PIK Group Annual Report 2007

# Chairman's Statement

**"By any measure, 2007 was a year of outstanding achievements for the Group."**

**Zhukov Y.V.**
*Chairman of the Board of Directors PIK Group*

*'Nagatinskaya Embankment' development, Moscow*

# Contents

# Chairman's statement

Dear Shareholders,

On behalf of the Board, it is a great pleasure to present PIK's Annual Report for 2007. By any measure, the year was one of outstanding achievements for the Group.

On June 1 2007, we successfully completed our Initial Public Offering ('IPO') on the London and Russian (Micex, RTS) stock exchanges. The IPO followed an intensive year-long period of preparation. On completion, it was the largest ever real estate IPO in Europe. With an offer size of $1.93 billion it was also the largest ever non-REIT property IPO globally.

During the course of the year we delivered on a core IPO promise to take advantage of low land prices and extended PIK's presence in the regions. 2007 saw the total net saleable space increase by 61% to 14.2 million square meters, driving the portfolio market value to $12.3 billion, a 40% rise.

In August 2007, we entered the commercial sector of the market with the acquisition of a majority stake in Storm Properties, a dynamic and growing Russian commercial developer of small, convenience office concepts. The acquisition enables us to harness the expertise of proven professionals from the commercial office development market.

In December 2007, we received our first credit rating, 'BB-', from the Fitch rating agency, the highest rating of any company in the Russian real estate sector.

December also saw the completion of a milestone transaction with GIC Real Estate, the real estate investment arm of the Government of Singapore. An unprecedented deal, it saw a foreign investor take a major stake for the first time in a large mass market residential project, Mytischi, located in Moscow region. Under the partnership agreement, an affiliate of GIC Real Estate acquired a 25% stake in the project for $233 million.

Overall, we have made significant progress in transforming PIK into an internationally recognized real estate developer focused on sustainable growth in the mass-market residential sector. PIK Group's management and staff have worked hard to meet the challenges associated with this transformation. I wish to thank all of them for their efforts.

I would also like to take this opportunity to thank all our shareholders, business partners and customers. With your continued support, I am confident PIK Group will continue to perform well in 2008.

**Zhukov Y.V.**
*Chairman of the Board of Directors PIK Group*

# Key Operational Highlights

**Since its foundation in 1994, PIK has completed over 6.5 million square meters of housing, equivalent to over 110,000 units.**

### Key Operational Highlights

### Business overview

**PIK's core activity is the development and sale of residential real estate in Russia with a focus on mass-market neighborhood centers for raising middle class families.** In addition to real estate development, the Group is engaged in the production and assembly of pre-fabricated mass-market housing, facility management of finished apartments and production of construction materials including aggregates (sand, crushed rock and gravel).

In 2007 PIK entered the commercial market with the acquisition of a majority share in Storm Properties. This will give PIK the expertise to exploit stand-alone commercial opportunities, and those associated with its residential development activities.

### Competitive strengths

Our main competitive strengths are the following:

- a large and diversified land bank: 14.2 million square meters of unsold saleable area (as of January 1 2008)
- a vertically integrated business model that allows us to manage and control the most important stages of the development process
- the capacity and ability to produce large-scale residential developments, approximately 1.3 million square meters of 'in-house' prefabricated capacity.
- a leading market position in Moscow and the Moscow region, and a significant and growing presence in other regions of Russia
- a largely self-funding business model driven by pre-sales of residences
- strong brand recognition, a well-established reputation and long-standing relationships with governmental authorities
- an experienced and dedicated management team enhanced by a strong board of directors.

### Russian residential market

The last three years have seen a Russian economic boom. In 2007 alone, there was a 7.8% increase in real GDP. This was driven by a combination of fiscal and budgetary discipline, falling interest-rates, structural economic reforms, decreasing unemployment, supported by growing oil and gas revenues.

Russia's residential market has tracked this growth driven by a number of factors. There has been strong growth in real disposable income, 10% increase p.a. during the last 3 - 4 years; a comprehensive government housing program, which has prescribed the necessity to build 140 million square meters of housing annually by 2015; decreasing household size and urbanization of the population. Falling interest rates and the increasing propensity of households to spend on housing have also contributed.

Further detail on the Russian real estate market is provided on page 8.

**With increasing wealth at their disposal, improving on their obsolete apartments has become a high-priority for Russian families**

## Strategy

**PIK is well positioned to take advantage of these economic trends. The Group has established itself as the market leader for mass-market housing in Moscow and Moscow region.**

Since 2006, PIK has been expanding and diversifying into the regions beyond Moscow, entering important cities such as Kaluga, Kaliningrad, Omsk, Perm, Novorossiysk, Rostov, Yaroslavl, Taganrog and Nizhny Novgorod.

PIK's regional expansion will be supported by replicating the business model in Moscow and Moscow region area, where PIK's development activity is backed by execution capacity through a number of production assets (e.g. prefabricated production facilities)

PIK's stated intention is to extend its reach further, by moving into St. Petersburg, Ukraine and Kazakhstan, the latter marking the Group's first moves outside the Russian Federation. Over the next few years management intends, through land purchases and by acting to consolidate Russia's fragmented real estate development industry, to extend PIK's reach even further. We will also look at entering new territories within the CIS where we believe the demographic and socio-economic profile is right for our product.

We also see opportunities in the commercial sector, principally related to our residential developments, in office and retail developments in and around PIK constructed mini-cities.

Following the sale of a 25% stake in one of our flagship projects to Singapore's GIC sovereign wealth fund, the Group is also exploring new methods of attracting finance for its development pipeline. The GIC Real Estate transaction was a first for Russian residential mass-market real estate, and management believes the deal structure can be replicated for other large projects and other investors. In another innovation, we have recently established PIK Capital Partners, the real estate private equity arm of PIK Group, which has launched the PIK Real Estate Fund to invest in a broad range of Group real estate transactions.

Further detail on our strategy is provided on page 14.

## Corporate governance

**We comply with the corporate governance requirements applicable to Russian public companies listed on the Russian stock exchanges. We aim to introduce best practice international standards of corporate governance.**

In line with Russian requirements, we comply with a number of corporate governance requirements. We are obliged to undertake the following: to have at least one independent director, to form an audit committee, to adopt a bylaw on insider trading and implement internal control procedures. We are in full compliance with these requirements. In addition, we observe the Code of Corporate Conduct, as recommended by the Russian Federal Service for the Financial Markets.

Further detail on our corporate governance is provided on page 59.

# Key Operational Highlights / Russian Real Estate Market Overview

**The Russian real estate market has strong fundamentals, both on a macro and on a micro level.**

### Outlook

Forecasts for Russian economic growth in 2008 range between 7-8%. Although there are some signs of inflationary pressure within the financial system, the overall economic background remains solid, supported by continuing strength in the global oil price.

Mortgage accessibility in Russia, due to its low penetration across the country, has been affected insignificantly by the credit crunch that has affected residential markets in some Western countries. We expect to see continuing demand for new, modern housing from consumers across Russia. The management of PIK is confident that further growth will be delivered to shareholders in line with current market expectations.

### Russian real estate market overview

**For the last few years, the Russian economy has shown a steep rise in GDP, recording increases of between 6 – 8% per annum (2007: 7.8%). Accordingly, in recent years, Russia has been assigned investment grade ratings of Baa2 (Moody's) and BBB+ (S&P).**

**As of and for the year ended December 31 2007**

| | 2003 | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|---|
| Real GDP growth, year on year (a) | 7.3% | 7.2% | 6.4% | 7.4% | 8.1% |
| Real disposable income growth, year on year (a) | 15.0% | 10.4% | 12.4% | 13.3% | 10.4% |
| CPI, Dec/Dec (a) | 12.0% | 11.7% | 10.9% | 9.0% | 11.9% |
| RUB/$ exchange rate, end of period (b) | 29.45 | 27.75 | 28.78 | 26.33 | 24.55 |
| Fixed investments, year on year (a) | 12.5% | 13.7% | 10.9% | 16.7% | 21.1% |
| Budget balance (% of GDP) (c) | 2.4% | 4.9% | 7.5% | 7.4% | 5.9% |
| Construction real growth, year on year (a) | 7.7% | 12.6% | 6.1% | 16.1% | 19.4% |

*Source: (a) Rosstat, (b) CBR, (c) MSM*

Robust economic growth has been driven by a combination of fiscal and budgetary discipline, structural economic reforms, decreasing unemployment, growing disposable income and high oil prices.

Russia has also remained relatively insulated from the credit crunch so far, and benefits from the cushion provided by the support of state-financed banks and an economy underpinned by high oil and gas fuelled cash surpluses.

## Russian residential real estate market overview

**Russia's residential market demonstrates stable growth driven by the fundamental forces of lack of supply and pent up demand.**

Prior to the break-up of the Soviet Union, most residential construction was financed by the government. With the political instability of the early 1990s, there was a dramatic decrease in government finance for housing. Construction volumes fell sharply, from a historical high of 75 million square meters registered in 1987 to 61.7 million square meters in 1990, and further to 30.3 million square meters in 2000 (source: Rosstat).

In 2000, however, residential construction began to recover, growing at an average rate of 8.7% per annum to reach 50.2 million square meters in 2006 and 60.2 million square meters in 2007 (+19% 2007 vs. 2006).

**Residential completion volumes**

| | 1990 | 1995 | 1990-95 CAGR | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2000-07 CAGR |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Total square meters of residential construction in Russia (millions) | 61.7 | 41.0 | –7.8% | 30.3 | 31.7 | 33.8 | 36.4 | 41.0 | 43.6 | 50.6 | 60.4 | 10.3% |
| Moscow | 2.3 | 2.5 | 2.5% | 3.3 | 3.7 | 4.3 | 4.4 | 4.6 | 4.6 | 4.8 | 4.8 | 5.4% |
| Moscow region | 2.4 | 2.4 | –0.3% | 2.6 | 2.8 | 3.4 | 4.1 | 5.7 | 5.3 | 6.5 | 7.6 | 16.5% |
| St Petersburg | 1.1 | 1.0 | –1.0% | 1.1 | 1.1 | 1.2 | 1.8 | 2.0 | 2.3 | 2.4 | 2.6 | 13.6% |
| Leningrad region | 0.8 | 0.4 | –11.1% | 0.4 | 0.4 | 0.4 | 0.4 | 0.5 | 0.5 | 0.7 | 0.8 | 11.6% |
| Other regions | 55.2 | 34.7 | –8.9% | 22.9 | 23.7 | 24.5 | 25.7 | 28.2 | 30.7 | 35.9 | 44.5 | 10.0% |
| *Share of other regions* | *89%* | *85%* | | *75%* | *75%* | *72%* | *70%* | *69%* | *71%* | *72%* | *74%* | |

*Source: Rosstat*

# Russian Real Estate Market Overview

**Residential construction volume**

| | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | CAGR '02-'07 |
|---|---|---|---|---|---|---|---|
| Krasnodar Region | 1,645 | 1,580 | 1,810 | 1,940 | 2,705 | 3,704 | 17.6% |
| – Novorossiysk [(a)] | 30 | 68 | 76 | 52 | 168 | 180 | 43.1% |
| N. Novgorod Region | 485 | 576 | 684 | 748 | 826 | 1,072 | 17.2% |
| – Nizhny Novgorod [(a)] | 198 | 265 | 331 | 366 | 443 | 607 | 25.1% |
| Perm Region | 361 | 416 | 449 | 638 | 718 | 884 | 19.6% |
| – Perm [(a)] | 149 | 221 | 245 | 369 | 426 | 498 | 27.3% |
| Rostov Region | 984 | 1,005 | 1,119 | 1,186 | 1,388 | 1,706 | 11.6% |
| – Rostov-on-Don [(a)] | 453 | 506 | 582 | 620 | 707 | 860 | 13.7% |
| – Taganrog [(a)] | 27 | 24 | 70 | 70 | 87 | 106 | 31.5% |
| Omsk Region | 230 | 318 | 520 | 756 | 906 | 1,104 | 36.9% |
| – Omsk [(a)] | 169 | 221 | 398 | 595 | 723 | 820 | 37.1% |
| Yaroslavl Region | 175 | 215 | 218 | 224 | 247 | 420 | 19.1% |
| – Yaroslavl [(a)] | 92 | 146 | 122 | 120 | 184 | 240 | 21.1% |
| Kaliningrad Region | 198 | 232 | 245 | 266 | 501 | 753 | 30.6% |
| – Kaliningrad [(a)] | 149 | 162 | 167 | 178 | 369 | 740 | 37.8% |

*(in square meters, thousands)*

Source: Rosstat, (a) MSM

Growth in the residential market is driven by structural undersupply and by the government housing program prescribing the construction of 140 million square meters of housing annually by 2015 (equivalent to 1 square meter per capita). Furthermore, increasing urbanization of the population is being matched by decreasing household size.

Additionally, interest rates on mortgages are falling, and there is an increasing propensity of households to spend their disposable income on housing, with strong real disposal income growth of 10% p.a. during the last 3-4 years. Significantly mortgage sales have been growing, with small penetration as to % of GDP.

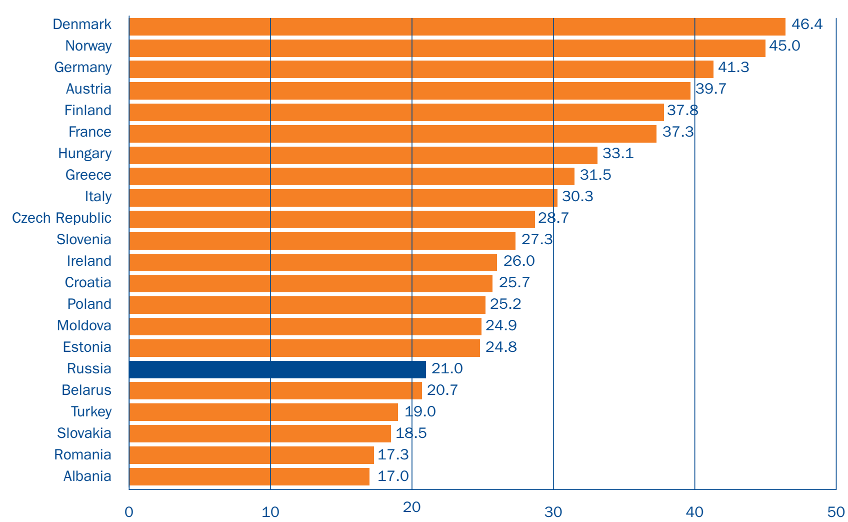
## Existing housing stock

**Poor maintenance, insufficient additions and lack of replacements in existing housing stock during the 1990s, means apartment blocks across Russia have became obsolete**. Various sources confirm that approximately one third of the total housing stock needs to be replaced in the near term.

Moreover, the large majority of Russians still live in small flats built over the last 40-60 years. Statistically Russia has only 21.1 square meters per capita compared to a European average figure of 29 square meters per capita. In order to keep pace with its replacement housing needs, the country needs to construct one square meter per capita per annum, roughly a third of the existing stock.

As a result, the residential market has seen significant price appreciation, both in Moscow and in Russia's regions.

Housing stock per capita in Russia and other countries
(square meters per capita)




*Source: Rosstat; UNECE annual report 2004; www.bnp.ru, Expert Ra*

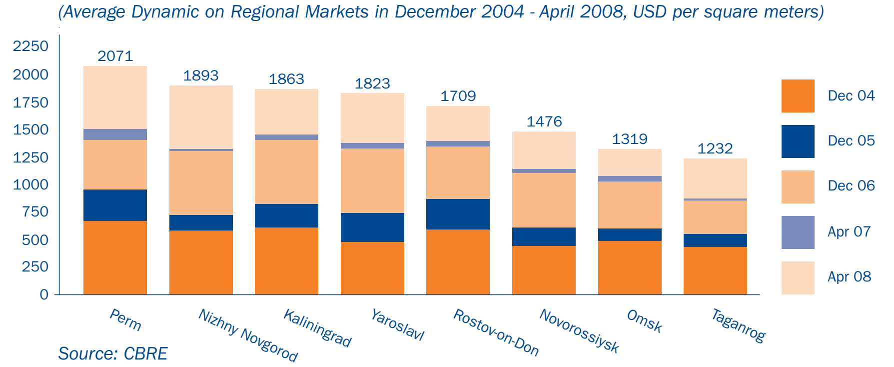
**According to the EIU, Russia has the fastest growing middle-class among the BRIC countries. This socio-economic group, where demand for housing is strongest, is PIK Group's target customer group.**

**Average Regional Residential Price Dynamic over time**

| USD per square meters | Apr. 2008 | Apr. 2007 | Apr. 2008-Apr. 2007 | Dec. 2006-Dec. 2005 | Dec. 2005-Dec. 2004 |
|---|---|---|---|---|---|
| Perm | 2071 | 1500 | 38% | 47% | 43% |
| N.Novgorod | 1893 | 1320 | 43% | 81% | 24% |
| Kaliningrad | 1863 | 1450 | 28% | 71% | 34% |
| Yaroslavl | 1823 | 1374 | 33% | 79% | 56% |
| Rostov-on-Don | 1709 | 1390 | 23% | 55% | 47% |
| Novorossiysk | 1476 | 1140 | 29% | 80% | 39% |
| Omsk | 1319 | 1075 | 23% | 71% | 24% |
| Taganrog | 1232 | 870 | 42% | 55% | 28% |

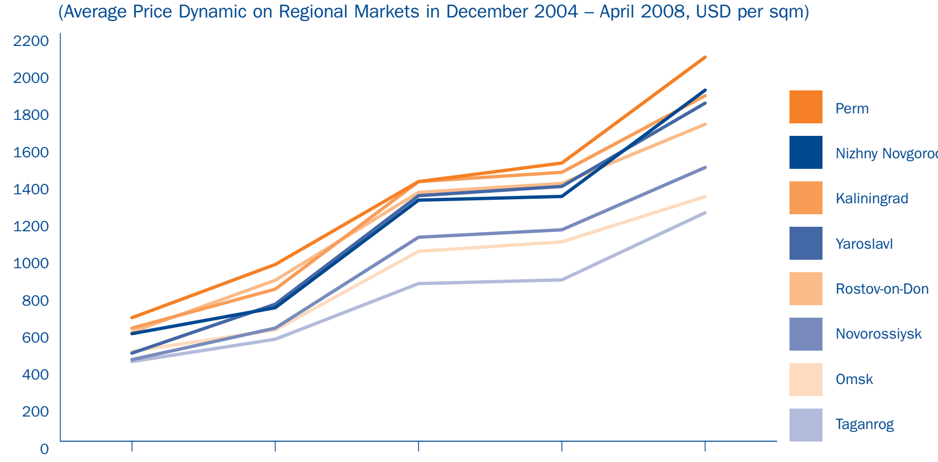
*Source: CBRE*

Residential price evolution in the regions
*(Average Dynamic on Regional Markets in December 2004 - April 2008, USD per square meters)*




*Source: CBRE*

Prices in Regions for the last years
(Average Price Dynamic on Regional Markets in December 2004 – April 2008, USD per sqm)

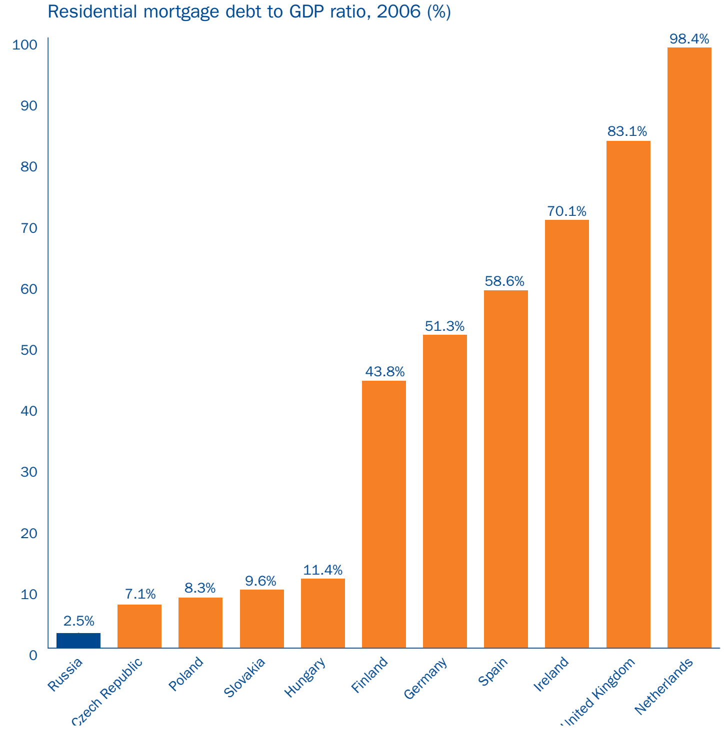



*Source: CBRE*

## Homes and mortgages for growing Russian middle-class

**As their wealth increases, Russian families have been looking to improve their living conditions.** Due to the strong economy, they are now more confident about their future and more likely to consider a mortgage. This represents a significant change in the national mindset. However, although mortgages are being widely offered to the consumer, mortgage penetration remains relatively low as compared to CEE countries, representing a significant growth opportunity for residential developers.

Residential mortgage debt to GDP ratio, 2006 (%)




*Source: European Mortgage Federation National Experts, Central Banks, National Statistics Offices, Eurostat*

Typically, mortgages in Russia will be offered with interest rates of between 10-12%, with loan to value (LTV) ratios of up to 70-80%. Typical loan tenures are between 20-30 years.

| | **Share of mortgage in total no. of residential transactions** | **Number of mortgage contracts** |
|---|---|---|
| Russia | 9% | 206,123 |
| Central region | 7% | 38,722 |
| North West | 6% | 15,151 |
| South | 5% | 12,330 |
| Volga | 9% | 54,240 |
| Urals | 12% | 35,237 |
| Siberia | 13% | 44,780 |
| Far East | 6% | 5,663 |

*Source: Rosregistratsia, AHML*

However, in real terms interest rates are still behind CEE levels, which are close to zero (or in some cases negative). They are also offset by wage inflation of approximately 20% per annum over the last four years. Recent government announcements have pointed towards a decrease of up to 7-8% in interest rates by the end of 2010, to be funded through an injection of liquidity into the mortgage system. As a result, going forward, increased mortgage penetration allied to decreasing interest rates should serve as a catalyst for growth.

When affordability reaches a certain level and the supply is not available real estate prices turn upwards. We believe that this is the basic dynamic that has been at work in Moscow and Moscow region, and which is now being felt further afield in Russia's regions. Demand is strong and prices have shown strength for a number of years. Currently PIK is the only listed company offering investors exposure to the strong economic fundamentals at play in this segment of the Russian property market.

# Strategy Overview

### Strategy

**The Board of Directors continually reviews the Group's strategy for generating shareholder value. Following our IPO, we have focused on PIK's long-term development in a climate of strong economic growth and rising demand for residential housing in Russia and the CIS. The principal elements of this strategy are summarized here.**

**Maintain our focus on the middle-income, residential real estate market nationwide in Russia and CIS.**

We will continue to capitalize on growth opportunities in the residential real estate market in Russia, particularly in middle-income, mass-market housing. The experience we have gained over 13 years in developing residential real estate projects in Russia places us in a strong position to take advantage of this growth, and expand the scale and reach of our residential real estate operations.

Our reputation as a high-quality developer, combined with our financial resources, gives us an advantage over many of our competitors. We intend to strengthen significantly our market position in the medium term.

**Ensure sustained growth in residential real estate development across Russia and CIS countries through entering new cities, deploying vertical integration in the regions, and providing the necessary land for future development.**

We became a nationwide developer in 2006 through the acquisition of a middle-sized Russian developer with a presence in around ten regional cities in Russia. Currently, we are represented in over 20 cities in the country. In 2008 we plan to enter another ten Russian cities. In April 2008, we announced our intention to enter the St. Petersburg market. During the remainder of the year, we plan to enter a number of other strategically important Russian cities.

Our goal over the next five to seven years is for PIK to be a holding company, owning approximately 20 geographically diversified regional development companies. Each of these will have a footprint in three to six different cities. This will give us a multiregional presence in over 60 cities in total, concentrated in several regions in western, central and southern Russia.

We believe that these regions will continue to provide strong growth in the residential real estate market. Moreover, we believe that the opportunity still exists in 2008 for the acquisition of land across the country at attractive prices. We will look for opportunities to enter into the major cities of Ukraine and Kazakhstan in addition to those in Russia.

To sustain our expansion in the regions, we are rolling out our successful integrated business model; supporting development activity with pre-cast facilities. During 2007 we acquired existing industrial pre-fabricated housing production sites and implemented new, more flexible pre-cast technology. Currently, we are in the process of modernizing four sites, which will add approximately 780,000 square meters of housing to our existing capacity during 2008 and 2009.

**Unlock additional shareholder value by entering other profitable segments of the Russian real estate market, such as the commercial market.**

In 2007, we acquired a majority stake in Storm Properties, a dynamic and growing Russian commercial developer. Storm will be responsible for the development of PIK's existing and future commercial project portfolio. In terms of commercial projects, we intend to consider sectors such as Class A office complexes and hotels.

We have a number of such projects in the portfolio, situated in prime locations, at early stages of development. As of January 1 2008, these included our prominent Park City development (PIK share in this project is 25% as of January 1 2008), situated on the bank of the Moscow river, and through Storm Properties, the North West Towers development to the west of Moscow, by the Moscow orbital ring road (MKAD). This project links up with the planned buildings of the Moscow Region Government and a well-known deluxe shopping centre.

In addition to stand-alone commercial projects, we are exploring ways of maximizing value from our existing neighborhood developments via additional commercial components such as shopping centres, where it is economically desirable. We will consider retaining commercial premises, including the first floors from our existing developments, with the intention of leasing them to provide cash flows to the business, independent of the residential segment of the market.

**Accelerate regional growth by attracting co-investors on project levels.**

We intend accelerating growth by attracting co-investors into neighborhood developments. This will help provide necessary funding for new projects and to seize the higher value at early stages of development, and reduce our risk exposure to large, individual projects.

In December 2007, we closed the first significant deal of this kind with GIC Real Estate, the real estate investment arm of the Government of Singapore. Under the partnership agreement, an affiliate of GIC Real Estate acquired a 25% stake in the Mytischi project and will share the associated project risks with us. We will look for similar partnerships with other investors, where the economics are attractive. We have earmarked some projects, where we believe the GIC deal structure can be replicated.

**Continue our successful record of acquiring and integrating businesses that strengthen our position in the Russian real estate market.**

We began our diversification into industrial activities in 2001 with the acquisition of DSK-2, a concrete panel manufacturer in Moscow. In 2005, we acquired DSK-3, a second concrete panel manufacturer in Moscow, and 100 KGI, a pre-fabricated concrete panel plant located in the Moscow region.

These acquisitions give us the ability to provide our own materials for construction on a significantly larger scale, and allow us to become a major player in the residential real estate market in Moscow. With the acquisition of DSK-3, we own two out of the three concrete panel manufacturers in Moscow. Together, DSK-2 and DSK-3 are capable of producing approximately 950,000 square meters of housing per year. Our other facilities (160 DSK, 480 KZHI, 100 KZHI) have approximately 370,000 square meter capacity per year. During 2007 we have added a number of facilities in the regions, which we are currently modernizing.

We plan to evaluate opportunities to acquire additional production and construction facilities and developers with existing land banks or production capacities in order to strengthen our vertically integrated development model further.

**Improve cost efficiencies at our integrated operations, with focus on product modernization and the improvements in the construction process.**

We intend to improve cost efficiencies at our integrated operations by optimizing the business processes at each level of the vertical chain. Maintaining our own production and construction activities is essential. It ensures we can reduce construction costs through the control and improvement of our planning and construction techniques, our purchasing processes and economies of scale.

