowings	242,907	433,303
Repayment of short-term loans and borrowings	(352,110)	(396,396)
Proceeds from long-term loans and borrowings	388,506	292,000
Repayment of long-term loans and borrowings	(450,996)	(88,599)
Proceeds from issuance of shares, net of costs incurred of U.S. Dollar 10,716	299,284	-
Bonus received from depositary	8,560	-
Proceeds from long-term loans and borrowings from related parties	45,013	4,574
Repayments of long-term loans and borrowings from related parties	(44,797)	(100,000)
Purchase of treasury shares	(50)	-
Redemption of bonds	-	(27,680)
Capital lease payments	(7,102)	(17,725)
Net cash provided byfinancing activities	**129, 654**	**99,477**
Exchange effects on cash balances	475	1,762
Net decrease in cash and cash equivalents	**(1,513)**	**(12,393)**
Cash and cash equivalents at the beginning of the year	6,532	18,925
Cash and cash equivalents at the end of the period	**5,019**	**6,532**

Supplementary cash flow information

Interest paid	18,800	27,024
Income taxes paid	2,345	22,328

The accompanying consolidated notes are integral part of these consolidated financial statements.

JOINT STOCK COMPANY POLYMETAL

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2007
(In thousands of U.S. Dollars, except share data)

		Number of shares	Share capital	Additional paid-in capital	Treasury shares	Accumulated other comprehen-sive (loss)/ income	Retained earnings	Total share-holders' equity
Balance at December 31, 2005		**275,000,000**	**6,397**	**56,710**	**-**	**(4,299)**	**56,993**	**115,801**
Comprehensive income:								
Net income							61,687	61,687
Currency translation adjustment						14,746		14,746
Total comprehensive income								76,433
Balance at December 31, 2006		**275,000,000**	**6,397**	**56,710**	**-**	**10,447**	**118,680**	**192,234**
Comprehensive income:								
Net loss							(22,826)	(22,826)
Currency translation adjustment						45,761		45,761
Total comprehensive income								22,935
Share issuance, net of transaction costs of 10,716	17	40,000,000	301	299,835				300,136
Share based compensation				10,584				10,584
Acquisition of treasury shares	17	(5,540,323)			(50)			(50)
Balance at December 31, 2007		**309,459,677**	**6,698**	**367,129**	**(50)**	**56,208**	**95,854**	**525,839**

The accompanying consolidated notes are integral part of these consolidated financial statements.

1. BACKGROUND

Ownership structure

Open Joint Stock Company “Interregional Research and Production Association “Polymetal” was incorporated on March 12, 1998 in the Russian Federation. On December 19, 2006, the Open Joint Stock Company “Interregional Research and Production Association “Polymetal” was renamed as Open Joint Stock Company “Polymetal” (hereinafter, JSC “Polymetal” or “the Company”).

The Company’s majority shareholder prior to November 2005 was Closed Joint Stock Company ICT (“CJSC ICT”), which, together with its subsidiaries formed the ICT group. In November 2005, CJSC ICT sold their interests in the Company to Open Joint Stock Company Nafta Moskva (“JSC Nafta Moskva”).

In 2006, after restructuring of JSC Nafta Moskva, Nafta Moskva (Cyprus) Limited ,a subsidiary of JSC Nafta Moskva, became the sole shareholder of the Company until the Company’s public offering. In February 2007, the Company placed
40,000,000 ordinary shares with par value of Rouble 0.2 per share in the form of Global Depositary Receipts (“GDR’s”) on the London Stock Exchange, as well as shares on the Non-for-profit Partnership “Stock Exchange “Russian Trading System” and Closed Joint Stock Company “Moscow Interbank Currency Exchange”.

In June 2008 Nafta Moskva (Cyprus) Limited sold all of its interest in the Company (68.0%) to three parties: Quotan International Limited, controlled by ICT Group (24.05%), PPF Group NV, controlled by Petr Kellner (24.9%), and Inure Enterprises Limited, controlled by Alexander Mamut (19.05%).

Mr. V. N. Nesis, the General Director of JSC “Polymetal”, has a close family relationship with the owner of CJSC ICT. Accordingly, transactions with companies of the ICT group continue to be disclosed in these consolidated financial statements as related party transactions.

Composition of the Group

The Company and its subsidiaries are collectively referred to as “the Group”. As at December 31, 2007, the Company had the following significant mining subsidiaries:

Name of subsidiary	Field	Voting interest %	Effective ownership interest %
CJSC Zoloto Severnogo Urala	Vorontsovkoye	100	100
JSC Okhotskaya GGC	Khakandjinskoye, Urjevskoe	100	100
CJSC Serebro Territorii	Lunnoe, Arylakh	100	100
CJSC Serebro Magadana	Dukat	100	100

Changes in the Group structure and voting and ownership interests in major production subsidiaries in 2007 and 2006 are described in Note 24.

Business activities

The Group is engaged in gold and silver mining and related activities, including exploration, extraction, processing and reclamation. Since incorporation, the Group has acquired a number of gold and silver mining properties, which require significant investment to bring to commercial

production. The Group owns producing assets at Vorontsovkoye and Lunnoe fields, Dukat and Khakandjinskoye mines.

The Group has three reportable segments which are based on regional locations in Russia. All of the Group's customers, operations and assets are located in Russia.

The Group holds the following significant mining licenses: Vorontsovskoye field (Sverdlovsk region), Lunnoe field, Arylakh field and Dukat field (Magadan region), Khakandjinskoye field and Urjevskoe field (Khabarovsk region).

2. BASIS OF PRESENTATION

These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP"). The Company and its significant subsidiaries are all domiciled in the Russian Federation and maintain their accounting records and prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation ("RAR"). The accompanying consolidated financial statements have been prepared from these accounting records and adjusted, where necessary, to comply with U.S. GAAP.

Recent issued accounting pronouncements

Accounting pronouncements effective during the period

In June 2006, the Emerging Issues Task Force ("EITF") reached a consensus on EITF Issue No. 06-03, How *Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That is, Gross versus Net Presentation)* ("EITF No. 06-03"). EITF No. 06-03 provides that the presentation of taxes assessed by a governmental authority that is directly imposed on a revenue-producing transaction between a seller and a customer on either a gross basis (included in revenues and costs) or on a net basis (excluded from revenues) is an accounting policy decision that should be disclosed. The provisions of EITF No. 06-03 became effective for fiscal years beginning after December 15, 2006. The Group continues to present such taxes on a net basis in the consolidated statement of operations, and therefore, the adoption of EITF No. 06-03 had no effect on the Group's consolidated financial position or results of operations.

In June 2006, the Financial Accounting Standards Board ("FASB") issued Financial Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken in a tax return. It also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 became effective for fiscal years beginning after December 15, 2006. The Group adopted FIN 48 on January 1, 2007. The adoption of FIN 48 had no impact on the Group's beginning retained earnings.

