Management report

(Management's discussion and analysis of financial condition and results of operations for the first six months of 2009)

The following Management report (Management discussion and analysis of the Polyus Group's financial condition and results of operations) should be read in conjunction with the Polyus Group's (the Group) unaudited interim condensed consolidated financial statements and the related notes.

The Polyus Group is the largest gold producer in the Russian Federation and among the largest gold mining companies in the world, based on mineral resources and production volumes.

Polyus Gold Shares are traded on the leading Russian stock exchanges, MICEX and RTS. Polyus Gold's ADRs are listed on the main market of the London Stock Exchange and traded on the over-the-counter markets in the United States. Polyus Gold Shares are included in the key Russian stock exchange indices of MICEX and RTS, and international stock exchange indices such as FTSE Gold Mines and MSCI Emerging Markets.

The following discussion and analysis represents the management's opinion in relation to the Polyus Group's operating and financial results, including discussions of:

- key performance indicators;
- financial position as at 30 June 2009 and 31 December 2008;
- results of operations for the six months ended 30 June 2009 and 30 June 2008;
- the Polyus Group's liquidity, solvency and capital sources;
- significant events affecting the Polyus Group's operating performance for these periods; and

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1. The Polyus Group's operating results

1.1 External factors affecting the Polyus Group's financial results

The results of the Polyus Group are significantly affected by movements in average exchange rates between the USD and the RUR, and prices of commodities, such as gold, oil and steel.

The Polyus Group revenue from gold sales is denominated in USD, whereas up to 80% of the Group's expenses are denominated in RUR, which means that movements in the RUR/USD exchange rate influence the Polyus Group financial results. A significant portion of costs included in the Polyus Group's cost of sales are also directly or indirectly impacted by the prices of oil and steel. Changes in oil prices impact the prices of heating oil, diesel fuel, gasoline and lubricants for mining and construction equipment. Steel forms the basis for the price of all rolled metal products, pipes, machinery and vehicles.

Since 30 June 2008 commodities prices experienced significant changes. Following global markets breakdown in 2008, prices for oil and steel declined substantially. At the same time, the RUR materially depreciated against the USD.

Average price/ rate	**Six months ended 30 June**		**Change,**
	2009	**2008**	**%**
Oil (Brent brand) (USD per barrel)(1)	58.0	102.7	(43.5)
Steel (hot rolled) (USD per tonne)	491.0(1)	760.0(2)	(35.4)
Average USD/RUR rate	33.07	23.94	38.1
Period end USD/RUR rate	31.29	23.46	33.4

1. Source: Bloomberg.
2. Source: Metaltorg, spot price FOB Russia.

1.2 Summary of performance results

The following table shows the summary of performance results of the Polyus Group's operations for the first six months of 2009 related to financial statements.

USD' 000	**Six months ended 30 June**		**Change, %**
	2009	**2008**	
Gold sales	**441,686**	**505,730**	**(12.7)**
Other sales	10,273	13,179	(22.1)
Cost of gold sales	(209,358)	(243,644)	(14.1)
Cost of other sales	(9,248)	(13,230)	(30.1)
Gross profit, including:	**233,353**	**262,035**	**(10.9)**
Gross profit on gold sales	**232,328**	**262,086**	**(11.4)**
Gross profit margin, including:	**51.6%**	**50.5%**	**-**
Gross profit margin on gold sales	52.6%	51.8%	-
Selling, general and administrative expenses	(45,542)	(64,954)	(29.9)
Finance costs, income from investments and foreign exchange gain	15,119	23,002	(34.3)

Profit before income tax	**191,297**	**213,050**	**(10.2)**
Pretax margin	**42.3%**	**41.1%**	**-**
Income tax expense	(41,284)	(52,163)	(20.9)
Profit for the period	**150,013**	**160,887**	**(6.8)**
Net loss attributable to minority interest	(297)	(312)	(4.8)
Profit for the period attributable to shareholders of the parent company	**150,310**	**161,199**	**(6.8)**
Net profit margin	**33.2%**	**31.0%**	**-**
Earnings per share – basic and diluted (USD)	**0.84**	**0.90**	**(6.7)**

The following table shows the summary of performance results of the Polyus Group's operations for the first six months of 2009 related to non-GAAP financial measures:

USD' 000	**Six months ended 30 June**		**Change, %**
	2009	**2008**	
Operating profit[1]	176,178	190,048	(7.3)
Operating profit margin	39.0%	36.6%	-
EBITDA[2]	218,003	235,057	(7.3)
EBITDA margin	48.2%	45.3%	-

1. Operating profit is calculated as Gross profit, less Research and exploration expenses, Selling, general and administrative expenses, Other expenses (net).

2. For details of EBITDA calculation refer to Section 2.1 of this document.

1.2 Gold sales

The following table shows the results and breakdown of the Polyus Group's gold sales for the six months ended 30 June 2009 and 2008:

	Six months ended 30 June		**Change, %**
	2009	**2008**	
Gold sales (USD thousand)	441,686	505,730	(12.7)
Gold sales (thousand troy ounces)[1]	477	559	(14.7)
The weighted-average gold selling price (USD per troy ounce)	926.0	904.7	2.4
The average PM fixing price in London (USD per troy ounce) [2]	915.2	910.9	0.5
Excess/(deficit) of weighted-average selling price over/(under) average evening fixing price (USD per troy ounce)	10.8	(6.2)	-

1. All the produced gold was sold in domestic market.

2. Source: LBMA

In the reporting period the Group's gold sales revenues amounted to USD 441,686 thousand, compared to USD 505,730 thousand in the first half of 2008. The reduction in gold sales revenues resulted from the decreased sales volumes. In the first six months of 2009 sales volumes amounted to 14.9 tonnes (477 k oz), compared to 17.4 tonnes (559 k oz) in the same period of the previous year.

