Open Joint Stock Company AZOT

Consolidated financial statements for the year ended 31 December 2007

OPEN JOINT STOCK COMPANY AZOT

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

The following statement, which should be read in conjunction with the independent auditors' report set out on page 2 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 Azot and its subsidiaries (the "Group").

Management is responsible for the preparation of consolidated financial statements that present fairly the financial position of the Group as at 31 December 2007 and the results of its operations, cash flows and changes in equity for the year then ended, in accordance with International Financial Reporting Standards ("IFRS").

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

- selecting suitable accounting principles and applying them consistently;
- making judgements and estimates that are reasonable and prudent;
- stating whether IFRS have been followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- 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, within its competencies, is also responsible for:

- designing, implementing and maintaining an effective system of internal controls, throughout the Group;
- maintaining statutory accounting records in compliance with legislation and accounting standards in the Russian Federation;
- taking steps to safeguard the assets of the Group; and
- detecting and preventing fraud and other irregularities.

The consolidated financial statements for the year ended 31 December 2007 were approved on 11 July 2008 by:

On behalf of OJSC Azot Dmitry V. Osipov Chief Executive Officer of LLC Management Company Uralchem	Ekaterina I. Shuvarikova Chief Accountant of OJSC Azot

Moscow, Russia
11 July 2008

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INDEPENDENT AUDITORS' REPORT

To the shareholders of Open Joint Stock Company Azot:

We have audited the accompanying consolidated financial statements of Open Joint Stock Company Azot and its subsidiaries (the "Group"), which comprise the consolidated balance sheet as at 31 December 2007, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the consolidated financial statements

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

Auditors' responsibility

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

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

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

Opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2007, and the results of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Deloitte & Touche

Moscow, Russia
11 July 2008

CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007
All amounts are in thousands of US Dollars unless otherwise stated

	Notes	Year ended 31 December 2007	Year ended 31 December 2006
Revenue			
Mineral fertilisers sales	5	304,735	207,521
Other sales		4,879	3,521
Total revenue		**309,614**	**211,042**
Cost of sales	6	(163,122)	(134,620)
Gross profit		**146,492**	**76,422**
Distribution expenses	7	(32,784)	(19,458)
General and administrative expenses	8	(22,489)	(13,751)
Other operating income	9	10,481	1,423
Other operating expenses	9	(6,038)	(4,330)
Operating profit		**95,662**	**40,306**
Interest income	10	2,472	2,138
Interest expense	11	(460)	(1,487)
Foreign exchange loss, net		(335)	(145)
Profit before tax		**97,339**	**40,812**
Income tax expense	12	(21,997)	(6,008)
Profit for the year		**75,342**	**34,804**
Earnings per share			
Weighted average number of ordinary shares in issue during the year	23	405,871	405,871
Basic and diluted earnings per share (US dollars per share)		185.63	85.75

CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2007
All amounts are in thousands of US Dollars unless otherwise stated

	Notes	31 December 2007	31 December 2006
ASSETS			
Non-current assets			
Property, plant and equipment	13	166,066	148,963
Catalytic agents		11,051	14,099
Long-term available-for-sale financial assets	14	91	8,796
Letters of credit	15	531	6,278
Other financial assets	16	1,106	-
Other non-current assets		911	1,095
		179,756	**179,231**
Current assets			
Inventories	17	18,582	10,871
Trade and other receivables	18	3,547	2,268
Advances paid and prepaid expenses	19	24,375	4,379
Taxes receivable	20	12,550	11,678
Bank deposits	21	-	52,206
Other financial assets	16	29,037	-
Cash and cash equivalents	22	15,881	6,282
		103,972	**87,684**
TOTAL ASSETS		**283,728**	**266,915**
EQUITY AND LIABILITIES			
Capital and reserves			
Share capital	23	6,567	6,567
Financial assets revaluation reserve		-	3,748
Foreign currency translation reserve		25,343	10,982
Retained earnings		172,994	195,403
Total equity		**204,904**	**216,700**
Non-current liabilities			
Deferred tax liabilities	24	18,070	16,387
Employee benefit obligations	25	5,756	3,413
Other non-current liabilities	26	130	1,022
		23,956	**20,822**
Current liabilities			
Short-term borrowings	27	3,264	5,642
Trade and other payables	28	11,090	8,967
Advances received		35,852	12,437
Income tax payable		3,374	1,235
Other taxes payable	29	1,288	1,112
		54,868	**29,393**
Total liabilities		**78,824**	**50,215**
TOTAL EQUITY AND LIABILITIES		**283,728**	**266,915**

The notes on pages 7 to 38 are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2007
All amounts are in thousands of US Dollars unless otherwise stated

	Year ended 31 December 2007	Year ended 31 December 2006
Operating activities		
Profit before income tax	**97,339**	**40,812**
Adjustments for:		
Depreciation of property, plant and equipment	20,994	18,014
Gain on disposal of available-for-sale financial assets	(5,025)	-
Interest income	(2,472)	(2,138)
Gain on revaluation of forward exchange contracts	(1,551)	-
Loss on disposal of property, plant and equipment	866	-
Dividend income	(481)	(81)
Interest expense	460	1,487
Change in provision for unused vacation	211	541
Foreign exchange loss, net	155	152
Other non-monetary expense	247	545
Operating cash flows before working capital changes	**110,743**	**59,332**
Increase in inventories	(2,733)	(2,486)
(Increase)/decrease in trade and other receivables	(952)	15,323
(Increase)/decrease in advances paid and prepaid expenses	(18,884)	1,289
(Increase)/decrease in taxes receivable	(21)	7,064
Increase/(decrease) in trade and other payables	1,624	(7,508)
Increase in advances received	21,603	4,756
Increase in other taxes payable	92	306
Cash generated from operations	**111,472**	**78,076**
Income tax paid	(18,553)	(11,615)
Interest received	2,820	1,642
Interest paid	(485)	(267)
Net cash generated from operating activities	**95,254**	**67,836**
Investing activities		
Receipt of cash from bank deposits	66,993	30,965
Placement of cash in bank deposits	(14,251)	(69,763)
Proceeds from disposal of available-for-sale financial assets	8,951	-
Purchase of available-for-sale financial assets	-	(1,684)
Proceeds from disposal and redemption of promissory notes	-	3,625
Purchase of promissory notes	-	(2,264)
Purchase of property, plant and equipment	(22,503)	(26,848)
Proceeds from sale of property, plant and equipment	736	-
Loans issued	(28,596)	-
Proceeds from repayment of loans issued	1,520	10
Dividends received	481	81
Net cash generated from/(used in) investing activities	**13,331**	**(65,878)**
Financing activities		
Dividends paid	(97,067)	-
Repayment of borrowings	(9,685)	(12,082)
Proceeds from borrowings	6,940	11,981
Net cash used in financing activities	**(99,812)**	**(101)**
Net increase in cash and cash equivalents	**8,773**	**1,857**
Cash and cash equivalents at beginning of the year	**6,282**	**3,994**
Effect of translation to presentation currency and exchange rate changes on the balance of cash held in foreign currencies	826	431
Cash and cash equivalents at end of the year	**15,881**	**6,282**

The notes on pages 7 to 38 are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 2007
All amounts are in thousands of US Dollars unless otherwise stated