Accounting pronouncements effective in the future

In September 2006, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 157, *Fair Value Measurements* ("SFAS No. 157"). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. SFAS No. 157 creates a fair value hierarchy, which prioritizes the inputs that should

be used in determining fair value. Under this pronouncement, companies must provide disclosures containing relevant information in the financial statements, allowing users to assess inputs used to measure fair value, as well as the effect of those measurements on earnings for the periods presented, including a reconciliation of the beginning and ending balances separately for each major category of assets and liabilities. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Group is currently evaluating the provisions of SFAS No. 157 to determine the potential impact, if any, the adoption will have on the Group's consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financials Liabilities – Including an Amendment of FASB Statement No. 115* ("SFAS No. 159"). This standard permits, but does not require, measurement of certain financial assets and financial liabilities at fair value. If the fair value option is elected, the unrealized gains and losses are reported in earnings at each reporting date. Generally, the fair value option may be elected on an instrument-by-instrument basis, as long as it is applied to the instrument in its entirety. The fair value option election is irrevocable, unless a new election date occurs. SFAS No. 159 requires prospective application and also establishes certain additional presentation and disclosure requirements. The standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Group adopted the provisions of SFAS No. 159 effective January 1, 2008. Management has decided not to designate any additional financial instruments to be accounted for at the fair value effective January 1, 2008 and therefore believes that the adoption will not have a material impact on the Group's financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* ("SFAS No. 141R"). SFAS No. 141R significantly changes the accounting for business combinations. Under SFAS No. 141R, an acquirer entity will be required to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition date fair value with limited exceptions. SFAS No. 141R will change the accounting treatment for certain specific acquisition related items including expensing acquisition related costs as incurred, valuing noncontrolling interest at fair value at the acquisition date and expensing restructuring costs associated with the acquired business. SFAS No. 141R is to be applied prospectively to the business combinations for which the acquisition date is on or after January 1, 2009. The Group is currently assessing the impact of adopting the statement.

In December 2007, FASB issued SFAS No. 160, N*oncontrolling Interest in Consolidated Financial Statements –an amendment of Accounting Research Bulletin ("ARB") 51, Consolidated Financial Statements* ("SFAS No. 160"). SFAS No. 160 establishes accounting and reporting standards for ownership interests in subsidiaries held by third parties, the amount of consolidated net income attributable to the parent and to the noncontrolling interest, changes in a parent's ownership interest, and the valuation of retained noncontrolling equity investments when the subsidiary is deconsolidated. SFAS No. 160 also establishes disclosure requirements that clearly identify and distinguish between the interests of the parent and the interest of the noncontrolling owners. SFAS No. 160 is effective for fiscal periods beginning on or after December 15, 2008. Earlier adoption is prohibited. The Group will apply this standard for its consolidated financial statements issued for fiscal year beginning January 1, 2009. The Group has not yet determined the impact of this standard will have on the Group's consolidated results of operations, financial position or cash flows.

In May 2007, the FASB issued FASB Staff Position FIN 39-1, *Amendment of FASB Interpretation No. 39 ("FSP FIN 39-1")*. FSP FIN 39-1 modifies FASB Interpretation No. 39, Offsetting of Amounts Related to Certain Contracts ("FIN No. 39") and permits companies to offset cash collateral receivables or payables with net derivative positions under certain circumstances. FSP FIN 39-1 is effective for fiscal years beginning after November 15, 2007, with early adoption permitted.

The Group believes that the adoption of FSP FIN 39-1 will not have material effect on its consolidated financial statements.

Use of estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, including discussion and disclosure of contingent liabilities. Significant areas requiring the use of management estimates relate to the determination of mineral reserves, mine closure liabilities, reclamation and environmental obligations, impairment of assets and valuation allowances for deferred tax assets. Actual results could differ from these estimates.

Reporting and functional currency

The Russian Ruble ("Ruble") is considered to be the functional currency of the Company and all its subsidiaries domiciled in the Russian Federation. Most of the Group's sales revenues and purchases and certain financing agreements are settled in Russian Rubles. The U.S. Dollar is the reporting currency selected by the Group for purposes of financial reporting in accordance with U.S. GAAP.

As a result, the transactions and balances in the accompanying consolidated financial statements have been translated into U.S. Dollars in accordance with the relevant provisions of SFAS No. 52, Foreign Currency Translation. Consequently, assets and liabilities are translated at period closing exchange rates. Revenues, expenses, gains and losses have been translated using period average exchange rates. Translation differences resulting from the use of these exchange rates have been included as a separate component of shareholders' equity.

Transactions in foreign currencies are recorded at the exchange rate prevailing on the date of the transaction. Assets and liabilities denominated in foreign currencies are expressed in the functional currency at the exchange rates in the effect at the balance sheet date.

The following exchange rates were used at the reporting dates:

	December 31, 2007	December 31, 2006
U.S. Dollar	24.55	26.33
Average exchange rate for the year, U.S. Dollars	25.55	27.14

3. SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation

The consolidated financial statements include the results of operations of all entities in which the Company directly or indirectly controls more than 50 percent of the voting power and all variable interest entities in which the Company, or a subsidiary in the Group is regarded to be the primary beneficiary.

All intercompany transactions and balances between Group companies have been eliminated.

Business acquisitions

Business acquisitions from third parties are accounted for using the purchase method of accounting. Under this method, the purchase price is allocated to the assets acquired and liabilities assumed based on the fair value at the time of the acquisition. The excess purchase price over the fair value of identifiable assets and liabilities acquired is treated as goodwill. The results of operations of entities acquired from third parties are included in the Group's results of operations from the date of acquisition.

Acquisitions of entities under common control are accounted for on a carryover basis, which results in the historical book value of assets and liabilities of the acquired entity being combined with the assets and liabilities of the Group. The consolidated and combined historical statements of the Group are retroactively restated to reflect the effect of the acquisition during the entire period in which the entities where under common control. Any different between the purchase price and the net assets acquired is reflected in shareholders' equity.

Asset impairment

The Group assesses its held-for-use long lived assets for impairment when events or changes in circumstances indicate that the related carrying amount may not be recoverable. If the sum of estimated future cash flows on an undiscounted basis is less than the carrying amount of the related assets, an impairment is considered to exist. The related impairment loss is measured by comparing the estimated future cash flows on a discounted basis to the carrying amount of the asset.

An individual operating mine is not a typical "going-concern" business because of the finite life of its reserves. The allocation of goodwill to an individual operating mine will result in an eventual goodwill impairment due to the wasting nature of the mine reporting unit. In accordance with the provisions of SFAS 142, *Goodwill and Other Intangibles* ("SFAS 142"), the Group performs a review of goodwill for impairment, at least annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

In accordance with SFAS No. 142, goodwill is reviewed for impairment by comparing the carrying value of each reporting unit's net assets (including allocated goodwill) to the fair value of those net assets. If the reporting unit's carrying amount is greater than its fair value, then a second step is performed whereby the portion of the fair value that relates to the reporting unit's goodwill is compared to the carrying value of that goodwill. The Company recognizes a goodwill impairment charge for the amount by which the carrying value of goodwill exceeds the fair value. The Company has determined that there are no impairment losses in respect of goodwill for any of the reporting periods covered by these financial statements.

Cash and cash equivalents

Cash and cash equivalents include cash and other highly liquid investments that are readily convertible to known amounts of cash and with an original maturity of three months or less at the date of purchase.

Accounts receivable

Accounts receivable are measured at cost less an allowance for doubtful accounts, which is established based upon an assessment of the aging of accounts and the Group's past experience of collecting payments. The Group had no allowance for doubtful accounts outstanding at December 31, 2007 or 2006.

Inventories and spare parts

Inventories including gold and silver in process, refined metals, dore, ore stockpiles, spare parts and consumable supplies are stated at the lower cost or market value. Cost is determined as the sum of the applicable expenditures and charges directly or indirectly incurred in bringing inventories to their existing condition and location.

Gold and silver in process, dore are valued at the average total production costs at the relevant stage of production. Ore stockpiles are valued at the average moving cost of mining ore. Spare parts and consumable supplies are valued at the lower of weighted average cost or market value. Refined metals are valued at the cost of production of per unit of gold or silver.

Write downs are made for unrealizable inventory in full.

Financial instruments

A financial instrument is defined as cash, evidence of an ownership interest in an entity, or a contract that imposes an obligation to deliver or right to receive cash or another financial instrument. The fair values of financial instruments are determined with reference to various market information and other valuation methods, as considered appropriate. However, considerable judgment is required to interpret market data and to develop the estimates of fair value. Accordingly, the estimates presented herein may differ from the amounts the Group could receive in current market exchanges.