# Summary Consolidated Financial and Operating Information

**Summary of consolidated financial and operating information.**

**The summary set forth below shows the Company's historical consolidated financial information and other operating information as of, and for, the years ended December 31 2004, 2005, 2006 and 2007.**

The financial information for the years ending December 31 2004, 2005, 2006 and 2007, under the captions 'Consolidated Income Statement Data', 'Consolidated Balance Sheet Data', and 'Consolidated Statement of Cash Flows Data' has been derived from, and should be read in conjunction with the audited financial statements included elsewhere in this Report.

The Group's Consolidated Financial Statements have been audited by KPMG. For presentation purposes, however, certain financial information from the consolidated financial statements presented in Russian roubles have been converted into US$ at the average RR/US$ exchange rates of the Central Bank of Russian Federation (FY07: 25.55; FY06: 27.19) for the income statements items and at the closing balance sheet RR/US$ exchange rates (December 31 2007: 24.55; December 31 2006: 26.33) for the balance sheet items. The above US$ equivalent figures are provided for information purposes only and do not form part of the audited consolidated financial statements of the Group.

The information presented below under the caption 'Selected Operating Data' is not derived from the audited financial statements. EBITDA and EBITDA margin are non-IFRS measures and were calculated based on data derived from the audited financial statements.

The summary of consolidated financial and operating information should be read in conjunction with 'Management's Discussion and Analysis of Financial Condition and Results of Operations.' See also 'Presentation of Financial and Other Information' for important guidance about the financial information presented herein.

**Consolidated Income Statement Data**

**Years ended December 31**

| | 2004 | 2005 | 2006 | 2007 | 2006 | 2007 |
|---|---|---|---|---|---|---|
| | *(in RUR million)* | | | | *(in USD million)* | |
| Revenues | 12,695 | 22,139 | 42,046 | 69,050 | 1,546 | 2,703 |
| Cost of sales | (11,514) | (19,519) | (32,265) | (51,206) | (1,187) | (2,004) |
| Gross profit | 1,181 | 2,620 | 9,780 | 17,844 | 360 | 698 |
| Gain on disposals of development rights | – | – | 2,851 | 9,502 | 105 | 372 |
| Distribution expenses | (272) | (322) | (467) | (879) | (17) | (34) |
| Administrative expenses | (420) | (531) | (1,511) | (3,114) | (56) | (122) |
| Other income and expenses | 358 | – | 1,552 | (55) | 57 | (2) |
| Financial income | 413 | 148 | 571 | 569 | 21 | 22 |
| Financial expenses | (555) | (736) | (1,362) | (2,363) | (50) | (92) |
| Share of loss of equity accounted investees (net of income tax) | (7) | (8) | (10) | (24) | (0,4) | (1) |
| Profit before income tax | 697 | 1,172 | 11,405 | 21,480 | 419 | 841 |
| Income tax expense | (193) | (607) | (3,305) | (3,595) | (122) | (141) |
| Net profit for the year | 504 | 564 | 8,100 | 17,885 | 298 | 700 |
| Attributable to: | | | | | 0 | 0 |
| Shareholders of the Company | 509 | 556 | 8,105 | 17,854 | 298 | 699 |
| Minority interest | (5) | 8 | (5) | 31 | (0,2) | 1 |
| | 504 | 564 | 8,100 | 17,885 | 298 | 700 |

**Consolidated Statement of Cash Flows Data**
**As of December 31**

| | 2004 | 2005 | 2006 | 2007 | 2006 | 2007 |
|---|---|---|---|---|---|---|
| | *(in RUR million)* | | | | *(in USD million)* | |
| Cash and cash equivalents | 566 | 701 | 1,134 | 17,056 | 43 | 695 |
| Total assets | 20,189 | 44,268 | 65,654 | 126,753 | 2,494 | 5,163 |
| Loans and borrowings, non-current | 3,300 | 9,200 | 10,040 | 10,460 | 381 | 426 |
| Loans and borrowings, current | 3,994 | 9,066 | 13,983 | 24,180 | 531 | 985 |
| Total equity | 979 | 1,877 | 9,931 | 50,339 | 377 | 2,050 |

**Consolidated Statement of Cash Flows Data**
**Years ended December 31**

| | 2004 | 2005 | 2006 | 2007 | 2006 | 2007 |
|---|---|---|---|---|---|---|
| | *(in RUR million)* | | | | *(in USD million)* | |
| Cash flows from/(utilized by) operating activities | 244 | (4,745) | 3,544 | (2,973) | 135 | (121) |
| Cash flows utilized by investing activities | (1,129) | (4,281) | (8,190) | (13,197) | (311) | (538) |
| Cash flows from financing activities | 930 | 9,010 | 5,084 | 32,586 | 193 | 1,327 |

**Years ended December 31**

| | 2004 | 2005 | 2006 | 2007 | 2006 | 2007 |
|---|---|---|---|---|---|---|
| | *(in RUR million, except percentages)* | | | | *(in USD million, except percentages)* | |
| **Non-IFRS Measures** | | | | | | |
| EBITDA (1) | 1,410 | 1,987 | 13,217 | 23,949 | 486 | 937 |
| EBITDA margin (2) | 11% | 9% | 31% | 35% | 31% | 35% |

Reconciliation of EBITDA to net profit for the year attributable to shareholders of the Company is as follows for the periods indicated:

**EBITDA calculation**
**Years ended December 31**

| | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|
| | *(in RUR million)* | | | |
| Net profit for the year attributable to the Shareholders of the Company | 509 | 556 | 8,105 | 17,854 |
| Depreciation and amortization | 299 | 411 | 676 | 777 |
| Interest expense | 555 | 554 | 1,361 | 2,063 |
| Interest income | (146) | (141) | (230) | (340) |
| Income tax expense | 193 | 607 | 3,305 | 3,595 |
| EBITDA | 1,410 | 1,987 | 13,217 | 23,949 |

(1) EBITDA represents net profit for the year attributable to shareholders of the Company before income tax expense, interest income, interest expense and depreciation and amortization. EBITDA is not a measure of financial performance under IFRS. You should not consider it an alternative to net profit for the year as a measure of operating performance or to cash flows from operating activities as a measure of liquidity. Our calculation of EBITDA may be different from the calculation used by other companies and therefore comparability may be limited. We believe that EBITDA provides useful information to investors because it is an indicator of the strength and performance of our ongoing business operations, including our ability to fund discretionary spending such as capital expenditures, acquisitions of subsidiaries and other investments and our ability to incur and service debt. While depreciation and amortization are considered operating costs under IFRS, these expenses primarily represent non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods.

(2) Margins are calculated as a percentage of revenues.

**Years ended December 31**

| | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|
| **Selected Operating Data** | | | | |
| Total square meters completed (thousands) (1), including: | 497 | 827 | 1,244 | 1,542 |
| Total number of residential units completed (1) | 6,608 | 12,238 | 17,314 | 23,239 |

(1) Includes housing constructed for the Moscow city government by our Construction Services segment.


'Krylatskie Ogni' development, Moscow

# Chief Executive Officer's Statement

**"PIK is a strategically positioned residential developer that can execute large scale projects right across the country and provide Russia's rising housing they need."**

**Pisarev K.V.**
*Chief Executive Officer* PIK Group

# Chief Executive Officer's Statement

Dear Shareholders,

**In addition to the major corporate events described in the Chairman's statement, 2007 marked a year of significant achievement in terms of PIK's operational and financial performance.**

During the year we completed over 23,000 apartments up from 17,000 in 2006, volume growth that has driven a record financial performance.

Sales for the year ending December 31 2007 increased 75% up to $2.7 billion. Net profit rose by 135% to $700 million, compared to $298 million in the same period for 2006.

Earnings per share for the year ended December 31 2007 increased to $1.46 compared to $0.65 in the previous year.

The Company's cash balance at December 31 2007 was $695 million (December 31 2006: $43.0 million).

Total asset value rose to $5.2 billion (December 31 2006: $2.5 billion).

General economic and residential real estate market conditions in Russia remain positive and provide strong fundamentals for our business. Russia has been relatively insulated from the effects of the financial crisis that has affected other parts of the world, due to its continuing growth in GDP, consumers' real disposable income, and increasing mortgage penetration. We believe these fundamentals will continue to drive our business forward in the years ahead.

PIK is well-positioned as a residential developer to execute large-scale projects across the country. We can provide Russia's rising middle classes with the new housing they want. PIK has a strong track record and a clearly defined strategy for completing current developments, and in identifying new opportunities for growth. We look forward confidently in delivering another positive set results for the current financial year.

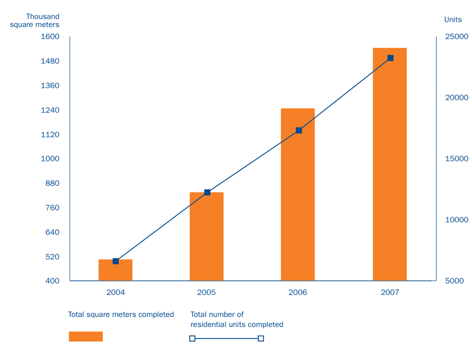
I would like to thank all our employees and everyone on the Management Board for their energy and commitment in 2007. Despite the IPO we all kept our focus on driving value through the business. I am confident that we are well-placed to sustain our success going forward.

Yours sincerely,

**Pisarev K.V.**
*Chief Executive Officer*
PIK Group

# Organisational Change

Annual Housing Completions




## Organisational structure

**The Group completed 2007 with the organisational structure that served it well during a period of rapid growth. Following the year end, we began the process of implementing a new structure designed to maximize the benefits of PIK's vertically integrated model for the next phase of its growth.**

The key management priority for the year ahead will be to maintain PIK's growth profile, while at the same time, minimizing the execution risk attached to operational expansion.

Under our previous structure, the holding company, OJSC PIK Group, supervised all aspects of group operations centrally. Two subsidiary companies CJSC PIK and CJSC PIK Region, were responsible to oversee real estate development in Moscow and the regions respectively.

The main change to the Group's structure will see PIK Region divide into new regional development companies to oversee development projects locally. These companies will be responsible for preparing financial models for potential new projects and their execution once they have been approved. By 2015, management expects the Group to have approximately 20 regional development companies in place, with a presence in 4-6 regional cities.

In Moscow, CJSC PIK has been renamed OJSC PIK and will continue to be responsible for developments in the capital, including Moscow region.

Approval and financing for all new development projects will come from the holding company, which will now focus on the analysis of financial models, the completion of legal due diligence and the implementation of high project management standards at the local level. Two separate new companies, OJSC PIK ExpertService and OJSC PIK Realty have been created to provide accountancy and sales and marketing support across the Group.

Our management team has achieved great success, growing PIK from a start-up, expanding out from the Group's central Moscow heartland, and taking it into Russia's regions. The new Group structure will maintain this success as we enter new territories in Russia and the CIS.

The new structure is illustrated by the organization map below.

## PIK GROUP

**Investment & Development**

- **PIK** Moskva
- **PIK Podmoskovye**
- **PIK Severo-Zapad** St Petersburg
- **PIK Baltika** Kalningrad
- **PIK Verkhnaya Volga** Yaroslavl
- **PIK Povolzhye** Nizhnly Novgorod
- **PIK Don** Rostov-on-Don
- **PIK Kuban** Krasnodar
- **PIK Kama** Perm
- **PIK Zapadnaya Sibir** Omsk
- **PIK Ukraina** Kiev
- **Storm Properties**
- **PIK Razvitiye territory**

**Architectural-Design Institutes**

- **Evroproekt**
- **Novorosgrazhdanproekt**
- **PIK Proekt**
- **SIR Proekt**

**Raw Materials**

- **PIK Nerud**
  - **SPTK** Sychevo, Moscow region
  - **Khromtsov Karier** Ivanovo region
  - **SPTK** Sortavala Rep. of Karella

**Realtors activity**

- **PIK Realty**

**Buildings Maintenance**

- **PIK Comfort**

**Press Office, Advertising & PR**

- **PIK Design**

**Production & Construction Enterprises**

- **DSK-2** Moscow
- **DSK-3** Moscow
- **100 KZHI** Sergiev Posad Moscow region
- **480 KZHI** Aleksin Tula Region
- **NSS** Obninsk
- **Stroyinvest** Kaluga
- **Volga Form** Nizhnly Novgorod
- **Stroyformat** Novocherkassk
- **Podmokovye 160 DSK** Korolev Moscow region
- **MFS-PIK** Moscow
- **PIK Development** Moscow
- **Torgoviy Dom Osnova** Moscow
- **PIK Profile** Moscow
- **PIK Technology** Moscow
- **PIK Autotrans** Moscow
- **PIK Podyom** Moscow

# Portfolio of Properties Overview

### Portfolio of properties overview

**Our total land bank, as of January 1 2008, amounted to 14.2 million square meters of unsold saleable area, an equivalent 800 properties. Valuation was conducted by CB Richard Ellis, the internationally recognized and independent real estate consultants and the market value totaled $12.3 billion.**

The portfolio of properties, as of January 1 2007, was 8.8 million square meters of unsold saleable area, equivalent to 413 properties and valued at $8.8 billion. As of January 1 2008, the share of properties in the course of development reached 40% (2006: 34%), while in absolute terms the total number of square meters amounted to 15.1 million (2006: 10.5 million).

During 2007, PIK made significant additions to its land bank, partially financed by the IPO proceeds. Over 6 million square meters were added, of which approximately 85% were situated outside Moscow. These additions were part of management's strategic initiative to grow the business in Russia's regions.

A summary of key projects within the property portfolio is provided below:

| Selected Key Projects | Location | Number of properties | Net Selling th. sq m | PIK Share th. sq m | Unsold Area th. sq m | Parking Space | Unsold Space | Market value USD |
|---|---|---|---|---|---|---|---|---|
| Kuntsevo | Moscow | 8 | 173 | 170 | 167 | 1,868 | 1,868 | 489 |
| Yaroslavsky, Mytischi | Moscow region | 90 | 908 | 881 | 881 | 11,654 | 11,654 | 998 |
| Novokurkino, Khimki | Moscow region | 38 | 916 | 890 | 742 | 5,074 | 4,853 | 1,196 |
| Park City | Moscow | n/a | 122 | 122 | 122 | 1,204 | 1,204 | 977 |
| English Neighbourhood | Moscow | n/a | 70 | 70 | 63 | 570 | 570 | 693 |
| Centralny, Dolgoprudny | Moscow region | 21 | 284 | 270 | 270 | 500 | 500 | 209 |
| Sovhoznaya, Khimki | Moscow region | 28 | 399 | 301 | 301 | 4,960 | 4,960 | 361 |
| Kommunarka, Leninsky region | Moscow region | n/a | 1,055 | 1,023 | 1,023 | n/a | n/a | 745 |

*Note: The project portfolio described herein should be read in connection with CBRE valuation report as of January 1 2008.*

For detail on key projects review refer to page 27.

# Initial Public Offering Summary

**PIK Group's share offer was the largest ever non-REIT real estate IPO, the largest European real estate IPO ever and the 3rd largest Russian IPO.**

## Initial public offering summary

**On June 1 2007, PIK Group listed on the London and Russian (Micex, RTS) stock exchanges. PIK Group's share offer was the largest ever non-REIT real estate IPO, the largest European real estate IPO ever and the 3rd largest Russian IPO.**

PIK's management undertook a global roadshow over two weeks, visiting potential investors in Hong Kong, Singapore, the major European capitals, and the United States. They met with over 200 investors during the global coordination of the IPO.

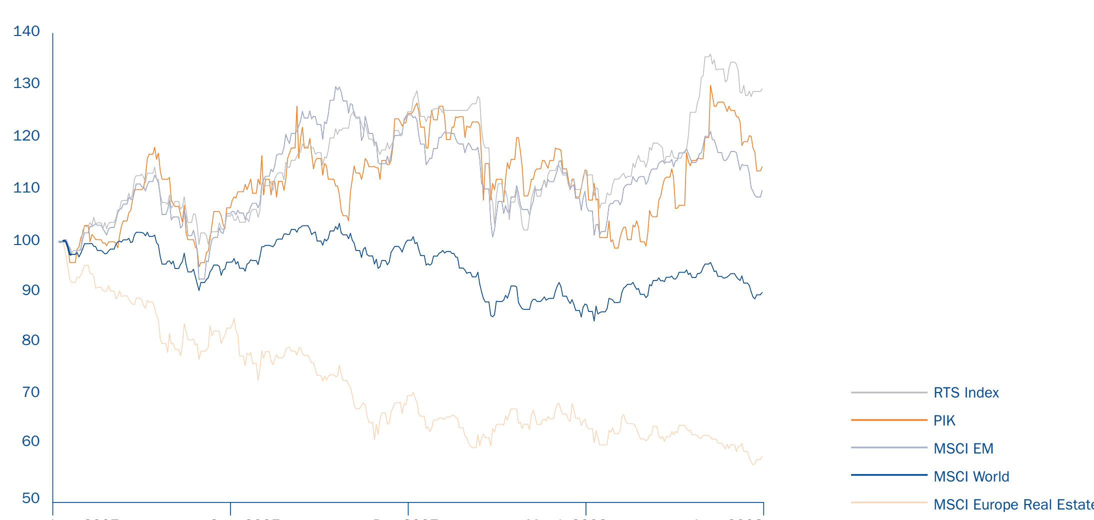
The record placement succeeded despite challenging market conditions. By the time of the listing the benchmark RTS index was down more than 7% on the year, and during the period global indexes such as MSCI were also in the red. Despite these difficulties, the Offering was well over-subscribed. As a result, the Group obtained a strong pool of high quality investors from Asia, Europe and the US. The funds raised have been used to improve the Group's capital structure and further its acquisition strategy. The IPO valued the company at $12.3 billion.

Before the IPO the Group was owned on a parity basis by Kirill Pisarev, the company's CEO, and Yury Zhukov, its Chairman. Following the offering and the exercise of the over-allotment (Green Shoe) option, each retained a stake of approximately 42%.

The details of PIK Group's IPO were:

| | |
|---|---|
| Date: | June 1 2007 |
| Offer Size | $1.93 billion (post Green Shoe) |
| Free Float: | Approximately 16% (post Green Shoe) |
| Offer Price: | $25 |
| GDR Ratio: | 1:1 |
| Share Type: | 50% primary / 50% secondary |
| Implied Market Capitalization | $12.3 billion |
| Offer Structure | Reg S and Rule 144A |
| Joint Global Coordinators | Deutsche Bank, Morgan Stanley, Nomura International |

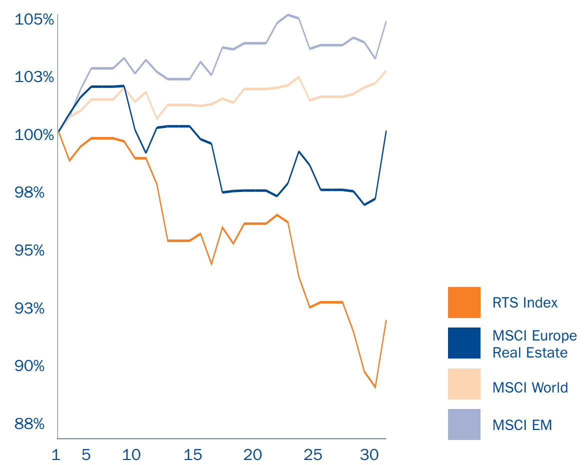
PIK post IPO stock performance




*Source: Bloomberg, LSE closing price*
*Note: Represents period from IPO date to June 1 2008 (1 year stock performance)*

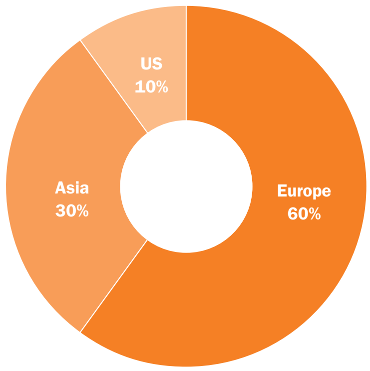
# Dividend Policy

Challenging market conditions in May 2007

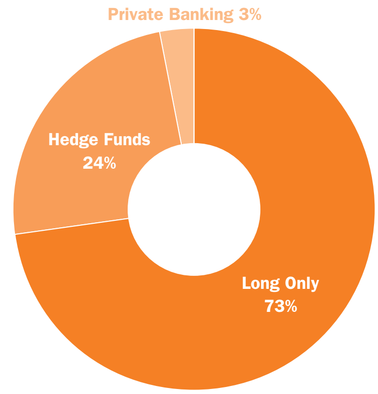



*Source: Bloomberg*

Breakdown of demand by region




Breakdown of demand by type of investor




*Source: Company Data*

## Dividend policy

As a Russian holding company, our ability to pay dividends depends upon receipt of dividends and distributions from our subsidiaries, and our ability to make dividend payments under Russian law. The payment of dividends by our subsidiaries is contingent upon the sufficiency of their earnings, cash flows and distributable reserves and their ability to make dividend payments to us in accordance with relevant legislation, Russian company law and foreign exchange controls.

Under Russian accounting standards ('RAS'), PIK Group's financial results are prepared on a stand alone basis, using a different method to IFRS accounting principles.

Our current dividend policy, adopted by our Board of Directors on May 29 2006, provides that the size of the dividend and the relevant part of net profit, from which the dividends are paid, are determined in accordance with the recommendations of our Board of Directors. Such recommendations are prepared on the basis of the amount of net profits determined according to Russian accounting standards, adjusted in accordance with the expected results to be determined under IFRS, and our investment needs.

At the AGM held on June 25 2008 the shareholders approved non-dividend payment for 2007 financial year as per the recommendation of the Board of Directors.

We currently expect to pay dividends in rubles. To the extent that we declare and pay dividends, owners of our Ordinary Shares and Global Depository Receipts (GDR) on the relevant respective record dates will be entitled to receive dividends payable in respect of our Ordinary Shares or, as the case may be, our Ordinary Shares underlying the GDRs, subject to the terms of the Deposit Agreements.

The Depositary, as our shareholder, will receive rubles and convert the rubles into US dollars for distribution to GDR holders. Accordingly, the value of dividends received by GDR holders will be subject to fluctuations in the exchange rate between the ruble and the US dollar. Under the Deposit Agreements, the Depositary may also deduct a fee of up to $0.02 per GDR and other fees and expenses with respect to distributions of dividends to GDR holders. In addition, our dividend payments to the Depositary will be subject to applicable Russian withholding taxes.

# Development and Real Estate Operations/ Key Projects

**Key Project Review**

**'Yaroslavsky' development, Mytischi (Moscow Region)**

Mytischi is located to the North-East of Moscow Region, 5 km from Moscow city border.

The project represents an urban neighborhood development. It comprises 90 properties, predominantly residential, with some commercial properties and stand alone parking. It is located in a desirable residential area and development plans include infrastructure such as kindergartens, schools, nurseries, and athletics fields.

In general, the location of each individual project meets the requirements of its intended potential users. There are 32 underground multi-level garages planned with a total of 12,014 (PIK Share) parking spaces, including city share.

Net sellable space (PIK Share): 881,000 sq m

Parking spaces: 11,654 spaces

Value: $998 million

Another 25% stake in this project is owned by GIC Real Estate, the real estate investment arm of the Government of Singapore.

**'Novokurkino' development, Khimki (Moscow Region)**

Khimki lies at the intersection of three important Russian transport corridors, namely the Moscow-St. Petersburg highway, the Oktyabsrkaya Railroad, and the Moscow River. Russia's largest airport, Sheremetyevo 2, is also in the Khimki region and not far from the site. Access to the site is convenient for both public and private transport.

The project is PIK's first large-scale residential neighborhood development in Moscow Region. We plan to develop three adjacent micro-districts, (micro-districts six, seven and eight) consisting of a total of 23 multi-apartment residential buildings. Three retail centers will be located close to the micro-districts selling all the necessary goods for fitting out an apartment. The centers will also contain a variety of shops, cafes and restaurants.

Net sellable space (PIK Share): 890,000 sq m

Parking spaces: 5,074 spaces

Value: $1,196 million

*'Yaroslavsky' development, Mytischi (Moscow Region)*

1.

2.

3.

4.

*1 - 4: 'Novokurkino' development, Khimki (Moscow region)*

1.

2.

3.

*1 - 3: 'Centralny' development, Dolgoprudny (Moscow region)*

# Key Projects

**‘Centralny’ development, Dolgoprudny (Moscow Region)**

Dolgoprudny is a small town located in the Moscow region, approximately five kilometers from the MKAD, to the north of Moscow. We intend to develop a micro-district of 21 buildings, with an approximate net selling area (PIK share) of 270,000 square meters. The Centralny real estate development is expected to be completed in 2012 and will consist of P3M, P3M-17/23, KOPE-M Parus and poured-concrete buildings, and townhouses.

In the courtyard of this micro-district we plan to construct several children's pre-school establishments, comprehensive schools, pharmacies and guest parking spaces. For the convenience of inhabitants, the project will include shops, cafes, a communication center, and an arts center.

Net sellable space (PIK Share): 270,000 sq m

Parking spaces: 500 spaces

Value: $209 million

**‘Sovhoznaya’ development, Khimki (Moscow Region)**

Our second development in Khimki is Sovkhoznaya, a project consisting of 14 multi-apartment residential buildings, 8 garages and six shopping & recreation centres. The net selling area will be approximately 301,000 square meters (PIK share). As of January 1 2008, we had 22 buildings under development and 6 buildings held for development. The Sovkhoznaya 11 project is expected to completed in 2012, and will consist of P3M, P3M-17/23, KOPE-M Parus, 111M – all our range of pre-fabricated panel series of house and poured-concrete buildings.

Net sellable space (PIK Share): 301,000 sq m

Parking spaces: 4,960 spaces

Value: $361 million

*‘Centralny’ development, Dolgoprudny, (Moscow Region)*

*'Sovhoznaya' development, Khimki, (Moscow Region)*

**'Kommunarka' development,**
**Leninsky area (Moscow region)**

The Kommunarka real estate development is located to the southwest of Moscow, 2 kilometers from the ring motorways (MKAD) along Kashirskoye Highway. Access to the site is convenient for both public and private transport. The development will consist of poured-concrete residential buildings and cottages covering a total area of 127 hectares. Net selling area is approximately 1,023,000 square meters (PIK share). This project is expected to complete in 2015.

Net sellable space (PIK Share): 1,023,000 sq m

Value: $745 million

# Key Projects

*'Park City' development, Moscow*

**'Park City' development, Moscow**

Park City is located between the Garden Ring Road and the Third Ring Road on one of Moscow's main streets, and one of its most prestigious retail corridors, Kutuzovsky Prospekt. The project is a mixed-use poured-concrete development of Class 'A' office space and luxury apartments over 14.3 hectares. Park City is a new city quarter, masterplanned to combine world-class architecture, progressive landscaping and a particular sensitivity to heritage buildings.

Net sellable space (PIK Share): 122,000 sq m

Parking spaces: 1,204 spaces

Value: $977 million

# Key Projects

**‘English Town’ development, Moscow**

The English Town residential development is located at Mytnaya street 13, south-central Moscow, between the Garden Ring Road and the Third Ring Road. Highly popular with home-buyers, the area contains over 20 embassies. We intend to develop a single, luxury, poured-concrete residential building with a net selling area (PIK share) of 70,000 square meters. Completion is planned for 2011.

Net sellable space (PIK share): 70,000 sq m

Parking spaces: 570 spaces

Value: $693 million

**‘Kuntsevo’ development, Moscow**

In Kuntsevo we have three projects under development: Akademika Pavlova Street, Yarcevstkaya Street and Rublevskoe Shosse.