	Share capital	Financial assets revaluation reserve	Foreign currency translation reserve	Retained earnings	Total
Balance at 1 January 2006	**6,567**	**1,432**	**(5,414)**	**160,599**	**163,184**
Increase in fair value of available-for-sale financial assets	-	2,316	-	-	**2,316**
Effect of translation to presentation currency	-	-	16,396	-	**16,396**
Total income recognised directly in equity	**-**	**2,316**	**16,396**	**-**	**18,712**
Profit for the year	-	-	-	34,804	**34,804**
Total recognised income and expense	**-**	**2,316**	**16,396**	**34,804**	**53,516**
Balance at 31 December 2006	**6,567**	**3,748**	**10,982**	**195,403**	**216,700**
Effect of translation to presentation currency	-	-	14,361	-	**14,361**
Total income recognised directly in equity	**-**	**-**	**14,361**	**-**	**14,361**
Transfer to profit or loss on disposal of available-for-sale financial assets	-	(3,748)	-	-	**(3,748)**
Profit for the year	-	-	-	75,342	**75,342**
Total recognised income and expense	**-**	**(3,748)**	**14,361**	**75,342**	**85,955**
Dividends (refer to note 23)	-	-	-	(97,751)	**(97,751)**
Balance at 31 December 2007	**6,567**	**-**	**25,343**	**172,994**	**204,904**

1. GENERAL INFORMATION

Organisation

Open Joint Stock Company Azot (the "Company" or "Azot") was established as a state-owned enterprise in 1932 and incorporated as an open joint stock company on 2 December 1992, as part of the Russian Federation's privatisation program. At 31 December 2007, the Company was a 78.7% subsidiary of Limited Liability Company Management Company Uralchem, a 100% subsidiary of Open Joint Stock Company Uralchem. Both these entities are ultimately owned and controlled by Mr. Dmitry A. Mazepin.

The Company and its subsidiaries (the "Group") are registered and located at Churtanskoye road, 75, 618401, Berezniki, Perm region, Russian Federation.

Principal business activities

The principal activities of the Group are the production and distribution of mineral fertilisers. The main products of the Group are nitrogen fertilisers, including, ammonium nitrate, urea, ammonia, nitric acid and others.

The major production facilities of the Group are located in the Perm region of the Russian Federation. The principal business activities of the Company's subsidiaries and effective ownership are presented below:

		Effective ownership, %	
Subsidiaries	**Principal activities**	**31 December 2007**	**31 December 2006**
LLC Azotstroyremont	Construction and repairs	100.0	100.0
LLC Nedelya.ru	Publishing	100.0	100.0
LLC Promkanal	Processing of waste water	99.8	99.8

Standards and interpretations effective in the current period

In the current year, the Group has adopted all new International Financial Reporting Standards ("IFRS") and interpretations issued by International Financial Reporting Interpretation Committee ("IFRIC") that are mandatory for adoption in the annual periods beginning on or after 1 January 2007. Adoption of these standards and interpretations did not have any effect on the financial performance or position of the Group but gave rise to additional disclosures in the consolidated financial statements as follows:

IAS 1 *Presentation of Financial Statements (amendment)*

This amendment required the Group to provide new disclosures to enable users of the consolidated financial statements to evaluate the Group's principal objectives; policies and procedures for managing capital (refer to note 33).

IFRS 7 *Financial Instruments: Disclosures*

This standard introduced new disclosures that enable users of the consolidated financial statements to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments.

IFRIC Interpretations

The following IFRIC interpretations were issued and effective for the current period: IFRIC 7 *Applying the Restatement Approach under IAS 29*; IFRIC 8 *Scope of IFRS 2*; IFRIC 9 *Reassessment of Embedded Derivatives*; and IFRIC 10 *Interim Financial Reporting and Impairment*. The adoption of these interpretations has not led to any changes in the Group's accounting policies or disclosures provided in the consolidated financial statements.

Standards and interpretations in issue but not yet adopted

At the date of authorisation of these consolidated financial statements, the following Standards and Interpretations were in issue but not yet effective:

Standards and Interpretations	Effective for annual periods beginning on or after
IAS 1 *Presentation of Financial Statements (amendment)*	1 January 2009
IAS 16 *Property, Plant and Equipment (amendment)*	1 January 2009
IAS 19 *Employee Benefits (amendment)*	1 January 2009
IAS 20 *Government Grants and Disclosure of Government Assistance (amendment)*	1 January 2009
IAS 23 *Borrowing Costs (amendment)*	1 January 2009
IAS 27 *Consolidated and Separate Financial Statements (amendment due to revision of IFRS 3)*	1 July 2009
IAS 28 *Investments in Associates (amendments due to revision of IFRS 3)*	1 July 2009
IAS 31 *Investments in Joint Ventures (amendments due to revision of IFRS 3)*	1 July 2009
IAS 32 *Financial Instruments: Presentation (amendment)*	1 January 2009
IAS 36 *Impairment of Assets (amendment)*	1 January 2009
IAS 38 *Intangible Assets (amendment)*	1 January 2009
IAS 39 *Financial Instruments: Recognition and Measurement (amendment)*	1 January 2009
IAS 40 *Investment Property (amendment)*	1 January 2009
IAS 41 *Agriculture (amendment)*	1 January 2009
IFRS 1 *First-time Adoption of International Financial Reporting Standards (amendment)*	1 January 2009
IFRS 2 *Share-based Payment (amendment)*	1 January 2009
IFRS 3 *Business Combinations (revised on applying the acquisition method)*	1 July 2009
IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations (amendment)*	1 July 2009
IFRS 8 *Operating segments*	1 January 2009
IFRIC 11 *IFRS 2: Group and Treasury Share Transactions*	1 March 2007
IFRIC 12 *Service Concession Arrangements*	1 January 2008
IFRIC 13 *Customer Loyalty Programmes*	1 July 2008
IFRIC 14 *IAS 19: The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*	1 January 2008
IFRS 15 *Agreements for the Construction of Real Estate*	1 January 2009
IFRS 16 *Hedges of a Net Investment in a Foreign Operation*	1 October 2008

The impact of adoption of these standards and interpretations in the preparation of the consolidated financial statements in future periods is currently being assessed by management. Management anticipates that the adoption of these standards and interpretations will have no material impact on the consolidated financial statements of the Group in the period of initial adoption.

2. SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards.

Basis of preparation

The consolidated financial statements have been prepared on the historical cost basis except for mark-to-market valuation of certain financial instruments, in accordance with IAS 39 *Financial Instruments: Recognition and Measurement*.

Basis of consolidation

The consolidated financial statements incorporate financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with those used by the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

Revenue recognition

Revenue is derived from the sale of mineral fertilisers and the provision of other services. Revenue is measured at the fair value of the consideration received or receivable, excluding:

- value added tax;
- custom duties; and
- estimated customer returns, rebates and other similar allowances.

Revenue is recognised to the extent that it is probable that economic benefit will flow to the Group and the revenue and costs incurred or to be incurred in respect of transaction can be reliably measured.

Cash received in advance from customers is not included in current year revenue, and is recognised within advances received.

Mineral fertilisers sales

Revenue from the sale of mineral fertilisers and their by-products is recognised when significant risks and rewards of ownership are transferred to the buyer in accordance with the shipping terms specified in the sales agreements.

Other sales

The Group provides the following principal types of services:

- processing services;
- supply of utility services;
- construction, repairs and maintenance services; and
- transportation services.

Revenue from contracts to provide services is recognised when the services are rendered.

Dividend and interest income

Dividend income from investments is recognised when the Group's right to receive payment has been established.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Leasing – the Group as lessee

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments.

The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss in accordance with the Group's general policy on borrowing costs (see below). Contingent rentals are recognised as expenses in the periods in which they are incurred. Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

Foreign currencies

The individual financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency), which reflects the economic substance of its operations. The functional currency of the Company and its subsidiaries is the Russian Rouble ("RUR").

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing at the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognised in the income statement in the period in which they arise.

Management of the Group has chosen to present consolidated financial statements in USD for the convenience of the users of these consolidated financial statements.