For long-term borrowings, the difference between the fair value and carrying value was not material as interest rate as at December 31, 2007 approximates market rate and there were no change for the credit rating of the Group in 2007. The carrying values of cash and cash equivalents, other short-term investments, accounts and notes receivable, accounts and notes payable, other accrued liabilities, taxes payable and short-term debt, approximate their fair values because of the short maturities of these instruments.

Derivatives

SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities, as amended* ("SFAS No. 133"), establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. SFAS No. 133 requires an entity to recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. SFAS No. 133 provides that normal purchase and normal sale contracts, when appropriately designated, are not subject to the statement. Normal purchases and normal sales are contracts which provide for the purchase or sale of something other than a financial instrument or derivative instrument that will be delivered in quantities expected to be used or sold by the reporting entity over a reasonable period in the normal course of business. To qualify for the normal purchases and normal sales exception, it must be probable at inception and throughout the term of the individual contract that the contract will not settle net and will result in physical delivery. The Group's forward sales contracts are designated as normal purchases and sales. The Group does not have any other derivative financial instruments.

Property, plant and equipment

Property, plant and equipment consist of assets of the Group directly related to mining and processing of ore and include costs of development of the mining properties, the costs of acquisition or construction of property, plant and equipment and capitalized interest. Expenditures for major improvements and renewals are capitalized. The cost of maintenance, repairs and replacement of minor items of plant and equipment is charged to operations as incurred. Interest attributable to the

acquisition or construction of property, plant and equipment is capitalized using an overall borrowing rate as a cost of the asset up to the time the asset is put into use. All other interest is expensed as incurred. Gains and losses on the disposal of assets are included in the statement of operations in the period of disposal.

Mineral exploration costs are expensed as incurred. When it has been determined that a mineral property can be economically developed as a result of established proven and probable reserves, the costs incurred in exploration and development of such property, including costs to further delineate the ore body and remove any overburden to initially expose the ore body are capitalized.

In accordance with EITF Issue 04-6, *Accounting for Stripping Costs in the Mining Industry*, post production stripping costs are considered the costs of the extracted minerals under a full absorption costing system and recognized as a component of inventory to be recognized in cost of sales in the same period as the revenue from the sales of inventory.

Leased property, plant and equipment meeting the criteria of capital lease are capitalized; valued at the lower of the assets fair value and net present value of the total minimum future lease payments. The corresponding part of lease payments is recorded as a liability. Amortization of capitalized leased assets related to mining is computed using the units-of-production method or over the term of the lease, if shorter.

Depletion of property, plant and equipment related to mining are computed using the units-of-production method based on the actual production for the period compared with total estimated proven and probable reserves. In respect of those items of property, plant and equipment whose useful lives are expected to be less than the life of mine, depreciation over the period of the items' useful life is applied.

Depreciation of non-mining assets is provided on a straight-line basis over the economic useful lives of these assets at the following annual rates:

- machinery and equipment 1–20 years;
- transport and other 1–10 years.

Property, plant and equipment are assessed for possible impairment in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* ("SFAS No. 144"). SFAS No. 144 requires long-lived assets with recorded values that are not expected to be recovered through future cash flows to be written down to current fair value. Fair value is generally determined from estimated discounted future net cash flows.

Construction-in-progress comprises costs directly related to mine development, construction of buildings, infrastructure, processing plant, machinery and equipment. Cost also includes finance charges capitalized during the development and construction periods where such costs are financed by borrowings. Amortization or depreciation of these assets commences when the assets are put into production.

Pension obligations

The Group pays mandatory contributions to the state social funds, which are expensed as incurred. For the year ended December 31, 2007 and 2006, the Group contributed U.S. Dollar 11,781 and 14,919, respectively.

Reclamation and mine closure

The Group accounts for reclamation, site restoration and closure obligations based on the provisions of SFAS No. 143, *Accounting for Asset Retirement Obligations*. When the liability is initially recorded, the Group capitalizes the cost by increasing the carrying amount of the related long lived asset. Over time, the liability is accreted to its present value at the end of each period, and capitalized cost is amortized over the mine life or the useful life of the related asset.

Income taxes

The Group accounts for income taxes using the balance sheet liability method required by SFAS No. 109. Deferred income tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, in accordance with SFAS No. 109. Deferred income tax assets and liabilities are measured using enacted tax rates for periods in which these temporary differences are expected to reverse. Valuation allowances are provided for deferred income tax assets when management believes that it is more likely than not that the assets will not be realized.

In the normal course of business the Group is subject to examination by taxing authorities throughout the Russian Federation. Interregional Inspectorate of the Federal Tax Service ("IIFTS") have commenced examinations of the Group's tax returns for 2003 through 2005. No significant adjustments have been proposed by IIFTS as at December 31, 2007.

Uncertain tax positions are recognized in the financial statements for positions which are considered more likely than not of being sustained based on the technical merits of the position on audit by the tax authorities. The measurement of the tax benefit recognized in the financial statements is based upon the largest amount of tax benefit that, in management's judgement, is greater than 50% likely of being realized based on a cumulative probability assessment of the possible outcomes. As at December 31, 2007, the Group's liability for unrecognized tax benefit was U.S. Dollar 1,839. The whole amount would affect the Group's effective tax rate if recognized.

The Group records penalties and accrued interest related to uncertain tax positions in income tax expense. As at December 31, 2007, U.S. Dollar 91 were included in the liability for uncertain tax positions for the probable payment of interest and penalties.

There are no items that are affected by expiring statute of limitations within the next 12 months.

Revenue recognition

Revenue is derived principally from the sale of gold and silver and is measured at the fair value of consideration received or receivable, after deducting discounts. A sale is recognised when the significant risks and rewards of ownership have passed. This is usually when title and risk have passed to the customer and the goods have been delivered to the customer. Revenue is presented in consolidated statement of operations net of VAT.

The Group sells metal to banks through long-term agreements. The sales price, as determined in the agreement, may be variable based upon the London Metal Exchange spot price or fixed.

Share based compensation

The Group's board of directors awards share options to certain employees. The Group applies SFAS No. 123 (revised 2004), *Share-Based Payment* ("SFAS 123(R)"), to its accounting for share based compensation. SFAS 123(R) requires companies to recognize compensation costs for share-based payments to employees based on the grant-date fair value of the award.

The fair value of the share-based payments is calculated at the grant date using the Black-Scholes option pricing model. For equity-settled share-based payments, the fair value is determined using the Black-Scholes model and expensed on a straight-line basis over the vesting period based on the Group's estimate of the shares that will eventually vest.

Share options are subject to a three year vesting condition and the fair value is recognized as an employee benefit expense with a corresponding increase in additional paid-in-capital over the vesting period. The proceeds received, net of any directly attributable transaction costs are credited to ordinary share capital (nominal value) and additional paid-in-capital when the options are exercised.

Comprehensive income

Comprehensive income is defined as all changes in shareholders' equity, except those arising from transactions with shareholders. Comprehensive income includes net income and other comprehensive income (loss), which for the Group consists of changes in foreign currency translation gains or losses.

4. RECLASSIFICATIONS

Certain comparative information presented in the consolidated balance sheet as at December 31, 2006 has been reclassified in order to achieve comparability with the presentation used in the consolidated balance sheet as at December 31, 2007. After considering all relevant quantitative and qualitative information, the Group concluded that these reclassifications are not material to the consolidated financial statements as at December 31, 2006:

	Before reclassifications	After reclassifications	Difference
Accounts receivable	17,090	3,218	(13,872)
Prepayments to suppliers	-	13,872	13,872
Short-term loans to third parties	442	-	(442)
Related party receivables and prepayments	126	-	(126)
Other current assets	13,336	13,904	568
Investments and long-term loans to third parties	-	615	615
Investments	250	-	(250)
Long-term loans to third parties	365	-	(365)
Total	**31,609**	**31,609**	**-**

In previous reporting periods prepayments to suppliers were not presented separately in the consolidated balance sheet, and were instead included in accounts receivable. In 2007, it was decided to present the balance of prepayments to suppliers separately.