During the first half of 2009, the gold price on the global market increased by almost 7%. On 2 January 2009, the first business day of the reporting period, the gold price was USD 874.5 per troy ounce. On 30 June 2009, the last business day of the reporting period, the gold price was USD 934.5 per ounce.

The Polyus Group's policy of selling gold at spot market prices made it possible to take advantage of the increasing gold price environment. Weighted-average gold selling price amounted to USD 926.0 per oz, compared to USD 904.7 per oz in the first half of 2008 (an increase of 2.4%, in comparison to the increase of 0.5% in the average PM fixing price for the same period). This was achieved as the largest monthly volume of gold sales fell to June, when the Polyus Group enhanced production at the Titimukhta deposit and at the group of alluvial deposits. At the same time, the average gold PM fixing price in June was the highest in the first half of 2009.

In the reporting period the Polyus Group sold all gold produced, thus the reduction in sales was a result of reduced production volumes. During the period under review the Group produced 14.9 tonnes (477 k oz) of refined gold, compared to 17.4 tonnes (559 k oz) in the same period of the previous year. The 14% reduction was due to the production decrease at the Group's key mine – Olimpiada, which was a result of: 1) the reduction in the average gold grade of sulfide ore processed at the Olimpiada mine from 4.1 g/t to 3.5 g/t while processing of this type of ores increased from 1.9 million tonnes in the first six months of 2008 to 3.6 million tonnes in the same period of 2009; 2) the fact that 1.2 tonnes of Dore gold had been delivered to the refining plant, but had not been refined in the reporting period[1]; 3) Mill No.2 at the Olimpiada mine was closed to perform regular maintenance works, previously planned for the second half of 2009.

In the reporting period the Company sold gold only on the domestic market due to better contractual terms achieved with Russian banks.

In the period under review the produced metal was sold under once-off deals within general contract. Within the centralized distribution system CJSC Polyus sold both its own gold and the metal of the other subsidiaries of the Group on the basis of agency agreements signed with these subsidiaries.

[1] For more information refer to the Group' press-release on operating results dated July 29, 2009

1.4 Cost of gold sales

The following table shows the results of the Polyus Group's cost of gold sales for the six months ended 30 June 2009 and 2008:

USD' 000	Six months ended 30 June		Change, %
	2009	2008	
Cash operating costs[1]	212,952	246,435	(13.6)
Consumables and spares, out of which:	101,832	105,520	(3.5)
Materials and spares	*66,183*	*68,770*	*(3.8)*
Fuel	*35,649*	*36,750*	*(3.0)*
Labour	53,657	84,946	(36.8)
Tax on mining	37,207	34,209	8.8
Utilities, out of which:	10,352	14,205	(27.1)
Power	*10,076*	*13,220*	*(23.8)*
Other	*276*	*985*	*(72.0)*
Outsourced mining services	2,132	2,851	(25.2)
Refining costs	1,793	2,019	(11.2)
Sundry costs	5,979	2,683	122.8
Amortisation and depreciation of operating assets	38,433	52,805	(27.2)
Deferred stripping costs expensed/(capitalised)	6,277	(57,817)	-
(Increase)/decrease in gold-in-process and refined gold	(51,154)	1,603	-
Increase in provision for land restoration	2,850	618	361.2
Cost of gold sales	209,358	243,644	(14.1)

1. The presentation of cash operating costs is more detailed than that presented in the financial statements. The amounts are derived from the management accounts, and agree in total with the amounts presented in the financial statements.

In the six months of 2009 the cost of gold sales decreased by USD 34,286 thousand or 14.1% and totaled USD 209,358 thousand.

Cash operating costs

During the first half of 2009, the Polyus Group achieved a decrease in cash operating costs. In the period under review, cash operating costs included in cost of sales amounted to USD 212,952 thousand, compared to USD 246,435 thousand in the same period of the previous year.

Polyus Gold believes that it is correct to provide the analysis of cash operating costs calculated per tonne of ore processed. Overall decrease in cash operating costs of 13.6% is not representative, as the Group enhanced the volumes of ore processed by 27% from 9,194 tonnes in the first half of 2008 to 11,638 tonnes in the reporting period.[2] The calculation of cash operating costs per tonne of ore processed gives a decrease of

[2] The volumes of ore processed include the volumes of sands washed converted using a bulk density of 2 metric tonnes per 1 cubic meter.

almost 31.7%, and for some crucial components of cash costs, as labour expenditures and utilities, the decrease was over 40%.