Rublvskie ogni, an apartment complex 30, 33 and 40 floors high, stands on highway Rublevsk, in the prestigious area of Kuntsevo, the border of Rublevsky park and Serebrianiy bor forest. The complex has underground parking and panoramic views of Moscow, the adjoining large forests and open water.

Net sellable space (PIK Share): 170,000 sq m

Parking spaces: 1,868 spaces

Value: $489 million

*‘English Town’ development, Moscow*

PIK Group Operations


*Source: Company Data as of June 2008*

### Other development projects

1. 'Krylatskie Ogni' development, Moscow
2. 'Okskaya' development, Moscow
3. 'Yubileyny' development Khimki, (Moscow Region)
4. 'Krasnaya Gorka' development, Lubertsy (Moscow Region)

*5. 'Presnya House' development, Moscow*
*6. 'New Peredelkino' development, Moscow*
*7. 'Nagatinskaya Embankment' development, Moscow*
*8. 'New Peredelkino' development, Moscow*

# Key Projects / Production and Construction

**Our production capacity of concrete panels is among the largest in Moscow and Moscow region.**

### Significant land bank acquisitions since January 1 2008:

#### 'Marine Façade' development, Saint Petersburg

The Group intends a flagship development in St. Petersburg, aimed at higher-end segments of the real estate market. Located in an exclusive area.

The project comprises a total site area of approximately 400 hectares, reclaimed from the sea, of which approximately 200 hectares are proposed for office, retail and residential development. The total acquisition is 63.4 hectares and PIK plans to develop 1.3 million square meters of which 1.1 million square meters of business–class housing.

### Other acquisitions

In addition to the 'Marine Façade' real estate development, PIK has acquired significant land plots in Yaroslavl approximately 0.9 million square meters, Izhevsk approximately 1.5 milliion square meters. Additionally, together with Storm Properties PIK has added a commercial project, 'Pulkovo', in Saint Petersburg with total gross area of 80,000 square meters.

### Production and construction

Two concrete panel manufacturers in Moscow, DSK-2 and DSK-3 are now owned by PIK, as well as 100 KGI, a concrete panel manufacturer located in the Moscow region. During 2007 we have acquired an additional five facilities, one in Tula Region, two in Kaluga Region, one in Rostov Region and one in Nizhny Novgorod Region.

Our major production assets are:

**DSK-2**, founded in 1962, was acquired by PIK in 2001, is the third largest residential construction company in Moscow. DSK-2 production capacity is approximately 450,000 square meters of housing per annum. The company produced the KOPE, KOPE-Tower and KOPE-Parus series of prefabricated housing. KOPE-Tower is a new modernized type of housing, the first building of which was completed in 2008 at the 'Yubileyny' development, Khimki (Moscow Region)

DSK-2's construction processes are of a high standard and meet international standard ISO 9001-2001. As of December 31 2007, DSK-2 had over 3,100 employees.

**DSK-3** was founded in 1964 and acquired by PIK in 2005. DSK-3 is the second largest residential construction company in Moscow and has the capacity to produce approximately 500,000 square meters of housing per year. The company produced the P3M series of prefabricated housing. As of December 31 2007, DSK-3 had over 3,400 employees.

**100 KZHI** was founded in 1965 and acquired by PIK in 2005. 100 KZHI has the capacity to produce approximately 150,000 square meters of housing per year and produced 111-M series of prefabricated housing. As of December 31 2007, 100 KZHI had over 700 employees.

**480 KZHI** was founded in 1945 and acquired by us in 2007. 480 KZHI has capacity to produce approximately 165,000 square meters of housing per year and produced 111-M series of prefabricated housing. As of December 31 2007, 480 KZHI had over 1,000 employees.

All the panels used for our pre-fabricated concrete panel developments in Moscow and the Moscow region are manufactured by DSK-2, DSK-3 and 100 KZHI. The companies also produce a limited number of concrete panels for areas outside of Moscow and Moscow region. High transport costs generally mean however that outside the Moscow region we source concrete panels locally.

The window frames for all our concrete panel housing are manufactured by PIK Profile, based at the DSK-2 plant. Our subsidiary PIK Technology provides the aluminum facades for our buildings. The elevators for most of our developments in Moscow and the Moscow region are supplied and assembled by PIK Podyom. Our subsidiary 160 DSK manufactures and assembles individual wood-framed houses at small sites in Moscow and the Moscow region.

# Raw Materials / Others

**Our ability to provide gravel, sand and crushed rock to our cement suppliers allows us more favorable and longer-term contracts for cement used in our operations, and gives us a significant competitive advantage.**

### Construction services

**In addition to our core development activity, we also provide a construction service, mainly to the City of Moscow, in the production, delivery and assembly of 'core and shell', and the fit-out of pre-fabricated housing. We also install windows, facades and electrical wiring for the buildings.**

Co-operation with the City of Moscow on social housing construction enables us to support our development activity, and helps maintain a positive relationship with city government. However, the relative proportion of buildings that we construct for the City of Moscow government is gradually declining, as we focus our efforts on expanding development activities in other regions in Russia.

Besides construction services, as part of the development process of new neighborhoods we also develop social infrastructure, such as schools and kindergartens. When these assets are finished, they are in general passed on to the local municipalities. In 2007, we finished two schools and one kindergarten.

### Raw materials

**Our raw materials division is operated through our wholly owned subsidiary Trading House Osnova, created to provide materials and services for our real estate development activity.**

These operations allow us to extract gravel, sand and crushed rock from quarries for the production of construction materials. Our gravel and non-ferrous quarry operator is PIK Nerud, which has activities in the Moscow region, Ivanovo region and Republic of Karelia.

Approximately 30% of the raw materials we produce are used by DSK-2, DSK-3 and our other manufacturing and construction facilities. The majority of our raw materials is sold on to third parties, including to other developers. We believe that our ability to provide gravel, sand and crushed rock to our cement suppliers allows us to negotiate more favorable and longer-term contracts for cement used in our operations, which we believe gives us a significant advantage over our competitors.

### Other activities

### Real Estate servicing and maintenance

**Through our wholly owned subsidiary PIK Comfort LLC, we provide servicing and maintenance in Russia for residential buildings and developments and some non-residential premises such as shopping centres, underground garages and parking lots.**

These services are for our own properties and properties developed by third parties. Although currently we do not provide service and maintenance to all the properties that we develop, it is our goal for every residential property we complete.

In 2007, the total area of properties serviced by PIK Comfort grew by 70% compared to 2006. As of December 31 2007, we serviced approximately 1,545,000 square meters of residential and commercial properties. Most of these are located in Moscow (1,004,000 square meters) and the Moscow region (399,000 square meters), but also include properties located in other regions (142,000 square meters).

*Children's recreation area*

'Yubileyny' development, Khimki (Moscow Region)

# Chief Financial Officer's Review

**"For the year ended December 31 2007, we have achieved revenues of RUR 69.1 billion and net profit of RUR 17.9 billion."**

**Luneev E.D.**
*Chief Financial Officer PIK Group*

# Chief Financial Officer's Review

## Introduction

*The following discussion of our financial condition and results of operations should be read in conjunction with our financial statements, and the relevant notes. This section contains statements that involve predicting risk and uncertainty. Actual results may differ materially from those discussed.*

*The Group's Consolidated Financial Statements have been audited by KPMG. For presentation purposes, however, certain financial information from the consolidated financial statements presented in Russian roubles have been converted into US$ at the average RR/US$ exchange rates of the Central Bank of Russian Federation (FY07: 25.55; FY06: 27.19) for the income statements items and at the closing balance sheet RR/US$ exchange rates (December 31 2007: 24.55; December 31 2006: 26.33) for the balance sheet items. The above US$ equivalent figures are provided for information purposes only and do not form part of the audited consolidated financial statements of the Group.*

## Management discussion and analysis of financial conditions and results of operations

### General review

**We are one of the leading residential developers in Russia, with a concentration in Moscow and the Moscow region and an increasing presence in many of Russia's other regions.**

For the year ended December 31 2007, we had revenues and net profit of RUR 69.1 billion and RUR 17.9 billion, respectively. The Sales of Real Estate Property segment is the largest part of our business, accounting for 73.0% of our revenues for the year ended December 31 2007. The following table sets our revenues and net profit for the year by segment.

Our revenues are derived principally from the following activities: (1) sales of real estate property; (2) construction services; and (3) sales of construction materials and other activities.

**Years ended December 31**

| Revenues | 2006 | % of revenues | 2007 | % of revenues |
|---|---|---|---|---|
| Sales of Real Estate Property | 30,305 | 72.1 | 50,421 | 73.0 |
| Construction Services | 15,587 | 37.1 | 18,934 | 27.4 |
| Sales of Construction Materials and Other Activities | 3,014 | 7.2 | 5,521 | 8.0 |
| Eliminations | (6,860) | (16.4) | (5,826) | (8.4) |
| **Total** | **42,046** | **100.0** | **69,050** | **100.0** |

*(in RUR million, except percentages)*

**Years ended December 31**

| Net Profit [1] | 2006 | % of net profit for the year | 2007 | % of net profit for the year |
|---|---|---|---|---|
| Sales of Real Estate Property | 8,322 | 102.7 | 17,489 | 97.8 |
| Construction Services | 343 | 4.2 | 65 | 0.4 |
| Sales of Construction Materials and Other Activities | 223 | 2.8 | 365 | 2.0 |
| Eliminations | (789) | (9.7) | (34) | (0.2) |
| **Total** | **8,100** | **100.0** | **17,885** | **100.0** |

*(in RUR million, except percentages)*

(1) Net profit for the segments was determined based on the gross profit for each segment.

Earnings before interest income, interest expense, income taxes, depreciation and amortization (EBITDA) represents the Group's net profit for the year. EBITDA is not a measure of financial performance under IFRS. This should not be considered an alternative to net profit for the year as a measure of operating performance or to cash flows from operating activities as a measure of liquidity.

Our calculation of EBITDA may be different from the calculation used by other companies and therefore comparability may be limited. We believe that EBITDA provides useful information to investors because it is an indicator of the strength and performance of our ongoing business operations, including our ability to fund discretionary spending such as capital expenditure, acquisitions of subsidiaries and other investments and our ability to incur and service debt. While depreciation and amortization are considered operating costs under IFRS, these expenses primarily represent non-cash current period allocation of costs associated with long-lived assets acquired or constructed in prior periods.

**Years ended December 31**

| | **2006** | **2007** |
|---|---|---|
| Net profit for the year attributable to the shareholders of the company | 8,105 | 17,854 |
| Depreciation and amortization | 676 | 777 |
| Interest expense | 1,361 | 2,063 |
| Interest income | (230) | (340) |
| Income tax expense | 3,305 | 3,595 |
| **EBITDA** | **13,217** | **23,949** |
| **EBITDA margin[2]** | **31%** | **35%** |

*(in RUR million, except percentages)*
(2) Margins are calculated as a percentage of revenues.

### Consolidated financial statements

We prepare our financial statements in accordance with IFRS from 2004. Previous audited financial statements are available at our web site www.pik.ru.

### Operating Segments

*Sales of Real Estate Property*
Activities in this segment primarily relate to the implementation of developments planned and undertaken by us, including the identification of investment opportunities, performing feasibility studies, obtaining the necessary construction permits, carrying out construction of projects and performing project management activities, and marketing our real estate projects to potential buyers.

Revenues in this segment primarily consist of revenues generated from the sale of apartments in the buildings we develop. A substantial proportion of the construction services contracted by this segment are procured from our Construction Services segment.

*Construction Services*
Activities in this segment primarily relate to contracting activities, construction of concrete panels, assembly of prefabricated panel buildings and production of other construction materials. This segment provides such services to our Sales of Real Estate Property segment as well as to third parties, including the Moscow city government. Most inter-segment sales within the Group and eliminations noted in our financial statements are attributable to services provided by this segment.

*Sales of Construction Materials and Other Activities*
Activities of this segment primarily related to (i) the production of raw materials, (ii) servicing and maintenance of residential properties and (iii) production of doors, windows and facades. This segment supplies raw materials and construction materials to our Construction Services segment and the Sales of Real Estate Property segment as well as to third parties.

*Transactions eliminated on consolidation*

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

As of December 31 2007 the Group controlled 103 legal entities (December 31 2006: 57). Their assets, liabilities, revenues and expenses have been included in these consolidated financial statements. Our segments are constituted on the basis of the grouping of our significant operating subsidiaries as follows:

| Segment Entity Business | | Ownership interest as of March 31 2008 |
|---|---|---|
| **Sales of Real Estate Property** | | |
| PIK Moscow LLC | Development activities in Moscow | 100% |
| PIK Region | Development activities in the Moscow region and other regions of Russia | 100% |
| **Construction Services** | | |
| DSK-2 | Concrete panel manufacturing plant | 98% |
| DSK-3 | Concrete panel manufacturing plant | 84% |
| 100 KZHI | Concrete panel manufacturing plant | 92% |
| 480 KZHI | Concrete panel manufacturing plant | 100% |
| PIK Development | General contractor and developer of poured concrete buildings in Moscow and the Moscow region | 100% |
| PIK Invest | Construction manager for projects in Moscow and the Moscow region | 100% |
| MFS-PIK | General contractor for panel housing constructed by us in Moscow and the Moscow region | 100% |
| **Sales of Construction Materials and Other Activities** | | |
| Trading House Osnova | Raw materials supplier | 100% |
| PIK Nerud | Raw materials production | 100% |
| PIK Comfort | Servicing and maintenance of residential and non-residential properties | 100% |
| PIK Profile | Production of windows and doors | 100% |
| PIK Design | Advertising | 100% |

**Events subsequent to the balance sheet date**

In January 2008 the Group initiated a restructuring process with a view to establishing an organisational structure for the development operations on geographical basis. A number of new legal entities were established for this purpose to support the regional expansion of the Group's operations in certain Russian regions, the Ukraine and Kazakhstan.

**Certain Factors Affecting Our Results of Operations**

Our results are affected by a variety of factors, including the following:

### Acquisitions of subsidiaries in 2007

*Foton GBI and Foton ABZ*

In April 2007 the Group acquired a 100% interest in Foton GBI and Foton ABZ for a total consideration of RUR 1 037 million settled in cash. The main activity of the subsidiaries acquired is the production of concrete mix and reinforced concrete products at production facilities located in the Kaluga Region, Russia. The acquisition of these subsidiaries resulted in goodwill amounting to RUR 299 million. The goodwill arose on the acquisition mainly because of the limited supply of production facilities for the manufacture of concrete products in the region.

*Storm Properties Group*

In September 2007 the Group acquired 50% plus 1 share in Storm Properties, the parent company of the Storm Properties Group, for a consideration of RUR 1 347 million settled in cash. The Storm Properties Group is a leading developer operating in the commercial real estate segment in Russia. The purchase agreement provides for an option to acquire an additional 25% interest in the Storm Properties Group for a market price at the date of the transaction. The option vests in three years from the date of the acquisition and expires in two years from the vesting date. The acquisition of the Storm Properties Group resulted in goodwill amounting to RUR 591 million. The goodwill arose on the acquisition due to the well-established reputation of Storm Properties Group as a leading-edge company with exceptional innovation capabilities in the commercial estate segment.

*480 KZHI*

In July 2007 a related party of the Group acquired a 100% interest in 480 KZhI for a consideration of RUR 639 million. In November 2007 the Group purchased from the related party the 100% interest in 480 KZhI for a consideration determined in the independent internationally recognised appraisal company's report amounting to RUR 1 237 million settled in cash. Because the control of the related party over the acquiree was transitory, the acquisition of the company by the Group from the related party was not accounted for as a common control transaction.

The transaction was accounted for as a business combination under IFRS 3 Business Combinations. The difference between the consideration paid by the Group and the consideration paid by the related party of RUR 598 million was recognised directly in equity. The acquisition of the subsidiary resulted in goodwill amounting to RUR 274 million.

*Khromtsovsky Karier*

In May 2007 the Group obtained control over Khromtsovsky Karier, a sand pit, by acquiring an additional 25% interest for a consideration of RUR 32 million settled in cash. This acquisition increased the Group's interest from 48% to 73%. The acquisition of the subsidiary resulted in goodwill amounting to RUR 28 million. The goodwill was assessed for impairment as at 30 June 2007 and an impairment loss of RUR 28 million was recognised as a result.

*NovorosGragdanproekt*

In September 2007 the Group acquired a 57% interest in NovorosGragdanproekt for a consideration of RUR 160 million settled in cash. The main activity of acquired entity is the provision of design and architectural services. The acquisition of the subsidiary resulted in goodwill amounting to RUR 78 million. The goodwill arose on the acquisition mainly due to the expected growth of the company's architectural and design expertise.

The impact of acquiring the subsidiaries was to increase profit for the year by RUR 15 million.

### Revenue Recognition

Revenue recognition policies have a significant impact on the results of operations. Below we have summarized key elements of our revenue recognition policies for each of the segments.

*Sales of Real Estate Property*
Revenue from the sale of real estate is accounted for as a sale of goods and is recognized when the significant risks and rewards of ownership have been transferred to the buyer, which is considered to be the date when the respective building is approved by the local or regional regulatory authorities for acceptance of completed buildings. We do not recognize revenue in respect of sales of residences in a building before such residences are sold.

As a result, for sales of our residences that occur before the local authorities has accepted the completion of the relevant building, we only recognize revenue for such sales on the date of the local authorities' acceptance. For sales of our residences that occur after the local authorities has accepted the completion of the relevant building, we recognize revenue on the date of such sales. We therefore recognize revenue for each of our buildings gradually until all of the residences in the relevant building are sold.

We recognize revenue from sales of real estate at sale prices. Sale prices may differ substantially from market prices that exist at the date the sale is recognized. This means that if prices increase between the time residences in a particular building are sold and the time the local authorities accepts such building, we are not able to capture this appreciation in residential housing prices.

In part because of long development cycles, we have experienced significant variations in revenues from our development activities during the periods under review: for the years ended December 31 2006 and 2007 our revenues from sales of real estate were RUR 30.3 billion and RUR 50.4 billion respectively.

We expect that due to long development cycles for our projects, the revenues of our Sales of Real Estate Property segment will continue to vary significantly from period to period.

*Construction Services*
Revenue from construction services rendered is recognized on a monthly basis in accordance with the actual volume of work completed.

There are certain construction projects in which we act as an investor or co-investor and a third party acts as the developer. In such cases, certain of our subsidiaries may provide construction services to the developer. Revenues from construction services relating to such projects are recognized separately from the sales proceeds we may receive in connection with our role as an investor.

*Sales of Construction Materials and Other Activities*
Revenue from the sale of raw materials and other construction materials is recognized when the significant risks and rewards of ownership have been transferred to the buyer, which is determined based on specific contract terms such as payment and delivery. Revenue received from the servicing and maintenance of residential properties is recognized on a monthly basis in accordance with the actual volume of work completed.

### Costs of Land and Construction and Other Development Costs

During the periods under review, we have experienced increases in development and construction costs, including costs of materials, labor, pre-project documentation and land and property acquisition costs. Prices of construction materials have been outpacing the rate of inflation in Russia, especially with respect to cement and metal. Labor and other costs have been increasing due to labor shortages and high costs of living in Russia, particularly in Moscow. These cost increases have generally resulted in increases in the prices for which we offer our residences once construction is completed, and may continue to do so in the future.

**Seasonality**

Our revenues are generally higher during the third and fourth quarters of the year because the majority of buildings receive approval for acceptance by the applicable local authorities during these quarters. Local authorities generally approve more buildings during the third and fourth quarters as a means of managing year-end budgetary and construction targets.

Our revenues decrease to some extent during the first quarter as a result of decreased production and construction activity related to cold weather. Our non-ferrous raw materials production usually decreases during the winter months of December and January. Sand, for example, is more difficult to extract in cold temperatures. In addition, MFS-PIK and PIK Development experience some reduction in productivity in the winter months with respect to their activities relating to the foundations and framework of poured concrete buildings, as the technological processes for these activities are susceptible to low temperatures. The activities of DSK-2 and DSK-3, including assembly of pre-fabricated panel buildings in Moscow and the Moscow region, are less subject to seasonal effects.

**Macroeconomic Factors**

All our current properties and projects are located in Russia. As a result, macro-economic trends and country-specific risks relating to Russia significantly influence our performance. The following table sets out certain information for Russia as of and for the dates indicated.

**Years ended December 31**

| | 2006 | 2007 |
|---|---|---|
| GDP growth[1] | 7.4% | 8.1% |
| Consumer price index[1] | 9.0% | 11.9% |
| Average exchange rate (RURles per US dollar)[1] | 27.2 | 25.6 |
| Real RURle appreciation against US dollar[1] | 10.7% | 15.0% |

(1) Ministry for economic development of the Russian Federation

As detailed in the table above, the Russian economy has experienced generally positive trends in the last few years. During 2007, the rates of economic growth were maintained at a high level. The high economic growth rates were fuelled by the high growth in consumer and investment demands. In 2007, the consumer price inflation amounted to 11.9 percent (higher then last three years). Inflation in 2007 was determined to a considerable extent by the continuing pronounced rise in prices for foodstuffs in global markets, structural imbalances in Russia's domestic production and sales of high-priority food products. The Russian government has generally followed conservative fiscal and monetary policies, resulting in federal budget surpluses, reductions in its foreign debt, large foreign currency reserves and a large stabilization fund. These positive trends have been accompanied by significant growth in the demand for residential space. Sales prices for real estate have also increased.

**Results of Operations**

Year Ended December 31 2007 compared to the Year Ended December 31 2006

The following table sets forth income statement data, including as a percentage of revenues, for the years ended December 31 2006 and 2007.

| Years ended December 31 | | | | |
|---|---|---|---|---|
| | 2006 | % of revenues | 2007 | % of revenues |
| Revenues | 42,046 | 100.0 | 69,050 | 100.0 |
| Cost of sales | (32,265) | (76.7) | (51,206) | (74.2) |
| Gross profit | 9,781 | 23.3 | 17,844 | 25.8 |
| Gain on disposal of development rights | 2,851 | 6.8 | 9,502 | 13.8 |
| Distribution expenses | (467) | (1.1) | (879) | (1.3) |
| Administrative expenses | (1,511) | (3.6) | (3,114) | (4.5) |
| Other income and expenses | 1,522 | 3.6 | (55) | (0.1) |
| Financial income | 571 | 1.4 | 569 | (0.8) |
| Financial expenses | (1,362) | (3.2) | (2,363) | (3.4) |
| Share of loss of equity accounted investees (net of income tax) | (10) | (0.02) | (24) | (0.03) |
| **Profit before income tax** | **11,405** | **27.1** | **21,480** | **(31.1)** |
| Income tax expense | (3,305) | (7.9) | (3,595) | (5.2) |
| **Net profit for the year** | **8,100** | **19.3** | **17,885** | **25.9** |

*(in RUR million, except percentages)*

For the year ended December 31 2007, we had revenues and net profit of RUR 69.1 billion and RUR 17.9 billion, respectively. The Sales of Real Estate Property segment is the most part of our business, accounting for 73.0% of our revenues for the year ended December 31 2007. The following table sets forth our revenues and net profit for the year by segment.

**Operating Segments**

Our revenues are derived principally from the following activities: (1) sales of real estate property; (2) construction services; and (3) sales of construction materials and other activities.

| Years ended December 31 | | | | |
|---|---|---|---|---|
| **Revenues** | 2006 | % of revenues | 2007 | % of revenues |
| Sales of Real Estate Property | 30,305 | 72.1 | 50,421 | 73.0 |
| Construction Services | 15,587 | 37.1 | 18,934 | 27.4 |
| Sales of Construction Materials and Other Activities | 3,014 | 7.2 | 5,521 | 8.0 |
| Eliminations | (6,860) | (16.4) | (5,826) | (8.4) |
| **Total** | **42,046** | **100.0** | **69,050** | **100.0** |

*(in RUR million, except percentages)*

| Years ended December 31 | | | | |
|---|---|---|---|---|
| **Net Profit[1]** | 2006 | % of net profit for the year | 2007 | % of net profit for the year |
| Sales of Real Estate Property | 8,322 | 102.7 | 17,489 | 97.8 |
| Construction Services | 343 | 4.2 | 65 | 0.4 |
| Sales of Construction Materials and Other Activities | 223 | 2.8 | 365 | 2.0 |
| Eliminations | (789) | (9.7) | (34) | (0.2) |
| **Total** | **8,100** | **100.0** | **17,885** | **100.0** |

*1 Net profit for the segments was determined based on the gross profit for each segment. (In RUR million, except percentages)*

### Revenues

Revenues increased by RUR 27.1 billion, or 64.5%, from RUR 42.0 billion for the year ended December 31 2006 to RUR 69.1 billion for the year ended December 31 2007.

Revenues of the Sales of Real Estate Property segment increased by RUR 20.1 billion, or 66.3%, from RUR 30.3 billion for the year ended December 31 2006 to RUR 50.4 billion for the year ended December 31 2007. The increase was primarily the result of an increase in selling prices and an increase in the number of buildings accepted by the local authorities.

Revenues of the Construction Services segment increased by RUR 3.3 billion, or 21.2%, from RUR 15.6 billion for the year ended December 31 2006 to RUR 18.9 billion for the year ended December 31 2007 due to an increase in prices.

Revenues of the Sales of Construction Materials and Other Activities segment increased by RUR 2.5 billion, or 83.3%, from RUR 3.0 billion for the year ended December 31 2006 to RUR 5.5 billion for the year ended December 31 2007 mainly because of increase in prices and secondary because of increase of sales of raw materials and other services.

### Cost of Sales

Cost of sales increased by RUR (18.9) billion, or 58.5%, from RUR (32.3) billion for the year ended December 31 2006 to RUR (51.2) billion for the year ended December 31 2007.

The increase in cost of sales was due primarily to an increase in sales and a growth of prices on raw materials.

Cost of sales of the Sales of Real Estate Property segment relate primarily to the acquisition of land plots and development rights and the construction of developments. Cost of sales of this segment increased by RUR (16.7) billion, or 89.8%, from RUR (18.6) billion for the year ended December 31 2006 to RUR (35.3) billion for the year ended December 31 2007. The increase was primarily the result of an increase in the number of buildings accepted by the local authorities and the number of sold apartments recognized in revenue.

Cost of sales of the Construction Services segment relate primarily to services provided to JSC GK PIC and PIK Region and to third parties such as the Moscow city government. Cost of sales of this segment increased by RUR (3.9) billion, or 29.1%, from RUR (13.4) billion for the year ended December 31 2006 to RUR (17.3) billion for the year ended December 31 2007.

Cost of sales of the Sales of Construction Materials and Other Activities segment related primarily to production of raw materials and construction materials provided to our group and to third parties. Cost of sales of this segment decreased by RUR 0.5 billion, or 12.8%, from RUR (3.9) billion for the year ended December 31 2006 to RUR (4.4) billion for the year ended December 31 2007.

### Gross Profit

Gross profit increased by RUR 8.0 billion, or 81.6%, from RUR 9.8 billion for the year ended December 31 2006 to RUR 17.8 billion for the year ended December 31 2007. Operating margin increased from 23.3% for the year ended December 31 2006 to 25.8% for the year ended December 31 2007.

Gross profit for the Sales of Real Estate Property segment increased by RUR 3.4 billion, from RUR 11.7 billion for the year ended December 31 2006 to RUR 15.1 billion for the year ended December 31 2007. The increase was primarily the result of an increase in selling prices and an increase in the number of buildings accepted by local authorities.

# Chief Financial Officer's Review

Gross profit for the Construction Services segment decreased by RUR 500 million, or 22.7%, from RUR 2.2 billion for the year ended December 31 2006 to RUR 1.7 billion for the year ended December 31 2007 due to an increase in the cost of sales in comparison with sale prices.