In previous reporting periods short-term loans to third parties and related party receivables and prepayments were presented separately in the consolidated balance sheet. As at December 31, 2007 as there is no balance in short-term loans to third parties and related party receivables and prepayments, management decided to aggregate the December 31, 2006 balances within other current assets.

In previous reporting periods investments and long-term loans to third parties were presented separately in the consolidated balance sheet. As at December 31, 2007, as there is no balance in long-term loans to third parties, management decided to aggregate the December 31, 2006 balances of investments and long-term loans to third parties.

5. INVENTORIES

	December 31, 2007	December 31, 2006
Consumables and spare parts	73,613	66,336
Ore stock piles	62,106	48,634
Work-in-process	35,566	28,340
Dore	12,784	1,890
Refined metals	29,072	10,429
Total	**213,141**	**155,629**

6. VAT RECEIVABLE

	December 31, 2007	December 31, 2006
Short-term VAT receivable	52,078	45,335
Long-term VAT receivable	10,288	9,019
Total	**62,366**	**54,354**

Long-term value-added tax (“VAT”) receivable primarily represents VAT balances resulting from capital expenditures and operating activities which are not expected to be recovered within the next calendar year due to specific requirements of the tax regulations. Management believes that these balances are fully recoverable from the tax authorities when the respective capital assets qualify as having been put into operation for VAT purposes.

7. DEFERRED TAX

The components of deferred tax assets and liabilities were as follows:

	December 31, 2007	December 31, 2006
Deferred tax assets:		
Tax losses carried forward	2,140	3,962
Deferred payments	1,785	-
Other current assets	1,327	517
Accounts payable	2,480	299
Total deferred tax assets	**7,732**	**4,778**
Deferred tax liabilities:		
Property, plant and equipment	(37,628)	(35,284)
Inventories	(11,437)	(14,902)
Total deferred tax liabilities	**(49,065)**	**(50,186)**
Net deferred tax liabilities	**(41,332)**	**(45,408)**
Deferred tax asset, short-term	3,806	816
Deferred tax asset, long-term	3,926	3,962
Deferred tax liability, short-term	(11,437)	(14,902)
Deferred tax liability, long-term	(37,628)	(35,284)

The tax losses carried forward represent the amounts, which will be off-set against future taxable income to be generated by CJSC Serebro Territorii, CJSC Serebro Magadana, JSC Okhotskaya GGC and the Company during the period up to 2015. Each legal entity within the Group represents a separate tax-paying component for income tax purposes. The tax losses of one entity cannot be used to reduce taxable income of other entities in the Group.

As at December 31, 2007 and 2006 the aggregated tax losses carried forward were U.S. Dollar 8,817 (Rubles 216,420 thousand) and U.S. Dollar 16,509 (Rubles 434,711 thousand) respectively.

As at January 1, 2007 the Group changed the tax base calculation of its work-in-progress, ore, dore and refined metals, allocating certain direct production costs previously treated as costs of the period incurred and not allocated to inventory for statutory tax purposes. As a result of the change, deferred tax liability as at December 31, 2007 and net loss for the year ended December 31, 2007 decreased by U.S. Dollar 8,136, basic and diluted loss per share decreased by U.S. Dollars 0.027.

The Group does not recognize a deferred tax liability on undistributed earnings of its subsidiaries as it expects that these earnings will ultimately be recovered in tax-free transactions.

8. OTHER CURRENT ASSETS

	December 31, 2007	December 31, 2006
Taxes receivable	12,442	7,977
Other receivables	4,111	2,000
Other current assets	1,504	3,927
Total	**18,057**	**13,904**

9. PROPERTY, PLANT AND EQUIPMENT

	December 31, 2007	December 31, 2006
Buildings and underground workings	210,710	147,358
Machinery and equipment	155,607	161,571
Transport and other	52,079	22,130
Mineral rights	159,294	130,175
Construction-in-progress	96,060	58,770
Total cost	**673,780**	**520,004**
Less: Accumulated depreciation and depletion	**(171,310)**	**(113,586)**
Net book value	**502,470**	**406,418**

At December 31, 2007, capital leases included within property, plant and equipment total U.S. Dollar 47,555 (of which machinery and equipment was U.S. Dollar 39,197 and transport and other was U.S. Dollar 8,358) (as at December 31, 2006: U.S. Dollar 79,335, of which machinery and equipment was U.S. Dollar 62,183 and transport and other was U.S. Dollar 17,152).

At December 31, 2007, total accumulated depreciation and depletion of capitalized leases was U.S. Dollar 31,749 (of which machinery and equipment was U.S. Dollar 26,525 and transport and other was U.S. Dollar 5,224). At December 31, 2006, total accumulated depreciation and depletion of capitalized leases was U.S. Dollar 20,328, of which machinery and equipment was U.S. Dollar 15,972 and transport and other was U.S. Dollar 4,356).

Long-term deferred exploration expenditures, which are included within construction-in-progress, amounted to U.S. Dollar 41,520 and U.S. Dollar 11,766 at December 31, 2007 and 2006, respectively.

Mineral rights of the Group are comprised of mineral rights acquired by the Group upon purchase of subsidiaries. Accumulated depletion of mineral rights was U.S. Dollar 28,467 and U.S. Dollar 10,969 at December 31, 2007 and 2006, respectively.

Construction-in-progress in the amount of U.S. Dollar 96,060 and U.S. Dollar 58,770 is not being amortized as it was not yet put into use as at December 31, 2007 and 2006, respectively.

In 2007, management of the Group decided that it was no longer economically viable to mine the open pit reserves located at Lunnoe field. Therefore, the related open pit mine is not currently used in

operations and has been written off entirely, which has resulted in impairment losses of U.S. Dollar 6,676 (see Note 21), which relates entirely to Magadan segment.

As at December 31, 2007, property, plant and equipment with carrying value of U.S. Dollar 13,860 was pledged as collateral for the loan from ABN Amro (see Note 14).

10. GOODWILL

	December 31, 2007
Beginning balance	31,896
Additions during the current year (see Note 29)	10,183
Reclassification	(13,226)
Effect of foreign exchange rate	1,288
Total	**30,141**

During the year ended December 31, 2007, the Group has reclassified certain amounts from goodwill to mineral rights within property, plant and equipment related to 2006 acquisitions. Subsequent to the issuance of the consolidated financial statements of the Group for the year ended December 31, 2006, management determined that in accordance with EITF 04-3, *Mining Assets: Impairment and Business Combination*, value beyond proven and probable reserves not previously identified separately from goodwill in the purchase price allocation, should instead be classified as mineral rights, which are a component of property, plant and equipment. In addition, management determined that the interests acquired during 2006 in ZAO Enisey Mining-and-Geological Company and Albazino Resources LLC did not meet the definition of acquired businesses in accordance with SFAS No. 141, *Business Combinations*, and should instead have been accounted for as acquisitions of mineral rights. After considering all relevant quantitative and qualitative information, the Group concluded that these reallocations were not material to the consolidated financial statements for the year ended December 31, 2006. As a result, an amount of goodwill of U.S. Dollar 13,226 as at December 31, 2007 was reclassified to mineral rights within property, plant and equipment, net of deferred taxes equal to U.S. Dollar 2,422.