The table below sets forth the Polyus Group cash operating costs per tonne of ore processed for the six months ended 30 June 2009 and 2008:

USD' 000 per tone	**Six months ended 30 June**		**Change, %**
	2009	**2008**	
Cash operating costs	18.3	26.8	(31.7)
Consumables and spares, out of which:	8.7	11.5	(24.3)
Materials and spares	5.7	7.5	(24.0)
Fuel	3.1	4.0	(22.5)
Labour	4.6	9.2	(50.0)
Utilities, out of which:	0.9	1.5	(40.0)
Power	0.9	1.4	(35.7)
Other	0.0	0.1	(100.0)
Outsourced mining services	3.2	3.7	(13.5)
Refining costs	0.2	0.3	(33.3)
Sundry costs	0.2	0.2	(0.0)

In the first six months of 2009, expenses on consumables and spares were the main item included in cash operating costs (48% of cash operating costs). They included expenses on spare parts for trucks and excavators, as well as for construction machinery, expenses on rolled metal products and cables, technological materials for plants and other materials and spares, used in mining, smelting and concentrating, as well as fuel.

Within the whole Polyus Group, in the first half of 2009 expenses on materials and spare parts were 4% below the levels of the first half of 2008 and amounted to USD 66,183 thousand (31% of cash operating costs). On per tonne processed basis, the decrease was 24%. A significant part of the Group's materials and spares costs (approximately 18%) is denominated in USD (spare parts for tipper trucks, excavators and road-building machines), making this part of materials and spares unexposed to the exchange rate fluctuations. Thus, the decrease in these expenses reflects primarily the depreciation of the national currency, and the decline in prices of underlying commodities, such as hot rolled steel.

On the contrary, fuel is purchased in domestic market. Therefore, expenses on gasoline, diesel fuel and lubricants are denominated in RUR. Expenses on acquisition of oil products represent a 17% stake in cash operating costs. The movements in prices for these products on the national market do not strictly follow the trends of the international market. During the reporting period, the purchase price for gasoline showed a significant decline, but at the same time prices for diesel fuel didn't change materially. Besides this, the main volume of fuel required in 2009 was purchased in the first half of the year. Thereby, expenses on fuel decreased by 3% in total and by 23% per tonne of ore processed as a result of the strong RUR depreciation against the USD.

The next largest item within cash operating costs is payroll expenses (25% of cash operating costs). Labour expenses for operating personnel totaled USD 53,657 thousand, which represents a 36.8% decrease in comparison with the first half of 2008. Labour costs per tonne of ore processed decreased even more - by 50%.

Such a significant decline was mostly due to the exchange rate factor, and reduction in the number of the Polyus Group's employees by 320 people following planned restructuring of staff at some deposits, primarily at the Zapadnoye mine in the Irkutsk region and the Kuranakh mine in the Republic of Sakha (Yakutia).

In the period under review power expenses showed a substantial decrease of 23.8%. On per tonne processed basis, the decrease was 35.7%, which occurred primarily under influence of the exchange rate factor. Expenses on power represent 5% of cash operating costs.

In the first half of 2009, the Polyus Group accrued USD 37,207 thousand in a tax on mining, which is USD 2,988 thousand more than in the same period of the previous year. This was due to the increased average gold selling price, and payment of mining tax on the significant amounts of gold produced, but not refined in the reporting period, and the metal remaining in the production wastes for the reporting period.

Amortisation and depreciation of operating assets

Amortisation and depreciation of operating assets included in cost of sales decreased by 27.2% from USD 52,805 thousand to USD 38,433 thousand. This decrease is primarily the result of the changes in the USD/RUR exchange rate. On a RUR basis, depreciation of fixed assets increased on the back of enlarged RUR-denominated asset base.

Deferred stripping costs expensed/(capitalised)

In the first half of 2008, the Polyus Group capitalized excessive stripping works relating to the extension of the Vostochny pit of Olimpiada (Krasnoyarsk business unit) within transition of production from oxide to sulfide ores. However, in the first half of 2009, the Polyus Group started to expense previously capitalized stripping costs. The Polyus Group's accounting policy is that stripping costs incurred in the period are deferred to the extent that the current period stripping ratio exceeds the expected life-of-mine ratio. In case the current stripping ratio falls short of the average life-of-mine stripping ratio, the stripping costs are charged to operating costs. Deferred stripping costs expensed for the reporting period amounted to USD 6,277 thousand.

1.5 Selling, general and administrative expenses

The following table sets forth the selling, general and administrative expenses of the Polyus Group for the six months ended 30 June 2009 and 2008:

USD' 000	**Six months ended 30 June**		**Change, %**
	2009	**2008**	
Salaries	23,375	31,265	(25.2)
Taxes other than mining and income taxes	7,789	9,711	(19.8)
Professional services and bank charges	2,640	11,637	(77.3)
Depreciation	1,486	2,103	(29.3)
Other	10,252	10,238	0.1
Total	**45,542**	**64,954**	**(29.9)**

1. The presentation of Selling, general and administrative expenses is more detailed than that presented in the financial statements. The amounts are derived from the management accounts, and agree in total with the amounts presented in the financial statements.

During the first six months of 2009 selling, general and administrative expenses decreased by USD 19,412 thousand from USD 64,954 thousand to USD 45,542 thousand.

Salaries

In the first half of 2009, the payroll costs for administrative staff reduced by approximately a quarter and amounted to USD 23,375 thousand. The decrease resulted mainly from national currency depreciation.