Gross profit for the Sales of Construction Materials and Other Activities segment increased by RUR 2.1 billion, from RUR (970) million for the year ended December 31 2006 to RUR 1.1 billion for the year ended December 31 2007 due to increase of sales of volumes of construction materials.

**Gains on disposal of development rights**

Gains on disposal of development rights increased by RUR 6,651 million, or 233%, from RUR 2,851 million for the year ended December 31 2006 to RUR 9,502 million for the year ended December 31 2007.

**Gain on disposal of development rights in 2007:**

*Mytischy Project*
In December 2007 the Group entered into an agreement to sell to an affiliate of GIC Real Estate, for a consideration of RUR 5,770 million, a 25% interest in Viniso Investments Limited, a subsidiary. This company was the parent company of a number of entities operating a project to develop residential housing in Mytischy, Moscow Region. The carrying amount of the minority interest disposed of amounted to RUR 6 million. The disposal of the minority interest resulted in a gain of RUR 5,764 million.

This was a milestone transaction and an unprecedented deal for the Russian real estate sector, where a foreign investor invested into a typical, large scale mass market residential project located in Moscow region.

*Park City*
As at December 31 2006 the Group owned a 25% interest in Park City Investments Limited and KRPT. The investments in Park City Investments Limited and KRPT are accounted for as equity accounted investees. The two entities effectively owned a 21% interest in Park City, a project to develop real estate property on a land plot located at Kutuzovsky Prospect, Moscow.

In addition, at December 31 2006 the Group also owned a 100% interest in Viktor that was a party to a co-investment agreement with a 15% share in the Park City project.

In 2007 Viktor transferred the right under the co-investment agreement to a Cyprus-based subsidiary and subsequently the Group sold a 75% interest in the subsidiary in two transactions for a total consideration of RUR 3,701 million. These transactions resulted in a decrease in the effective interest of the Group in the project to 25%. The carrying amount of the investment in the development right disposed of was RUR 338 at the date of disposal. The gain on disposal amounted to RUR 3,363 million. The outstanding balance of accounts receivable from the above transactions as at December 31 2007 amounted to RUR 2,455 million.

*Yubileyny district*
At December 31 2006 assets held for sale comprised a 100% interest in an entity which owned the development rights for a land plot at Yubileiny District, Khimki, Moscow Region, including the land lease contract and the construction permit. The Group acquired the entity from a third party for a consideration of RUR 2,300 million with the intention of selling it to another developer; therefore, the development right was accounted for as an asset held for sale in the consolidated financial statements as at and for the year ended December 31 2006. In April 2007 the Group sold the interest in the legal entity to a third party for a consideration of RUR 2,675 million. The gain on disposal amounted to RUR 375 million.

**Gain on disposal of development rights in 2006:**

*Mantulinskaya Street*

In June 2005 the Group acquired development rights through a purchase of 70% of the shares in a production plant occupying two land plots located at Mantulinskaya Street, Moscow. At the date of the acquisition almost all the activities of the plant had been relocated. The legal entity leased the land plots for production purposes on a long-term basis. The acquisition was accounted for as a purchase of the right to lease the land plots. The Group had intentions to apply to the municipal authorities for permission to develop real estate on the land plots. At December 31 2005 the development rights had a carrying value of RUR 707 million.

In March 2006 the Group disposed of these development rights to a third party for RUR 2,272 million realizing a gain of RUR 1,565 million. The purpose of this disposal was to realize an immediate profit rather than to continue the development under circumstances of continual disagreement with the plant's minority shareholders. At December 31 2006 the Group had outstanding accounts receivable of RUR 1,092 million in relation to this transaction.

Later in 2006 the same third party acquired an additional 28% of the shares in the plant. The Group was subsequently offered 98% of the shares in the plant for a consideration of RUR 5,326 million. The transaction was accounted for as an acquisition of assets. At December 31 2006 the Group had outstanding accounts payable to the seller of RUR 1,057 million.

In December 2006 the Group sold a 50% shareholding in the project for a consideration of RUR 3,950 million with a resulting gain of RUR 1,286 million in order to finance future construction activities. As at December 31 2006 and 2007 the Group's effective interest in the project of 49% was classified as an investment in an equity accounted investee.

**Distribution expenses**

Distribution expenses consist of transportation costs, marketing costs, advertising costs and promotion expenses. Distribution expenses increased by RUR (412) million, or 88.2%, from RUR (467) million for the year ended December 31 2006 to RUR (879) million for the year ended December 31 2007. This increase resulted primarily from an increase in marketing and advertising expenses due to an expansion of PIK Group in regions.

**Administrative expenses**

Administrative expenses consist of compensation paid to employees, lease payments, fees paid to auditors and consultants, and charitable and social expenses. Administrative expenses increased by RUR (1.6) billion, or 107%, from RUR (1.5) billion for the year ended December 31 2006 to RUR (3.1) billion for the year ended December 31 2007. This increase resulted primarily from an increase in labor expenses (of RUR 1,361 million) caused by an expansion of PIK Group into Regions and, as a result, a necessity in increasing of labor resources for an executions of the new projects.

**Other expenses**

Other expenses include those from loss on impairment of property, plant and equipment, and loss on impairment of goodwill. For the year ended December 31 2007, net other expenses amounted to RUR (55) million.

**Financial income and expenses**

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income, gains on the disposal of available-for-sale financial assets, and foreign currency gains. Interest income is recognised as it accrues in the income statement, using the effective interest method. Dividend income is recognised in the income statement on the date that the Group's right to receive payment is established.

Finance expenses comprise interest expense on borrowings, unwinding of the discount on provisions, foreign currency losses and impairment losses recognized on financial assets. All borrowing costs are recognized in the income statement using the effective interest method, except for borrowing costs related to qualifying assets that are recognized as part of the cost of such assets.

**Foreign currency gains and losses are reported on a net basis.**

Financial income decreased by RUR 2 million, or 0.4%, from RUR 571 million for the year ended December 31 2006 to RUR 569 million for the year ended December 31 2007.

Financial expenses increased by RUR (1.0) billion, or 71.4%, from RUR (1.4) billion for the year ended December 31 2006 to RUR (2.4) billion for the year ended December 31 2007. This increase resulted primarily from an increase in interest expenses (of RUR 701 million).

**Income tax expenses**

Income tax expenses include expenses relating to profits tax, which consist of our current profits tax and deferred tax liabilities.

In accordance with IFRS, revenues from the sale of residences are recognized on the date the local authorities issues an acceptance certificate. At the same time, profits tax accrues with respect to the profit gained from the buildings accepted by the local authorities, which constitutes a deferred tax liability.

We pay income tax to the Russian government in accordance with tax legislation. Under this legislation profit gained from projects is recognized upon the execution of a certificate confirming that an investment agreement has been fulfilled. The period between this date and the date that the local authorities issues an acceptance certificate can be as long as two years, so we recognize deferred income tax expenses.

Income tax expenses increased by RUR (290) million, or 8.8%, from RUR (3.3) billion for the year ended December 31 2006 to RUR (3.6) billion for the year ended December 31 2007. This increase resulted primarily from an increase in profit before tax. But income tax didn't increase as fast as profit before income tax because significant part of the income was taxed at lower rates due to revenue contributions from outside Russia.

**Net profit for the year**

As a result of the above, net profit for the year ended December 31 2007 was RUR 17.9 billion as compared to RUR 8.1 billion for the year ended December 31 2006.

**Liquidity and Capital Resources**

*Capital Requirements*

**Real estate investment and development is a capital-intensive business, and we expect to have significant ongoing liquidity and capital requirements in order to finance our growth strategy, including investing in new properties and development projects in our target market segments, while making additional investments into our existing properties and real estate development projects.**

We require capital to finance a variety of capital expenditures from cash outlays for capital investments in real estate development projects to the acquisition of real estate properties, land rights (ownership or leasehold) and production facilities or any other purchases of property. In addition, capital is required for plant and equipment and intangible assets, the repayment of debt, for changes in working capital and general corporate activities.

Cash outflows for acquisition of property, plant and equipment and development rights, for each of the years ended December 31 2006 and 2007 amounted to the following:

**Years ended December 31**

| | 2006 | 2007 |
|---|---|---|
| Acquisition of property, plant and equipment | (2,838) | (3,623) |
| Acquisition of development rights and other intangible assets | (8,274) | (16,183) |
| **Total** | **(11,112)** | **(19,806)** |

(In RUR million)

We invested RUR 19.8 billion for the year ended December 31 2007. We expect our capital expenditures for the year 2008 will amount to almost RUR 23.0 billion, including acquisitions. These investments will be focused on acquiring land and purchasing fixed assets. We expect that acquisitions of land plots, development companies or projects and production facilities will be a key part of our growth strategy. Our cash requirements relating to potential acquisitions may vary significantly according to market opportunities.

### Capital Resources

**For the year ended December 31 2006, our primary sources of funding were net cash flows from operations (RUR 3.5 billion) and net proceeds from borrowings (RUR 5.1 billion). For the year ended December 31 2007, our primary sources of funding were net cash flows from operations and net proceeds from borrowings (RUR 32.6 billion).**

Over the next several years, we expect to finance most of our capital expenditure needs through operating cash flows, co-investment arrangements, advance payments from customers and additional debt and equity financing. We expect that our capital expenditures in connection with the development of real estate properties will be the majority of our cash outflows for the foreseeable future.

The availability of debt financing is influenced by many factors, including our profitability, operating cash flows, debt levels, credit ratings, contractual restrictions and market conditions. We have also pledged shares of certain of our subsidiaries and real properties in connection with our borrowings. We cannot guarantee that we will be able to continue to obtain debt financing in the future.

In line with our strategy for growth, we may acquire other real estate companies or developments. Our cash requirements relating to potential acquisitions may vary significantly based on market opportunities. We may also finance these acquisitions through swapping interests in our existing projects and properties.

As of December 31 2007, our loans and borrowings were comprised of the following:

| | Currency | Aggregate Principal Amount Outstanding at December 31 2007 |
|---|---|---|
| Bank loans | | |
| Sberbank | RUR | 18,580,102 |
| Absolutbank | RUR | 1,467,000 |
| VTB | RUR | 2,700,000 |
| ROSBANK | USD | 2,331,889 |
| Sobinbank | USD | 1,227,310 |
| Garantibank | USD | 306,828 |
| ORGRES Bank | USD | 300,415 |
| NOMOS Bank | USD | 736,386 |
| Deutsche Bank | RUR | 3,000,000 |
| Credit Suisse | USD | 499,884 |
| Raiffeisen | USD | 471 |

| | | |
|---|---|---|
| Bank ZhilFinans (related) | RUR | 8,568 |
| **Bonds (PIK-05)** | **RUR** | **560,000** |
| **Loans and borrowing from third parties and related parties** | | |
| Related parties | RUR | 192,143 |
| Third parties | USD | 1,558,692 |
| Third parties | RUR | 803,789 |
| **Non-current and current loans and borrowings less finance lease liabilities and interest payable** | | **34,273,476** |
| Finance lease liabilities | | 208,483 |
| Interest payable | | 158,241 |
| **Total loans and borrowings, non-current and current** | | **34,640,200** |
| Bank loans | | 21,116,459 |
| Bonds | | 560,000 |
| Related parties | | 177,867 |
| Third parties | | 2,048,241 |
| **Current loans and borrowings less finance lease liabilities and interest payable** | | **23,902,567** |
| Finance lease liabilities | | 118,853 |
| Interest payable | | 158,241 |
| **Current loans and borrowings** | | **24,179,661** |
| Bank loans | | 10,033,826 |
| Related parties | | 22,843 |
| Third parties | | 314,240 |
| **Non-current loans and borrowings less finance lease liabilities and interest payable** | | **10,370,909** |
| Finance lease liabilities | | 89,630 |
| **Non-current loans and borrowings** | | **10,460,539** |

*(in RUR thousands)*

**Cash Flows**

A summary of our cash flows is presented in the table below for the periods indicated:

| **Years ended December 31** | **2006** | **2007** |
|---|---|---|
| **Operating Activities** | | |
| **Profit for the year** | **8,100** | **17,885** |
| Adjustments for: | | |
| Depreciation and amortization | 676 | 777 |
| Foreign exchange loss/(gain), net | (341) | 300 |
| Loss on disposal of property, plant and equipment | 215 | 225 |
| Gain on disposals of development rights | (2,851) | (9,502) |
| Gain on disposal of available-for-sale financial assets | – | (229) |
| Negative goodwill on acquisition of subsidiaries and minority interests | (1,552) | 28 |
| Share of loss of equity accounted investees | 10 | 24 |
| Interest expense | 1,362 | 2,063 |
| Interest income | (231) | (340) |
| Income tax expense | 3,305 | 3,595 |
| **Operating profit before changes in working capital and provisions** | **8,693** | **14,826** |
| Increase in inventories | (1,818) | (9,122) |
| Increase in trade and other receivables | (184) | (10,805) |
| Increase/(decrease) in trade and other payables | (704) | 5,487 |
| Decrease in provisions | (74) | (4) |

| | | |
|---|---|---|
| **Cash flows from operations before income taxes and interest paid** | **5,913** | **382** |
| Income taxes paid | (559) | (709) |
| Interest paid | (1,800) | (2,646) |
| **Cash flows (utilized by)/from operating activities** | **3,544** | **(2,973)** |
| | | |
| **Investing Activities** | | |
| Proceeds from disposal of property, plant and equipment | 51 | 28 |
| Interest received | 83 | 315 |
| Acquisition of property, plant and equipment | (2,838) | (3,623) |
| Acquisition of development rights and other intangible assets | (8,274) | (16,183) |
| Acquisition of equity accounted investees | (334) | – |
| Acquisition of minority interests | (11) | (15) |
| Loans advanced | (2,925) | (8,861) |
| Proceeds from sale of minority interests and development rights | 5,130 | 10,745 |
| Repayment of loans advanced | 2,022 | 6,809 |
| Acquisition of subsidiaries, net of cash acquired | (1,094) | (2,412) |
| **Cash flows utilized by investing activities** | **(8,190)** | **(13,197)** |
| | | |
| **Financing Activities** | | |
| Proceeds from borrowings | 23,394 | 35,675 |
| Repayment of borrowings | (18,310) | (25,157) |
| Proceeds from share issue | – | 23,016 |
| Transactions with Majority Shareholders | – | (948) |
| **Cash flows from financing activities** | **5,084** | **32,586** |
| | | |
| Net increase in cash and cash equivalents | 448 | 16,416 |
| Effect of exchange rate fluctuations on cash and cash equivalents | – | (185) |
| Cash and cash equivalents at beginning of year | 367 | 815 |
| Cash and cash equivalents at end of year | 815 | 17,046 |

*(in RUR million)*

**Year Ended December 31 2007 compared to Year Ended December 31 2006**

Net cash used in operating activities amounted to RUR (2.97) billion for the year ended December 31 2007 compared to net cash used in operating activities of RUR 3.5 billion for the year ended December 31 2006. This was primarily the result of significant land plot acquisitions. The impact of these acquisitions is reflected as in the increase in inventories.

Foreign exchange losses for the year ended December 31 2007 amounted to RUR 300 million compared to foreign exchange gains for the year ended December 31 2006 of RUR 340,5 million. This loss primarily resulted from a significant decrease in value of the US dollar against the ruble in 2007.

Income from disposals of development rights for the year ended December 31 2007 amounted to RUR 9,502 million compared to income for the year ended December 31 2006 of RUR 2,851 million. This resulted primarily from gains from disposals of stakes in the Yaroslavsky and Park City projects.

Interest expenses for the year ended December 31 2007 amounted to RUR 2,063 million compared to interest expenses for the year ended December 31 2006 of RUR 1,362 million. This change was primarily the result of a significant increase in borrowings used for the acquisition of land plots and development rights.

The increase in trade and other receivables for the year ended December 31 2007 amounted to RUR (10,805) million compared to an increase for the year ended December 31 2006 of RUR (184) million. This increase resulted primary from the sale by PIK Region of residential sites to the Department of Residential Policy, which had not paid in full by the end of 2007.

The increase in trade and other payables for the year ended December 31 2007 amounted to RUR 5,487 million compared to decrease in trade and other payables for the year ended December 31 2006 of RUR (704,4) million. This increase resulted primary from an increase in accruals for costs to complete constructions recognized in revenues in 2007.

Cash flows utilized by investing activities decreased by RUR 5.0 billion, or 61%, from RUR (8.2) billion for the year ended December 31 2006 to RUR (13.2) billion for the year ended December 31 2007. The decrease was primarily due to cash outflows for the acquisition of development rights and other intangible assets of RUR (16.2) billion and loans advanced in the amount of RUR (8.9) billion.

Proceeds from disposal of minority interest and development rights for the year ended December 31 2007 amounted to RUR 10,745 million compared to proceeds for the year ended December 31 2006 of RUR 5,130 million. This amount primary consisted of revenue from disposal of development rights upon the Yaroslavsky and Park City projects.

Acquisition costs for subsidiaries for the year ended December 31 2007 amounted to RUR (2,412) million compared to acquisition costs for the year ended December 31 2006 of RUR (1,094) million. This increase is primary due to significant acquisitions in 2007 including Storm Properties and 480 KZHI.

Net cash provided by financing activities increased by RUR 27.5 billion from RUR 5.1 billion for the year ended December 31 2006 to RUR 32.6 billion for the year ended December 31 2007. The increase was primarily due to proceeds from the Group's IPO in May 2007.

**Liquidity**

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of our cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

As of December 31 2006 and 2007 we had cash and cash equivalents of RUR 815 million and RUR 17.0 billion respectively.

**Years ended December 31**

| | **2006** | **2007** |
|---|---|---|
| Petty cash | 22 | 26 |
| Bank balances, RUR denominated | 1,080 | 16,800 |
| Bank balances, USD denominated | 32 | 230 |
| Cash and cash equivalents in the balance sheet | 1,134 | 17,056 |
| Bank overdrafts | (319) | (10) |
| Cash and cash equivalents in the statement of cash flows | 815 | 17,046 |

*(in RUR million)*

**Significant accounting policies**

*Revenues*

Revenues from segments were described above.

*Development rights*

Expenditure on identifying land plots with the purpose of obtaining new development projects is recognised in the income statement as an expense as incurred.

Expenditure on obtaining development rights necessary to start construction activities is recognised in intangible assets if the projects are technically and commercially feasible and the Group has sufficient resources to accomplish the development of the projects.

The cost of development rights includes the cost of obtaining the right to lease a land plot, and the cost of obtaining the registered permit to construct a specific property.

Capitalised development rights recognised on initial acquisition as intangible assets are measured at cost less accumulated impairment losses until the development starts. On commencement of construction such development rights are reclassified as construction-in-progress intended for sale, included in inventories.

When the Group does not act as a developer, but participates in projects in the capacity of an investor or co-investor, the cost of development rights contributed to such projects is recognised within inventories.

*Onerous contracts*

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Group recognises any impairment loss on the assets associated with that contract.

The Group enters into investment or co-investment agreements to develop residential buildings. These contracts may require the Group to deliver certain properties to the local authorities upon completion of the construction or construct certain infrastructure facilities in exchange for the ability to develop the property for no consideration.

In addition the Group enters into agreements with local authorities to complete construction of certain residential properties where the apartments had been pre-sold by a predecessor developer to the general public; however, the construction was subsequently stopped due to the insolvency of the predecessor developer or other similar reasons.

When such agreements cannot be directly attributable to any of the Group's projects and the agreements are assessed as onerous, a provision is recognised in the Group's consolidated financial statements when entering into the agreement to complete the construction. The provision is estimated based on the present value of estimated unavoidable net costs to complete the construction.

*Income tax expenses*

Income tax expenses comprise current and deferred tax. Income tax expenses are recognised in the income statement except to the extent that it relates to items recognised directly in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which a temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

**New Standards and Interpretations not yet adopted**

A number of new standards, amendments to Standards and Interpretations, are not yet effective as at December 31 2007, and have not been applied in preparing these consolidated financial statements. Of these pronouncements, IFRS 8 Operating Segments will potentially have an impact on the Group's operations.

IFRS 8 Operating Segments introduces the 'management approach' to segmental reporting. IFRS 8 Operating Segments, which becomes mandatory for the Group's 2009 financial statements, will require the disclosure of segment information based on the internal reports regularly reviewed by the Group's Chief Operating Decision Maker in order to assess each segment's performance and to allocate resources to them. Currently, the Group presents segmental information in respect of its business and geographical segments. The new standard will not have any impact on the Group's financial position or performance. The Group plans to adopt this new standard when it becomes effective.

**Financial risk management**

*Overview*

**PIK has exposure to the following risks from its use of financial instruments: credit risk, liquidity risk, market risk. Through its training and management standards and procedures, PIK, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.**

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Group's risk management policies are established to identify and analyse the risks, set appropriate risk limits and controls, and to monitor risks and adherence to limits. Policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

The Group's Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The Group's Audit Committee is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

*Credit risk*

Credit risk is the risk of financial loss to the Group if a customer or counter-party to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investment securities.

*Sales of apartments to individuals*
The Group is not exposed to significant credit risk in connection with sales of apartments to customers, as such sales are undertaken only on a prepayment basis.

*Trade receivables from organisations*
The Group's exposure to credit risks is influenced mainly by the individual characteristics of each customer.

As of December 31 2007, 33% of the Group's trade and other receivables is attributable to one customer. As at December 31 2006 there was no significant concentration of credit risk in respect of receivables from customers.

The Group has established a credit policy under which each new customer is analysed individually for creditworthiness before the Group's standard payment and delivery terms and conditions are offered. These provide for penalties in the event of late payment. The Group's review includes external ratings, when available, and in some cases bank references.

In monitoring customer credit risk, customers are grouped according to their credit characteristics, including whether they are a governmental agency or commercial organisation, age profile, maturity and existence of previous financial difficulties.

The Group does not require collateral in respect of trade and other receivables.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables and investments. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loss component established for groups of similar asset in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

*Other investments*
The Group has established a formal procedure in relation to investments in other loans and equity securities available-for-sale. The procedure includes organisation of working groups which assess the feasibility of a potential investment. The working groups consist of representatives of major management bodies of the Group. The groups study legal, financial and economic implications of any suggested investment. Management does not expect any counterparties to fail to meet their obligations.

*Guarantees*
The Group's policy is to provide financial guarantees only to the Group's subsidiaries and related parties.

*Liquidity risk*
Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The liquidity risk is centrally managed for all subsidiaries of the Group. Management monitors the risks which the Group would face in the long, medium and short-term periods.

For the long-term perspective the Group analyzes five-year forecasts covering financial, operational and investing activities.

For medium and short-term periods, management considers the availability of different market instruments.

In addition, the Group monitors short and medium-term maturities within its credit portfolio. It also considers the replacement of existing instruments with more favourable facilities.

The Group maintains credit lines with a number of banks, at December 31 2007, approximately RUR 20 000 million, to ensure sufficient liquidity levels are available on demand.

*Market risk*

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

*Currency risk*

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the Russian Rouble (RUR). The currency in which these transactions primarily are denominated is U.S. Dollars (USD).

Interest on borrowings is denominated in currencies that match the cash flows generated by the underlying operations of the Group, primarily RUR, but also USD. This provides an economic hedge and no derivatives are entered into.

*Interest rate risk*

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy for determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

*Other market price risk*

The Group does not enter into commodity contracts other than to meet the Group's expected usage and sale requirements; such contracts are not settled net.

*Capital management*

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board of Directors monitors the return on capital. The Board of Directors also monitors the level of dividends to ordinary shareholders.

There were no changes in the Group's approach to capital management during the year.

Neither the Group nor any of its subsidiaries are subject to externally imposed capital requirements.

# Corporate Governance

**“PIK Group’s Corporate Governance system is based on principles of accountability, transparency and openness."**

**Zhukov Y.V.**
*Chairman of the Board of Directors PIK Group*

*'Okskaya' development, Moscow*

# Principles / Corporate Governance

**PIK Group's Corporate Governance system is based on principles of accountability, transparency and openness**

### Corporate governance principles

PIK Group's Corporate Governance system is based on the following principles:

- Observation of shareholders' rights and interests
- Accountability of the Board, the President and the Management of PIK Group to shareholders
- Transparency and openness of management and financial information
- Efficient internal audit and control systems
- Observation of norms and requirements of current legislation, operating in compliance with Russian corporate governance standards;

### Corporate governance structure

The Annual General Meeting of shareholders is the ultimate governance mechanism for PIK Group.

In addition, the following bodies exist for efficient governance:

- The Board of Directors for the general management of PIK Group
- The Management Board for the operational management of PIK Group

For the observance of shareholders' rights and interests and for the efficient running of Group corporate and commercial affairs, PIK Group has appointed and created

- A Corporate Secretary and Corporate Secretary Division;
- A standing Audit Committee, Personal and Compensation Committee and Strategic Committee;

For ensuring the efficient control and audit of financial and economic activities PIK Group has created:

- An Audit Commission;
- An internal Audit Department, reporting to the Board of Directors.
- Appointed an independent auditor

### Board of Directors as of January 1 2008

Our Board of Directors has seven members elected by a majority vote of shareholders at each annual General Meeting of Shareholders through cumulative voting. Directors may be re-elected an unlimited number of times.

The Board of Directors is responsible for our overall management, except matters reserved for our shareholders. See 'Description of Share Capital and Certain Requirements of Russian Legislation - General Meetings of Shareholders' for more information regarding the competence of our General Meeting of Shareholders.

### Management Board as of January 1 2008

Our day-to-day activities are managed by the Management Board, led by its Chairman Kirill Pisarev. The Management Board currently comprises four members: Artem Eyramdzhants, Tatiana Tikhonova, Evgeny Luneev and Fedor Sapronov. Members of the Management Board are re-elected annually by the Board of Directors from nominees submitted by members of the Board of Directors and our President.

The Management Board reports to and is responsible for the implementation of decisions taken by shareholders and the Board of Directors. Among other things, the Management Board co-ordinates activities of our subsidiaries, develops and controls the implementation of our investment and financial projects, adopts certain of our internal bylaws and represents us in labour disputes.

### Audit Committee as of January 1 2008

The Audit Committee currently comprises two members: Will Andrich and Anselm Schmucki. Mr. Andrich serves as Chairman of the Committee. The Audit Committee must be chaired by an independent director, who may not be the Chairman of the board of directors. The Audit Committee convenes as often as necessary, but at least once every quarter.

The Audit Committee is authorized to carry out the following functions relating to the control of our financial and business operations:

- Co-ordinate with the Company's independent auditors and prepare recommendations for its board of directors in connection with the election and removal of the independent auditors and on the fees and scope of services to be provided by auditors.
- Co-ordinate with the auditing commission and examine the auditing commission's conclusions on the verification of the Company's financial activities and annual accounts.
- Co-ordinate with the internal control division and make recommendations for appointment of the division's managers, review its plan of annual checks and the division's reports.
- Review the Company's standards and internal controls procedures and make appropriate reports and recommendations.
- Assess the Company's financial reports.

### Strategy Committee as of January 1 2008

The Strategy Committee currently comprises five members: Lee Timmins, Kirill Pisarev, Artem Eyramdzhants, Will Andrich and Anselm Schmucki. Mr. Timmins serves as Chairman of the Committee. The committee must be chaired by a non-executive director, who may not be the Chairman of the Board of Directors. The Strategy Committee is responsible for developing recommendations to the Board of Directors with respect to our strategic development, long-term planning and investment policy.

### Personnel and Compensation Committee as of January 1 2008

The Personnel and Compensation Committee currently comprises three members: Sergey Kanaev, Yury Zhukov and Lee Timmins. Mr. Kanaev serves as Chairman of the Committee. The committee must be chaired by a non-executive director, who may not be the Chairman of the Board of Directors.