11. LONG-TERM LOANS TO RELATED PARTIES

	Interest Rate	December 31, 2007	December 31, 2006
Accord-Invest LLC	10.5%	5,334	5,343
Employees	1%	785	795
Total		**6,119**	**6,138**

Accord-Invest LLC together with JSC “Polymetal” was under common control of the parent company Nafta Moskva (Cyprus) Limited (see Note 1). The loan to Accord-Invest is unsecured and is due in January 2010.

12. SHORT-TERM DEBT AND CURRENT PORTION OF LONG-TERM DEBT

	Interest rate	December 31, 2007	December 31, 2006
U.S. Dollar denominated			
Sberbank	7.6 - 8%	-	69,591
Uralsib	9%		20,000
Alfa Bank	8%	-	14,920
Current portion of long-term debt (see Note 14)		152,006	122,105
Total U.S. Dollar denominated		**152,006**	**226,616**
Russian Ruble denominated			
Investros LLC	0%	-	3,154
Total Russian Ruble denominated		**-**	**3,154**
Total		**152,006**	**229,770**

Short-term debt facilities are not collateralized.

13. CAPITAL LEASE LIABILITIES

The Group entered into certain Russian Ruble denominated financial leases for machinery, equipment and transport vehicles.

Future minimum lease payments for the assets under capital leases at December 31 are as follows:

	December 31, 2007	December 31, 2006
Current portion	2,417	4,210
Long-term portion	147	2,445
Present value of minimum payments	**2,564**	**6,655**
Interest payable over the term of lease	239	1,329
Total future minimum lease payments	**2,803**	**7,984**

The table below summarizes the maturities of the capital lease liabilities:

	December 31, 2007
For the year ending December 31, 2008	2,628
2009	141
2010	34
Total	**2,803**

14. LONG-TERM DEBT

	Interest rate	December 31, 2007	December 31, 2006
U.S. Dollar denominated			
Sberbank	Libor + 2%	98,000	132,000
ABN Amro Bank	Libor + 2%	50,525	60,000
Bank Uralsib	8%	44,000	-
Gazprombank	8%	15,200	100,000
Total		**207,725**	**292,000**
Russian Ruble denominated			
Gazprombank	8%	15,481	-
		15,481	**-**
Total		**223,206**	**292,000**
Less current portion of long-term debt (see Note 12)		(152,006)	(122,105)
Total		**71,200**	**169,895**

The table below summarizes the maturities of long-term debt:

	December 31, 2007
Year ending December 31, 2008	152,006
2009	71,200
Total	**223,206**

Sberbank. In December 2006, the Group received a long-term loan facility from Sberbank of Russia which allows the Group to borrow up to U.S. Dollar 153,000 to finance its current operations, contract financing, including replenishment of working capital. The credit facility is valid until December 2009. Interest is payable monthly, and is based on LIBOR plus 2%, which resulted in rates of 6.4875% and 5.3138% as at December 31, 2007 and 2006, respectively. As at December 31, 2007, the outstanding balance under the credit facility was U.S. Dollar 98,000.

The Group has to comply with certain financial and non-financial covenants to prevent the closure of the Sberbank credit facility. One such covenant is a requirement to obtain consent for the granting of collateral interests under the Company's subsequent financing arrangements. During 2006 the Group breached these covenants by pledging collateral to secure its U.S. Dollar 100 million loan from Gazprombank without obtaining prior written approval from Sberbank. In January 2007 Sberbank confirmed in writing that, taking into account the planned early redemption during 2007 of the Gazprombank loan, it would not demand early repayment of the Sberbank loan.

ABN Amro Bank. In December 2006, the Group received a long-term loan from ABN Amro Bank ("ABN Amro") in the amount of U.S. Dollar 60,000 to refinance its debt to Standard Bank London. The loan is repayable in monthly instalments commencing in June 2007 up to the last installment in December 2008. Interest is payable monthly and is based on LIBOR plus 2%, which resulted in rates of 6.4875% and 5.3138% as at December 31, 2007 and 2006, respectively. Under the loan agreement with ABN Amro, the Group has to comply with certain financial and non-financial covenants. The loan agreement restricts the Group from:

(i) disposing of its assets (including transfers, leases or sales);
(ii) undertaking any type of corporate reorganization (including mergers and demerges);
(iii) creating or incurring other forms of financial indebtedness (such as making loans or granting guarantees); and
(iv) taking any actions in respect of its shares, capital or participatory interest (including issuing new shares or otherwise altering its existing share capital) without the prior written consent of ABN Amro except for the offer and listing of up to 40% of the Company's share capital.

The loan agreement restricts the Company's ability to pay dividends for any of its financial years during the term of the loan or to make acquisitions in excess of U.S. Dollar 5 million without the prior written consent of ABN Amro.

As at December 31, 2007, property, plant and equipment with a carrying value of U.S. Dollar 13,860 was pledged as collateral for the loan from ABN Amro (see Note 9).

Gazprombank. In July 2006, the Group received a long-term loan from Gazprombank amounting to U.S. Dollar 100,000 for equipment purchase and replenishment of working capital. The loan was repayable in monthly instalments due to commence July 31, 2007 up to the last instalment in 2009. As a condition of Sberbank waiving any right to early repayment of the Sberbank loan as a result of a covenant violation, the Group committed to repay the Gazprombank loan in 2007. Accordingly, the total debt to Gazprombank as at December 31, 2006 was classified as short-term and included in the current portion of long-term debt (see Note 12). In March 2007, the loan to Gazprombank was fully repaid.

In September 2007, the Group received a long-term facility from Gazprombank which allows the Group to borrow funds, denominated in either U.S. Dollar or rubles, up to U.S. Dollar 62,969 (1,545,654 thousand rubles as at December 31, 2007) to finance its current operations. The credit facility is valid until December 2008. Interest is payable on a monthly basis. As at December 31, 2007, the outstanding balance under the credit facility was U.S. Dollar 30,681, including U.S. Dollar 15,200 denominated in U.S. Dollars and U.S. Dollar 15,481 (380,000 thousand rubles as at December 31, 2007) denominated in rubles.

Covenants to the loan agreements require the Group to maintain certain financial ratios, prohibit any change to the general nature of the business and limit the disposal of assets.

Bank Uralsib. In June 2007, The Group received a long-term facility from Bank Uralsib which allows the Group to borrow up to U.S. Dollar 60,000 to finance its current operations. The credit facility is valid until July 2008. Interest is payable on a monthly basis. As at December 31, 2007, the outstanding balance under the credit facility was U.S. Dollar 44,000. Covenants to the loan agreements require the Group to maintain certain financial ratios, prohibit any change to the general nature of the business and limit the disposal of assets.

15. RECLAMATION AND MINE CLOSURE OBLIGATION

Mine closure obligations include decommissioning and land restoration costs and are recognized on the basis of existing project business plans as follows**:**

Name of subsidiary	CJSC Zoloto Severnogo Urala	JSC Okhotskaya GGK	CJCS Serebro Magadana	GJSC Serebro Territorii	Total
Balance as at December 31, 2006	**1,495**	**2,272**	**2,253**	**1,210**	**7,230**
Accretion of reclamation and mine closure obligation	57	157	37	28	**279**
Translation effects	108	167	163	88	**526**
Balance as at December 31, 2007	**1,660**	**2,596**	**2,453**	**1,326**	**8,035**

The Group does not have assets that are legally restricted for purposes of settling asset retirement obligations.

16. DEFERRED PAYMENTS

Deferred payments as at December 31, 2007 comprised of an upfront payment received from Deutsche Bank Trust Company Americas. This payment was made to the Company in exchange for the Company selecting Deutsche Bank Trust Company Americas (the “Bank”) as its executive depositary bank for GDR programme at the London Stock Exchange. According to the terms of depositary agreement, the Bank should execute the function of the depositary for a seven year period. In case of early termination of the depositary agreement, the Company will have to pay back certain part of the granted bonus as compensation.