Taxes, other than mining tax and income taxes

In addition to mining tax and income tax the Polyus Group pays property tax, VAT (which for the purpose of this item includes non-recoverable VAT) and other taxes. In the period under review the Polyus Group accrued USD 7,789 thousand in federal and regional taxes other than mining tax and income tax, which is 19.8% less than in the same period of the previous year. The decrease in the amount of VAT and property tax paid resulted from the USD/RUR exchange rate movements. The actual accruals of VAT and property tax in Rubles, the Polyus Group's functional currency, were higher in comparison to the same period of the previous year.

The table below shows the components of taxes, other than income and mining taxes, for the six months ended 30 June 2009 and 2008:

USD' 000	Six months ended 30 June		Change, %
	2009	2008	
Taxes, other than mining and income taxes	7,789	9,711	(19.8)
VAT	1,983	2,314	(14.3)
Property tax	5,072	5,858	(13.4)
Other taxes	734	1,539	(52.3)

Professional services and bank charges

In the reporting period, professional and banking services costs decreased by 77% from USD 11,637 thousand in 2008 to USD 2,640 thousand in 2009. The decrease mainly resulted from a 65% reduction in charges for legal, audit and consulting services and a 90% reduction in bank charges. In the first half of 2008, the one-time increase in professional services fees was largely due to consulting services provided on a proposal to carve out the exploration assets into another entity.

Other selling, general and administrative expenses

Other selling, general and administrative expenses (in which for the purpose of this review we include rental payments, repair and maintenance costs, communication costs and other costs) amounted to USD 10,252 thousand, which is almost the same as in the same period of the previous year. On a RUR basis, other selling, general and administrative expenses significantly increased mainly as a result of growth in transportation expenses.

1.6 Research and exploration expenses

In the period under review, research and exploration expenses decreased significantly from USD 4,430 thousand in the first half of 2008 to USD 909 thousand in the first half of 2009. The volume of research and exploration works was substantially reduced due to cost reduction measures undertaken in response to deterioration of global market conditions in the second half of 2008.

1.7 Other expenses, net

Other operating expenses amounted to USD 10,724 thousand, compared to USD 2,603 thousand in the same period of the previous year. The increase in other operating expenses was largely due to the increased charitable contributions to USD 6,978 thousand for the six months ended 30 June 2009, compared to 2,257 thousand in the comparative period. In addition, the Polyus Group incurred a loss on disposal of fixed assets in the first half of 2009 in the amount of USD 1,371 thousand compared to a profit of USD 1,951 thousand realized in the first half of 2008.

1.8 Finance costs, income from investments and foreign exchange gain

The following table sets forth the components of financial and investment activity for the six months ended 30 June:

USD'000	Six months ended 30 June		Change, %
	2009	2008	
Finance costs	(1,754)	(2,335)	(24.9)
Income from investments	10,394	25,047	(58.5)
Foreign exchange gain	6,479	290	-

During the reporting period finance costs decreased by 24.9% as a result of the redemption of short-term borrowings by the end of the first half of 2008.

Income from investment activity in the first half of 2009 amounted to USD 10,394 thousand and related to interest income accrued on bank deposits and recoveries in investments in securities and other financial assets.

Due to significant movements in the USD/RUR exchange rate, the Polyus Group received a foreign exchange gain of USD 6,479 thousand as compared to USD 290 thousand in the first half of 2008.

1.9 Income tax

During the six months ended 30 June 2009 the Polyus Group accrued USD 41,284 thousand in income tax, while in the same period last year it was USD 52,163 thousand. The decrease in income tax expense was driven by lower profit before taxation and the reduction of statutory income tax rate in Russia from 24% in 2008 to 20% since 1 January 2009. The effective income tax rate (ratio of current and deferred tax to IFRS income before tax) in the first half of 2009 was 22%, whereas the statutory income tax rate in Russia was 20%. The excess of effective tax rate over the statutory income tax rate was due to a number of non-deductible expenses and other permanent differences.

1.10 Other sales and cost of other sales

Revenues received by the Polyus Group from the sale of products other than gold and services decreased by 22% compared to the first half of 2008 and amounted to USD 10,273 thousand primarily as a result of USD/RUR exchange rate movements, the amount of sales in RUR didn't change significantly. Other sales included proceeds from sale of electricity, rent services, transportation, handling, storage, and other sales.

Sale of electricity to third parties accounts for the largest part of other revenues – USD 4,807 thousand. These sales relate to CJSC Vitimenergosbyt, the Polyus Group's subsidiary located in the Bodaibo district of the Irkutsk region.

Cost of other sales totaled USD 9,248 thousand in the first half of 2009, compared to USD 13,230 thousand in the first half of 2008. Cost of other sales included, apart from electricity costs, depreciation, expenses on fuel and materials, and payroll costs related to non-mining activities.

In the period under review revenue from sale of other products and services exceeded cost of other sales, which resulted in a the gross profit of USD 1,025 thousand compared to a loss of USD 51 thousand in the first half of 2008.

2. Non-GAAP financial measures

In its analysis of the Polyus Group's results, Polyus Gold uses key performance indicators which are not measures determined in accordance with IFRS.