The translation from functional currency into presentation currency is performed as follows:

- assets and liabilities are expressed in USD using exchange rates prevailing at the balance sheet date;
- income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuated significantly during that period, in which case the exchange rates at the dates of the transactions are used;
- exchange differences arising, if any, are classified as equity in the foreign currency translation reserve; and
- in the consolidated statement of cash flow, cash balances at beginning and end of each period presented are translated at exchange rates at the respective dates. All cash flows are translated at the average exchange rates for the periods presented. Resulting exchange differences, if any, are presented as *Effect of translation to presentation currency and exchange rates changes on the balance of cash held in foreign currencies*.

The RUR is not a freely convertible currency outside the Russian Federation and, accordingly, any translation of RUR-denominated assets and liabilities into USD for the purpose of presenting consolidated financial statements of the Group does not imply that the Group could or will in the future realise or settle in USD the translated values of these assets and liabilities.

Exchange rates used in the preparation of the consolidated financial statements, as quoted by the Central Bank of the Russian Federation, were as follows (RUR to 1 US Dollar):

	31 December 2007	31 December 2006
Year-end rates	24.55	26.33
Average for year ended	25.58	27.19

Borrowing costs

All borrowing costs are recognised in profit or loss in the period in which they are incurred.

Income tax

Income tax expense represents the sum of the tax currently payable and deferred tax.

Income tax is recognised as an expense or income in the income statement, except when it relates to items credited or debited directly to equity, in which case the tax is also recognised directly in equity.

Current tax

Current tax is based on taxable profit for the year. Taxable profit differs from profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax

Deferred tax is recognised on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit, and are accounted for using the balance sheet liability method. Deferred tax liabilities are recognised for all taxable temporary differences, and deferred tax assets are recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from initial recognition of assets and liabilities in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognised for taxable temporary differences associated with investments in subsidiaries, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognised to the extent that it is probable that there will be sufficient taxable profits against which to utilise the benefits of the temporary differences and they are expected to reverse in the foreseeable future. The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities. Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Property, plant and equipment

The Group has adopted IFRS for the first time effective 1 January 2005 and has elected to utilise exemptions available for first-time adopters under IFRS 1 and has recorded property, plant and equipment at fair value (deemed cost). The fair value of property, plant and equipment was determined by an independent appraiser as at 1 January 2005. After that date the property, plant and equipment are stated at deemed cost less accumulated depreciation and impairment losses.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other costs are recognised in the income statement as incurred.

The gain or loss arising on disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the income statement.

Depreciation

Depreciation is calculated on a straight-line basis over the estimated useful life of each part of an item of property, plant and equipment. Assets held under finance lease arrangements are depreciated over the shorter of their estimated useful lives and lease terms. If there is reasonable certainty that the lessee will obtain ownership of an asset by the end of the lease term, the period of expected use is the useful life of the asset. Land is not depreciated.

The estimated useful lives for the major classes of assets are as follows:

Buildings and structures	15-100 years
Machinery, equipment and transport	5-30 years
Other	2-10 years

Construction-in-progress

Construction-in-progress comprises costs directly related to construction of property, plant and equipment including an appropriate allocation of directly attributable variable overheads that are incurred in construction as well as costs of purchase of other assets that require installation or preparation for their use. Depreciation of these assets is calculated on the same basis as for other property assets and commences when the assets are put into operation. Construction-in-progress is reviewed regularly to determine whether its carrying value is fairly stated and an appropriate provision for impairment is made, if necessary.

Impairment of tangible assets

At each balance sheet date, the Group reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest group of cash-generating units for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Financial assets

Financial assets are recognised and derecognised on a trade date where the purchase or sale of an investment is under a contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, net of transaction costs, except for those financial assets classified as financial assets at fair value through profit or loss, which are initially measured at fair value.

Financial assets of the Group are classified into the following specified categories:

- financial assets at fair value through profit or loss ("FVTPL");
- available-for-sale financial assets ("AFS"); and
- loans and receivables.

The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Income is recognised on an effective interest rate basis for debt instruments other than those financial assets designated as at FVTPL.

Financial assets at fair value through profit or loss

Financial assets are classified as FVTPL where the financial asset is either held for trading or it is designated as FVTPL.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial asset other than a financial asset held for trading may be designated as FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 permits the entire combined contract (asset or liability) to be designated as FVTPL.

Financial assets at FVTPL are stated at fair value, with any gain or loss resulting from re-measurement recognised in profit or loss. The net gain or loss recognised in profit or loss includes any dividend or interest earned on the financial asset. Fair value is determined in the manner described in note 32.

Available-for-sale financial assets

AFS financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within twelve months of the balance sheet date.

AFS financial assets are measured at fair value. Investments in quoted equity instruments classified as AFS financial assets are measured at quoted market prices as of the reporting date. Investments in equity instruments for which there are no available market quotations and whose fair value cannot be reliably measured are accounted at cost.

Gains and losses arising from changes in fair values are recognised directly in equity in the *Financial assets revaluation reserve* with the exception of impairment losses, interest calculated using the effective interest method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the *Financial assets revaluation reserve* is included in profit or loss.

Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest method less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted. For financial assets carried at amortised cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade and other receivables where the carrying amount is reduced through the use of an allowance account. When a trade or other receivable is uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in profit or loss.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised. In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognised directly in equity in the *Financial assets revaluation reserve*.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined by using the weighted average method. The cost of finished goods and work in progress includes direct costs and the allocation of related production overheads. Net realisable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale. Where the net realisable value is lower than costs, an allowance for obsolete and slow-moving raw materials is recognised.

Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, current accounts and cash deposits with banks and highly liquid investments with maturities of three months or less, that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

Financial liabilities

Financial liabilities are classified into the following specified categories:

- financial guarantee contract liabilities; and
- other financial liabilities.

Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with *IAS 37 Provisions, Contingent Liabilities and Contingent Assets*; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies set out above.

Other financial liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

Provisions and accruals

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Employee benefit obligations

Remuneration to employees in respect of services rendered during reporting period, including accrual for unused vacation and bonuses and related unified social tax ("UST"), is recognised as an expense in the period when it is earned.

Defined contribution plan

The Company and its subsidiaries are registered in the Russian Federation and are legally obliged to make defined contributions to the State Pension Fund. This defined contribution plan is financed on a pay-as-you-go basis.

In the Russian Federation all obligatory social contributions, including contributions to the State Pension Fund, are collected through UST calculated by the application of a regressive rate varying from 2% to 26% of the annual gross remuneration of each employee. UST is allocated to three state social funds, including the State Pension Fund at rates varying from 2% to 20% of the annual gross remuneration of each employee.

Defined benefit plan

The Group operates an unfunded defined benefit plan for its employees.

Under this plan a retired employee (or his/her family members) is entitled to the following payments:

- *one-time payment on retirement* varying from one to three average monthly salaries, depending on their seniority;
- *quarterly allowance* varying from USD 9 to USD 16 for the rest of his/her life;
- *one-time payment upon death* which is calculated by reference to the official minimum monthly salary. At 31 December 2007 the official minimum monthly salary was USD 98 (2006: USD 42); and
- other payments stipulated in labour agreements such as anniversary payments, disability compensation, etc.

For the defined benefit retirement plan, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out as at 31 December 2007 and with immediate recognition of all actuarial gains and losses in the income statement. Past service cost is amortised on a straight-line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognised past service cost.

Segment information

The Group is organised in one business segment, being the production and distribution of mineral fertilisers and its by-products. Other Group operations do not constitute separate business segments.

The Group's production entities operate in the Perm region of the Russian Federation. The revenue by geographical location of Group's customers is presented in note 5.

3. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, described in note 2, management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities and recognised amounts of income and expenses that are not readily apparent from other sources. The estimates and underlying assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The most significant areas requiring the use of management estimates and assumptions relate to:

- useful economic lives of property, plant and equipment;
- impairment of assets;
- allowances for doubtful debts, obsolete and slow-moving raw materials;
- employee benefit obligations; and
- taxation.

Useful lives of property, plant and equipment

The estimation of the useful lives of items of property, plant and equipment is a matter of judgement based on the Group's experience with similar assets. The future economic benefits embodied in the assets are consumed principally through use. However, other factors, such as technical or commercial obsolescence and condition of the assets (including operational factors and utilisation of maintenance programs), often will result in a change of the future economic benefit from these assets.

Management periodically reviews the appropriateness of the remaining useful lives of property, plant and equipment. Revisions to estimates of the useful lives of property, plant and equipment are recognised prospectively in the period of the revision and where applicable, future periods. Accordingly, this may impact the amount of depreciation expense and the carrying amount of property, plant and equipment to be recognised in the future.

Impairment of assets

The Group reviews annually the carrying amounts of its tangible assets to determine whether there is any indication that those assets are impaired. In making the assessment for impairment, assets that do not generate independent cash flows are allocated to an appropriate cash-generating unit. Management necessarily applies its judgement in allocating assets that do not generate independent cash flows to appropriate cash-generating units, and also in estimating the timing and value of underlying cash flows within the value in use calculation. In determining the value in use, future cash flows are estimated at each cash-generating unit based on future cash flow projections utilising the latest budgeted information available.

Future cash flows projections involve significant estimates and assumptions regarding the market growth, market demand for the products, profitability of products and discount rates. The critical estimate in the Group's future cash flow projections is the expected increase of natural gas prices on the territory of the Russian Federation. This estimate was made based on the announced government policy on natural gas prices.

Allowances for doubtful debts, obsolete and slow-moving raw materials

The Group creates an allowance for doubtful debts to account for estimated losses resulting from the inability of customers to make required payments. As at 31 December 2007, the allowance for doubtful trade and other receivables amounted to USD 101 thousand (2006: USD 222 thousand). When evaluating the adequacy of an allowance for doubtful debts, management bases its estimates on the current overall economic conditions, the ageing of accounts receivable balances, historical write-off experience, customer creditworthiness and changes in payment terms. Changes in the economy, industry or specific customer conditions may require adjustments to the estimated allowance for doubtful debts.

The Group creates an allowance for obsolete and slow-moving raw materials. As at 31 December 2007, the allowance for obsolete and slow-moving items amounted to USD 1,679 thousand (2006: USD 2,224 thousand).

Estimates of the net realisable value of inventories are based on the most reliable evidence available at the time the estimates are made. These estimates take into consideration fluctuations of price or cost directly relating to events occurring subsequent to the balance sheet date to the extent that such events confirm conditions existing at the end of the reporting period. Changes in the supply and demand of the products, any subsequent changes to the price or cost may require adjustments to the estimated allowance for obsolete and slow moving raw materials.

Employee benefit obligations

The expected costs of providing pensions and post-retirement benefits under defined benefit arrangement and related employee current service cost during the period are charged to the income statement.

Assumptions in respect of the expected costs are set after consultation with actuaries. While management believes the assumptions used are appropriate, a change in the assumptions used would impact the results of the Group's operations.

The other principal assumptions used in calculating these benefits relate to:

- discount rate used in determining the present value of post employment benefit;
- projected salary and pension increase; and
- mortality projection.

Taxation

The Group is subject to income tax in the Russian Federation. Russian tax, currency and customs legislation is subject to varying interpretations. The Group recognises liabilities for anticipated additional tax assessments as a result of tax audits based on estimates of whether it is probable that additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax provisions in the period in which such determination is made.

Deferred tax assets are reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax assets to be utilised. The estimation of that probability includes judgements based on the expected performance of the Group. Various factors are considered to assess the probability of the future utilisation of deferred tax assets, including past operating results, operational plans, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from that estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected.

All amounts are in thousands of US Dollars unless otherwise stated

4. RECLASSIFICATIONS

Certain comparative information, presented in the consolidated financial statements for the year ended 31 December 2006, has been reclassified. Reclassifications were based upon management's decision to enhance disclosure of the Group's financial position and results of operations through separate presentation of certain types of income and expenses, and assets and liabilities on the face of consolidated income statement and consolidated balance sheet.

The effect of reclassification is summarised below:

	Before reclassi-fication	After reclassi-fication	Difference
CONSOLIDATED INCOME STATEMENT			
Other operating expenses, net	(2,907)	-	2,907
Other operating income	-	1,423	1,423
Other operating expenses	-	(4,330)	(4,330)
			-
CONSOLIDATED BALANCE SHEET			
Current assets			
Trade and other receivables	-	2,268	(2,268)
Advances paid and prepaid expenses	-	4,379	(4,379)
Accounts receivable, advances issued and prepayments	6,647	-	6,647
			-
Current liabilities			
Trade and other payables	-	8,967	(8,967)
Advances received	-	12,437	(12,437)
Accounts payable and other liabilities	21,404	-	21,404
			-

5. MINERAL FERTILISERS SALES

Year ended 31 December 2007	**Total**	**Export**	**Russian Federation**	**Other CIS countries**
Ammonium nitrate	153,555	41,306	81,697	30,552
Urea	81,160	75,626	5,479	55
Ammonia	38,487	34,781	3,701	5
Acids	13,826	-	13,741	85
Other	17,707	443	15,906	1,358
Total	**304,735**	**152,156**	**120,524**	**32,055**

All amounts are in thousands of US Dollars unless otherwise stated

Year ended 31 December 2006	Total	Export	Russian Federation	Other CIS countries
Ammonium nitrate	98,297	34,297	48,866	15,134
Urea	59,889	53,182	6,648	59
Ammonia	19,956	17,245	2,711	-
Acids	11,964	302	11,642	20
Other	17,415	2,052	15,157	206
Total	**207,521**	**107,078**	**85,024**	**15,419**

6. COST OF SALES

	Year ended 31 December 2007	Year ended 31 December 2006
Raw materials	100,345	78,935
Energy and utilities	21,728	16,036
Depreciation	19,222	16,991
Payroll and social taxes	15,341	16,363
Repairs and maintenance	2,893	2,591
Taxes	1,897	1,907
Other	1,696	1,797
Total	**163,122**	**134,620**

7. DISTRIBUTION EXPENSES

	Year ended 31 December 2007	Year ended 31 December 2006
Transportation expenses	24,458	10,229
Commissions and agent fees	3,684	3,084
Payroll and social taxes	2,241	2,133
Custom expenses	704	611
Repairs and maintenance	-	2,113
Other	1,697	1,288
Total	**32,784**	**19,458**

All amounts are in thousands of US Dollars unless otherwise stated

8. GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31 December 2007	Year ended 31 December 2006
Payroll and social taxes	9,890	7,796
Management services	4,174	-
Depreciation	1,303	846
Legal and consulting services	1,034	412
Materials	893	783
Insurance	884	825
Security	840	919
Taxes other than income tax	538	409
Repairs and maintenance	417	165
Credit organisations services	340	236
Other	2,176	1,360
Total	**22,489**	**13,751**