17. SHAREHOLDERS’ EQUITY AND EARNINGS PER SHARE

As at December 31, 2007 and 2006, the authorized share capital of the Company comprised of 2,444,000,000 ordinary shares with a par value of Ruble 0.2 per share and 100,000 series A preference shares with a par value of Ruble 100.

As at December 31, 2007 and 2006, the issued share capital of the Company comprised of 315,000,000 and 275,000,000 ordinary shares, respectively, with a par value of Ruble 0.2 per share. As at December 31, 2007 and 2006, the outstanding share capital of the Company comprised of 309,459,677 and 275,000,000, respectively, ordinary shares with a par value of Ruble 0.2 per share. No preference shares were issued or outstanding.

As discussed in Note 1, in February 2007, the Company placed 40,000,000 ordinary shares with a par value of Ruble 0.2 per share in the form of GDR’s on the London Stock Exchange. The Company received U.S. Dollar 307,844 in cash, which was reduced by transaction costs of U.S. Dollar 10,716..

In September 2007, as part of the Group’s acquisition of Polymetal ESOP, the Group acquired 5,540,323 treasury shares (see Note 24).

Reserves available for distribution to shareholders are based on the statutory financial statements of the Company as a stand-alone entity, which are prepared in accordance with Regulations on Accounting and Reporting of the Russian Federation, and which differ significantly from U.S. GAAP. Russian legislation identifies the basis of distribution as accumulated profit. However, current legislation and other statutory regulations dealing with distribution rights are open to legal interpretation; consequently, actual distributable reserves may differ from the amount of accumulated profit under Russian statutory accounting rule.

The Company has potentially dilutive securities including the Group's share option plan, which was established during 2007 (see Note 18). As the Company was in a net loss position for the period ended December 31, 2007, the stock options were anti-dilutive and therefore excluded from the calculation of diluted (loss)/earnings per share. Accordingly, basic and diluted (loss)/earnings per share were equal for the year ended December 31, 2007. The Group had no potentially dilutive securities outstanding during 2006, and accordingly, basic and diluted (loss)/earnings per share were also equal for the year ended December 31, 2006.

Basic (loss)/earnings per share were calculated by dividing net (loss)/income, as appropriate, by the weighted average number of ordinary shares outstanding during the respective reporting period.

18. SHARE-BASED PAYMENTS

In 2007, the Group established a share option plan (the "Option Plan") for executive directors and senior employees of the Group.

The number of shares which a qualifying participant has become entitled to was determined by the Board of Directors on March 1, 2007. The options vest over a three year period from the grant date, contingent on continued employment with the Group.

A summary of the Group's Option Plan is presented below:

	Number of shares	Weighted average exercise price (per share), U.S. Dollar	Weighted average fair value of options (per share), U.S. Dollar	Aggregate intrinsic value, U.S. Dollar
Outstanding at December 31, 2006	**-**	**-**	**-**	**-**
Granted	5,540,332	0.04	6.97	38,848
Exercised	-	-	-	-
Forfeited	(230,847)	0.04	6.97	(1,155)
Outstanding at December 31, 2007	**5,309,485**	**0.04**	**6.97**	**37,693**

As at December 31, 2007 the Group had the following share options outstanding:

Exercise prices, U.S. Dollar	Number of shares	Remaining weighted average life in years	Average intrinsic value
0.04	5,309,485	2.17	7.10

None of the share options outstanding as at December 31, 2007 were fully vested, and will vest over a three-year period from the grant date.

The fair value of share options granted during the year ended December 31, 2007, was estimated using the Black-Scholes option pricing model. The following assumptions were used to value share based awards:

- *Expected forfeitures.* This assumption is estimated using historical trends of employees turnover. As the Group typically only grants options to senior employees and the turnover rate for such employees is minimal, the Group has estimated expected forfeitures to be 5% a year.
- *Expected volatility.* Since the Group's ordinary shares are publicly traded only since February 2007, expected volatility has been estimated based on an analysis of the historical stock price volatility of comparable public companies for a preceding period equal to the expected term of the option grant being valued.
- *Expected term.* As the option plan has a three year vesting condition and the participant may exercise his right to redeem shares within three month of the date of obtaining the right to do so, the Group has estimated expected term as three years.
- *Fair value of common stock* is equal to the market price of underlying shares at the grant date.
- *Risk-free interest rate.* To estimate the risk-free rate, the Group used the implied yield currently available on Russian Eurobonds with a remaining term equal to the expected term of the option grant being valued.

Risk free rate	5.5%
Expected dividend yield	0%
Expected volatility	35.0%
Expected life, years	3
Fair value of shares, U.S. Dollars	7.05

For the year ended December 31, 2007, share based compensation in the amount of U.S. Dollar 10,584 (2006 – nil) was recognized in general, administrative and selling expenses. As at December 31, 2007, the Group had U.S. Dollar 28,761 of unrecognized share based compensation.

19. REVENUES

	Year ended December 31, 2007	**Year ended December 31, 2006**
Sales to third parties		
Sberbank	115,510	59,915
ABN Amro Bank	104,079	-
Gazprombank	60,674	12,001
Uralsib	25,644	6,606
Standard Bank London	-	165,885
IBG NIKoil	-	3,329
Total sales to third paries	**305,907**	**247,736**
Sales to related party		
Nomos Bank	-	67,169
Subtotal revenue from gold and silver sales	**305,907**	**314,905**
Other	2,840	691
Total	**308,747**	**315,596**

Revenues from Sberbank, ABN Amro Bank and Gazprombank individually exceed 10% of total revenue of the Group for 2007. Revenue from Sberbank was included in revenue of the North Ural segment – U.S. Dollar 65,476; the Khabarovsk segment – U.S. Dollar 45,773; and the Magadan segment – U.S. Dollar 4,261. Revenue from ABN Amro Bank was entirely included in revenue of the Magadan Segment. Revenue from Gazprombank was included in revenue of the North Ural segment – U.S. Dollar 14,632; the Khabarovsk segment – U.S. Dollar 26,155; and the Magadan segment – U.S. Dollar 19,887.

Revenues analysed by geographical regions are presented below:

	Year ended December 31, 2007	**Year ended December 31, 2006**
Sales within Russian Federation	204,668	149,711
Sales to Europe	104,079	165,885
Total	**308,747**	**315,596**

Presented below is an analysis of revenue from gold and silver sales:

	Year ended December 31, 2007			Year ended December 31, 2006		
	Thousand ounces	**Average price (U.S. Dollar per troy ounce)**	**U.S. Dollars**	**Thousand ounces**	**Average price (U.S. Dollar per troy ounce)**	**U.S. Dollars**
Gold	235	701.13	164,622	255	603.33	153,849
Silver	16,152	8.75	141,285	17,267	9.33	161,056
Total			**305,907**			**314,905**

In 2007, the Group delivered silver to ABN Amro Bank at fixed prices as determined by the terms of the sales contract ranging from U.S. Dollar 7.7891 to U.S. Dollar 7.82 per troy ounce for total sales of 14,493,940 troy ounces. The variance between the sales at fixed prices under the contract as compared to market prices quoted on the London Bullion Market Assosiation ("LBMA") resulted in a reduction to revenues of U.S. Dollar 75,704.

In 2006, the Group delivered silver to the Standard Bank London ("SBL") at fixed prices as determined by the terms of the sales contract ranging from U.S. Dollar 6.6575 to U.S. Dollar 7.95 per troy ounce for total sales of 9,015,036 troy ounces. The variance between the sales at fixed prices under the contract as compared to market prices quoted on the LBMA resulted in a reduction to revenues of U.S. Dollar 38,701.