2.1 EBITDA

"EBITDA" is defined by Polyus Gold as profit before finance costs, income tax, income/(losses) from in vestments, depreciation, amortisation and interest, and is further adjusted by certain items included in the table below. As these line items are not of a recurring nature, Polyus Gold has made these adjustments in calculating EBITDA to provide a clearer view of the performance of its underlying business operations and to generate a metric that it believes will give greater comparability over time with peers in its industry. Polyus Gold believes that EBITDA is a meaningful indicator of its profitability and performance. This measure should not be considered as an alternative to profit for the period and operating cash flows based on IFRS and should not necessarily be construed as a comprehensive indicator of the Polyus Group's measure of profitability or liquidity.

The following table sets forth the Polyus Group's EBITDA for the six months ended 30 June 2009 and 2008:

USD' 000	Six months ended 30 June		Change, %
	2009	2008	
Profit for the year	150,013	160,887	(6.8)
+ Income tax charged	41,284	52,163	(20.9)
+ Depreciation and amortisation for the period	40,454	46,960[1]	(13.9)
+ Interest expense	1,754	2,335	(24.9)
– Interest income	(6,817)	(24,632)	(72.3)
+ Income from investments in listed companies held for trading	(3,577)	(415)	-
– Foreign exchange gain	(6,479)	(290)	-
+ Loss/(profit) from disposal of property, plant and equipment and work-in-progress	1,371	(1,951)	-
EBITDA	218,003	235,057	(7.3)

1. Depreciation and amortisation for the six months ended 30 June 2008 is adjusted for non-monetary changes in excessive stripping works and differs from that presented in the financial statements.

In the period under review, the Polyus Group's EBITDA was USD 218,003 thousand, a decrease of USD 17,054 thousand or 7.3%, reflecting reduction in sales volumes partially offset by increased gold selling prices and decreased costs (See paragraph 1.2 Gold sales above).

2.2 Total Cash Costs

The Polyus Group presents the financial items "total cash costs" ("TCC") and "total cash costs per troy ounce" which have been calculated and presented by management as TCC presentation is common industry practice, although its calculations of these items may differ from those of its industry peers. These items are not IFRS measures. An investor should not consider these items in isolation or as alternatives to cost of sales, profit for the period attributable to shareholders of the parent company, net cash generated from operating activities or any other measure of financial performance presented in accordance with IFRS. The calculation of total cash costs may vary significantly among gold mining companies, and by themselves do not necessarily provide a basis for comparison with other gold mining companies.

Total cash costs are defined by the Polyus Group as cost of sales reduced by property, plant and equipment depreciation, provision for annual vacation payment, provision for land rehabilitation and adjusted by non-monetary changes in inventories and non-monetary changes in deferred stripping costs. Total cash costs per troy ounce are the attributable total cash costs divided by the attributable troy ounce of gold sold.

The following table shows the Polyus Group's TCC for the six months ended 30 June 2009 and 2008:

USD' 000	Six months ended 30 June		Year ended 31 December 2008	1H2009 against 1H2008
	2009	2008		
Cost of gold sales	209,358	243,644	558,118	(14.1)
– property, plant and equipment depreciation	(38,433)	(52,805)	(98,999)	(27.2)
– provision for annual vacation payment	(2,509)	(7,116)	(6,124)	(64.7)
– provision for land rehabilitation	(2,850)	(618)	8,530	361.2
+ non-monetary changes in inventories(1)	6,755	(350)	1,140	-
+ non-monetary changes in deferred stripping works(2)	-	8,673	17,490	-
TCC	172,321	191,428	480,155	(10.0)
Gold sales, thousand troy ounces	477	559	1,226	(14.7)
TCC, USD/oz	361	342	392	5.6
TCC, RUR/oz	11,935	8,200	9,734	45.5

1. "Non-monetary changes in inventories" is a calculation to estimate the non-cash portion of costs included in the change in the amount of inventory, primarily representing depreciation and amortisation.
2. "Non-monetary changes in deferred stripping works" is a calculation to estimate the non-cash portion of costs included in the change in the amount of deferred stripping costs, primarily representing depreciation and amortisation.

In the reporting period, TCC per troy ounce grew by 5.6% on a USD basis in comparison to the first half of 2008. On the contrary, TCC decreased by 7.9% from USD 392 per ounce for the full year 2008 to USD 361 per ounce in the first half of 2009, as a result of reduced cash operating costs (See paragraph 1.4 Cost of gold sales above).

2.3 Analysis of profitability indicators

Polyus Gold defines adjusted net profit as profit for the period attributable to shareholders of the parent company adjusted for gain/loss on disposal of investments, income/loss from investments in listed companies held for trading and impairment of available for sale investments. Adjusted return on assets is calculated as the adjusted net profit divided by the average assets for the period. Adjusted return on equity is calculated as the adjusted net profit divided by the average equity attributable to shareholders of the parent for the period. Adjusted return on invested capital is calculated as the adjusted net profit divided by the sum of the average equity attributable to shareholders of the parent and average non-current and current loans and borrowings for the period.

We have made these adjustments as these items are not considered by Polyus Gold to be of a recurring nature, to provide a clearer view of the performance of our underlying business operations and to generate a metric that we believe will give greater comparability over time with peers in our industry. Polyus Group believes that adjusted net profit, adjusted return on assets, adjusted return on equity and adjusted return on invested capital are meaningful indicators of its profitability and performance. These measures should not be considered alternatives to profit for the period and operating cash flows based on IFRS and should not necessarily be construed as a comprehensive indicator of Polyus Group's measure of profitability or as a measure of liquidity.