9. OTHER OPERATING INCOME AND EXPENSES

	Year ended 31 December 2007	Year ended 31 December 2006
Other operating income		
Gain on disposal of available-for-sale financial assets	5,025	-
Fines and penalties receivable	1,992	1,059
Gain on revaluation of forward exchange contracts	1,551	-
Dividend income	481	81
Gain on disposal of other assets	438	-
Foreign currency exchange gain on operating activities	180	-
Other	814	283
Total	**10,481**	**1,423**
Other operating expenses		
Social expenses	2,640	1,678
Charity and donations	1,411	518
Loss on disposal of property, plant and equipment	866	-
Loss from foreign currency sales and purchases	660	1,304
Foreign currency exchange loss on operating activities	-	518
Other	461	312
Total	**6,038**	**4,330**

All amounts are in thousands of US Dollars unless otherwise stated

10. INTEREST INCOME

	Year ended 31 December 2007	Year ended 31 December 2006
Interest on bank deposits	1,999	1,680
Interest on current accounts	249	354
Interest on loans issued and other receivables	224	104
Total	**2,472**	**2,138**

11. INTEREST EXPENSE

	Year ended 31 December 2007	Year ended 31 December 2006
Interest on trade payables	324	1,242
Interest on obligations under finance leases	104	170
Interest on bank loans and borrowings	32	75
Total	**460**	**1,487**

12. INCOME TAX EXPENSE

	Year ended 31 December 2007	Year ended 31 December 2006
Current tax expense	20,519	11,447
Deferred tax expense/(benefit)	1,478	(5,439)
Income tax expense	**21,997**	**6,008**

The corporate income tax rate in the Perm region of the Russian Federation, the location of the Group's production entities, was 20% for 2007 and 2006.

A reconciliation of statutory income tax, calculated at the rate effective in the Perm region of the Russian Federation to the amount of actual income tax expense is as follows:

	Year ended 31 December 2007	Year ended 31 December 2006
Profit before tax	**97,339**	**40,812**
Income tax expense calculated at 20%	19,468	8,162
Non-deductible social expenses	638	755
Non-deductible actuarial losses	402	-
Non-deductible employee benefits	342	-
Other non-deductible expenses	1,147	485
Effect of change in statutory rate	-	(3,394)
Income tax expense	**21,997**	**6,008**

All amounts are in thousands of US Dollars unless otherwise stated

13. PROPERTY, PLANT AND EQUIPMENT

	Buildings and structures	Machinery, equipment and transport	Other	Construction-in-progress	Total
Cost					
Balance at 31 December 2005	**25,995**	**123,065**	**1,710**	**966**	**151,736**
Additions	3,030	11,138	1,707	1,720	**17,595**
Transfers	302	795	117	(1,214)	**-**
Disposals	(159)	(319)	(25)	(71)	**(574)**
Effect of translation to presentation currency	2,523	11,834	217	103	**14,677**
Balance at 31 December 2006	**31,691**	**146,513**	**3,726**	**1,504**	**183,434**
Additions	2,478	12,788	288	13,810	**29,364**
Transfers	201	12,316	450	(12,967)	**-**
Disposals	(751)	(1,430)	(268)	(69)	**(2,518)**
Effect of translation to presentation currency	2,385	11,648	291	142	**14,466**
Balance at 31 December 2007	**36,004**	**181,835**	**4,487**	**2,420**	**224,746**
Accumulated depreciation					
Balance at 31 December 2005	**(1,957)**	**(12,520)**	**(207)**	**-**	**(14,684)**
Charge for the year	(2,435)	(15,161)	(391)	-	**(17,987)**
Eliminated on disposals	32	100	13	-	**145**
Effect of translation to presentation currency	(260)	(1,654)	(31)	-	**(1,945)**
Balance at 31 December 2006	**(4,620)**	**(29,235)**	**(616)**	**-**	**(34,471)**
Charge for the year	(2,708)	(18,276)	(759)	-	**(21,743)**
Eliminated on disposals	120	566	230	-	**916**
Effect of translation to presentation currency	(445)	(2,870)	(67)	-	**(3,382)**
Balance at 31 December 2007	**(7,653)**	**(49,815)**	**(1,212)**	**-**	**(58,680)**
Carrying value					
At 31 December 2006	**27,071**	**117,278**	**3,110**	**1,504**	**148,963**
At 31 December 2007	**28,351**	**132,020**	**3,275**	**2,420**	**166,066**

Assets pledged as collateral

The Group leases production equipment and transport assets under a number of finance lease agreements (refer to notes 26 and 28). The leases transfer ownership of the leased assets to the Group by the end of the lease terms or the Group has an option to purchase leased assets at a beneficial price. As at 31 December 2007, the Group's finance lease obligations were secured by the lessor's title to the leased assets with a carrying value of USD 923 thousand (2006: USD 604 thousand).

All amounts are in thousands of US Dollars unless otherwise stated

14. LONG-TERM AVAILABLE-FOR-SALE FINANCIAL ASSETS

	31 December 2007	31 December 2006
Equity instruments, at fair value	-	4,902
Equity instruments, at cost	91	3,894
Total	**91**	**8,796**

At 31 December 2006, equity instruments accounted for at fair value represented a 0.1% investment in Sberbank of Russia, and equity instruments accounted for at cost included a 17.59% investment in Ekoprombank of USD 3,233 thousand (refer to note 30).

15. LETTERS OF CREDIT

Letters of credit were issued by Sberbank in favour of suppliers of production equipment to the Group. Letters of credit were denominated in Euro and was interest free (2006: 7.5%).

16. OTHER FINANCIAL ASSETS

	31 December 2007	31 December 2006
Non-current		
Foreign currency forward contracts, at FVTPL	862	-
Long-term bank deposit, at amortised cost	244	-
	1,106	**-**
Current		
Loans issued, at amortised cost	28,283	-
Foreign currency forward contracts, at FVTPL	754	-
	29,037	**-**
Total	**30,143**	**-**

At 31 December 2007, the interest rate on the long-term bank deposit was 7%. The long-term deposit is RUR-denominated and matures in 2009.

At 31 December 2007, fixed interest rates on loans issued varied from 9% to 10.5%. The majority of loans issued were unsecured, RUR-denominated and receivable from related parties.

All amounts are in thousands of US Dollars unless otherwise stated

17. INVENTORIES

	31 December 2007	31 December 2006
Finished goods	9,411	3,233
Raw and auxiliary materials	4,748	3,711
Work-in-progress	1,810	773
Packing materials and implements	1,132	1,587
Other materials	3,160	3,791
	20,261	**13,095**
Less: allowance for obsolete and slow-moving inventories	(1,679)	(2,224)
Total	**18,582**	**10,871**

As at 31 December 2007, raw materials with a carrying value of USD 573 thousand (2006: USD 1,700 thousand) were pledged as guarantee for short-term borrowings granted to the Group.

18. TRADE AND OTHER RECEIVABLES

	31 December 2007	31 December 2006
Trade receivables	3,231	1,640
Other receivables	417	850
	3,648	**2,490**
Less: allowance for doubtful trade and other receivables	(101)	(222)
Total	**3,547**	**2,268**

The average credit period for the Group's customers varies from 20 to 30 days. During this period no interest is charged on the outstanding balances. The Group has provided fully for all receivables over 360 days because historical experience is such that receivables that are outstanding beyond 360 days are generally not recoverable. Before accepting any new customer, the Group uses an internal credit system to assess the potential customer's credit quality and defines credit limits separately for each individual customer. Credit limits available to customers are reviewed on an annual basis.