The committee carries out the following functions:

- determines the criteria for appointment of candidates to the board of directors, members of the management board and the Company's President and considers potential candidates;
- makes recommendations as to the term of service and removal of the Company's President and members of the management board;
- makes recommendations with respect to service contracts for the Company's President and members of the management board;
- evaluates the activities of the Company's President and members of management board
- prepares proposals on the level of remuneration of the members of the management board as well as the Company's advisory committees, the Company's President, and members of the Company's board committees.

### Audit Commission as of January 1 2008

The Audit Commission verifies the accuracy of our financial reporting under Russian law and generally supervises our financial activity. Members of the Audit Commission are nominated and elected by the shareholders for a term of one year. A member of the Audit Commission may not simultaneously serve as a member of our Board of Directors or accounting commission or as our President or Chief Accountant. The Audit Commission has three members: (1) Valery Ropay, (2) Dmitry Nazarov, and (3) Elena Krutitskaya.

### Remuneration of Directors and Executive Officers

The aggregate amount of remuneration paid by us for the period from January 1 2007 to December 31 2007 to the above named directors and executive officers as a group for services in all capacities provided to us during the year ended December 31 2007 was approximately RUB 113 million in salary and bonuses. We do not have employment contracts with directors. Employment contracts with executive officers generally provide for a payment of up to one year's salary and bonus upon termination of employment by the Company for cause or upon resignation by the employee due to a material change by the company of the employee's responsibilities, authority or duties. We do not provide pension, retirement or similar benefits to our directors or executive officers.

### Share Bonus and Option Plan

We intend to establish a share bonus or share option plan for members of our Board of Directors, senior management and other key personnel. We may use up to 2% of our shares for such plans. We believe that our plan will be an effective financial incentive for retaining our top managers and ensuring that their interests are aligned with those of our shareholders.

### Loans to Directors and Executive Officers

As of the date of this prospectus, there were no outstanding loans granted by us to our directors and executive officers and no guarantees provided for their benefit, with the exception of an interest-bearing loan to an executive director amounting to RUR 15 million outstanding as of December 31 2007.

### Corporate Governance

We comply with the corporate governance requirements applicable to Russian public companies listed on Russian stock exchanges. Our Ordinary Shares have been admitted to list 'V' on MICEX since May 24 2007 (transferred to list ''B" on November 20 2007) and to list 'V' on RTS since April 26 2007 (transferred to list "B" on October 11 2007) and, as a result, we are required to comply with a number of corporate governance requirements as of the listing date. Such requirements include:

(1) the obligation to have at least one independent director,

(2) formation of an audit committee,

(3) adoption of a bylaw on insider trading

(4) implementation of internal control procedures.

We are in full compliance with these requirements. In addition, we observe the code of corporate conduct, as recommended by the FSFM.

### Interests of Directors and Officers

Certain of our directors and executive officers have direct interests and hold positions in management bodies in affiliated and non-affiliated companies with which the Company has engaged in transactions, including those in the ordinary course of business.

There are no potential conflicts of interest between any duties owed to the Company by our directors and executive officers referred to above and their private interests or other duties, except for potential conflicts of interest of Mr. Pisarev and Mr. Zhukov, our beneficial owners.

Under Russian legislation, certain transactions defined as 'interested party transactions' require approval by our disinterested directors or shareholders.

Certain of our directors and executive officers have beneficial ownership interests in our Ordinary Shares.

# Relevant Biographies

### Litigation Statement about Directors and Officers

At the date of this prospectus, none of our directors or executive officers for at least the previous five years:

- have any convictions in relation to fraudulent offenses
- have held an executive function in the form of a senior manager or a member of the administrative, management or supervisory bodies, of any company at the time of, or preceding, any bankruptcy, receivership or liquidation.
- have been subject to any official public incrimination or sanction by any statutory or regulatory authority (including any designated professional body)
- nor has ever been disqualified by a court from acting as a member of the administrative, management or supervisory bodies of a company or from acting in the management or conduct of the affairs of any company.

### Relevant Biographies

### Directors and Executive Officers

Our directors and executive officers are as follows:

| Name | Year of Birth |
|---|---|
| Yury Zhukov (1)<br>Chairman | 1969 |
| Kirill Pisarev (2)<br>President and Director | 1969 |
| Artem Eyramdzhants (2)(4)<br>First Vice President and Director | 1969 |
| Tatiana Tikhonova (4)<br>Vice President, Investments | 1960 |
| Evgeny Luneev (4)<br>Vice President, Economics & Finance | 1975 |
| Fedor Sapronov (4)<br>Director of Legal Department | 1973 |
| Sergey Kanaev (1)<br>General Director of PIK Region and Director | 1969 |
| Will Andrich (2)(3)(5)<br>Director | 1969 |
| Lee Timmins (1)(2)(5)<br>Director | 1961 |
| Anselm Schmucki (2)(3)(5)<br>Director | 1969 |

(1) Member of the Personnel and Compensation Committee of the Board of Directors.

(2) Member of the Strategy Committee of the Board of Directors.

(3) Member of the Audit Committee of the Board of Directors.

(4) Member of the Management Board.

(5) Independent Director according to the requirements of the Federal Service for Financial Markets.


*Yury Zhukov*


*Kirill Pisarev*


*Artem Eyramdzhants*


*Sergey Kanaev*

**Yury Zhukov** has served as our Chairman and as a Director since December 2005. Mr. Zhukov currently serves as Chairman of the board of directors of DSK-2 and DSK-3, is a member of the board of directors of PIK Region and 160 DSK and a member of the management board of PIK Interior. Each of these companies is affiliated with PIK Group.

From 1999 to 2004 Mr. Zhukov was an executive director of Zhilstroyindustriya, a construction investment company. Since 2001 Mr. Zhukov has served as director of London International Business Limited, an investment company. Since 1996 he has been a member of the board of directors of Housing Finance Bank.

Mr. Zhukov graduated from the Moscow Institute of Electronic and Mathematics with a degree in Electronic Devices and Electronics in 2003 and from the Moscow Institute of Municipal Management and Construction with a degree in Governmental and Municipal Management in 2002.

**Kirill Pisarev** has served as our President since 1994 and as a Director since December 2005. Mr. Pisarev currently serves as Chairman of our management board. Since 1996 Mr. Pisarev has been chairman of the board of directors of Housing Finance Bank and a member of the Advisory Board of Storm Properties since November 2007. Since 2001 he has served as director of London International Business Limited, an investment company. He is a member of a number of governmental and social organizations, such as the Housing Construction Board of the Chairman of the Federation Council and the Moscow Construction Union and is Vice President of the Russian Builders Association.

Mr. Pisarev graduated from the State Finance Academy of the Russian Government with a degree in Finance and Credit in 1995.

**Artem Eyramdzhants** has served as our First Vice President since August 2006 and as a Director since December 2005. He has also been a member of our management board since March 2006 and a member of the Advisory Board of Storm Properties since November 2007. Mr. Eyramdzhants has been one of our managers since 1996 and is also a member of the board of directors of DSK-2, DSK-3, PIK Region and 100 KGI, each of which is affiliated with PIK Group. Since 2000 he has been a member of the board of directors of Housing Finance Bank.

Mr. Eyramdzhants graduated from the State Finance Academy of the Russian Government with a degree in Interantional Economic Relations in 1992.

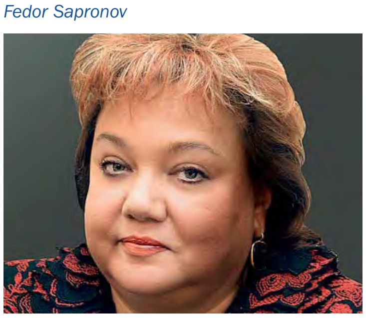
**Sergey Kanaev** has served as Executive Director of PIK Region since 1997, General Director of PIK Region since 1999 and as a Director since December 2005. Mr. Kanaev currently serves as Chairman of the Personnel and Compensation Committee of our Board of Directors and is a member of the board of directors of DSK-2, DSK-3, PIK Region, 100 KGI and Podmoskovye 160 DSK. Since March 2008 he has also been appointed as First Vice President of PIK Group and also General Director of PIK-Yug, Rostovskoe More since March 2008. From 1999 to 2004 Mr. Kanaev was the General Director of Zhilstroyekspluatatsia (now PIK Comfort) and from 2000 to 2005 he was a member of the board of directors of Housing Finance Bank. From 1991 to 1996 he worked at the USSR Ministry of Foreign Economic Relations (Foreign Economic Organization Vneshintorg). He is a member of the Presidium of the Chamber of Commerce and Industry of the Moscow Region.

Mr. Kanaev graduated from the Moscow Economical Statistics Institute with a degree in Organization of Mechanized Economical Information Processing in 1993.

# Relevant Biographies

*Evgeny Luneev*

*Fedor Sapronov*



*Tatiana Tikhonova*

**Evgeny Luneev** has served as our Vice President, Economics and Finance, since August 2006 and as a member of our management board since March 2006. Mr Luneev is also a member of the board of directors of DSK-2 and PIK Region, a member of the Advisory Board of Storm Properties since November 2007. Since June 2007, he is also a member of the Board of Directors of PIK-Moskva. From 1999 to 2002 he worked as a senior accountant and lead accountant at Haliburton International Inc. in the oil and gas sector and from 2002 to 2003 Mr. Luneev worked as financial controller at the Sputnik Group investment bank. From 2003 to 2004 he acted as financial controller and from 2004 to 2006 as finance director at CJSC National Timber Company in the timber sector dealing with economics and finance matters.

Mr. Luneev graduated from the Moscow State Institute of International Relations with a degree in international economic relations in 1997 and also earned a Certified Public Accountant Certificate in the US.

**Fedor Sapronov** has served as the Director of our Legal Department since 2002 and as a member of our management board since March 2006. Mr. Sapronov is also Chairman of the board of directors of 160 DSK, a member of the board of directors of DSK-3 and PIK Region, a member of the Advisory Board of Storm Properties since November 2007 and a member of the Board of Directors of PIK-Moskva since June 2007. He has been employed by PIK since 1998. From 1995 to 1996 Mr. Sapronov worked for the military justice authorities and from 1996 to 1997 taught administrative, finance and civil law at the Russian Military University. From 1997 to 1998 he worked in the banking sector at Joint Stock Commercial Bank SBS AGRO. Mr. Sapronov is a member of a working group on the national project for Available and Comfortable Housing for Russian Citizens.

Mr. Sapronov graduated from the Military University of the Russian Ministry of Defense with a degree in jurisprudence in 1995.

**Tatiana Tikhonova** has served as our Vice President, Investments, since August 2006 and as a member of our management board since March 2006. Ms. Tikhonova is a member of the Advisory Board of Storm Properties since November 2007 and the General Director of PIK-Moskva since March 2008. Ms. Tikhonova has worked at PIK since 1994. She held the position of chief accountant from 1994 to 2003 and was director of our investment policy department in 2006. She is also a member of the board of directors of DSK-2 and DSK-3 and a member of the management board of PIK LLC and PIK Interior. Each of these companies is affiliated with PIK Group.

Ms. Tikhonova graduated from the Moscow Automobile and Road Institute with a degree in Economics and Organization of Motor Transport in 1983 and from the International Independent Environmental and Political Science University with a degree in jurisprudence in 2000.

*Will Andrich*

*Lee Timmins*

*Anselm Schmucki*

**Will Andrich** has served as our Director since March 2006. Mr. Andrich also serves as Chairman of our Audit Committee. Currently, Mr. Andrich is the president of Astor Capital Group. He has been working in international capital markets since 1997 in London, New York and San Francisco. From 1997 to 2000 Mr. Andrich worked at Morgan Stanley in the UK and the US, in 2001 at LCF Rothschild, a UK structured fund and from 2004 to 2005 at Savills, a UK investment and consultancy company.

Mr. Andrich graduated from the University of California at Berkeley with a Masters in Business Administration and is a CFA charterholder.

**Lee Timmins** has served as our Director since June 2006. Mr. Timmins also serves as Chairman of the Strategy Committee. Since 1987, Mr. Timmins has managed the implementation of projects in the US and Eastern Europe. He has worked for Hines since 1988 and has been the Head of the Hines Moscow Representative Office since 1993.

Mr. Timmins graduated from the University of Texas in Austin, Texas with a degree in Business Administration and from Southern Methodist University in Dallas, Texas with a Masters degree in Business Administration.

**Anselm Schmucki** has served as a Director since June 2006. Mr. Schmucki has eight years of experience in investment and finance at UBS and previously in teaching European law at the University of St. Gallen in Switzerland.

Mr. Schmucki graduated from the University of St. Gallen in 1997. His business address is 2/2 Paveletskaya Square, 115054 Moscow, Russian Federation.

Directors are elected for one-year terms. The current terms of the Directors expire on the date of our next annual general shareholders' meeting, which will take place in June 2008.

# Social Responsibility

**Concern for employees, environmental protection and charity are the key elements of PIK Group's social responsibility programme**

### Social Responsibility

Concern for employees, environmental protection and charity are the key elements of PIK Group's social responsibility programme. We place great importance on corporate training, occupational safety and health, contribution into sport and financial support for culture and the arts.

Our programme reflects a culture where the wellbeing of our employees is of primary concern. This ethos gives the Group a competitive advantage that allows it to attract the best employees, build strong relations with clients, partners and suppliers, as well as contribute into society's development.

The Group is actively building its social policy observing international Corporate Social Responsibility standards. PIK Group sees CSR as a means of making a contribution into sustainable economic development for bringing overall living standard to a higher level. The company aims to account for interests of all company stakeholders: clients, local communities, employees, investors and authorities of various levels.

### Social Programs for Employees

Each PIK employee is respected and valued. In 2006 the company adopted the 'Statement on guarantees to PIK Group employees', according to which each staff member has the right to participate in voluntary healthcare insurance and corporate fitness programs.

As a public company, PIK offer employees programs in healthcare and workplace safety, staff training and further training, sport development and cultural support in all regions of presence.

### Occupational Safety and Health

Employees' safety is the top priority at all enterprises of the PIK Group. Group companies use up-to-date safety equipment to prevent accidents. A number of health and occupational safety measures are implemented at the company's expense:

- all company premises are maintained to a good standard
- good sanitation and drinking water facilities are available
- employees are provided with certified special workwear and footwear in compliance with the standards established in Russian law
- company management organizes regular medical screenings for the employees; first-aid kits with modern, quality medicines are available at all workplaces
- introductory, initial, refresher, extra and special-purpose occupational safety and health training are offered at workplaces
- employees working under testing labour conditions are provided with additional 6 to 8 days off per annum
- employees working under testing labour conditions receive extra pay comprising 4-12% of their salary;
- employees are provided with cleaning and disinfection agents as required by current legislation.

### Environmental Protection

PIK Group considers environmental protection as a key priority. In this regard PIK Group rigorously observes the requirements of environmental laws and observes the environmental protection requirements of clients and other stakeholders. We always seek always to find ways in which to reduce the impact of our activities on the environment. During the construction of its projects, PIK Group observes all environmental standards and norms of the construction industry.

PIK Group strives for open dialogue with the public regarding environmental protection, prompt reaction to environmental claims and complaints from members of the public, public organizations and economic entities.

### Training and Human Resources

Staff training and development is a vital component in the success of PIK Group, and allows employees to work efficiently in complicated and changing business conditions. Therefore training is a priority, arranged in the following forms:

- corporate training programs (participation in seminars and conferences, advanced training).
- individual education programs (second university education, MBA programs, long-term and expensive advanced training courses).

The Company fully pays for corporate training programs, and compensates up to 80% of the cost of individual training.

### Charitable Work

PIK Group performs charity activities in the following areas:

- children and youth
- sport – healthy lifestyle promotion
- due respect to war veterans
- the future depends on us – environment improvement
- various regional social programs.

In 2007, PIK Group spent around $6 million on social programs and charity. The company sponsored the International Tchaikovsky Competition, the Arch Moscow exhibition, Multisport tennis tournament and the Boxing Against Drugs tournament (Omsk).

As the General Sponsor of the Kaliningrad city recreation and leisure park Yunost (Youth), PIK Group took an active part in the preparation of sport and cultural activities. The company sponsored the "My Vmeste" ("We are together") public event in Perm city. It also sponsors "Khimki" hockey club (Moscow Region) and "Dinamo Yantar" volleyball club (Kaliningrad).

The company regularly participates in social issue oriented conferences and events in the regions in which operates.

*'Nagatinskaya Embankment' development, Moscow*

# Appendix

# OAO Group of Companies PIK Consolidated Financial Statements for the year ended 31 December 2007

## Contents

ZAO KPMG
Naberezhnaya Tower Complex, Block C
18 Krasnopresnenskaya Naberezhnaya
Moscow 123317
Russie

Telephone +7 (495) 937 4477
Fax +7 (495) 937 4400/99
Internet www.kpmg.ru

## Independent Auditors' Report

The Board of Directors
OAO Group of Companies PIK

### Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of OAO Group of Companies PIK (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated balance sheet as at December 31 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 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 financial statements that are free from material misstatements, 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 relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

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

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

***Opinion***

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

ZAO KPMG

May 6 2008

| | Note | 2007 mln RUR | 2006 mln RUR |
|---|---|---|---|
| Revenue | 8 | 69 050 | 42 046 |
| Cost of sales | 9 | (51 206) | (32 265) |
| **Gross profit** | | **17 844** | **9 781** |
| Gain on disposal of development rights | 11 | 9 502 | 2 851 |
| Distribution expenses | 12 | (879) | (467) |
| Administrative expenses | 13 | (3 114) | (1 511) |
| Other income and expenses | 14 | (55) | 1 552 |
| Finance income | 15 | 569 | 571 |
| Finance expenses | 15 | (2 363) | (1 362) |
| Share of loss of equity accounted investees (net of income tax) | | (24) | (10) |
| **Profit before income tax** | | **21 480** | **11 405** |
| Income tax expense | 16 | (3 595) | (3 305) |
| **Profit for the year** | | **17 885** | **8 100** |
| *Attributable to:* | | | |
| Shareholders of the Company | | 17 854 | 8 105 |
| Minority interest | | 31 | (5) |
| | | 17 885 | 8 100 |
| Basic and diluted earnings per share | 25 | 37.4 RUR | 17.8 RUR |

These consolidated financial statements were approved on May 6 2008:

Kirill V. Pisarev
President

Evgeny D. Luneev
Vice-President, Economics and Finance

The consolidated income statement is to be read in conjunction with the notes to and forming part of the consolidated financial statements.

| **ASSETS** | **Note** | **2007 mln RUR** | **2006 mln RUR** |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | 17 | 12 556 | 7 835 |
| Intangible assets | 18 | 21 213 | 4 088 |
| Investments in equity accounted investees | 19 | 3 419 | 3 744 |
| Other investments | 20 | 295 | 82 |
| Deferred tax assets | 21 | 112 | 60 |
| Other non-current assets | | 131 | 20 |
| **Total non-current assets** | | **37 726** | **15 829** |
| **Current assets** | | | |
| Inventories | 22 | 50 272 | 38 694 |
| Other investments | 20 | 3 376 | 2 043 |
| Assets held for sale | 11(c) | – | 2 300 |
| Income tax receivable | | 227 | 132 |
| Trade and other receivables | 23 | 18 096 | 5 522 |
| Cash and cash equivalents | 24 | 17 056 | 1 134 |
| **Total current assets** | | **89 027** | **49 825** |
| **Total assets** | | **126 753** | **65 654** |
| **EQUITY AND LIABILITIES** | | | |
| **Equity** | 25 | | |
| Share capital | | 30 843 | 28 530 |
| Additional paid-in capital | | 19 401 | |
| Reserve resulting from additional share issue | | (28 506) | (28 506) |
| Retained earnings | | 27 335 | 9 481 |
| **Total equity attributable to shareholders of the Company** | | **49 073** | **9 505** |
| Minority interest | | 1 266 | 426 |
| **Total equity** | | **50 339** | **9 931** |
| **Non-current liabilities** | | | |
| Loans and borrowings | 26 | 10 460 | 10 040 |
| Provisions | | 68 | 19 |
| Deferred tax liabilities | 21 | 8 006 | 4 461 |
| **Total non-current liabilities** | | **18 534** | **14 520** |
| **Current liabilities** | | | |
| Loans and borrowings | 26 | 24 180 | 13 983 |
| Trade and other payables | 28 | 32 706 | 26 176 |
| Provisions | 27 | 891 | 876 |
| Income tax payable | | 103 | 168 |
| **Total current liabilities** | | **57 880** | **41 203** |
| **Total liabilities** | | **76 414** | **55 723** |
| **Total equity and liabilities** | | **126 753** | **65 654** |

The consolidated balance sheet is to be read in conjunction with the notes to and forming part of the consolidated financial statements.

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| **OPERATING ACTIVITIES** | | |
| **Profit for the year** | **17 885** | **8 100** |
| *Adjustments for:* | | |
| Depreciation and amortisation | 777 | 676 |
| Foreign exchange loss/(gain), net | 300 | (341) |
| Loss on disposal of property, plant and equipment | 225 | 215 |
| Gain on disposals of development rights | (9 502) | (2 851) |
| Gain on disposal of available-for-sale financial assets | (229) | – |
| Negative goodwill on acquisition of subsidiaries and minority interests | 28 | (1 552) |
| Share of loss of equity accounted investees | 24 | 10 |
| Interest expense | 2 063 | 1 362 |
| Interest income | (340) | (231) |
| Income tax expense | 3 595 | 3 305 |
| **Operating profit before changes in working capital and provisions** | **14 826** | **8 693** |
| Increase in inventories | (9 122) | (1 818) |
| Increase in trade and other receivables | (10 805) | (184) |
| Increase/(decrease) in trade and other payables | 5 487 | (704) |
| Decrease in provisions | (4) | (74) |
| **Cash flows from operations before income taxes and interest paid** | **382** | **5 913** |
| Income taxes paid | (709) | (559) |
| Interest paid | (2 646) | (1 800) |
| **Cash flows (utilised by)/from operating activities** | **(2 973)** | **3 544** |
| **INVESTING ACTIVITIES** | | |
| Proceeds from disposal of property, plant and equipment | 28 | 51 |
| Interest received | 315 | 83 |
| Acquisition of property, plant and equipment | (3 623) | (2 838) |
| Acquisition of development rights and other intangible assets | (16 183) | (8 274) |
| Acquisition of equity accounted investees | – | (334) |
| Acquisition of minority interests | (15) | (11) |
| Loans advanced | (8 861) | (2 925) |
| Proceeds from sale of minority interests and development rights | 10 745 | 5 130 |
| Repayment of loans advanced | 6 809 | 2 022 |
| Acquisition of subsidiaries, net of cash acquired (note 7) | (2 412) | (1 094) |
| **Cash flows utilised by investing activities** | **(13 197)** | **(8 190)** |
| **FINANCING ACTIVITIES** | | |
| Proceeds from borrowings | 35 675 | 23 394 |
| Repayment of borrowings | (25 157) | (18 310) |
| Proceeds from share issue | 23 016 | – |
| Transactions with Majority Shareholders | (948) | – |
| **Cash flows from financing activities** | **32 586** | **5 084** |
| Net increase in cash and cash equivalents | 16 416 | 448 |
| Effect of exchange rate fluctuations on cash and cash equivalents | (185) | – |
| Cash and cash equivalents at beginning of year | 815 | 367 |
| **Cash and cash equivalents at end of year (note 24)** | **17 046** | **815** |

The consolidated statement of cash flows is to be read in conjunction with the notes to and forming part of the consolidated financial statements.

| | Attributable to shareholders of the Company | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Share capital** | **Additional paid-in-capital** | **Reserve resulting from additional share issue** | **Retailed earnings** | **Subtotal** | **Minority interest** | **Total equity** |
| **Balance at January 1 2006** | **28 530** | **–** | **(28 506)** | **1 376** | **1 400** | **477** | **1 877** |
| Profit and total recognised income and expense for the year | – | – | – | 8 105 | 8 105 | (5) | 8 100 |
| Acquisition of minority interests | – | – | – | – | – | (47) | (47) |
| Acquisition of subsidiaries (note 7) | – | – | – | – | – | 1 | 1 |
| **Balance at December 31 2006** | **28 530** | **–** | **(28 506)** | **9 481** | **9 505** | **426** | **9 931** |
| Profit and total recognised income and expense for the year | – | – | – | 17 854 | 17 854 | 31 | 17 885 |
| Proceeds from share issue, net of related costs (note 25) | 2 313 | 20 703 | – | – | 23 016 | – | 23 016 |
| Excess of consideration paid to Majority Shareholders to acquire interest in a subsidiary (note 7) | – | (598) | – | – | (598) | – | (598) |
| Consideration paid to Majority Shareholders to acquire subsidiaries (note 25) | – | (704) | – | – | (704) | – | (704) |
| Dilution of minority interest in a subsidiary | – | – | – | – | – | (15) | (15) |
| Acquisition of subsidiaries (note 7) | – | – | – | – | – | 819 | 819 |
| Increase in minority interest due to shares disposed of | – | – | – | – | – | 5 | 5 |
| **Balance at December 31 2007** | **30 843** | **19 401** | **(28 506)** | **27 335** | **49 073** | **1 266** | **50 339** |

The consolidated statement of changes in equity is to be read in conjunction with the notes to and forming part of the consolidated financial statements.

# 1 Background

### (a) Organisation and operations

OAO Group of Companies PIK (the “Company”) and its subsidiaries (together referred to as the “Group”) includes closed and open joint stock companies and limited liability companies incorporated under requirements of the Civil Law of the Russian Federation and entities registered in Cyprus and in the British Virgin Islands.

The Company was established as a privately owned enterprise in 1994. The Company’s registered office is 19 Barrikadnaya st., Moscow, 123001, Russian Federation.

The main activities of the Group are investing in development projects for construction of residential buildings and sales of real estate properties; construction services; production of construction materials, including concrete panels, window frames and other construction elements; mining, refining, concentration of sand and gravel and production of crushed stone and sand. During the years 2007 and 2006 the Group mostly operated in Moscow, Moscow region and other regions of Russia.

During 2006 and 2007, the Group was ultimately owned by two individuals, Kirill V. Pisarev and Yury V. Zhukov (the “Majority Shareholders”), who both have equal power to direct the operations of the Group at their own discretion and for their own benefit. They also have interests in a number of other businesses outside of the Group. Related party transactions are disclosed in note 32.

On June 1 2007 the Group completed listings on the London Stock Exchange (in the form of global depositary receipts), Russian Trading System (RTS) and Moscow Interbank Currency Exchange (MICEX) in Russia. On July 2 2007 the over-allotment option was partially exercised by the underwriters. As a result of the above transactions, Mr. Zhukov and Mr. Pisarev own 84% of the outstanding shares in equal proportions, and the remainder represents free floating shares.

### (b) Russian business environment

The Russian Federation has been experiencing political and economic change that has affected, and may continue to affect, the activities of enterprises operating in this environment. Consequently, operations in the Russian Federation involve risks that typically do not exist in other markets. The consolidated financial statements reflect management’s assessment of the impact of the Russian business environment on the operations and the financial position of the Group. The future business environment may differ from management’s assessment.

# 2 Basis of preparation

### (a) Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRSs”).

### (b) Basis of measurement

The consolidated financial statements are prepared on the historical cost basis except that financial investments classified as available-for-sale are stated at fair value; property, plant and equipment was revalued to determine deemed cost as part of the adoption of IFRSs at January 1 2004; and the carrying amounts of non-monetary assets, liabilities and equity items in existence at December 31 2002 include adjustments for the effects of hyperinflation, which were calculated using conversion factors derived from the Russian Federation Consumer Price Index published by the Russian Statistics Agency, GosKomStat. Russia ceased to be hyperinflationary for IFRS purposes as at January 1 2003.