The following table shows the Polyus Group's calculation of adjusted net profit, adjusted return on assets, adjusted return on equity and adjusted return on invested capital for the six months ended 30 June 2009 and 2008:

USD' 000	Six months ended 30 June		Change, %
	2009	2008	
Profit for the period attributable to shareholders of the parent company	150,310	161,199	(6.8)
– Gain on disposal of investments	-	-	
– Income from investments in listed companies held for trading	(3,577)	(415)	761.9
Adjusted net profit	146,733	160,784	(8.7)
Assets (average for the period)	3,112,817	3,923,817	(20.7)
Equity attributable to shareholders of the parent (average for the period)	2,768,276	3,384,629	(18.2)
Non-current and current loans and borrowings (average for the period)	-	10,454	-
Adjusted return on assets, %	4.71	4.10	-
Adjusted return on equity, %	5.30	4.75	-
Adjusted return on invested capital, %	5.30	4.74	-

In the six months ended 30 June 2009, adjusted return on assets equaled to 4.71 percentage points, adjusted return on equity was equal to adjusted return on invested capital and amounted to 5.30. In the reporting period, the asset base decreased mainly under the influence of the exchange rate factor. Adjusted return on equity improved due to the reduction of share capital and reserves. This reduction was driven mainly by two factors: a decrease of translation reserve as a result of the considerable USD/RUR exchange rate fluctuations and an elimination of investment revaluation reserve by the end of 2008 following decrease in fair value of investments. These factors more than offset an increase in retained earnings during the periods under review. At the same time in 2008 all the Polyus Group's outstanding loans and borrowings were redeemed, resulting in improvement of return on invested capital.

3. Review of financial sustainability and solvency

3.1 Analysis of consolidated statement of financial position items

The table below shows extracts of the Polyus Group's consolidated balance sheet as at 30 June 2009 and 31 December 2008:

USD' 000	As at 30 June 2009	As at 31 December 2008	Change, %
ASSETS			
Non-current assets			
Property, plant and equipment	1,768,162	1,772,319	(0.2)
Deferred stripping costs	147,344	163,988	(10.1)
Other non-current assets(1)	49,574	54,510	(9.1)
Total non-current assets	**1,965,080**	**1,990,817**	**(1.3)**
Current assets			
Inventories	263,126	233,001	12.9
Investments in securities and other financial assets	291,092	285,236	2.1
Cash and cash equivalents	441,367	398,826	10.7
Other current assets(2)	186,107	170,982	8.8
Total current assets	**1,181,692**	**1,088,045**	**8.6**
TOTAL ASSETS	**3,146,772**	**3,078,862**	**2.2**
EQUITY AND LIABILITIES			
Equity attributable to shareholders of the parent company	2,779,818	2,756,733	0.8
Minority interest	34,722	37,808	(8.2)
TOTAL EQUITY	**2,814,540**	**2,794,541**	**0.7**
Total non-current liabilities	**193,512**	**182,623**	**6.0**
Current liabilities			
Trade and other payables and accrued expenses	110,214	83,527	32.0
Other current liabilities(3)	28,506	18,171	56.9
Total current liabilities	**138,720**	**101,698**	**36.4**
TOTAL LIABILITIES	**332,232**	**284,321**	**16.9**
TOTAL EQUITY AND LIABILITIES	**3,146,772**	**3,078,862**	**2.2**

1. Other non-current assets consist of investments in securities and other financial assets, inventories, long-term portion of reimbursable value added tax and other non-current assets.
2. Other current assets consist of reimbursable value added tax, accounts receivable, advances paid to suppliers, income tax pre-paid and other current assets.
3. Other current liabilities consist of income tax payable and other taxes payable.

3.1.1 Assets

Non-current assets

The table below analyses the Polyus Group's property, plant and equipment at 30 June 2009 and 31 December 2008:

USD' 000	As at 30 June 2009	As at 31 December 2008	Change, %
Exploration and evaluation assets	221,589	214,920	3.1
Mining assets, out of which:	1,178,971	1,218,349	(3.2)
Mineral rights	400,382	433,112	(7.6)
Non-mining assets	35,389	39,814	(11.1)
Capital construction-in-progress	332,213	299,236	11.0
Total property, plant and equipment	1,768,162	1,772,319	(0.2)

During the six months ended 30 June 2009, the Polyus Group's assets structure remained stable.

In the period under review, the Polyus Group continued extensive construction and mine development works within its expansion program. This led to a 3.1% increase in the value of capitalized exploration and evaluation assets and an 11% increase in the value of capital construction-in-progress, even despite the material RUR depreciation against the USD (a 6.5% increase from 29.38 RUR per USD at the beginning of the reporting period to 31.29 RUR per USD at the end of the reporting period). Mining assets, which account for the largest part of the Polyus Group's fixed assets, decreased by 3.2% and at 30 June 2009 amounted to USD 1,178,971 thousand, including mineral rights of USD 400,382 thousand. The decrease mainly related to the USD/RUR exchange rate movements more than offsetting additions during the period. The value of non-mining assets decreased by 11.1% and amounted to USD 35,389 thousand at the end of the period, principally due to the absence of any material additions. As a result, the closing balance of the Polyus Group's property plant and equipment totaled USD 1,768,162 thousand as at 30 June 2009, compared to USD 1,772,319 thousand as at 31 December 2008.