Movements in the allowance for doubtful trade and other receivables were as follows:

	31 December 2007	31 December 2006
Balance at beginning of the year	**222**	**137**
Recognised in the income statement	19	79
Amounts written off during the year	(23)	-
Amounts recovered during the year	(128)	(10)
Effect of translation to presentation currency	11	16
Balance at end of the year	**101**	**222**

All amounts are in thousands of US Dollars unless otherwise stated

19. ADVANCES PAID AND PREPAID EXPENSES

	31 December 2007	31 December 2006
Advances paid	23,709	4,093
Prepaid expenses	666	286
Total	**24,375**	**4,379**

20. TAXES RECEIVABLE

	31 December 2007	31 December 2006
Value added tax reimbursable	12,336	11,426
Other taxes	214	252
Total	**12,550**	**11,678**

21. BANK DEPOSITS

	31 December 2007	31 December 2006
RUR-denominated bank deposits at nominal rate of 7%	-	34,393
USD-denominated bank deposits at nominal rate of 5% to 6%	-	17,300
Interest receivable on USD-denominated bank deposits	-	289
Interest receivable on RUR-denominated bank deposits	-	224
Total	**-**	**52,206**

22. CASH AND CASH EQUIVALENTS

	31 December 2007	31 December 2006
Current accounts, including:		
RUR-denominated	12,160	6,230
USD-denominated	721	52
USD-denominated bank deposit	3,000	-
Total	**15,881**	**6,282**

At 31 December 2007, the interest rate on the USD-denominated bank deposit at HSBC bank was 4% with maturity in January 2008.

23. SHARE CAPITAL

Authorised, issued and fully paid share capital

As at 31 December 2007 and 2006, the share capital of the Company consisted of 405,871 authorised, issued and fully paid ordinary shares with a par value of RUR 1, carrying one vote per share and a right to dividends.

Included in share capital is an adjustment for the effect of hyperinflation in the amount of USD 6,552 thousand.

All amounts are in thousands of US Dollars unless otherwise stated

Retained earnings and dividends

The statutory financial statements of the Group entities are the basis for the profit distribution and other appropriations.

On 24 May 2007, a dividend of USD 240.84 per share, amounting to a total dividend of USD 97,751 thousand, was declared to shareholders.

The movement of dividends payable was as follows:

	31 December 2007	31 December 2006
Balance at beginning of the year	**-**	**-**
Dividends declared during the year	97,751	-
Dividends paid during the year	(97,067)	-
Effect of translation to presentation currency	29	-
Balance at end of the year	**713**	**-**

Earnings per share

Basic earnings per share is calculated by dividing the net profit attributable to the shareholder of the Company by the weighted average number of ordinary shares in issue during the year. As at 31 December 2007 and 2006, the Company had no dilutive potential ordinary shares.

24. DEFERRED TAX LIABILITIES

	1 January 2007	Recognised in the income statement	Recycled from equity	Effect of translation to presentation currency	31 December 2007
Property, plant and equipment	**17,963**	(196)	-	1,300	**19,067**
Long-term available-for-sale financial assets	**980**	-	(1,009)	29	**-**
Other financial assets	**-**	260	-	11	**271**
Inventories	**(721)**	584	-	(28)	**(165)**
Trade and other receivables	**(824)**	(147)	-	(66)	**(1,037)**
Employees benefits obligations	**(683)**	703	-	(20)	**-**
Finance lease liabilities	**(61)**	(31)	-	(6)	**(98)**
Accounts payable and accrued charges	**(267)**	305	-	(6)	**32**
Total	**16,387**	**1,478**	**(1,009)**	**1,214**	**18,070**

All amounts are in thousands of US Dollars unless otherwise stated

	1 January 2006	Recognised in the income statement	Recognised directly in equity	Effect of translation to presentation currency	31 December 2006
Property, plant and equipment	**20,729**	(4,549)	-	1,783	**17,963**
Long-term available for sale financial assets	**441**	-	481	58	**980**
Inventories	**(198)**	(488)	-	(35)	**(721)**
Trade and other receivables	**(980)**	239	-	(83)	**(824)**
Employees benefits obligations	**(696)**	76	-	(63)	**(683)**
Finance lease liabilities	**(104)**	50	-	(7)	**(61)**
Accounts payable and accrued charges	**480**	(767)	-	20	**(267)**
Total	**19,672**	**(5,439)**	**481**	**1,673**	**16,387**

25. EMPLOYEE BENEFIT OBLIGATIONS

Defined benefit plan

The Group operates an unfunded defined benefit plan. The most recent actuarial valuation of defined benefit obligations as at 31 December 2007 was performed by an independent actuary.

The principal assumptions used for the purposes of the actuarial valuation were as follows:

	31 December 2007	31 December 2006
Discount rate	6.6%	6.6%
Expected salary increase	9.2%	8.8%
Expected pension increase	5.0%	6.4%
Employee turnover rate	5.0%	10.0%
Age of retirement		
Male	53 years	52 years
Female	50 years	52 years
Average life expectancy of members from date of retirement		
Male	20 years	23 years
Female	31 years	23 years

Amounts recognised in the income statement in respect of the defined benefit plan were as follows:

	31 December 2007	31 December 2006
Actuarial losses	1,584	67
Interest on obligation	358	205
Current service cost	220	82
Total	**2,162**	**354**

All amounts are in thousands of US Dollars unless otherwise stated

As at 31 December 2007, the present value of unfunded defined benefit obligations included in the balance sheet in respect of defined benefit plan was USD 5,756 thousand (2006: USD 3,413 thousand).

Movements in the present value of the unfunded defined benefit obligations were as follows:

	31 December 2007	31 December 2006
Balance at beginning of the year	**3,413**	**2,898**
Actuarial losses	1,584	67
Interest on obligation	358	205
Current service cost	220	82
Benefits paid	(152)	(117)
Effect of translation to presentation currency	333	278
Balance at end of the year	**5,756**	**3,413**

26. OTHER NON-CURRENT LIABILITIES

	31 December 2007	31 December 2006
Long-term trade accounts payable	-	878
Long-term finance lease liabilities	130	144
Total	**130**	**1,022**

Long-term trade accounts payable represent gas supply liabilities which were restructured under an amicable agreement and court decisions in 2003 and 2004. Long-term liabilities are accounted for at amortised cost using an effective interest rate of 15% to 17%.

During the period from 2003 to 2007, the Group entered into a number of finance lease agreements. As at 31 December 2007, the Group's obligations under finance leases were secured by the lessor's title to the leased assets with a carrying amount of USD 923 thousand (2006: USD 604 thousand) (refer to note 13).

27. SHORT-TERM BORROWINGS

	Currency	Rate	31 December 2007	31 December 2006
Sberbank	RUR	9.2%	3,264	-
Sberbank	Euro	9.0%	-	5,642
Total			**3,264**	**5,642**

The RUR-denominated loan bears interest at a fixed rate of 9.2% per annum and was repayable in one installment on 11 January 2008. At 31 December 2007, the loan was secured by catalytic agents with a carrying value of USD 2,412 thousand.

The Euro-denominated loan bore interest at a fixed rate of 9.0% per annum and was fully repaid on 25 July 2007. The loan was obtained for arrangement of letters of credit (refer to note 15), and was secured by catalytic agents with a carrying value of USD 8,640 thousand.

All amounts are in thousands of US Dollars unless otherwise stated

28. TRADE AND OTHER PAYABLES

	31 December 2007	31 December 2006
Trade payables	5,871	5,896
Accrued liabilities and other creditors	2,516	985
Provision for unused vacation	1,628	1,722
Dividends payable	713	201
Current portion of finance lease liabilities	362	163
Total	**11,090**	**8,967**

During the period from 2003 to 2007, the Group entered into a number of finance lease agreements. As at 31 December 2007, the Group's obligations under finance leases were secured by the lessor's title to the leased assets with a carrying amount of USD 923 thousand (2006: USD 604 thousand) (refer to note 13).

The average credit period on the purchase of the majority of inventories and services in the Russian Federation varies from 10 to 30 days.