### (c) Functional and presentation currency

The national currency of the Russian Federation is the Russian Rouble ("RUR"), which is the functional currency of the Company and its subsidiaries and the currency in which these consolidated financial statements are presented. All financial information presented in RUR has been rounded to the nearest million.

### (d) Use of judgments, estimates and assumptions

Management has made a number of judgments, estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these consolidated financial statements in conformity with IFRSs. Actual results may differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements is included in the following notes:

- Note 7 – Acquisition of subsidiaries;
- Note 9 – Cost of sales;
- Note 17 – Property, plant and equipment;
- Note 18(b) – Impairment of goodwill and other intangible assets;
- Note 27 – Provisions;
- Note 28 – Trade and other payables; and
- Note 31 – Contingencies.

## 3 Significant accounting policies

The significant accounting policies applied in the preparation of the consolidated financial statements are described in notes 3(a) to 3(s). These accounting policies have been consistently applied.

### (a) Basis of consolidation

#### *(i) Subsidiaries*

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

Acquisitions of controlling shareholdings in entities in which there is no integrated set of activities conducted and assets managed for the purpose of providing a return to investees, are accounted for as purchases of assets. The consideration paid for such companies (typically entities holding development rights) are allocated to the identifiable assets and liabilities based on their relative fair values. No minority interests, if any, are recognised.

#### *(ii) Special purpose entities*

The Group has established special purpose entities ("SPE"s) for the purpose of acquiring assets and holding investments. The Group does not have any direct or indirect shareholdings in these entities. A SPE is consolidated if, based on an evaluation of the substance of its relationship with the Group and the SPE's risks and rewards, the Group concludes that it controls the SPE. SPEs controlled by the Group were established under terms that impose strict limitations on the decision-making powers of the SPEs' management and that result in the Group receiving the majority of the benefits related to the SPEs' operations and net assets, being exposed to risks incident to the SPE's activities, and retaining the majority of the residual or ownership risks related to the SPE or its assets.

***(iii) Acquisitions from entities under common control***

Business combinations arising from transfers of interests in entities that are under the control of the Majority Shareholders are accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date that common control was established; for this purpose comparatives are restated. The assets and liabilities acquired are recognised at their book values as recognised in the individual financial statements of the acquiree. The components of equity of the acquired entities are added to the same components within Group equity except that any share capital of the acquired entities is recognised as part of share premium. Any cash paid for the acquisition is recognised directly in equity.

***(iv) Associates (equity accounted investees)***

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Associates are accounted for using the equity method. The consolidated financial statements include the Group's share of the income and expenses of equity accounted investees, after adjustments to align the accounting policies with those of the Group, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds its interest in an associate, the carrying amount of that interest (including any long-term investments) is reduced to nil and the recognition of further losses is discontinued, except to the extent that the Group has an obligation or has made payments on behalf of the investee.

***(v) Transactions eliminated on consolidation***

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

### (b) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising in translation are recognised in the income statement, except for differences arising on the translation of available-for-sale equity instruments.

### (c) Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity and debt securities, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

Accounting for finance income and expenses is discussed in note 3(o).

***(i) Held-to-maturity investments***

If the Group has the positive intent and ability to hold debt securities to maturity, then they are classified as held-to-maturity. Held-to-maturity investments are measured at amortised cost using the effective interest method, less any impairment losses.

***(ii) Available-for-sale financial assets***

The Group's investments in equity securities and certain debt securities are classified as available-for-sale financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses (see note 3(j)), and foreign exchange gains and losses on available-for-sale monetary items (see note 3(b)), are recognised directly in equity. When an investment is derecognised, the cumulative gain or loss in equity is transferred to the income statement.

***(iii) Other***

Other non-derivative financial instruments are measured at amortised cost using the effective interest method, less any impairment losses. Investments in equity securities that are not quoted on a stock exchange and where fair value cannot be estimated on a reasonable basis by other means are stated at cost less impairment losses.

**(d) Share capital**

Issued capital is stated at par value of shares issued adjusted for the effect of hyperinflation as described in note 25(a).

Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity, net of any tax effects.

**(e) Property, plant and equipment**

***(i) Recognition and measurement***

Items of property, plant and equipment, except for land, are measured at cost less accumulated depreciation and impairment losses. The cost of property, plant and equipment, other than construction in progress at January 1 2004, the date of transition to IFRSs, was determined by reference to its fair value at that date.

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

Gains and losses on disposal of property, plant and equipment are recognised net in "Other income and expenses" in the income statement.

***(ii) Subsequent costs***

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property, plant and equipment are recognised in the income statement as incurred.

***(iii) Depreciation***

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Group will obtain ownership by the end of the lease term. Land is not depreciated.

The estimated useful lives for the current and comparative periods are as follows:

- Buildings 20 to 60 years
- Plant and equipment 5 to 25 years
- Other fixed assets 5 to 20 years

Depreciation methods, useful lives and residual values are reassessed at the reporting date.

**(f) Intangible assets**

***(i) Goodwill***

Goodwill (negative goodwill) arises on the acquisition of subsidiaries, associates and joint ventures.

*Acquisitions prior to January 1 2004*

As part of its transition to IFRSs, the Group elected to restate only those business combinations that occurred on or after January 1 2004. In respect of acquisitions prior to January 1 2004, goodwill represents the difference between the Company's interest in a subsidiary's net identifiable assets on the date of transition and the cost of acquisition of that interest.

*Acquisitions on or after January 1 2004*

For acquisitions on or after January 1 2004, goodwill represents the excess of the cost of acquisition over the Group's interest in the net fair value of identifiable assets, liabilities and contingent liabilities of the acquiree. When the excess is negative (negative goodwill), it is recognised immediately in the income statement.

*Acquisitions of minority interests*

Goodwill arising on the acquisition of a minority interest in a subsidiary represents the excess of the cost of the additional investment over the carrying amount of the net assets acquired at the date of exchange.

*Subsequent measurement*

Goodwill is measured at cost less accumulated impairment losses. In respect of associates, the carrying amount of goodwill is included in the carrying amount of the investment.

***(ii) Development rights***

Expenditure on identifying land plots with the purpose of obtaining new development projects is recognised in the income statement as an expense as incurred.

Expenditure on obtaining development rights, necessary to start construction activities, are recognised in intangible assets if the projects are technically and commercially feasible and the Group has sufficient resources to accomplish the development of the projects.

The cost of development rights includes the cost of obtaining the right to lease a land plot and the cost of obtaining the registered permit to construct a specific property.

Capitalised development rights recognised on initial acquisition as intangible assets are measured at cost less accumulated impairment losses until the development starts. On commencement of construction such development rights are reclassified as construction-in-progress intended for sale, included in inventories.

When the Group does not act as a developer, but participates in projects in the capacity of an investor or co-investor, the cost of development rights contributed to such projects is recognised within inventories, refer note 3(h) below.

***(iii) Other intangible assets***

Other intangible assets, which are acquired by the Group and which have finite useful lives, are measured at cost less accumulated amortisation and impairment losses.

***(iv) Subsequent expenditure***

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including expenditure on internally generated goodwill and brands, is recognised in the income statement when incurred.

***(v) Amortisation***

Intangible assets, other than goodwill and development rights, are amortised on a straight-line basis over their estimated useful lives from the date the asset is available for use. The estimated useful lives of other intangible assets for the current and comparative periods are 3 – 10 years.

**(g) Leased assets**

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the leased assets are not recognised on the Group's balance sheet.

**(h) Inventories**

Inventories include construction work in progress when the Group acts in the capacity of a developer and the real estate is intended for sale, and prepayments made under investment and co-investment agreements for apartments intended for sale, raw materials, other work in progress and finished goods.

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

The costs of real estate properties under construction are determined on the basis of specific identification of their individual costs.

The costs of real estate property comprise costs of construction and other expenditure directly attributable to a particular development project, including finance costs. Where real estate property is not being actively developed, net rental and finance costs are taken to the income statement.

The Group enters into investment or co-investment agreements to develop residential buildings with local authorities. Such investment contracts may require that the Group for no consideration delivers certain properties to the local authorities upon completion of the construction or / and construct certain infrastructure facilities in exchange of the ability to develop the property. In such cases the construction costs are included in the total costs of construction of such buildings, when incurred. In addition the Group enters into agreements with local authorities to complete construction of certain residential properties where the apartments had been pre-sold by a predecessor developer to the general public; however, the construction was subsequently stopped due to insolvency of such predecessor developer or other similar reasons. When such contracts are negotiated with the local authorities as part of acquisition of certain development rights, and they cannot be assessed as onerous (as described in note 3(l)(ii)), the costs to complete the construction are included in the total costs of construction of properties which these development rights relate to.

The cost of inventories, other than construction work-in-progress intended for sale and prepayments for real estate properties intended for sale, is based on the weighted average cost formula and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. Cost of manufactured inventories and work in progress includes an appropriate share of overheads based on normal operating capacity.

Advances made under terms of co-investment contracts represent payments made by or assets transferred from the Group in its capacity of investor or co-investor to finance the construction of real estate, which is developed by a third party.

The Group's normal operating cycle for a construction project may exceed twelve months. Inventories are classified as current assets even when they are not expected to be realised within twelve months after the balance sheet date.

**(i) Assets held for sale**

The Group classifies a non-current asset as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. An asset held for sale is measured at the lower of its carrying amount and fair value less costs to sell. Assets classified as held for sale are not depreciated.

**(j) Impairment**

***(i) Financial assets***

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. An impairment loss in respect of an available-for-sale financial asset is calculated by reference to its fair value.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in the income statement. Any cumulative loss in respect of an available-for-sale financial asset recognised previously in equity is transferred to the income statement.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost and available-for-sale financial assets that are debt securities, the reversal is recognised in the income statement. For available-for-sale financial assets that are equity securities, the reversal is recognised directly in equity.

**(ii) Non-financial assets**

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, recoverable amount is estimated at each reporting date.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. 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. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit"). The goodwill acquired in a business acquisition, for the purpose of impairment testing, is allocated to cash-generating units that are expected to benefit from the synergies of the combination.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

**(k) Employee benefits**

***(i) Defined contribution plans***

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans, including Russia's State pension fund, are recognised in the income statement when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

***(ii) Short-term benefits***

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

**(l) Provisions**

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

***(i) Tax provisions***

The Group provides for tax risks including interest and penalties, when the tax becomes payable according to the effective laws and regulations. Such provisions are maintained, and updated if necessary, for the period over which the respective tax positions remain subject to review by the tax authorities. Upon expiry of the review period the provisions are released. Tax provisions are recognised as part of income tax expense or in another relevant line of the income statement.

***(ii) Onerous contracts***

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Group recognises any impairment loss on the assets associated with that contract.

As described in note 3(h), the Group enters into investment or co-investment agreements to develop residential buildings, the contracts may require that the Group deliver certain properties to the local authorities upon completion of the construction or / and construct certain infrastructure facilities in exchange of the ability to develop the property for no consideration. In addition the Group enters into agreements with local authorities to complete construction of certain residential properties where the apartments had been pre-sold by a predecessor developer to the general public; however, the construction was subsequently stopped due to insolvency of such predecessor developer or other similar reasons.

When such agreements cannot be directly attributable to any of the Group's projects and the agreements are assessed as onerous, a provision is recognised in the Group's consolidated financial statements when entering into the agreement to complete the construction. The provision is estimated based on the present value of estimated unavoidable net costs to complete the construction.

***(iii) Warranties***

A provision for warranties is recognised when the underlying products or services are sold. The provision is based on historical warranty data and a weighting of all possible outcomes against their associated probabilities.

**(m) Revenues**

***(i) Revenue from sale of real estate properties***

Revenues from sale of real estate properties comprise revenues from sale of standardised apartments, which are constructed without reference to a specific customer's request.

Revenue from the sale of real estate property is measured at the fair value of the consideration received or receivable, net of allowances and trade discounts, if any. Revenue is recognised when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible return of property can be estimated reliably, and there is no continuing management involvement with the property, and the amount of revenue can be measured reliably.

Transfers of risks and rewards vary depending on the individual terms of the contract of sale. For sales of real estate properties, transfer usually occurs when the respective building is approved by the State commission established by the local regulating authorities for acceptance of finished buildings ("State commission"). When contracts for sale of real estate are concluded after the State commission has accepted the construction of the respective building, revenue is recognised immediately.

Sales are recognised at prices valid at the date of concluding the sales contract, which may be significantly different from the prices as at the date when the sale is recognised.

***(ii) Revenue from construction services***

Revenue from construction services rendered is recognised in the income statement on a monthly basis in accordance with the actual volume of works completed. The stage of completion is assessed monthly and fixed in acts of completed works signed by the Group and the customer. The Group provides for estimated losses on uncompleted contracts in the period, in which such losses are identified.

There are certain construction projects, where one Group entity participates as an investor/co-investor while a third party acts as the developer. At the same time other Group entities may provide construction services to the developer. Revenues from construction services relating to such projects are recognised similarly to any construction services provided in the normal course of business, as described in the preceding paragraph. Sales of properties obtained as a result of investment/co-investment agreements with the developer are recognised in full. Although both types of revenues relate to one project, separate sales agreements are concluded. Accordingly revenues from sales of properties and revenues from the provision of construction services for the same real estate objects are accounted for separately.

***(iii) Other sales***

Revenue from the sale of construction materials is recognised in the income statement when significant risks and rewards of ownership have been transferred to the buyer.

**(n) Other expenses**

***(i) Lease payments***

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Contingent lease payments are accounted for by revising the minimum lease payments over the remaining term of the lease when the contingency no longer exists and the lease adjustment is known.

***(ii) Social expenditure***

To the extent that the Group's contributions to social programs benefit the community at large and are not restricted to the Group's employees, they are recognised in the income statement as incurred.

**(o) Finance income and expenses**

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income, gains on the disposal of available-for-sale financial assets, and foreign currency gains. Interest income is recognised as it accrues in the income statement, using the effective interest method. Dividend income is recognised in the income statement on the date that the Group's right to receive payment is established.

Finance expenses comprise interest expense on borrowings, unwinding of the discount on provisions, foreign currency losses and impairment losses recognised on financial assets. All borrowing costs are recognised in the income statement using the effective interest method, except for borrowing costs related to qualifying assets which are recognised as part of the cost of such assets.

Foreign currency gains and losses are reported on a net basis.

**(p) Income tax expense**

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognised for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax assets and liabilities, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

**(q) Earnings per share**

The Group presents basic earnings per share (EPS) data for its ordinary shares. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares. The Company has not issued any potential ordinary shares that may have a dilutive effect on EPS.

Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period.

**(r) Segment reporting**

A segment is a distinguishable component of the Group that is engaged either in providing related products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. Segment information is presented in respect of the Group's business and geographical segments. The business segments are determined based on the Group's management and internal reporting structure.

Inter-segment pricing is determined as agreed by the transacting parties and may not be on an arm's length basis.

Segment results, assets and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis. Unallocated items comprise mainly investments (other than investment property) and related revenue, loans and borrowings and related expenses, corporate assets (primarily the Company's headquarters) and head office expenses, and income tax assets and liabilities.

Segment capital expenditure is the cost incurred during the period to acquire property, plant and equipment, and intangible assets other than goodwill.

**(s) New Standards and Interpretations not yet adopted**

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at December 31 2007, and have not been applied in preparing these consolidated financial statements. Of these pronouncements, IFRS 8 Operating Segments potentially will have an impact on the Group's operations.

IFRS 8 Operating Segments introduces the "management approach" to segment reporting. IFRS 8 Operating Segments, which becomes mandatory for the Group's 2009 financial statements, will require the disclosure of segment information based on the internal reports regularly reviewed by the Group's Chief Operating Decision Maker in order to assess each segment's performance and to allocate resources to them. Currently the Group presents segment information in respect of its business and geographical segments (see note 6). The new Standard will not have any impact on the Group's financial position or performance. The Group plans to adopt this pronouncement when it becomes effective.

## 4 Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

### (a) Property, plant and equipment

The fair value of property, plant and equipment recognised as a result of a business combination is based on market values. The market value of property is the estimated amount for which a property could be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The market value of items of plant, equipment, fixtures and fittings is based on the quoted market prices for similar items.

In certain instances the market value of property, plant and equipment can not be estimated reliably because of specialised nature of the Group's property, plant and equipment which can not be sold on the open market other than as part of a continuing business. In the absence of the active market for similar items, the fair value of property, plant and equipment is primarily determined using depreciated replacement cost. This method considers the cost to reproduce or replace the property, plant and equipment, adjusted for physical, functional or economical depreciation, and obsolescence.

The depreciated replacement cost is estimated based on internal sources and analysis of the Russian and international markets for similar property, plant and equipment. Various market data is collected from published information, catalogues, statistical data and industry experts and suppliers of property, plant and equipment are contacted both in the Russian Federation and abroad. In addition to the determination of the depreciated replacement cost, cash flow testing is conducted in order to assess the reasonableness of depreciated replacement cost.

### (b) Intangible assets

The fair value of patents and trademarks acquired in a business combination is based on the discounted estimated royalty payments that have been avoided as a result of the patent or trademark being owned. The fair value of other intangible assets is based on the discounted cash flows expected to be derived from the use and eventual sale of the assets.

### (c) Inventories

The fair value of inventories, including real estate properties intended for sale under construction, acquired in a business combination is determined based on its estimated selling price in the ordinary course of business less the estimated costs of completion and sale, and a reasonable profit margin based on the effort required to complete and sell the inventories.

### (d) Investments in equity and debt securities

The fair value of financial assets at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets is determined by reference to their quoted bid price at the reporting date. The fair value of held-to-maturity investments is determined for disclosure purposes only.

### (e) Trade and other receivables

The fair value of trade and other receivables, excluding construction work in progress, is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

### (f) Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date. In respect of the liability component of convertible notes, the market rate of interest is determined by reference to similar liabilities that do not have a conversion option. For finance leases the market rate of interest is determined by reference to similar lease agreements.

## 5 Financial risk management

### (a) Overview

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk.

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk, and the Group's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Group's Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group. The Group's Audit Committee is assisted in its oversight role by Internal Audit. Internal Audit undertakes both regular and ad hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

### (b) Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and investment securities.

#### *(i) Sale of apartments to individuals*

The Group is not exposed to significant credit risk in connection with sales of apartments to individuals as such sales are undertaken only on a prepayment basis.

#### *(ii) Trade receivables from organisations*

The Group's exposure to credit risks is influenced mainly by the individual characteristics of each customer.

As at December 31 2007, 33% of the Group's trade and other receivables is attributable to one customer. As at December 31 2006 there was no significant concentration of credit risk in respect of receivables from customers.

The Group has established a credit policy under which each new customer is analysed individually for creditworthiness before the Group's standard payment and delivery terms and conditions are offered. These provide for penalties in the event of late payment. The Group's review includes external ratings, when available, and in some cases bank references.

In monitoring customer credit risk, customers are grouped according to their credit characteristics, including whether they are a governmental agency or commercial organisation, aging profile, maturity and existence of previous financial difficulties.

The Group does not require collateral in respect of trade and other receivables.

The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables and investments. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loss component established for groups of similar assets in respect of losses that have been incurred but not yet identified. The collective loss allowance is determined based on historical data of payment statistics for similar financial assets.

***(iii) Other investments***

The Group has established a formal procedure in relation to investments in other loans and equity securities available-for-sale. The procedure includes organisation of working groups which conclude on the feasibility of a potential investment. The working groups consist of representatives of major management bodies of the Group. The groups study legal, financial and economic implications of any suggested investment. Management does not expect any counterparty to fail to meet its obligations.

***(iv) Guarantees***

The Group's policy is to provide financial guarantees only to the Group's subsidiaries and related parties.

### (c) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

The liquidity risk is centrally managed for all subsidiaries of the Group. Management monitors the risks which the Group would face in the long-, medium- and short-term periods.

For the long-term prospective the Group analyzes five-year forecasts covering financial, operational and investing activities.

For the medium- and short-term periods, management considers the availability of different market instruments.

In addition, the Group monitors short- and medium-term maturities of its credit portfolio. It also considers replacement of existing instruments with more favorable facilities.

The Group maintains credit lines with a number of banks, which, at December 31 2007, totaled approximately RUR 20 000 million, to ensure sufficient liquidity levels are available on demand.

### (d) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Group's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

***(i) Currency risk***

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the Russian Rouble (RUR). The currency in which these transactions primarily are denominated is U.S. Dollars (USD).

Interest on borrowings is denominated in currencies that match the cash flows generated by the underlying operations of the Group, primarily RUR, but also USD. This provides an economic hedge and no derivatives are entered into.

***(ii) Interest rate risk***

Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the Group over the expected period until maturity.

***(iii) Other market price risk***

The Group does not enter into commodity contracts other than to meet the Group's expected usage and sale requirements; such contracts are not settled net.

### (e) Capital management

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Board of Directors monitors the return on capital. The Board of Directors also monitors the level of dividends to ordinary shareholders.

There were no changes in the Group's approach to capital management during the year.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

## 6 Segment reporting

### (a) Primary reporting format

The Group's primary segment reporting format is based on business segments. The Group comprises the following business segments:

- *Sale of real estate*: The implementation of developments planned and undertaken by the Group, including identification of investment opportunities, performance of feasibility studies, obtaining the necessary construction permits, carrying out construction of projects and performing project management activities, and marketing real estate projects to potential buyers.
- *Construction services*: Contracting activities, construction of concrete panels, assembly of prefabricated panel buildings and production of other construction materials.
- *Sale of construction materials and other activities*: The production and sale of raw materials, servicing and maintenance of residential properties and other activities.

### (b) Secondary reporting format

The Group's secondary segment reporting format is based on geographical segments.

The Group entities operate in two principal geographical areas, the Moscow Region, including Moscow City, and other regions in Russia. Prior to December 31 2006, the segment operating out of other regions was not identified as a reportable segment, as its revenue from sales to external customers and from transactions with other segments, results and assets were less than 10% of the Group's total revenue, results of operations and assets. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of the assets.

**Business segments**

| | Sale of real estate | | Construction services | | Sale of construction materials and other activities | | Eliminations | | Consolidated | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Mln RUR** | **2007** | **2006** | **2007** | **2006** | **2007** | **2006** | **2007** | **2006** | **2007** | **2006** |
| Revenue from external customers | 50 421 | 29 986 | 14 098 | 9 544 | 4 531 | 2 516 | – | - | 69 050 | 42 046 |
| Inter-segment revenue | – | 319 | 4 836 | 6 043 | 990 | 498 | (5 826) | (6 860) | - | - |
| **Total revenue** | **50 421** | **30 305** | **18 934** | **15 587** | **5 521** | **3 014** | **(5 826)** | **(6 860)** | **69 050** | **42 046** |
| Segment result | 23 175 | 11 270 | 155 | 754 | 334 | 356 | – | – | 23 664 | 12 380 |
| Unallocated expenses | | | | | | | | | (366) | (175) |
| Finance income | | | | | | | | | 569 | 571 |
| Finance expenses | | | | | | | | | (2 363) | (1 362) |
| Share of loss from equity accounted investees | | | | | | | | | (24) | (10) |
| Profit before income tax | | | | | | | | | 21 480 | 11 404 |
| Segment assets | 118 177 | 28 926 | 50 880 | 29 496 | 13 279 | 4 334 | (59 341) | (1 038) | 122 995 | 61 718 |
| Investments in equity accounted investees | | | | | | | | | 3 419 | 3 744 |
| Unallocated assets | | | | | | | | | 339 | 192 |
| **Total assets** | | | | | | | | | **126 753** | **65 654** |
| Segment liabilities | 28 816 | 874 | 42 514 | 24 705 | 7 008 | 2 530 | (44 673) | (1 038) | 33 665 | 27 071 |
| Unallocated liabilities | | | | | | | | | 42 749 | 28 652 |
| **Total liabilities** | | | | | | | | | **76 414** | **55 723** |
| Depreciation/amortisation, including impairment losses | 64 | 36 | 530 | 501 | 211 | 139 | – | – | 805 | 676 |
| Capital expenditure | 10 669 | 2 044 | 1 902 | 429 | 2 641 | 365 | – | – | 15 212 | 2 838 |

**Geographical segments**

| Mln RUR | Moscow and Moscow Region 2007 | Moscow and Moscow Region 2006 | Other Regions 2007 | Other Regions 2006 | Consolidated 2007 | Consolidated 2006 |
|---|---|---|---|---|---|---|
| Revenue from external customers | 60 993 | 39 854 | 8 057 | 2 192 | 69 050 | 42 046 |
| Segment assets | 101 814 | 51 627 | 21 181 | 10 091 | 122 995 | 61 718 |
| Capital expenditure | 14 161 | 2 723 | 1 051 | 115 | 15 212 | 2 838 |

## 7 Acquisition of subsidiaries

### (a) Acquisitions of subsidiaries in 2007

*OOO Foton GBI and OOO Foton ABZ*
In April 2007 the Group acquired a 100% interest in OOO Foton GBI and OOO Foton ABZ for a total consideration of RUR 1 037 million settled in cash. The main activity of the subsidiaries acquired is the production of concrete mix and reinforced concrete products at production facilities located in the Kaluga Region, Russia. The acquisition of these subsidiaries resulted in goodwill amounting to RUR 299 million. The goodwill arose on the acquisition mainly because of the limited supply of production facilities for the manufacture of concrete products in the region.

*Storm Properties Group*
In September 2007 the Group acquired 50% plus 1 share in Sturm Properties Limited, the parent company of the Storm Properties Group, for a consideration of RUR 1 347 million settled in cash. The Storm Properties Group is a leading developer operating in the commercial real estate segment in Russia. The purchase agreement provides for an option to acquire an additional 25% interest in the Storm Properties Group for a market price at the date of the transaction. The option vests in three years from the date of the acquisition and expires in two years from the vesting date. The acquisition of the Storm Properties Group resulted in goodwill amounting to RUR 591 million. The goodwill arose on the acquisition due to the well-established reputation of Storm Properties Group as a leading-edge company with exceptional innovation capabilities in the commercial estate segment.

*OAO 480 KZhI*
In July 2007 a related party of the Group acquired a 100% interest in OAO 480 KZhI for a consideration of RUR 639 million. In November 2007 the Group purchased from the related party the 100% interest in OAO 480 KZhI for a consideration determined in the independent internationally recognised appraisal company's report amounting to RUR 1 237 million settled in cash. Because the control of the related party over the acquiree was transitory, the acquisition of the company by the Group from the related party was not accounted for as a common control transaction. The transaction was accounted for as a business combination under IFRS 3 Business Combinations. The difference between the consideration paid by the Group and the consideration paid by the related party of RUR 598 million was recognised directly in equity. The acquisition of the subsidiary resulted in goodwill amounting to RUR 274 million.

*OAO Khromtsovsky Karier*
In May 2007 the Group obtained control over Khromtsovsky Karier, a sand pit, by acquiring an additional 25% interest for a consideration of RUR 32 million settled in cash. This acquisition increased the Group's interest from 48% to 73%. The acquisition of the subsidiary resulted in goodwill amounting to RUR 28 million. The goodwill was assessed for impairment as at June 30 2007 and an impairment loss of RUR 28 million was recognised as a result – refer note 14.

*OAO NovorosGragdanproekt*
In September 2007 the Group acquired a 57% interest in OAO NovorosGragdanproekt for a consideration of RUR 160 million settled in cash. The main activity of acquired entity is the provision of design and architectural services. The acquisition of the subsidiary resulted in goodwill amounting to RUR 78 million. The goodwill arose on the acquisition mainly due to the expected growth of the company's architectural and design expertise.