Discounts from the LBMA market prices on sales to banks for the year ended December 31, 2007, amounted to U.S. Dollar 722 (2006: U.S. Dollar 948) for gold and U.S. Dollar 1,752 (2006: U.S. Dollar 1,339) for silver sales. Sales are recorded in the financial statements net of discounts..

20. COST OF SALES

	Year ended December 31, 2007	**Year ended December 31, 2006**
Operating costs (excluding staff costs)	105,943	78,471
Staff costs	38,242	28,473
Depreciation and depletion	47,329	39,366
Purchase of metal from third party	20,499	-
Mining tax	15,763	15,307
Other taxes, except for income taxes	7,319	6,166
Effect of change in accounting estimate	7,068	-
Other	11,945	3,500
Total	**254,638**	**171,283**

The nature of the heap leaching process inherently limits the ability to precisely monitor inventory levels and ,as a result, the balancing process is constantly monitored and estimates of recovery rates are refined based on actual results over time. As a result of reviews done to meet regulatory requirements, during 2007 the Group determined that the estimated recovery rates for heap leach process at Vorontsovskoye field applied previously to record costs associated with heap leach activities should be revised to reflect actual experience. As a result of the change, an amount of U.S.

Dollar 7,068 was charged to costs of the period incurred as a result of this change in accounting estimate.

21. OTHER OPERATING EXPENSES

	Year ended December 31, 2007	Year ended December 31, 2006
Impairment of property, plant and equipment (see Note 9)	6,676	-
Consulting services	6,137	-
Social payments	4,407	2,976
Taxes, other than income	4,367	1,021
Exploration expenses	1,973	5,347
Bank services	713	6,788
Loss on fixed asset disposals	343	1,339
Other expenses	2,807	3,736
Total	**27,423**	**21,207**

22. INCOME TAX

	Year ended December 31, 2007	Year ended December 31, 2006
Current income taxes	12,442	21,954
Deferred income taxes	(6,379)	3,801
Total	**6,063**	**25,755**

A reconciliation between the reported amount of income tax expense attributable to (loss)/income before minority interest and the amount of income tax expense that would result from applying the statutory income tax rate for the years ended December 31, 2007 and 2006 is as follows:

	Year ended December 31, 2007	Year ended December 31, 2006
(Loss)/income before income tax and minority interest	**(16,833)**	**93,703**
Statutory income tax (benefit)/expense at tax rate of 24 percent	(4,040)	22,489
Share based compensation	2,540	-
Permanent tax differences (non-deductible expenses)	7,563	2,816
Other	-	450
Total income tax expense	**6,063**	**25,755**

The actual tax expense differs from the amount which would have been determined by applying the statutory rate of 24% (2006: 24%) to the (loss)/income from operations before tax and minority interest as a result of the application of Russian tax regulations, which disallow certain deductions which are included in determination of income before taxes under U.S. GAAP. These deductions include social related expenditures and other non-production costs, certain general, administrative, financing, foreign exchange related and other costs.

23. SEGMENTS

The Group has three reportable segments:

- North Ural region (CJSC Zoloto Severnogo Urala);
- Khabarovsk region (JSC Ohotskaya GGK); and
- Magadan region (CJSC Serebro Territorii and CJSC Serebro Magadana).

The reportable segments are determined based on the Group's geographic regional profile. Minor companies (management, exploration, purchasing and other companies) which were not included into operating segments, were included into Corporate and other.

Segment results comprises of segment gross profit, calculated as segment revenues less cost of sales for each segment. Segment expenses represent cost of sales, which are costs incurred to produce gold and silver at each operating mine, and exclude the following costs that are not allocated to operating segments: amortization of corporate assets; administration costs, costs of financing and other non-operating costs.

Corporate and other revenues comprise revenues from services provided to third parties by the Group's non-mining subsidiaries. These include exploration works for other mining companies and design services related to ore field development and precious metal extraction technologies.

For the year ended December 31, 2007	North Ural	Khabarovsk	Magadan	Corporate and other	Total
Revenue	80,132	77,822	148,557	2,236	**308,747**
Cost of sales	(57,729)	(59,649)	(136,246)	(1,014)	**(254,638)**
Gross profit	22,403	18,173	12,311	1,222	**54,109**
Interest expenses, net					**(15,260)**
Other expenses, net					**(60,353)**
Total income from continuing operations before income tax and minority interest:					**(16,763)**
Segment assets:					
Property, plant and equipment, net	96,269	145,229	190,265	70,707	**502,470**
Accounts receivable, inventories, prepayment to suppliers, and VAT receivables	62,316	65,679	109,119	50,934	**288,048**
Goodwill	-	16,592	10,183	3,366	**30,141**
Total segment assets	158,585	227,570	309,567	123,271	**820,659**
Unallocated assets:					
Cash and cash equivalents					**5,019**
Other assets					**32,176**
Total assets					**857,854**

For the year ended December 31, 2006	North Ural	Khabarovsk	Magadan	Corporate and other	Total
Revenue	62,189	86,975	166,052	380	**315,596**
Cost of sales	(41,647)	(39,001)	(92,829)	2,194	**(171,283)**
Segment results - Gross profit	20,542	47,974	73,223	2,574	**144,313**
Interest expenses, net					**(25,267)**
Other expenses, net					**(25,343)**
Total income from continuing operations before income tax and minority interest:					**93,703**
Segment assets:					
Property, plant and equipment, net	87,352	139,632	160,554	18,880	**406,418**
Accounts receivable, inventories, prepayment to suppliers, and VAT receivables	52,334	76,043	77,441	31,359	**237,177**
Goodwill	-	24,261	855	6,780	**31,896**
Total segment assets	139,686	239,936	238,850	57,019	**675,491**
Unallocated assets:					
Cash and cash equivalents					6,532
Other assets					15,331
Total assets					**697,354**

24. ACQUISITION OF SUBSIDIARIES

CJSC Serebro Magadana

In November 2004, the Group acquired the remaining 20% interest in its subsidiary CJSC Serebro Magadana, the license owner for the Dukat mine, from company P.A.S. Silver (Cyprus) Ltd.
The Group paid U.S. Dollar 21,226 in cash at the time of the acquisition and agreed to pay up to U.S. Dollar 22,500 in additional contingent future payments. The future payments were to be determined annually based on the average yearly silver price per troy ounce (“FPS”) in the range U.S. Dollar 5.5 per ounce to U.S. Dollar 10.0 per ounce:

Range of silver price per troy ounce	Annual installments
5.5 < FPS < 6.0	500
6.0 < FPS < 7.0	1,000
7.0 < FPS < 8.0	2,000
8.0 < FPS < 9.0	5,000
9.0 < FPS < 10.0	6,000
10.0 < FPS	8,000

The agreement also contained a provision for early repayment on the occurrence of certain events, such as a public share offering. In the event of public offering the Group would pay 50% of any remaining contingent consideration within 30 days after listing.

The Group paid U.S. Dollar 2,000 during 2006 related to 2005 actual silver prices. In March 2007, as a result of the IPO in February 2007, the Group paid U.S. Dollar 10,250, which represented 50% of the total remaining potential contingent consideration of U.S. Dollar 20,500. The Group paid an additional amount of U.S. Dollar 8,000 during 2007 related to 2006 actual silver prices. The remaining contingent consideration, which will be paid based upon 2007 actual silver prices, amounting to U.S. Dollar 2,250 must be paid no later than December 2008 and is recorded within accounts payable as of December 31, 2007.

As a result of the additional contingent payments made and accrued for during 2007, bringing the total consideration to U.S. Dollar 43,726, the Group recorded goodwill of U.S. Dollar 10,183, representing the excess cost of the acquisition over the fair value of net assets acquired of U.S. Dollar 33,543.