The table below summarises the maturity profile of the Group's trade and other payables based on contractual undiscounted payments:

	31 December 2007	31 December 2006
Due within three months	7,057	5,163
Due from three to six months	2,676	519
Due from six to twelve months	1,410	3,463
Total	**11,143**	**9,145**

29. OTHER TAXES PAYABLE

	31 December 2007	31 December 2006
Personal income tax	356	355
Property tax	339	278
Unified social tax	235	251
Other taxes	358	228
Total	**1,288**	**1,112**

All amounts are in thousands of US Dollars unless otherwise stated

30. RELATED PARTIES TRANSACTIONS AND OUTSTANDING BALANCES

Related parties include the Company's shareholders and entities under common ownership and control with the Group and members of key management personnel.

As at 31 December 2007 and 2006, the Group had the following outstanding balances with related parties:

	31 December 2007	31 December 2006
Shareholders of the Group		
Loans issued (refer to note 16)	4,808	-
Trade and other receivables	92	-
Trade and other payables	(489)	-
Entities under common ownership and control with the Group		
Long-term available-for-sale financial assets	-	3,233
Loans issued (refer to note 16)	23,474	-
Bank deposits	-	21,290
Trade and other receivables	58	1
Advances paid and prepaid expenses	5,196	-
Long term receivables	-	172
Trade and other payables	(919)	(1,657)
Advances received	(49)	-
Finance lease liabilities	-	(307)

During the years ended 31 December 2007 and 2006 the Group entered into the following transactions with related parties:

	Year ended 31 December 2007	Year ended 31 December 2006
Shareholders of the Group		
Sales of goods and services	91	-
Purchases of services	(4,203)	-
Loans issued	5,100	-
Proceeds from repayment of loans issued	(485)	-
Interest income	17	-
Entities under common ownership and control with the Group		
Sales of goods and services	54,495	21,058
Purchases of services	(20,108)	(6,786)
Interest income	1,325	1,163
Interest expense	-	(170)
Redemption of promissory notes	-	2,575
Purchase of promissory notes	-	(1,214)
Purchase of available-for-sale financial assets	-	(1,684)
Sale of available-for-sale financial assets	3,328	-
Placement of cash in bank deposits	-	(24,653)
Receipt of cash from bank deposits	21,918	15,545
Loans issued	22,520	-
Proceeds from repayment of loans issued	(392)	-

All amounts are in thousands of US Dollars unless otherwise stated

The amounts outstanding were unsecured and were expected to be settled in cash. No expense was recognised during the year ended 31 December 2007 and 2006 for bad or doubtful debts in respect of amounts owed by related parties.

The Group enters into transactions with related parties in the ordinary course of business for the purchase and sale of goods and services and in relation to the provision of financing arrangements to and from its parent entity or entities under common ownership.

Sales of goods and services to related parties were made on terms similar to those that were used in transactions with third parties, including average discounts of 3% to 5% applicable to the Group's largest customers.

Purchases from related parties which primarily included a management fee charged by Limited Liability Company Management Company Uralchem, one of the Company's shareholders, and re-charges of transport bills from Russian Railways and other independent carriers were made at market prices plus an insignificant premium of 1% to 2% as reimbursement for operating expenses of those entities.

During the year ended 31 December 2007 and 2006, agent's commission of 3.5% was incurred on purchase transactions with related parties.

On 30 May 2007, the Company sold its 17.59% ownership in Perm Ekoprombank with a book value of USD 3,328 thousand to related parties. No gain or loss was recognised in the income statement as a result of this transaction.

Loans to related parties were issued at market terms.

Compensation of key management personnel

The remuneration of key management personnel of the Group for the year ended 31 December 2007 comprised salaries and bonuses in the amount of USD 1,751 thousand (2006: USD 498 thousand).

31. COMMITMENTS AND CONTINGENCIES

Purchase of natural gas

In December 2007, the Group entered into binding purchase agreements with Gazprom and Novatek, to purchase defined volumes of natural gas.

Future minimum costs under non-cancellable purchase agreements are as follows:

	31 December 2007	31 December 2006
Due in one year	81,091	-
Due from one to five years	361,212	-
Total	**442,303**	**-**

All amounts are in thousands of US Dollars unless otherwise stated

Capital expenditure commitments

The Group's contractual capital expenditures commitments for the acquisition of property, plant and equipment and fulfilment of certain finance lease agreements are as follows:

	31 December 2007	31 December 2006
Acquisition of property, plant and equipment	666	7,357
Fulfilment of finance lease agreements	651	434
Total	**1,317**	**7,791**

Guarantees issued

The Group issued financial guarantees in respect of loans obtained by related parties. The total amount of the guarantees outstanding as at 31 December 2007 was USD 255,096 thousand (2006: nil).

The Group did not recognise a financial guarantee contract liability in respect of a financial guarantee provided by the Company to Sberbank in respect of a loan of USD 195,856 thousand obtained by one of the Company's shareholders, Limited Liability Company Management Company Uralchem, from Sberbank. The loan is secured by 77.6% of Azot's shares held by Limited Liability Company Management Company Uralchem.

The Group's maximum exposure to credit risk in the event of non-performance by parties to these financial guarantees is limited to the contractual amounts disclosed above. As at 31 December 2007, management assessed the risk of non-performance by parties to the financial guarantees as remote.

Litigation

The Group has a number of claims and litigation relating to sales and purchases. Management believes that none of these claims, individually or in aggregate, will have a material adverse impact on the Group.

Taxation contingencies in the Russian Federation

The taxation system in the Russian Federation is at a relatively early stage of development, and is characterised by numerous taxes, frequent changes and inconsistent enforcement at federal, regional and local levels.

The government of the Russian Federation has commenced a revision of the Russian tax system and passed certain laws implementing tax reform. The new laws reduce the number of taxes and overall tax burden on businesses and simplify tax litigation. However, these new tax laws continue to rely heavily on the interpretation of local tax officials and fail to address many existing problems. Many issues associated with practical implication of new legislation are unclear and complicate the Group's tax planning and related business decisions.

In terms of Russian tax legislation, authorities have a period of up to three years to re-open tax declarations for further inspection. Changes in the tax system that may be applied retrospectively by authorities could affect the Group's previously submitted and assessed tax declarations.

While management believes that it has adequately provided for tax liabilities based on its interpretation of current and previous legislation, the risk remains that tax authorities in the Russian Federation could take differing positions with regard to interpretive issues. This uncertainty may expose the Group to additional taxation, fines and penalties that could be significant.

Environmental matters

The Group is subject to extensive federal, state and local environmental controls and regulations in the Perm region of the Russian federation in which it operates. The Group's operations involve the discharge of materials, contaminants and waste water into the environment that could potentially impact on flora and fauna, and give rise to other environmental concerns.

The Group's management believes that its production facilities are in compliance with all current existing environmental legislation in the region in which it operates. However, environmental laws and regulations continue to evolve.

The Group is unable to predict the timing or extent to which those laws and regulations may change. Such change, if it occurs, may require that the Group modernise technology and upgrade production equipment to meet more stringent standards.

Management of the Group regularly reassesses environmental obligations related to its operations. Estimates are based on management's understanding of current legal requirements and the terms of licence agreements. Should the requirements of applicable environmental legislation change or be clarified and amended, the Group may incur additional environmental obligations.

Russian Federation risk

As an emerging market, the Russian Federation does not possess a fully developed business and regulatory infrastructure including stable banking and judicial systems, which would generally exist in a more mature market economy. The economy of the Russian Federation is characterised by a currency that is not freely convertible outside of the country, currency controls, low liquidity levels for debt and equity markets, and continuing inflation. As a result, operations in the Russian Federation involve risks that are not typically associated with those in more developed markets. The stability and success of the Russian economy and the Group's business mainly depends on the effectiveness of economic measures undertaken by the government as well as the development of legal and political systems.

32. FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of financial assets and liabilities is determined as follows:

- the fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices; and
- the fair value of other financial assets and financial liabilities are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions.

Management believes that the carrying values of all significant financial assets (refer to notes 16, 18 and 22) and financial liabilities (refer to notes 26, 27 and 28) recorded at amortised cost in the consolidated financial statements approximated their fair values.

33. FINANCIAL RISK MANAGEMENT

Capital risk management

The Group manages its capital to ensure that entities of the Group will be able to continue as a going concern while maximising the return to its shareholders through the optimisation of the debt and equity balance. The management of the Group reviews the capital structure on a regular basis. Based on the results of this review, the Group takes steps to balance its overall capital structure through the payment of dividends, new share issues as well as the issue of new debt or the redemption of existing debt.

Major categories of financial instruments

The Group's principal financial liabilities comprise loans and borrowings and trade payables. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various financial assets such as trade and other receivables, loans issued and cash and cash equivalents.

All amounts are in thousands of US Dollars unless otherwise stated

	31 December 2007	31 December 2006
Financial assets		
Long-term available-for-sale financial assets	91	8,796
Foreign currency forward contracts, at FVTPL	1,616	-
Long-term bank deposit, at amortised cost	244	-
Trade and other receivables	3,547	2,268
Bank deposits	-	52,206
Loans issued, at amortised cost	28,283	-
Cash and cash equivalents	15,881	6,282
Total financial assets	**49,662**	**69,552**
Financial liabilities		
Long-term trade accounts payable	-	878
Long-term finance lease liabilities	130	144
Short-term borrowings	3,264	5,642
Trade and other payables	9,462	7,245
Total financial liabilities	**12,856**	**13,909**

The main risks arising from the Group's financial instruments are foreign currency, interest rate, credit and liquidity risks.

Foreign currency risk

Currency risk is the risk that the financial results of the Group will be adversely impacted by changes in exchange rates to which the Group is exposed. The Group undertakes certain transactions denominated in foreign currencies. The Group uses derivatives to manage foreign currency risk exposure (see below).

The carrying amounts of the Group's foreign currency denominated monetary assets and liabilities as at the reporting date were as follows:

	31 December 2007	
	US Dollar-denominated	Euro-denominated
Assets		
Trade and other receivables	2,295	-
Cash and cash equivalents	3,721	-
Total assets	**6,016**	**-**
Liabilities		
Trade and other payables	145	176
Total liabilities	**145**	**176**
Total net position	**5,871**	**(176)**

All amounts are in thousands of US Dollars unless otherwise stated

	31 December 2006	
	US Dollar-denominated	Euro-denominated
Assets		
Trade and other receivables	652	5
Bank deposits	17,589	-
Cash and cash equivalents	52	-
Total assets	**18,293**	**5**
Liabilities		
Short-term borrowings	-	5,642
Trade and other payables	1	158
Total liabilities	**1**	**5,800**
Total net position	**18,292**	**(5,795)**

The table below details the Group's sensitivity to strengthening of the Russian Rouble against the US Dollar and the Euro by 10%. The analysis was applied to monetary items at the balance sheet date denominated in US Dollar and Euro.

	Year ended 31 December 2007	
	US Dollar - impact	Euro - impact
Loss/(profit)	587	(18)

	Year ended 31 December 2006	
	US Dollar - impact	Euro - impact
Loss/(profit)	1,829	(580)

Forward foreign exchange contracts

Starting from 2007, the Group enters into forward foreign exchange contracts in respect of its export revenues. As at and for the year ended 31 December 2007, no foreign currency exchange contracts were designated as cash flow hedges, accordingly, an amount of USD 1,551 thousand (refer to note 9) relating to the change in the fair value of derivative instruments was included in other operating income in the income statement.

All amounts are in thousands of US Dollars unless otherwise stated

The following table details the forward foreign currency contracts outstanding as at 31 December 2007:

		31 December 2007	
	Weighted average exchange rate	Contract value	Fair value
Sell USD			
Due within three months	24.60	34,120	176
Due from three to six months	24.69	25,548	167
Due from six months to twelve months	24.80	68,939	411
Total current		**128,607**	**754**
Due in second year	25.33	89,856	862
Total		**218,463**	**1,616**

Interest rate risk

Interest rate risk is the risk that changes in floating interest rates will adversely impact the financial results of the Group. All the Group's financial assets and liabilities are at fixed rates.

Credit risk

Credit risk is the risk that a customer may default or not meet its obligations to the Group on a timely basis, leading to financial losses to the Group.

Before accepting of any new customer, the Group uses an internal credit system to assess the potential customer's credit quality and defines credit limits separately for each individual customer. Credit limits attributable to each individual customer are regularly reviewed at least on an annual basis.

Revenue from the five largest customers constitute approximately 50% of the Group's total revenue, however management believes that there is no concentration of credit risk. The Group is not dependent on the largest customers because of the existence of a liquid commodity market for the majority of fertilisers and its by-products.

As at 31 December 2007, the Group's five largest debtors (individually exceeding 2% and (2006: 6%) of the total receivables balance) represented 77% (2006: 61%) from the outstanding balance of accounts receivable, respectively.

The summary below shows the top five outstanding balances receivable from debtors as at 31 December 2007:

	Location	Outstanding balance
First largest debtor	Europe	2,263
Second largest debtor	Russia	181
Third largest debtor	Russia	140
Fourth largest debtor	Russia	92
Fifth largest debtor	Russia	73
Total		**2,749**

All amounts are in thousands of US Dollars unless otherwise stated

The summary below shows the top five outstanding balances receivable from debtors as at 31 December 2006:

	Location	Outstanding balance
First largest debtor	Russia	650
Second largest debtor	Russia	211
Third largest debtor	Russia	193
Fourth largest debtor	Russia	190
Fifth largest debtor	Russia	139
Total		**1,383**

Liquidity risk

Liquidity risk is the risk that the Company will not be able to settle all liabilities as they fall due. The Group's liquidity position is carefully monitored and managed. The Company has a detailed budgeting and cash forecasting process to help ensure that it has adequate cash available to meet its payment obligations.

The following table summaries the maturity profile of the Group's loans and borrowings, trade and other payables (refer to notes 27 and 28) as at 31 December 2007 and 2006 based on undiscounted contractual payments, including interest payments:

	31 December 2007				
	Total	**Due within three months**	**Due from three to six months**	**Due from six to twelve months**	**Due after twelve months**
Fixed rate loan and borrowings	3,273	3,273	-	-	-
Finance lease liabilities	604	133	119	163	189
Trade and other payables	9,100	6,517	2,150	433	-
Total	**12,977**	**9,923**	**2,269**	**596**	**189**

	31 December 2006				
	Total	**Due within three months**	**Due from three to six months**	**Due from six to twelve months**	**Due after twelve months**
Fixed rate loan and borrowings	5,690	1,410	114	4,166	-
Finance lease liabilities	500	86	92	164	158
Trade and other payables	8,164	4,694	-	2,387	1,083
Total	**14,354**	**6,190**	**206**	**6,717**	**1,241**

34. EVENTS SUBSEQUENT TO THE BALANCE SHEET DATE

During the first quarter of 2008, the Group issued guarantees for related parties in the amount of USD 104,246 thousand.

On 4 June 2008, the Company issued a financial guarantee to Sberbank in respect of a loan facility agreement granted to its shareholder, Open Join Stock Company Uralchem, in the amount of USD 700,000 thousand, of which an amount of USD 533,414 thousand was utilised at the date of issue of these financial statements.