*Other disclosures*
The impact of acquiring the subsidiaries was to increase profit for the year by RUR 15 million.

Prior to the acquisition by the Group, the acquired subsidiaries prepared their financial statements in accordance with Russian accounting principles, which are, in certain respects, significantly different from IFRSs. Because the acquired subsidiaries did not prepare IFRS financial statements before they were acquired, it was impracticable to determine:

- the carrying amounts of the subsidiaries' assets and liabilities on an IFRS basis immediately prior to the date of acquisition;
- the Group's revenue and profit for the year had the acquisitions occurred on January 1 2007.

### (b) Acquisitions of subsidiaries in 2006

*ZAO Stroyinvestregion*
In March 2006 the Group acquired a 100% interest in ZAO Stroyinvestregion and its subsidiaries. In addition, the Group acquired 100% interests in four smaller entities from the same seller. The operations of these entities are closely related to the activities of ZAO Stroyinvestregion. The consideration of RUR 1 302 million was negotiated in total for all entities acquired. The main activity of acquired entities is investing in the development of residential housing mainly in Nizhny Novgorod, Rostov-on-Don, Perm, Yaroslavl, Kaliningrad and Omsk.

The acquisition of the entities resulted in negative goodwill amounting to RUR 1 517 million. The negative goodwill arose on the acquisition mainly because of the low bargaining power of the seller due to lack of alternative offers on the market whilst the seller required funds to finance other projects.

In November 2006 ZAO Stroyinvestregion merged with another Group entity, ZAO PIK Region.

*Other disclosures*
The impact of acquiring the subsidiaries was to increase profit for the year by RUR 8 million, excluding negative goodwill of RUR 1 517 million.

Prior to the acquisition by the Group, the acquired subsidiaries prepared their financial statements in accordance with the Russian accounting principles, which are, in certain respects, significantly different from IFRSs. Because the acquired subsidiaries did not prepare IFRS financial statements before they were acquired, it was impracticable to determine:

- the carrying amounts of the subsidiaries' assets and liabilities on an IFRS basis immediately prior to the date of acquisition;
- the Group's revenue and profit for the year had the acquisitions occurred on January 1 2006.

### (c) Purchase price allocation

Management engaged independent appraisers to perform purchase price allocations for the acquisitions of OOO Foton GBI and OOO Foton ABZ, Storm Properties Group, OAO 480 KZhI and ZAO Stroyinvestregion. Management used internal expertise to allocate the purchase price paid for OAO Khromtsovsky Karier and OAO NovorosGragdanproekt since the acquisitions do not have significant effect on these consolidated financial statements.

### (d) Effect on the financial statements

The acquisitions of the subsidiaries had the following effect on the Group's assets and liabilities at the dates of acquisitions:

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Intangible assets | 418 | – |
| Property, plant and equipment | 2 038 | 37 |
| Investments | 365 | 64 |
| Deferred tax assets | 5 | – |
| Inventories | 183 | 7 485 |
| Trade and other receivables | 526 | 228 |
| Cash and cash equivalents | 803 | 208 |
| Deferred tax liability | (447) | (913) |
| Loans and borrowings | (365) | (886) |
| Trade and other payables | (762) | (3 403) |
| **Net identifiable assets, liabilities and contingent liabilities** | **2 764** | **2 820** |
| Minority interest | ( 819) | (1) |
| Portion of consideration paid to a related party for the acquisition of the interest in OAO 480 KZhI (recognised in equity) | 598 | – |
| Goodwill on acquisition | 1 270 | (1 517) |
| **Consideration paid** | **3 813** | **1 302** |
| Cash acquired | (803) | (208) |
| **Net cash outflow** | **3 010** | **1 094** |

## 8 Revenue

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Revenues from sale of apartments | 50 421 | 29 986 |
| Revenues from construction services | 14 097 | 9 544 |
| Revenues from sale of construction materials and other sales | 4 532 | 2 516 |
| | 69 050 | 42 046 |

In 2007 the Group completed 81 buildings with a saleable area of 1 048 thousand square meters (2006: 63 buildings with a saleable area of 769 thousand square meters). Of the buildings completed in 2007, the Group sold 939 thousand square meters (2006: 682 thousand). In addition, approximately 53 thousand square meters were sold in 2007 in buildings completed in earlier periods.

Construction services in the amount of RUR 9 901 million (2006: RUR 5 567 million) were provided to developers of buildings where the Group participates as a co-investor.

## 9 Cost of sales

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Cost of construction | 34 311 | 16 998 |
| Salaries and wages | 5 347 | 4 368 |
| Materials | 4 855 | 3 478 |
| Overhead expenses | 4 724 | 5 347 |
| Depreciation and amortisation | 676 | 625 |
| Other | 1 293 | 1 449 |
| | 51 206 | 32 265 |

## 10 Total personnel costs

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Wages and salaries | 6 374 | 4 340 |
| Social charges | 1 148 | 821 |
| | 7 522 | 5 161 |

## 11 Gain on disposal of development rights

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Gain on disposal of shares in Mytischy project – note 11(a) | 5 764 | – |
| Gain on disposal of the right to develop Park City – note 11(b) | 3 363 | – |
| Gain on disposal of the right to develop real estate at Yubileiny district – note 11(c) | 375 | – |
| Gain on disposal of 70% in a development project at Mantulinskaya ul. – note 11(d) | – | 1 565 |
| Gain on disposal of 50% in a development project at Mantulinskaya ul. – note 11(e) | – | 1 286 |
| | 9 502 | 2 851 |

### (a) Gain on disposal of shares in Mytischy project

In December 2007 the Group entered into an agreement to sell, for a consideration of RUR 5 770 million, a 25% interest in Viniso Investments Limited, a subsidiary. This company was the parent company of a number of entities operating a project to develop residential housing in Mytischy, Moscow Region. The carrying amount of the minority interest disposed of amounted to RUR 6 million. The disposal of the minority interest resulted in a gain of RUR 5 764 million.

### (b) Gain on disposal of the right to develop Park City

As at December 31 2006 the Group owned a 25% interest in ZAO Park-City Investments Limited and OOO KRPT. The investments in ZAO Park-City Investments Limited and OOO KRPT are accounted for as equity accounted investees. The two entities effectively owned a 21% interest in Park City, a project to develop real estate property on a land plot located at Kutuzovsky Prospect, Moscow.

In addition, at December 31 2006 the Group also owned a 100% interest in ZAO Viktor which was a party to a co-investment agreement with a 15% share in the Park City project.

In 2007 ZAO Viktor transferred the right under the co-investment agreement to a Cyprus-based subsidiary and subsequently the Group sold a 75% interest in the subsidiary in two transactions for a total consideration of RUR 3 701 million. These transactions resulted in a decrease in the effective interest of the Group in the project to 25%. The carrying amount of the investment in the development right disposed of was RUR 338 at the date of disposal. The gain on disposal amounted to RUR 3 363 million. The outstanding balance of accounts receivable from the above transactions as at December 31 2007 amounted to RUR 2 455 million – refer to note 23.

**(c) Gain on disposal of the right to develop real estate at Yubileiny district**

At December 31 2006 assets held for sale comprised a 100% interest in an entity which owned the development rights for a land plot at Yubileiny District, Khimki, Moscow Region, including the land lease contract and the construction permit. The Group acquired the entity from a third party for a consideration of RUR 2 300 million with the intention of selling it to another developer; therefore, the development right was accounted for as an asset held for sale in the consolidated financial statements as at and for the year ended December 31 2006. In April 2007 the Group sold the interest in the legal entity to a third party for a consideration of RUR 2 675 million. The gain on disposal amounted to RUR 375 million.

**(d) Gain on disposal of 70% in a development project at Mantulinskaya ul.**

In June 2005 the Group acquired development rights through a purchase of 70% of the shares in a production plant which occupied two land plots located at Mantulinskaya ulitsa, Moscow. At the date of the acquisition substantially all activities of the plant had been relocated from the site. The legal entity leased the land plots for production purposes on a long-term basis. The acquisition was accounted for as a purchase of the right to lease the land plots. The Group had intentions to apply to the municipal authorities for permission to develop real estate on the land plots. At December 31 2005 the development rights had a carrying value of RUR 707 million.

In March 2006 the Group disposed of these development rights to a third party for RUR 2 272 million realizing a gain of RUR 1 565 million. The purpose of this disposal was to realize an immediate profit rather than to continue the development in the circumstances of constant disagreement with the plant's minority shareholders. At December 31 2006 the Group had outstanding accounts receivable of RUR 1 092 million in relation to this transaction, refer note 23.

**(e) Gain on disposal of 50% in a development project at Mantulinskaya ul.**

Later in 2006 the same third party acquired an additional 28% of the shares in the plant. The Group was offered to acquire the 98% of the shares in the plant for a consideration of RUR 5 326 million. The transaction was accounted for as an acquisition of assets. At December 31 2006 the Group had outstanding accounts payable to the seller of RUR 1 057 million – refer note 27.

In December 2006 the Group sold a 50% shareholding in the project for a consideration of RUR 3 950 million with a resulting gain of RUR 1 286 million in order to finance future construction activities. As at December 31 2006 and 2007 the Group's effective interest in the project of 49% was classified as an investment in an equity accounted investee – refer note 19.

## 12 Distribution expenses

| | 2007<br>mln RUR | 2006<br>mln RUR |
|---|---|---|
| Advertising expenses | 622 | 297 |
| Other | 257 | 170 |
| | 879 | 467 |

## 13 Administrative expenses

| | 2007<br>mln RUR | 2006<br>mln RUR |
|---|---|---|
| Wages and salaries | 2 127 | 766 |
| Professional services | 348 | 245 |
| Other administrative expenses | 639 | 500 |
| | 3 114 | 1 511 |

## 14 Other income and expenses

| | 2007<br>mln RUR | 2006<br>mln RUR |
|---|---|---|
| *Other income* | | |
| Negative goodwill (note 7) | – | 1 517 |
| Negative goodwill resulting from acquisition of minorities | – | 35 |
| **Total other income** | **–** | **1 552** |
| *Other expenses* | | |
| Loss on impairment of property, plant and equipment | (27) | – |
| Loss on impairment of goodwill (note 7) | (28) | – |
| **Total other expenses** | **(55)** | **–** |

## 15 Finance income and expenses

| | 2007<br>mln RUR | 2006<br>mln RUR |
|---|---|---|
| *Finance income* | | |
| Interest income | 340 | 231 |
| Gain on the disposal of available-for-sale financial assets | 229 | – |
| Foreign exchange gains | – | 340 |
| | 569 | 571 |
| *Finance expenses* | | |
| Interest expense | (2 063) | (1 362) |
| Foreign exchange losses | (300) | – |
| | (2 363) | (1 362) |

In addition to borrowing costs recognised as an expense in the current year, interest in the amount of RUR 626 million (2006: RUR 1 208 million) has been capitalised as part of construction work-in progress intended for sale.

## 16 Income tax expense

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Current tax expense | | |
| Current year | (544) | (591) |
| Tax provision (note 27) | – | (501) |
| | (544) | (1 092) |
| Deferred tax expense | | |
| Origination and reversal of temporary differences | (3 051) | (2 213) |
| | (3 595) | (3 305) |

The Group's applicable tax rate is the corporate income tax rate in the Russian Federation of 24% (2006: 24%). The subsidiaries domiciled in Cyprus are taxed at a rate of 10% (2006: 10%).

Reconciliation of effective tax rate:

| | 2007 mln RUR | % | 2006 mln RUR | % |
|---|---|---|---|---|
| Profit before income tax | 21 480 | 100 | 11 405 | 100 |
| Income tax expense at applicable tax rate | (5 155) | (24) | (2 737) | (24) |
| Effect of income taxed at lower rates | 2 288 | 11 | 316 | 3 |
| Non taxable income | – | – | 765 | 7 |
| Non-deductible expenses | (728) | (3) | (1 148) | (10) |
| Tax provision | – | – | (501) | (4) |
| | (3 595) | (16) | (3 305) | (28) |

## 17 Property, plant and equipment

| mln RUR | Buildings | Plant and equipment | Other fixed assets | Construction in progress | Total |
|---|---|---|---|---|---|
| *Cost / Deemed cost* | | | | | |
| Balance at January 1 2006 | 3 040 | 2 587 | 602 | 350 | 6 579 |
| Acquisitions through business combinations | 11 | 7 | 2 | 17 | 37 |
| Additions | – | 14 | – | 2 824 | 2 838 |
| Disposals | (115) | (91) | (83) | (51) | (340) |
| Reclassifications | 131 | 341 | 248 | (720) | – |
| Balance at December 31 2006 | 3 067 | 2 858 | 769 | 2 420 | 9 114 |
| Acquisitions through business combinations | 1 647 | 334 | 52 | 5 | 2 038 |
| Additions | – | 60 | – | 3 652 | 3 712 |
| Disposals | (142) | (140) | (63) | (43) | (388) |
| Reclassifications | 2 574 | 899 | 1 181 | (4 654) | – |
| Balance at December 31 2007 | 7 146 | 4 011 | 1 939 | 1 380 | 14 476 |

## 17 Property, plant and equipment *(continued)*

| mln RUR | Buildings | Plant and equipment | Other fixed assets | Construction in progress | Total |
|---|---|---|---|---|---|
| *Accumulated depreciation and impairment losses* | | | | | |
| Balance at January 1 2006 | (190) | (388) | (101) | – | (679) |
| Depreciation charge | (163) | (380) | (132) | – | (675) |
| Disposals | 41 | 18 | 16 | – | 75 |
| Balance at December 31 2006 | (312) | (750) | (217) | – | (1 279) |
| Impairment losses | – | (27) | – | – | (27) |
| Depreciation charge | (172) | (421) | (183) | – | (776) |
| Disposals | 26 | 93 | 43 | – | 162 |
| Balance at December 31 2007 | (458) | (1 105) | (357) | – | (1 920) |
| *Net book value* | | | | | |
| At January 1 2006 | 2 850 | 2 199 | 501 | 350 | 5 900 |
| At December 31 2006 | 2 755 | 2 108 | 552 | 2 420 | 7 835 |
| At December 31 2007 | 6 688 | 2 906 | 1 582 | 1 380 | 12 556 |

### (a) Determination of deemed cost as at January 1 2004

Management commissioned an independent appraiser to determine the deemed cost of property, plant and equipment, other than construction in progress, of Group entities as at January 1 2004 in order to determine its deemed cost on the date of the Group's adoption of IFRSs. In addition to the determination of the depreciated replacement cost, cash flow testing was conducted in order to assess the reasonableness of these values. The results of cash flow testing did not result in adjustments to the fair values determined on the basis of depreciated replacement cost.

### (b) Security

At December 31 2007 property, plant and equipment with a carrying value of RUR 643 million (2006: RUR 1 830 million) was pledged to secure bank loans (refer note 26).

### (c) Leased plant and machinery

During the years ended December 31 2007 and 2006 the Group leased production equipment under a number of finance lease agreements. At the end of each of the leases the Group has the option to purchase the equipment at a beneficial price. At December 31 2007 the net book value of leased plant and machinery was RUR 483 million (December 31 2006: RUR 470 million). The leased equipment secures lease obligations.

### (d) Construction in progress

At December 31 2006 the balance of construction in progress includes prepayments made by the Group for the acquisition of property, plant and equipment, including a prepayment made in April 2006 to acquire a new office building in the amount of RUR 1 929 million. In 2007 the costs related to the new building were reclassified to buildings.

## 18 Intangible assets

| mln RUR | Goodwill | Development rights | Other intangible assets | Total |
|---|---|---|---|---|
| *Cost* | | | | |
| Balance at January 1 2006 | 1 765 | 2 319 | 3 | 4 087 |
| Additions | – | 7 036 | 2 | 7 038 |
| Disposals | – | (3 370) | – | (3 370) |
| Development rights reclassified as prepayments for construction work-in-progress, intended for sale | – | (1 001) | – | (1 001) |
| Reclassification into equity accounted investees (notes 0 and 19) | – | (2 663) | – | (2 663) |
| Balance at December 31 2006 | 1 765 | 2 321 | 5 | 4 091 |
| Acquisitions through business combinations | 1 270 | – | 418 | 1 688 |
| Additions | – | 16 076 | 1 | 16 077 |
| Impairment losses | (28) | – | – | (28) |
| Reclassification into construction work-in-progress | – | (611) | – | (611) |
| Balance at December 31 2007 | 3 007 | 17 786 | 424 | 21 217 |
| *Accumulated amortisation and impairment losses* | | | | |
| Balance at January 1 2006 | – | – | (2) | (2) |
| Amortisation charge | – | – | (1) | (1) |
| Balance at December 31 2006 | – | – | (3) | (3) |
| Amortisation charge | – | – | (1) | (1) |
| Balance at December 31 2007 | – | – | (4) | (4) |
| Net book value | | | | |
| At January 1 2006 | 1 765 | 2 319 | 1 | 4 085 |
| At December 31 2006 | 1 765 | 2 321 | 2 | 4 088 |
| At December 31 2007 | 3 007 | 17 786 | 420 | 21 213 |

### (a) Development rights

The cost of development rights includes the cost of obtaining rights to lease land plots and the cost of obtaining registered permits to construct specific properties. Capitalised development rights are measured at cost less accumulated impairment losses until construction starts. On commencement of construction, development rights are reclassified as construction in progress intended for sale as part of inventory.

In February 2007, the Group acquired a 92% shareholding in OAO “Kuskovsky Ordena ‘Znak Pocheta’ Chemical Plant” (KCP) for a consideration of RUR 3 567 million. KCP owns a land plot located in east of Moscow. Pursuant to an investment contract KCP has the right to develop residential premises with maximum saleable area of 188 100 square meters.

In May 2007 and later in June 2007 the Group obtained control over two legal entities that own rights to two projects located in Kaluga and Obninsk for a total consideration of RUR 9 million.

In June 2007 the Group acquired a 100% shareholding OOO “Veistoun” for RUR 1 018 million. The entity has an investment contract with the Moscow authorities for development of residential premises in the south of Moscow.

As a result of the acquisition of Sturm Properties Limited the Group has recognised promotion and development fees as part of intangible assets amounting to RUR 418 million (refer to note 7).

At December 31 2007 and 2006, the balances of development rights consisted of the following items:

| | **2007** | **2006** |
|---|---|---|
| | **’000 RUR** | **’000 RUR** |
| Moscow, South-East | 5 071 | 1 521 |
| Moscow, South | 1 848 | – |
| Moscow Region, Kaluga | 388 | – |
| Moscow Region, North-West | – | 611 |
| Moscow Region, North-East | 189 | 189 |
| Moscow region, North-West (Royal, Sivar, Project B) (*) | 2 794 | – |
| Moscow, South-east (Krasny Vostok) (*) | 1 030 | – |
| Moscow, South, South-East (Zavod Gazstroymash) (*) | 1 097 | – |
| Moscow region, South-West (Status-Land) (*) | 1 786 | – |
| Kaliningrad region, Svetlogorsk (Priz, Rash) (*) | 995 | – |
| Krasnodar region, Novorossisk (Semigor) (*) | 649 | – |
| Others (*) | 1 939 | – |
| | 17 786 | 2 321 |

(*) Investments in development rights represent investments in shares of a number of subsidiaries which own or rent on a long-term basis certain land plots. The Group intends to obtain permissions required for further development of the sites. The subsidiaries do not have any other significant assets, liabilities, revenues and profits or losses as at and for the year ended December 31 2007. Accordingly, the consideration paid by the Group to acquire the subsidiaries was accounted as the acquisition of interests in land rights under development rights.

### (b) Impairment testing of goodwill

For the purposes of impairment testing, goodwill is allocated to the Group’s cash generating units, which primarily comprise production plants or development companies. These units represent the lowest level within the Group at which the goodwill is monitored for internal management purposes.

At December 31 2007 and 2006, the aggregate carrying amounts of goodwill allocated to respective production plants or development companies are as follows:

| | **2007** | **2006** |
|---|---|---|
| | **’000 RUR** | **’000 RUR** |
| OAO DSK-3 | 1 721 | 1 721 |
| Storm Properties Limited | 591 | – |
| OOO Foton GBI and OOO Foton ABZ | 299 | – |
| OAO 480 KZHI | 274 | – |
| Goodwill attributable to other sites | 122 | 44 |
| | 3 007 | 1 765 |

The recoverable amount of OAO DSK-3 represents value in use as determined by discounting the future cash flows generated from the continuing use of this plant. At December 31 2007, the recoverable amount exceeded the carrying amount of net assets of the plant, including goodwill grossed up for the part attributable to minority interests.

There are no indications at December 31 2007 that goodwill arising on the acquisition of Storm Properties Limited and OAO 480 KZhI may be impaired.

The following key assumptions were used in determining recoverable amounts:

| | OAO DSK-3 | OOO Foton GBI and OOO Foton ABZ | OAO 480 KZHI | Storm Properties |
|---|---|---|---|---|
| Basis | 5 years plan | 5 years plan | 5 years plan | 4 years plan |
| Remaining useful life of major assets | 18 years | 20 years | 20 years | 5 year |
| Plant utilisation capacity | 85% | 100% | 86% | 100% |
| Discount rate | 15.3% | 15.3% | 17% | 25% |

The values assigned to the key assumptions represent management's assessment of future trends in the construction industry and are based on both external sources and internal sources (historical data).

The above estimates are not sensitive to the following assumptions:

- A 10% decrease in revenue would result in no significant impairment loss; and
- A 1% increase in the discount rate would result in no impairment loss.

## 19 Investments in equity accounted investees

At December 31 2007 and 2006 the Group had the following equity accounted investees:

| | Country | Voting and effective | 2007 mln RUR | 2006 mln RUR |
|---|---|---|---|---|
| ZAO Gorodskoe razvitye | Russia | 49% | 2 676 | 2 664 |
| ZAO Park-City Investments/ OOO KRPT (i) | Russia | 25%/50% | 743 | 1 080 |
| | | | 3 419 | 3 744 |

In 2005, the Group acquired stakeholdings in ZAO Park-City Investments /OOO Kompania Reabilitatsii Promyshlennykh Territoriy (OOO KRPT). The purchase price of RUR 747 million has not been allocated between the two entities. The Group's ownership of the acquired investments will allow the Group to participate in a co-investment agreement for development of two adjacent land plots close to Moscow City. As at the date of acquisition both legal entities had no activities, except for holding controlling interests in two production plants, which have the rights to lease the land plots. No significant activities took place in 2007 and 2006; however, the production facilities were in existence and will be relocated at the start of the construction.

As at December 31 2007 and 2006 the above equity accounted investees did not have any significant assets, liabilities, revenues, and profits or losses other than rights to develop real estate properties located at Mantulinskaya ul. and Park City land plot.

## 20 Other investments

| Note | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| *Non-current* | | |
| Available-for-sale equity investments | 242 | 8 |
| Loans receivable and promissory notes | 53 | 74 |
| | 295 | 82 |
| *Current* | | |
| Unsecured loan receivable from third party | 1 718 | – |
| Unsecured loans receivable from an entity controlled by the majority shareholders (RUR denominated, 10-11% per annum) | 895 | 1 033 |
| Other unsecured loans receivable from third parties | 454 | 147 |
| Other unsecured loans receivable from related parties | 121 | 147 |
| Promissory notes | – | 394 |
| Available-for-sale equity investments in ZAO Housing Finance Bank, a related party | – | 300 |
| Others | 188 | 22 |
| | 3 376 | 2 043 |

The Group has issued a loan amounting to RUR 1 718 million to a third party to secure the acquisition of land plots for further development purposes. The loan was denominated in USD and bore an interest of 8% per annum. After the potential acquisition was analyzed in detail the Group decided to partially withdraw from the transaction. Of the outstanding amount RUR 1 232 million was repaid to the Group. Since the repayment was made under a different loan agreement with a Cyprus-based subsidiary the repayment was accounted for as a loan received (refer note 26). The remaining amount represents the approximate fair value of the land plots under consideration. In case the potential acquisition is considered not feasible, the loan will be repaid before December 2008.

## 21 Deferred tax assets and liabilities

### (a) Recognised deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following items:

| mln RUR | Assets | | Liabilities | | Net | |
|---|---|---|---|---|---|---|
| | 2007 | 2006 | 2007 | 2006 | 2007 | 2006 |
| Property, plant and equipment | 26 | 31 | (941) | (578) | (915) | (547) |
| Investments | 10 | – | – | – | 10 | – |
| Intangible assets | – | – | (42) | – | (42) | – |
| Inventories | 853 | 221 | (461) | (1 182) | 392 | (961) |
| Trade and other receivables | 113 | 80 | (874) | (66) | (761) | 14 |
| Loans and borrowings | 50 | – | – | – | 50 | – |
| Trade and other payables | 114 | 200 | (6 753) | (3 146) | (6 639) | (2 946) |
| Tax loss carry-forwards | 11 | 39 | – | – | 11 | 39 |
| Tax assets/(liabilities) | 1 177 | 571 | (9 071) | (4 972) | (7 894) | (4 401) |
| Set off of tax | (1 065) | (511) | 1 065 | 511 | – | – |
| Net tax assets/(liabilities) | 112 | 60 | (8 006) | (4 461) | (7 894) | (4 401) |

## 21 Deferred tax assets and liabilities *(continued)*

### (b) Movement in temporary differences during the year

| mln RUR | January 1 2006 | Recognised in income | Acquired | December 31 2006 |
|---|---|---|---|---|
| Property, plant and equipment | (520) | (27) | – | (547) |
| Inventories | (86) | 24 | (899) | (961) |
| Trade and other receivables | 27 | (14) | 1 | 14 |
| Trade and other payables | (747) | (2 183) | (16) | (2 946) |
| Tax loss carry-forwards | 51 | (13) | 1 | 39 |
| | (1 275) | (2 213) | (913) | (4 401) |

| mln RUR | January 1 2006 | Recognised in income | Acquired | December 31 2007 |
|---|---|---|---|---|
| Property, plant and equipment | (547) | 28 | (396) | (915) |
| Investments | – | 10 | – | 10 |
| Intangible assets | – | – | (42) | (42) |
| Inventories | (961) | 1 396 | (3) | 392 |
| Trade and other receivables | 14 | (754) | (21) | (761) |
| Loans and borrowings | – | 50 | – | 50 |
| Trade and other payables | (2 946) | (3 713) | 20 | (6 639) |
| Tax loss carry-forwards | 39 | (28) | – | 11 |
| | (4 401) | (3 051) | ( 442) | (7 894) |

## 22 Inventories

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Construction work in progress, intended for sale | 29 508 | 17 521 |
| Prepayments for real estate property intended for sale | 12 142 | 15 953 |
| Raw materials and consumables | 1 607 | 1 320 |
| Work-in-progress | 1 276 | 864 |
| Finished goods and goods for resale | 5 739 | 3 036 |
| | 50 272 | 38 694 |
| Write-down of inventories in the current year | (111) | (23) |

At December 31 2007 and 2006 the balances of construction work in progress and finished goods include the cost of development rights in respect of which the construction process commenced before the respective dates.

At December 31 2007, inventory with a carrying value of RUR 8 149 million (2006: RUR 9 236 million) was pledged to secure bank loans (refer note 26).

## 23 Trade and other receivables

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Trade accounts receivable | 13 521 | 3 581 |
| Accounts receivable for disposal of development rights (note 11) | 2 455 | 1 092 |
| Taxes receivable | 442 | 338 |
| Others | 1 678 | 511 |
| | 18 096 | 5 522 |
| Cumulative impairment losses | (139) | (41) |

The Group's exposure to credit and currency risks and impairment losses related to trade and other receivables are disclosed in note 29(c).