JSC Okhotskaya GGC

In July 2006, the Group acquired an additional 30.76% interest in JSC Okhotskaya GGC, an existing consolidated subsidiary of the Group, from a related party for U.S. Dollar 73,857. In August 2006, the Group purchased the remaining 1.89% of this company for U.S. Dollar 7,500. These acquisitions were recorded using the purchase method of accounting. Goodwill that arose on acquisition of additional interest in JSC Okhotskaya GGC was primarily attributable to the expected business synergy.

The final acquisition price allocation is presented below:

Assets acquired and liabilities assumed in 2006	
Property, plant and equipment	17,339
Mineral rights	27,557
Goodwill (see Note 10)	24,260
Deferred tax liabilities	(10,775)
Decrease in minority interest	22,976
Cash paid on acquisition	81,357

Other acquisitions

In September 2007, the Group acquired 100% of Polymetal Esop Limited, which holds 5,540,323 of the Company's shares, from its parent company Nafta Moskva (Cyprus) Limited. The purchase

consideration comprised of U.S. Dollar 50. The acquisition of Polymetal ESOP Limited was accounted for as acquisition of treasury shares as it did not constitute the business. These treasury shares will be used for distribution among the Share Option Plan participants (see Notes 17 and 18).

During 2007 the Group acquired a 100% of shares in Fiano Investment Limited, Imitzoloto Holdings Limited and Eniseyskaya Holdings Limited for U.S. Dollar 8. Net asset of the companies were equal to the purchase price at the date of acquisition.

In August 2006, the Group acquired a 0.01% interest in CJSC Zoloto Severnogo Urala from an unrelated party for U.S. Dollar 19. In October 2006, the Group acquired a residual 0.03% interest in CJSC Zoloto Severnogo Urala from a related party for U.S. Dollar 19.2.

In August-October 2006, the Group acquired a 0.48% interest in CJSC Serebro Territorii from an unrelated party for U.S. Dollar 33.4. In October 2006, the Group acquired a 2.41% interest in CJSC Serebro Territorii from a related party for U.S. Dollar 10.7.

Amursky Hydrometallurgy Plant LLC

In April 2007, the Group incorporated a new subsidiary –Amurskiy Hydrometallurgy Plant LLC. The Group plans on building a new plant in the Khabarovsky Region in order to process ore extracted by Albazino resources LLC.

25. RELATED PARTY TRANSACTIONS

Related parties are considered to include shareholders, affiliates and entities under common ownership and control with the Group and members of key management personnel. In the course of its business the Group entered in the various non-operating transactions with related parties.

In July 2006, the Group acquired an additional 30.76% interest in JSC Okhotskaya GGC, an existing consolidated subsidiary of the Company, from Accord-Invest LLC - a related party - for U.S. Dollar 73,857 (see Note 24).

In June 2007 the Group sold 85% in CJSC GRK Dukat for U.S. Dollar 0.3 to a related party. CJSC GRK Dukat did not perform any operations during 2006 and 2007. The amount of net assets at the date of disposal comprised U.S. Dollar 0.01.

As at December 31, 2007 and December 31, 2006 the amount of outstanding short-term loans provided to related parties comprised nil and U.S. Dollar 126 respectively.

As at December, 2007 and December 31, 2006 the amount of outstanding long-term loans provided to related parties comprised U.S. Dollar 6,119 and U.S. Dollar 6,138 respectively (see Note 11). The amount of interest income in 2007 is equal to U.S. Dollar 466.

26. COMMITMENTS AND CONTINGENCIES

Operating environment. Whilst there have been improvements in the economic situation in the Russian Federation in recent years, the country continues to display some 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 prospects for future economic stability in the Russian Federation are largely dependent upon the effectiveness of economic measures undertaken by the government, together with legal, regulatory, and political developments.

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 companies 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 its interpretation of the legislation and assessments. 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.

Out of the large operating companies of the Group, tax authorities audited JSC Okhotskaya GGC, CJSC Serebro Magadana and CJSC Serebro Territorii for the period up to 2004, and CJSC Zoloto Severnogo Urala for the period up to 2005. Nevertheless, according to the Russian tax legislation previously conducted audits do not fully exclude subsequent claims relating to the audited period.

The Group has identified contingencies related to taxes other than income tax. Such possible tax contingencies could materialize and require the Group to pay additional amounts of tax. As at December 31, 2007 management estimates such contingencies related to taxes other than income tax to be up to approximately U.S. Dollar 361. The Group believes the estimated loss related to these contingencies is not probable and, as such, it is not accrued at December 31, 2007.

Transfer pricing legislation, which was introduced from January 1, 1999, provides the possibility for tax authorities to make transfer pricing adjustments and impose additional tax liabilities in respect of all controlled 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), 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.

The Group companies occasionally enter into controllable transactions (e.g. intercompany transactions) and based on the terms the Russian tax authorities may qualify it as non-market. 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 although it may be significant.

Political environment. The operations and earnings of the Group are affected by political, legislative, fiscal and regulatory developments, including those related to environmental protection. Because of the capital-intensive nature of the industry, the Group is also subject to physical risks of various kinds. The nature and frequency of these developments and events associated with these risks, which generally are not covered by insurance, as well as their effect on future operations and earnings, are not predictable.

Forward sales commitments.

The Group is required to deliver a minimum quantity of 9,002,208 troy ounces of silver to ABN Amro over the period from January 1, 2008 to December 31, 2008 at the London silver fix price. If the Group defaults in the performance of its obligations under this contract, it shall pay to ABN Amro an amount, reasonably determined by ABN Amro, equal to the total cost and damages reasonably incurred, or to be reasonably incurred by ABN Amro, including without limitation, in respect of its insurance, vaulting, transportation and borrowing costs (if any) resulting from the default in the performance on such delivery obligation.

In connection with the General Framework Credit Line Agreement dated April 28, 2006 entered into between Sberbank and the Company's subsidiaries, CJSC Zoloto Severnogo Urala and JSC Okhotskaya GGC, JSC Okhotskaya GGC, CJSC Zoloto Severnogo Urala, CJSC Serebro Territorii and CJSC Serebro Magadana are required to sell certain quantity of gold and silver calculated based on the amount of loan facility outstanding to Sberbank during 2008 at the price determined by LBMA.

Litigation. During the year, the Group was involved in a number of court proceedings (both as a plaintiff and as a defendant) arising in the ordinary course of business. In the opinion of management of the Group, there are no current legal proceedings or other claims outstanding, which could have a material effect on the result of operations or financial position of the Group and which have not been accrued or disclosed in these consolidated interim financial statements.

Insurance policies. The Russian insurance market is in a developing stage and some forms of insurance protection common in other parts of the world are not yet generally available in the Russian Federation.

The Group has entered into insurance contracts to insure property, plant and equipment, land transport and purchased accident and health and medical insurance for employees. Furthermore, the Group has purchased civil liability coverage for operating entities with dangerous production units.

Environmental matters. The enforcement of environmental regulation in 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.

27. SUBSEQUENT EVENTS

In January 2008 the Group acquired 97% of shares in JSC Omolon Gold Mining Company from Kinam Magadan Gold Corporation, an unrelated party, for U.S. Dollar 15,000. In March 2008 the Group acquired 2% of shares in JSC Omolon Gold Mining Company from the Russian Federal Property Fund for U.S. Dollar 814.

In February 2008, the Group signed an agreement to set up strategic alliance and joint venture with AngloGold Ashanti Limited. Within the framework of this agreement each party will own 50% in the joint venture, to which the Group will contribute its shares in CJSC Enisey Mining and Geological Company and Imitzoloto LLC in addition to a cash contribution amounting to U.S. Dollar 13,454.

In February 2008 1,826,853 ordinary shares were transferred to the employees in accordance with share option plan (see Note 18).