In the first half of 2009, the Polyus Group began to expense previously capitalized stripping costs at the Krasnoyarsk business unit. During the reporting period, their value decreased by 10.1% and amounted to USD 147,344 thousand at 30 June 2009. The decrease is attributable to the amounts written off against profit and loss and represents the impact of the RUR depreciation.

Current assets

Current assets of the Polyus Group increased by 9% from USD 1,088,045 thousand as at 31 December 2008 to USD 1,181,692 thousand as at 30 June 2009, mostly due to a USD 42,541 increase in cash and cash equivalents, a USD 30,125 thousand increase in current inventories and a USD 20,336 increase in other current assets.

As at 30 June 2009, cash and cash equivalents of the Polyus Group amounted to USD 441,367 thousand, compared to USD 398,826 thousand as at 31 December 2008. The source of the increase in cash balance was a strong cash flow from operations partly offset by investing cash outflow.

The value of investment in securities and other financial assets increased by USD 5,856 thousand on the back of gradual financial markets recovery and at the end of the reporting period amounted to USD 291,092 thousand. Investments in listed companies held for trading were partly withdrawn and distributed to investment bank account. Increase in fair value of equity investments available for sale was recognized directly in equity.

Current inventories increased by 12.9% to USD 263,126 thousand as at 30 June 2009. The value of metal inventories doubled and totaled USD 101,731 thousand at the end of the reporting period. This increase is related to the gold which had been delivered to the refinery but was not refined in the reporting period and increased amounts of work in process. Stores and materials (net of allowance for obsolescence), which accounted for 61% of the total current inventories value at 30 June 2009, declined by 11% and equaled to USD 161,395 thousand as a result of material RUR depreciation against the USD.

Other current assets, which includes deferred expenditures and prepaid taxes and which more than doubled from USD 18,494 thousand at the end of 2008 to USD 38,830 thousand at the end of the first half of 2009. This increase occurred mainly on account of a 2.5-times growth of deferred expenditures due to seasonality of production of alluvial companies.

3.1.2 Equity and liabilities

The Polyus Group is financed primarily by equity capital and has no significant bank debt.

Share capital and reserves

Since the beginning of 2009, share capital, additional paid-in capital and treasury shares remained unchanged.

During the period under review, increase in fair value of available for sale investments resulted in a USD 5,007 thousand growth of investments revaluation reserve. Retained earnings increased by the sum of the profit for the period attributable to the shareholders of the parent company (USD 150,310 thousand) and amounted to USD 1,551,850 thousand as at 30 June 2009. Loss for the period attributable to minorities of the Polyus Group subsidiaries together with the dividends paid and effect of translation to presentation currency brought the total value of minority interest to USD 34,722 thousand at 30 June 2009 compared to USD 37,808 thousand at 31 December 2008. Due to substantial changes in the USD/RUR exchange rate translation reserve decreased by USD 132,232 thousand and equaled to USD 175,638 thousand at the end of the reporting period.

As a result of these movements, the Polyus Group’s share capital and reserves increased by USD 19,999 thousand and amounted to USD 2,814,540 thousand at 30 June 2009.

Non-current liabilities

Non-current liabilities as of 30 June 2009 and 31 December 2008 included deferred tax liabilities and environmental obligations.

At 30 June 2009, deferred tax liabilities, which account for 76% of non-current liabilities, totaled USD 146,905 thousand which is almost the same as at 31 December 2008 (USD 148,244 thousand).

During the first six months of 2009, environmental obligations increased by 36% from USD 34,379 thousand as at 31 December 2008 to USD 46,607 thousand as at 30 June 2009. This increase was primarily due to revision of the applied discount rate.

Total value of non-current liabilities didn’t significantly change from 31 December 2008, and the closing balance at 30 June 2009 was USD 193,512 thousand.

Current liabilities

During the first half of 2009, the sum of current liabilities increased by 36% from USD 101,698 thousand at 31 December 2008 to USD 138,720 thousand at 30 June 2009.

This growth was primarily the result of an increase in trade payables related to acquisition of equipment as a part of development of the Blagodatnoye and Natalka deposits. This was partly offset by an immaterial 6.8% decline in other payables and accrued expenses.

Moreover, in the reporting period the Polyus Group's current tax liabilities increased substantially. Income tax payable increased from USD 1,344 thousand at 31 December 2008 to USD 4,611 thousand at 30 June 2009. The amount of other taxes payable, including primarily mining tax, social taxes, personal income tax, property tax and VAT, grew by 37% and amounted to USD 23,089 thousand at the end of the period under review.