## 24 Cash and cash equivalents

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| Petty cash | 26 | 22 |
| Bank balances, RUR denominated | 16 800 | 1 080 |
| Bank balances, USD denominated | 230 | 32 |
| Cash and cash equivalents in the balance sheet | 17 056 | 1 134 |
| Bank overdrafts | (10) | (319) |
| Cash and cash equivalents in the statement of cash flows | 17 046 | 815 |

The Group's exposure to interest rate risk and a sensitivity analysis for financial assets and liabilities are disclosed in note 29.

## 25 Equity

### (a) Share capital

The share capital of RUR 10 million was formed prior to December 31 2002, when the Russian economy was considered to be hyperinflationary for IFRS purposes. Therefore the balance of the share capital was adjusted for the effect of hyperinflation amounting to RUR 13 million. As a result, the carrying value of the share capital as at December 31 2004 amounted to RUR 23 million.

In December 2005 the Company registered an additional issue of 456 100 384 shares with a total nominal value of RUR 28 506 million. The additional shares were issued to the existing shareholders. For statutory purposes, the registration of the share issue was based on a notional valuation of investments in certain subsidiaries, which amounted to RUR 23 523 million. In addition, the shareholders contributed cash into the Company's share capital of RUR 4 983 million, which was made out of the Group's funds transferred to the shareholders with the sole purpose of being re-invested as part of the above capital transaction. As such, no additional asset values were transferred into the Group.

A negative reserve resulting from the additional issue of shares was recognised in these consolidated financial statements to eliminate the effect of the transfers of shares.

As a result of the additional share issue in December 2005, the number of the Company's ordinary shares increased without an increase in resources.

As at December 31 2007 the number of shares authorised for additional issue was 21 000 000. The par value of the Company's shares is RUR 62.5.

The number of shares issued and paid up was as follows:

| | Shares | | At nominal value in historic (uninflated) rubles | |
|---|---|---|---|---|
| | **2007** | **2006** | **2007** | **2006** |
| On January 1 | 456 260 384 | 456 260 384 | 28 516 | 28 516 |
| Issued in May 2007 | 37 000 000 | – | 2 313 | – |
| On December 31 | 493 260 384 | 456 260 384 | 30 829 | 28 516 |

In May 2007 the Company was admitted for listing on the London Stock Exchange (LSE), the Russian Trading System Stock Exchange (RTS) and the Moscow Interbank Currency Exchange (MICEX). As part of the initial public offering the Company issued 37 000 000 new shares with the par value of RUR 62.5 per share, and the existing shareholders sold 37 000 000 shares. The shares were offered and sold at USD 25 / RUR 646 per share.

The difference between the total consideration received by the Group (RUR 23 911 million), reduced by the amount of expenses incurred on issue (RUR 895 million), and the nominal value of the shares issued (RUR 2 313 million) of RUR 20 703 million was recognised as additional paid in capital.

**(b) Dividends**

In accordance with Russian legislation the Company's distributable reserves are limited to the balance of retained earnings as recorded in the Company's statutory financial statements prepared in accordance with Russian Accounting Principles. As at December 31 2007 the Company had retained earnings, including the profit for the current year, of RUR 27 335 million (2006: RUR 9 481 million).

**(c) Additional paid-in capital**

***(i) Acquisition of shares in subsidiaries***

During 2007 the Group acquired legal ownership over the shares in OOO PP Eksplit, OOO PIK Profile and OOO SPTK for consideration of RUR 704 million from a related party. Those subsidiaries have been included in the Group's consolidated financial statements in prior periods as the previous legal owners held the respective interests on behalf of the Group; therefore, the consideration payable under the sale and purchase agreement was recognised as a decrease in additional paid-in capital. On December 31 2007 the outstanding amount payable to the related party in respect of this transaction amounted to RUR 353 million.

The Majority Shareholders intend to return the consideration paid by the Group in 2008 – note 34.

***(ii) Acquisition of shares in OAO 480 KZHI***

The difference between the consideration paid by the Group and the consideration paid by the related party to acquire control over OAO 480 KZHI of RUR 598 million was recognised as a decrease in additional paid-in capital – refer note 7.

**(d) Earnings per share**

The calculation of earnings per share is based upon the profit for the year and the weighted average number of ordinary shares outstanding during the year, calculated as shown below. The Company has no dilutive potential ordinary shares.

| In thousands of shares | 2007 | 2006 |
|---|---|---|
| Issued shares at January 1 | 456 260 | 456 260 |
| Effect of shares issued in May 2007 | 21 583 | – |
| Weighted average number of shares for the year ended December 31 | 477 843 | 456 260 |

## 26 Loans and borrowings

This note provides information about the contractual terms of the Group's loans and borrowings. For more information about the Group's exposure to interest rate and foreign currency risk, refer note 29.

| | 2007 mln RUR | 2006 mln RUR |
|---|---|---|
| *Non-current* | | |
| Secured bank loans | 8 567 | 9 002 |
| Unsecured bank loans | 1 467 | – |
| Unsecured loans from third parties | 314 | 205 |
| Unsecured loans from related parties | 23 | 171 |
| Bonds, PIK-05 | – | 560 |
| Finance lease liabilities | 89 | 102 |
| | 10 460 | 10 040 |
| *Current* | | |
| Unsecured bank loans | 12 377 | 6 399 |
| Secured bank loans | 8 738 | 4 989 |
| Unsecured loans from third parties | 2 048 | 1 342 |
| Bonds, PIK-05 | 560 | 560 |
| Unsecured loans from related parties | 169 | 141 |
| Overdrafts from a related party bank | 9 | 176 |
| Bank overdrafts | 1 | 143 |
| Current portion of finance lease liability | 120 | 117 |
| Interest payable | 158 | 116 |
| | 24 180 | 13 983 |
| | 34 640 | 24 023 |

At December 31 2007 the following assets secure bank loans:

- property, plant and equipment with a carrying value of RUR 643 million (2006: RUR 1 830 million);
- inventory with a carrying value of RUR 8 149 million (2006: RUR 9 236 million);
- 1 747 081 shares of OAO DSK-3 representing 81% of the share capital, 30 629 943 shares of OAO DSK-2 representing 58% of the share capital), 10 016 shares in OAO 100 KGI representing 73% of the share capital), 10 000 shares in OAO NSS representing 100% of the share capital, 1 454 600 shares in OAO KHZ representing 92% of the share capital, 50 000 shares in OAO Avtorita Holdings Limited representing 100% of the share capital, 100% of the shares of OOO SPTK, 100% of the shares of OOO Stroyinvest, 100% of the shares of OOO Foton ZhBI, and 100% of the shares of OOO Monetchik.

**Terms and debt repayment schedule**

Terms and conditions of outstanding loans were as follows:

**2007**

| **mln RUR** | **Total** | **Under 1 year** | **1 – 5 years** | **Over 5 years** |
|---|---|---|---|---|
| *Secured bank loans:* | | | | |
| RUR – fixed at 8% – 10% | 15 578 | 8 189 | 7 389 | – |
| USD – fixed at 8% – 12% | 1 727 | 549 | 1 178 | – |
| *Unsecured bank loans* | | | | |
| RUR – fixed at 8% – 10% | 10 168 | 8 701 | 1 467 | – |
| USD – fixed at 5% – 12% | 3 676 | 3 676 | - | – |
| *Bonds, PIK-05* | | | | |
| RUR – fixed at 10.2% – 13% effective at 11.7% | 560 | 560 | – | – |
| *Unsecured loans from third parties* | | | | |
| RUR – fixed at 0%-2% | 483 | 371 | 31 | 81 |
| RUR – fixed at 5% – 7% | 200 | – | 200 | – |
| RUR – fixed at 10% – 15% | 120 | 120 | – | – |
| USD – fixed at 2% | 5 | 3 | 2 | – |
| USD – fixed at 3% | 1 228 | 1 228 | – | – |
| USD – fixed at 13% | 326 | 326 | – | – |
| *Unsecured loans from related parties* | | | | |
| RUR – fixed at 0% | 169 | 169 | – | – |
| RUR – fixed at 11% | 23 | – | 23 | – |
| *Overdrafts in related bank* | | | | |
| RUR – fixed at 14% | 9 | 9 | – | – |
| *Bank overdrafts* | | | | |
| RUR – fixed at 9% | 1 | 1 | – | – |
| | 34 273 | 23 902 | 10 290 | 81 |

**2006**

| **mln RUR** | **Total** | **Under 1 year** | **1 – 5 years** |
|---|---|---|---|
| *Secured bank loans* | | | |
| RUR – fixed at 8% – 12% | 13 500 | 4 498 | 9 002 |
| RUR – fixed at 12% – 15% | 440 | 440 | – |
| USD – fixed at 8% – 12% | 51 | 51 | – |
| | | | |
| *Unsecured bank loans* | | | |
| RUR – fixed at 8% – 12% | 3 239 | 3 239 | – |
| USD – fixed at 8% – 12% | 3 160 | 3 160 | – |
| | | | |
| Bonds, PIK-05 | | | |
| RUR – fixed at 10.2% – 13% effective at 11.7% | 1 120 | 560 | 560 |
| | | | |
| *Unsecured loans from third parties* | | | |
| RUR – fixed at 0% | 350 | 349 | 1 |
| RUR – fixed at 5% – 6% | 201 | – | 201 |
| RUR – fixed at 10% – 14% | 993 | 993 | – |
| USD – fixed at 2% | 3 | – | 3 |
| | | | |
| *Unsecured loans from related parties* | | | |
| RUR – fixed at 0% | 185 | 50 | 135 |
| RUR – fixed at 11% | 23 | – | 23 |
| USD – fixed at 3% | 104 | 91 | 13 |
| | | | |
| *Overdrafts in related bank* | | | |
| RUR – fixed at 11% – 13% | 176 | 176 | – |
| | | | |
| *Bank overdrafts* | | | |
| RUR – fixed at 14 % -16% | 141 | 141 | – |
| USD – fixed at 13%-15% | 2 | 2 | – |
| | 23 687 | 13 749 | 9 938 |

## 27 Provisions

The provision of RUR 891 million (2006: RUR 876 million) primarily consists of a provision for tax risks in respect of income tax of RUR 572 million and other taxes of RUR 304 million (December 31 2006: income tax of RUR 572 million and other taxes of RUR 304 million). The amount of provision includes interest and penalties and has not been subject to discounting.

## 28 Trade and other payables

| | 2007<br>mln RUR | 2006<br>mln RUR |
|---|---|---|
| Advances from customers | 12 372 | 16 975 |
| Provision for construction costs to complete | 6 821 | 842 |
| Accounts payable for construction works and other trade payables | 6 011 | 3 342 |
| Other taxes payable | 4 395 | 2 080 |
| Accounts payable for acquisition of development rights | – | 1 057 |
| Other payables | 3 107 | 1 880 |
| | 32 706 | 26 176 |

Estimated costs to complete projects relate to projects in respect of which revenue has been recognised. They consist principally of landscaping and infrastructure works and the construction of local amenities, such as schools, which the Group is obliged to build as one of the conditions for obtaining the development right. The scope and estimated costs of such works are subject to significant estimation uncertainty.

The Group's exposure to currency and liquidity risks related to trade and other payables is disclosed in note 29.

## 29 Financial instruments

Exposure to credit, interest rate and currency risk arises in the normal course of the Group's business.

### (a) Credit risk

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

| | Carrying amount | |
|---|---|---|
| **mln RUR** | **2007** | **2006** |
| Available-for-sale financial assets | 242 | 308 |
| Loans and receivables | 21 214 | 7 021 |
| Cash and cash equivalents | 17 056 | 1 134 |
| | 38 512 | 8 463 |

The Group does not require collateral in respect of financial assets. Credit evaluations are performed on all customers, other than related parties, requiring credit over a certain amount.

**Impairment losses**

The aging of trade receivables at the reporting date was:

| mln RUR | Gross 2007 | Impairment 2007 | Gross 2006 | Impairment 2006 |
|---|---|---|---|---|
| Not past due | 13 382 | – | 3 540 | – |
| Past due 0-30 days | – | – | - | - |
| Past due 31-120 days | – | – | - | - |
| More than one year | 139 | (139) | 41 | (41) |
| | 13 521 | (139) | 3 581 | (41) |

Based on historic default rates, the Group believes that no impairment allowance is necessary in respect of trade receivables not past due.

No impairment loss has been recognised in respect of available-for-sale financial assets or loans and receivables.

The allowance account in respect of trade receivables is used to record impairment losses unless the Group is satisfied that no recovery of the amount owing is possible; at that point the amounts considered irrecoverable and is written off against the financial asset directly.

**(b) Liquidity risk**

The following are the contractual maturities of financial liabilities, including estimated interest payments and excluding the impact of netting agreements:

| 2007 | Average interest rate | | 0-6 | 6-12 | | | | |
|---|---|---|---|---|---|---|---|---|
| mln RUR | Contractual | Effective | mths | mths | 1-2 yrs | 2-3 yrs | 3-4 yrs | Total |
| Secured bank loans | 8-10% | 8-10% | 4 851 | 3 887 | 7 396 | 1 171 | – | 17 305 |
| Bonds | 10-13% | 12% | 560 | | | | – | 560 |
| Finance lease liabilities | | 16-25% | 85 | 35 | 77 | 12 | – | 209 |
| Unsecured bank loans | 6-12% | 6-12% | 3 911 | 8 466 | 1 467 | – | – | 13 844 |
| Trade and other payables | | | 15 939 | – | – | – | – | 15 939 |
| Bank overdraft | 9-15% | 9-15% | 10 | – | – | – | – | 10 |
| | | | 25 356 | 12 388 | 8 940 | 1 183 | – | 47 867 |

| 2006 | Average interest rate | | 0-6 | 6-12 | | | | |
|---|---|---|---|---|---|---|---|---|
| mln RUR | Contractual | Effective | mths | mths | 1-2 yrs | 2-3 yrs | 3-4 yrs | Total |
| Secured bank loans | 8-10% | 8-10% | – | 4 989 | 5 489 | 2 342 | 1 171 | 13 991 |
| Unsecured bond issues | 10-13% | 12% | – | 560 | 560 | – | – | 1 120 |
| Finance lease liabilities | | 16-25% | 64 | 53 | 66 | 32 | 4 | 220 |
| Unsecured bank loans | 8-12% | 8-12% | – | 6 399 | – | – | – | 6 399 |
| Trade and other payables | | | 7 121 | – | – | – | – | 7 121 |
| Bank overdraft | 15% | 15% | 319 | – | – | – | – | 318 |
| | | | 7 504 | 12 001 | 6 115 | 2 374 | 1 175 | 29 169 |

### (c) Currency risk

***Exposure to currency risk***

The Group's exposure to foreign currency risk was as follows based on notional amounts:

| mln RUR | USD-denominated 2007 | USD-denominated 2006 |
|---|---|---|
| Cash | 230 | 32 |
| Short-term investments | 181 | – |
| Receivables | 2 755 | 104 |
| Payables | – | (1 058) |
| Loans and borrowings | (6 962) | (3 320) |
| Net | (3 796) | (4 242) |

The RUR/USD exchange rates at December 31 2007 and December 31 2006 were 24.55 and 26.33 respectively.

***Sensitivity analysis***

A 10% strengthening of the RUR against the USD at December 31 2007 and December 31 2006 would have increased equity and profit by RUR 383 million and RUR 424 million respectively. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2006.

A 10% weakening of the RUR against the above currencies at December 31 2007 and December 31 2006 would have had the equal but opposite effect to the amounts shown above, on the basis that all other variables remain constant.

### (d) Interest rate risk

***Profile***

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

| | Carrying amount | |
|---|---|---|
| mln RUR | 2007 | 2006 |
| *Fixed rate instruments* | | |
| Financial assets | 3 241 | 1 401 |
| Financial liabilities | (34 340) | (24 023) |
| | (31 099) | (22 622) |

***Fair value sensitivity analysis for fixed rate instruments***

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit or loss, and the Group does not designate derivatives (interest rate swaps) as hedging instruments under a fair value hedge accounting model. Therefore a change in interest rates at the reporting date would not affect profit or loss.

### (e) Fair values

At December 31 2007 and December 31 2006, the carrying values of the Group's financial assets and liabilities approximated their fair values. The basis for determining fair values is disclosed in note 4.

## 30 Commitments

### (a) Commitments under co-investment and construction services contracts

During 2007 and 2006 the Group entered into a number of co-investment contracts, where payments have not been made in full, and contracts to provide construction services. As at December 31 2007 commitments under these contracts totalled approximately RUR 221 570 million (2006: RUR 53 179 million). These payments also cover the costs to construct apartments or/and social infrastructure for municipal authorities.

### (b) Commitments to complete construction

At December 31 2007 the Group had contractual commitments with municipal authorities to complete the construction of residential buildings where the apartments had been sold to customers by a predecessor construction company, which due to insolvency or other similar reasons, has not completed the construction. As at December 31 2007 costs to complete such construction were estimated to be approximately RUR 967 million and will become a part of construction work in progress intended for sale (December 31 2006: RUR 600 million).

### (c) Commitments to acquire property, plant and equipment

At December 31 2007 the Group had no contractual commitments to acquire property, plant and equipment (December 31 2006: RUR 736 million).

## 31 Contingencies

### (a) Insurance

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

The Group has insured its property and equipment to compensate for expenses arising from accidents. The Group has also insured certain professional risks in relation to quality of construction works. The Group does not have full coverage for business interruption, or third party liability in respect of property or environmental damage arising from accidents on Group property or relating to Group operations.

The Group does not have insurance in respect of any force majeure circumstances, which may arise in relation to constructed buildings in the period after the sales have been recognised until the time when ownership rights are registered with the customer. The risk of damage in case of force majeure circumstances in these periods of time is borne by the Group.

Until the Group obtains full insurance coverage, there is a risk that the loss or destruction of certain assets and other circumstances could have a material adverse effect on the Group's operations and financial position.

**(b) Litigation**

The Group is involved in various claims and legal proceedings arising in the normal course of business. Management does not believe that the ultimate resolution of such matters will have a material adverse impact on the Group's operating results or financial condition.

**(c) Taxation contingencies**

***Taxation system***

The taxation system in the Russian Federation is relatively new and is characterised by frequent changes in legislation, official pronouncements and court decisions, which are often unclear, contradictory and subject to varying interpretation by different tax authorities. Taxes are subject to review and investigation by a number of authorities, which have the authority to impose severe fines, penalties and interest charges. A tax year remains open for review by the tax authorities during the three subsequent calendar years, however, under certain circumstances a tax year may remain open longer. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in their interpretation and enforcement of tax legislation.

These circumstances may create tax risks in the Russian Federation that are substantially more significant than in other countries. Management believes that it has provided adequately for tax liabilities based on its interpretations of applicable Russian tax legislation, official pronouncements and court decisions, refer note 27. However, the interpretations of the relevant authorities could differ and the effect on these consolidated financial statements, if the authorities were successful in enforcing their interpretations, could be significant.

***Tax compliance of the Group's suppliers***

The Group entered into transactions with various suppliers in which it did not hold any direct or indirect equity interest. These entities are fully responsible for their own tax and accounting compliance. However, due to existing tax authorities' practice, if these entities' tax compliance is challenged by the tax authorities as not being in full conformity with the applicable tax legislation, this may result in additional tax risks for the Group. Should these suppliers be successfully challenged, the Group may become liable to additional tax payments, although management of these entities is primarily responsible for the correctness and timeliness of the entities' tax payments. Management of the Group believes that it is not practicable to estimate the financial effect of potential tax liabilities, which ultimately could be imposed on the Group due to transactions with suppliers. However, if such liabilities were imposed, the amounts involved, including penalties and interest, could be material.

If the cases described above were successfully challenged by the Russian tax authorities, the additional payments could become due together with penalties, ranging from 20% – 40% of the amount of underpaid taxes, and late-payment interest. Management has not provided any amounts in respect of such obligations in these consolidated financial statements as it believes that it is possible, but not probable, that an outflow of economic benefits will be required to settle such obligations.

**(d) Warranties and guarantees for work performed**

The Group is contractually responsible for the quality of construction works performed subsequent to the date when the property is sold, which, in accordance with applicable law, is a period of up to three years from the date of the sale. Based upon prior experience with warranty claims, which have not been significant, no liabilities have been recognised in the consolidated financial statements in relation to warranties and guarantees for work performed.

### (e) Financial guarantees

As at December 31 2007 the Group had not provided any significant financial guarantees to entities outside the Group.

In December 2006, the Group provided a guarantee to a third party in relation to the loan of RUR 1 315 million granted by that third party to Bank ZhilFinans, the Group's related party. The loan bears variable interest rate of 8%-11% p.a. and matures in December 2007; however, the loan can become payable earlier if certain circumstances occur. The guarantee was granted at nil consideration.

## 32 Related party transactions

### (a) Control relationships

The Company is ultimately controlled by two individuals, refer note 1(a). IBG Development Group Incorporated and FMC Realtors Holding Incorporated, both registered in the British Virgin Islands, represent the two individual shareholders and each own approximately 42% of the Company's issued share capital.

### (b) Transactions with management and close family members

Key management and their close family members control 84% of the voting shares of the Company.

#### *(i) Management remuneration*

Key management received the following remuneration during the year, which is included in personnel costs (see note 10):

| | 2007<br>mln RUR | 2006<br>mln RUR |
|---|---|---|
| Salaries and bonuses | 111 | 59 |
| Contributions to State pension fund | 2 | 1 |
| | 113 | 60 |

#### *(ii) Other transactions*

As at December 31 2007 an interest-bearing loan to an executive director amounting to RUR 15 million (2006: RUR 15 million) was included in other investments (see note 20).

In November 2007 the Group acquired a 100% interest in OAO 480 KZHI for a consideration of RUR 1 237 million settled in cash from a related party of the Group, refer note 7.

In 2007 the Group entered into an agreement with a related party for construction of office premises. As at December 31 2007 an advance paid to the related party of RUR 89 million is included in the closing balance of property, plant and equipment.

### (c) Transactions with other related parties

The Group's other related party transactions, which are with entities controlled by the Majority Shareholders, are disclosed below.

***(i) Loans receivable from related parties***

At December 31 2007 the Group had an outstanding interest-bearing loan (11% per annum) receivable from a related party amounting to RUR 1 016 million (2006: RUR 1 180 million), which is included in other investments. The loan matures in December 2008 (refer note 20).

***(ii) Loans payable to related parties***

The outstanding balances of loans payable to related parties controlled by the shareholders of the Group at December 31 2007 and 2006 are disclosed in note 26.

***(iii) Accounts receivable from related parties***

During 2007 the Group sold its shares in Bank Zhilfinans to a related party, the outstanding balance of accounts receivable from this operation at December 31 2007 amounted to RUR 464 million.

***(iv) Accounts payable to related parties***

During 2007 the Group participated as a contractor in construction contracts with related parties and the outstanding balance of accounts payable from this operation at December 31 2007 amounted to RUR 1 510 million (2006: RUR 882 million). During 2007 the Group purchased through related party and capitalised the construction services in the cost of inventory in the amount of RUR 664 million.

At December 31 2007 the Group had an outstanding accounts payable amounting to RUR 353 million, refer note 25(c).

***(v) Transactions with Bank ZhilFinance***

A summary of transactions and balances of settlements with Bank ZhilFinance, is as follows:

| | 2007 | | 2006 | |
|---|---|---|---|---|
| **mln RUR** | **Transaction value** | **Outstanding balance** | **Transaction value** | **Outstanding balance** |
| Promissory notes | – | – | – | 18 |
| Loans payable | – | – | – | (26) |
| Loans received during the year | 61 | – | 1 041 | – |
| Loans repaid during the year | 87 | – | 1 334 | – |

The loans from Bank ZhilFinance bear interest of 14% per annum and are repayable upon demand.

***(vi) Transactions with related parties under co-investment agreements***

In June 2005 the Group entered into a co-investment agreement with a fellow subsidiary, controlled by the Group's shareholders, for development of a land plot in the center of Moscow. At December 31 2006 an amount of RUR 280 million is included in the balance of advances to constructors representing development rights for the plot, which are registered with a related party. In April 2007 this company was acquired by the Group.

In May 2005 the Group made a payment of RUR 1 464 million to its equity accounted investee, ZAO Park-City Investments, for the purpose of providing funds for commencement of development of a land plot in the center of Moscow. In 2006 ZAO Park-City Investments repaid RUR 1 393 million. At December 31 2007 the amount of RUR 71 million (2006: RUR 71 million) is included in the balance of advances to contractors, as the development rights for the plot are registered with a related party.

***(vii) Transactions with PSG Osnova***

During 2007 the Group has made payment of RUR 38.9 million to PSG Osnova under property insurance contract.

***(viii) Sales to and purchases from related parties***

During 2006 the Group entered into the following transactions with the same related party:

- the Group sold raw materials to a related party and collected revenues of RUR 63 million;
- the Group rendered processing services to the same related party for a commission of RUR 105 million;
- the Group bought finished goods from the same related party for consideration of RUR 190 million.

There were no similar significant transactions in 2007.

## 33 Significant subsidiaries

As of December 31 2007 the Group controlled 103 legal entities (December 31 2006: 57). Their assets, liabilities, revenues and expenses have been included in these consolidated financial statements. The following is a list of the most significant subsidiaries:

| | | Effective ownership | | Voting rights | |
|---|---|---|---|---|---|
| | Country of incorporation | 2007 | 2006 | 2007 | 2006 |
| ZAO Pervaya Ipotechnaya Kompanya-Region (PIK-Region) | Russia | 100% | 100% | 100% | 100% |
| OAO DSK-2 | Russia | 98% | 98% | 98% | 98% |
| OAO DSK-3 | Russia | 84% | 84% | 84% | 84% |
| OOO PIK-Development | Russia | 100% | 100% | 100% | 100% |
| OOO PIK-Invest | Russia | 100% | 100% | 100% | 100% |
| OAO 100 KGI | Russia | 92% | 92% | 92% | 92% |
| OOO MFS-PIK | Russia | 100% | 100% | 100% | 100% |
| OOO TD Osnova | Russia | 100% | 100% | 100% | 100% |
| OOO PIK Nerud | Russia | 100% | 100% | 100% | 100% |
| Viniso Investments Limited | Cyprus | 75% | – | 75% | – |
| OAO 480 KZHI | Russia | 100% | – | 100% | – |
| Sturm Properties Limited | Cyprus | 50% | – | 50% | – |

## 34 Events subsequent to the balance sheet date

In January 2008 the Group initiated a restructuring process with the view to establishing an organisational structure for the development operations on geographical basis. A number of new legal entities were established for this purpose to support the regional expansion of the Group's operations in certain Russian regions, the Ukraine and Kazakhstan.

In February 2008 the Group acquired a land plot in the city of Azov with an area of 2.6 hectares for a consideration of RUR 3 million. The Group intends to develop residential properties on this plot.

In February 2008 the Group acquired two land plots located in the city of Yaroslavl with an area of 88 hectares and in the Moscow Region (126 hectares) for a total consideration of RUR 2 768 million. The Group intends to develop real estate properties on these land plots.

In April 2008 the Group acquired a land plot in the south of Moscow with an area of 11 hectares. The Group intends to develop real estate properties on this land plot.

In April 2008 the Group received contributions from the Majority Shareholders in the amount of RUR 681 million as part of the transaction to acquire shares in subsidiaries – refer note 25(c)

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For additional information please contact:

Viktor Szalkay
Head of Investor Relations

Tel: +7(495) 505 9733
Email: ir@pik.ru
Bld1, 19 Barrikadnaya Street
Moscow 123242
Russia

www.pik.ru

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GROUP

www.pik.ru