3.2 Cash flow analysis

The following table shows extracts of the Polyus Group's consolidated cash flow statement for the six months ended 30 June 2009 and 2008:

USD' 000	Six months ended 30 June		Change, %
	2009	2008	
Operating activities			
Profit before income tax	**191,297**	**213,050**	**(10.2)**
Adjustments(1)	36,551	27,879	31.1
Operating profit before working capital changes	**227,848**	**240,929**	**(5.4)**
Changes in working capital	(41,084)	(25,444)	61.5
Cash flows from operations	**186,764**	**215,485**	**(13.3)**
Interest paid	-	(2,527)	-
Income tax paid	(31,508)	(27,126)	16.2
Net cash generated from operating activities	**155,256**	**185,832**	**(16.5)**
Investing activities			
Capital expenditures, acquisition of subsidiaries and deferred stripping costs(2)	(116,314)	(325,480)	(64.3)
Other investment (spendings)/proceeds(3)	7,476	591,585	(98.7)
Net cash (used in)/generated from investing activities	**(108,838)**	**266,105**	**-**
Net cash generated from/(used in) financing activities	**-**	**(20,835)**	**(100.0)**
Effect of translation to presentation currency	(3,877)	14,834	-
Net (decrease)/increase in cash and cash equivalents	**42,541**	**445,936**	**(90.5)**
Cash and cash equivalents at beginning of the year	**398,826**	**226,174**	**76.3**
Cash and cash equivalents at end of the year	**441,367**	**672,110**	**(34.3)**

1. Adjustments for non-cash items include: amortisation and depreciation, expensed stripping costs, finance costs, loss/(profit) on disposal of property, plant and equipment, income from investments, foreign exchange gain and other items.

2. Capital expenditures, acquisition of subsidiaries and deferred stripping costs include: purchases of property, plant and equipment, acquisition of shares in subsidiaries, repayment of consideration on acquisition of subsidiaries, deferred stripping costs capitalised and proceeds from sale of property, plant.

3. Other investments (spendings)/proceeds include: interest received, purchase of promissory notes and other financial assets and proceeds from sale of promissory notes and other financial assets.

In the first half of 2009, the Polyus Group generated income before tax of USD 191,297 thousand. Operating profit before working capital changes amounted to USD 227,848 thousand, which was 5.4% lower than in the same period of the previous year. In the reporting period, net cash generated from operating activities decreased by USD 30,576 thousand to USD 155,256 thousand. The decrease in net cash inflow from operations resulted mainly from a substantial increase in inventories, and income tax payment.

During the period under review, the Polyus Group reduced its capital expenditures, acquisition of subsidiaries and deferred stripping costs. In the first half of 2009, these expenses totalled USD 116,314 thousand, compared to USD 325,480 thousand in the same period of the previous year.

While in the first half of 2008, the Polyus Group had significant cash inflow from investments as it closed its positions on the Rosbank promissory notes and a number of deposits and trust management contracts for a total amount of USD 574,506 thousand, in the first half of 2009, proceeds from sale of financial assets amounted to only USD 13,253 thousand.

As a result, in the reporting period the Polyus Group used USD 108,838 thousand in investment activities, while in the same period of the previous year it received USD 266,105 thousand from investing activities.

In the six months ended 30 June 2009 the Polyus Group had no cash flow from financing activities, while in the six months ended 30 June 2008 cash outflow from financing activities totaled USD 20,835 thousand, reflecting mainly repayment of the loan by the Polyus Group’s subsidiary OJSC SVMC.

3.3 Capital expenditures, acquisitions of subsidiaries and deferred stripping costs

Capital expenditures represent the Polyus Group’s purchase of property, plant and equipment adjusted for the proceeds from the sale of property, plant and equipment. The Polyus Group also presents capitalised deferred stripping costs and the acquisition of subsidiaries adjusted for the repayment of contingent consideration and proceeds from the disposal of such subsidiaries.

The following table shows the Polyus Group’s capital expenditures, acquisition of subsidiaries and deferred stripping costs for the six months ended 30 June 2009 and 2008:

USD’ 000	**Six months ended 30 June**		**Change, %**
	2009	**2008**	
+ Purchase of property, plant and equipment	117,373	230,101	(49.0)
– Proceeds from sale of property, plant and equipment	(1,059)	(4,635)	(77.2)
Net capital expenditures	**116,314**	**225,466**	(48.4)
+ Increase of ownership in subsidiaries	-	22,128	-
+ Repayment of consideration on acquisition of subsidiaries	-	20,069	-
Acquisition of subsidiaries, net of adjustments above	-	42,197	-
+ Deferred stripping costs capitalised	-	57,817	-
Total capital expenditures, acquisition of subsidiaries and deferred stripping costs	**116,314**	**325,480**	(64.3)

In the first six months of 2009, the Polyus Group spent USD 116,314 thousand on total capital expenditures, acquisition of subsidiaries and deferred stripping costs. This was 64.3% less than in the first half of 2008, when substantial amounts were spent to the increase of ownership in subsidiaries (OJSC Matrosov mine) and repayment of contingent consideration on acquisition of subsidiaries (Yakut gold mining companies) The acquisition of fixed assets during the reporting period (net of proceeds from sale of property, plant and equipment) was 48.4% below the levels of the same period of 2008 and amounted to USD 116,314 thousand.

In the first half of 2009, the Polyus Group continued modernization of Mill No.1 at Olimpiada, development of the Blagodatnoye and Verninskoye projects, and modernization programme at the Kuranakh mine. The capex program in the first half of 2009 was reduced as the Titimukhta and Blagodatnoe projects, and modernization program at the Kuranakh mine turned to the final stage. Moreover, most of materials and equipment supplied during the period were contracted in 2008.

During the reporting period the Polyus Group did not capitalize deferred stripping costs, while deferred stripping costs capitalised in the same period of the previous year amounted to USD 57,817 thousand.