Open Joint Stock Company Concern “Kalina” and subsidiaries

Independent Auditors’ Report

Consolidated Financial Statements
Year Ended December 31, 2006

OPEN JOINT STOCK COMPANY CONCERN “KALINA” AND SUBSIDIARIES

CONTENTS

STATEMENT OF MANAGEMENT’S RESPONSIBILITIES FOR THE PREPARATION AND APPROVAL OF THE CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEAR ENDED DECEMBER 31, 2006

The following statement, which should be read in conjunction with the independent auditors’ responsibilities stated in the independent auditor’s audit report set out on page 2, is made with a view to distinguishing the respective responsibilities of management and those of the independent auditors in relation to the consolidated financial statements Open Joint Stock Company Concern “Kalina” and subsidiaries (the “Group”).

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

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

Management is also responsible for:

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

The consolidated financial statements for the year ended December 31, 2006 were approved on March 15, 2007 by:

On behalf of the Management Board:

Timur Goryaev	**Alexander Petrov**
Chief Executive Officer	Chief Financial Officer

Deloitte.

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INDEPENDENT AUDITORS’ REPORT

To the Shareholders of OJSC Concern “Kalina”:

Report on the financial statements

We have audited the accompanying consolidated financial statements of OJSC Concern “Kalina”, which comprise of the balance sheet as at December 31, 2006, the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management’s responsibility

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

Auditor’s responsibility

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of OJSC Concern “Kalina” and subsidiaries as of December 31, 2006, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Deloitte & Touche

March 15, 2007

OPEN JOINT STOCK COMPANY CONCERN “KALINA” AND SUBSIDIARIES

INCOME STATEMENT
FOR THE YEAR ENDED DECEMBER 31, 2006

	Notes	Year ended 31/12/06 RUB’000	Year ended 31/12/05 RUB’000
Revenue	3	9,338,700	8,150,535
Cost of sales	4	(5,135,979)	(4,336,697)
Gross profit		4,202,721	3,813,838
Distribution expenses	5	(504,037)	(250,203)
Marketing expenses	5	(1,367,742)	(1,195,944)
Administration expenses	5	(1,606,773)	(1,462,133)
Finance costs, net	6	(141,209)	(67,717)
Gain on disposal of LLC Novoplast	22	27,441	-
Restructuring costs of Dr. Scheller	23	(85,086)	-
Foreign exchange gain/(loss)		17,920	(42,605)
Other losses, net		(779)	(1,895)
Profit before tax		542,456	793,341
Income tax expense	7	(157,726)	(85,704)
Profit for the year from continuing operations		384,730	707,637
Discontinued operations			
Income/(loss) for the year from discontinued operations	22	32,463	(39,616)
Profit for the year		417,193	668,021
Attributable to:			
Equity holders of the parent		417,193	650,610
Minority interest		-	17,411
		417,193	668,021
Earnings per share			
From continuing and discontinued operations:			
Basic and diluted (rubles per share)	8	43	68
From continuing operations:			
Basic and diluted (rubles per share)		39	73

OPEN JOINT STOCK COMPANY CONCERN "KALINA" AND SUBSIDIARIES

BALANCE SHEET
FOR THE YEAR ENDED DECEMBER 31, 2006

	Notes	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
ASSETS			
Non-current assets			
Property, plant and equipment	10	2,816,160	2,692,380
Goodwill	12	217,121	71,062
Other intangible assets	11	359,395	363,646
Long-term investments		29,012	69,158
Deferred tax assets	7	193,357	121,830
Total non-current assets		**3,615,045**	**3,318,076**
Non-current assets classified as held for sale	**9**	**153,335**	**143,991**
Current assets			
Inventories	15	1,834,188	2,410,314
Trade and other receivables	16	1,394,274	1,209,904
Advances paid to suppliers and prepaid expenses, net		184,194	323,964
Taxes recoverable	14	432,122	515,997
Short-term investments		-	2,860
Cash and bank balances	24	158,075	193,365
Total current assets		**4,002,853**	**4,656,404**
TOTAL ASSETS		**7,771,233**	**8,118,471**

BALANCE SHEET (CONTINUED)
FOR THE YEAR ENDED DECEMBER 31, 2006

	Notes	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
EQUITY AND LIABILITIES			
Capital and reserves			
Issued capital		851,843	851,843
Additional paid in capital		661,378	661,378
Translation reserve		(48,335)	(49,588)
Retained earnings		2,297,761	2,090,633
Equity attributable to equity holders of the parent		3,762,647	3,554,266
Minority interest		18,472	345,573
Total equity		**3,781,119**	**3,899,839**
Non-current liabilities			
Borrowings	17	455,106	472,853
Long-term obligations under finance lease	19	29,620	35,894
Retirement benefit obligation	20	127,995	173,694
Deferred tax liabilities	7	338,198	306,667
Total non-current liabilities		**950,919**	**989,108**
Liabilities directly associated with non-current assets classified as held for sale	9	**-**	**324,169**
Current liabilities			
Trade and other payables	18	1,440,297	1,521,527
Borrowings	17	1,464,770	1,246,079
Short-term obligations under finance lease	19	26,043	34,269
Taxes payable	14	108,085	103,480
Total current liabilities		**3,039,195**	**2,905,355**
Total liabilities		**3,990,114**	**4,218,632**
TOTAL EQUITY AND LIABILITIES		**7,771,233**	**8,118,471**

STATEMENT OF CHANGES IN SHAREHOLDERS’ EQUITY FOR THE YEAR ENDED DECEMBER 31, 2006

	Share Capital	Additional Paid in Capital	Translation reserve	Retained earnings	Total
	RUB’000	RUB’000	RUB’000	RUB’000	RUB’000
Balance at January 1, 2005	**851,843**	**661,378**	**-**	**1,584,261**	**3,097,482**
Exchange differences arising on translation of foreign operations	-	-	(49,588)	-	(49,588)
Profit for the year	-	-	-	650,610	650,610
Payment of dividends*	-	-	-	(144,238)	(144,238)
Balance at December 31, 2005	**851,843**	**661,378**	**(49,588)**	**2,090,633**	**3,554,266**
Exchange differences arising on translation of foreign operations	-	-	1,253	-	1,253
Profit for the year	-	-	-	417,193	417,193
Payment of dividends*	-	-	-	(210,065)	(210,065)
Balance at December 31, 2006	**851,843**	**661,378**	**(48,335)**	**2,297,761**	**3,762,647**

* In May and September 2006, a dividend of 22 rubles per share (15 rubles per share in 2005) was paid to holders of fully paid ordinary shares.

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2006

	Notes	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Cash flows from operating activities			
Profit for the year before tax		542,456	793,341
Finance costs recognized in income statement		141,209	67,717
Gain on disposal of long-term investment		(87,076)	(4,626)
Loss on disposal of property, plant and equipment		1,476	42,980
Depreciation and amortization of non-current assets		306,524	183,821
Operating cash flow before movements in working capital		904,589	1,083,233
Movements in working capital			
Increase in trade and other receivables		(184,370)	(687,856)
Decrease/(increase) inventories		548,789	(890,508)
Decrease/(increase) in taxes receivable		12,348	(2,435)
Increase/(decrease) in trade accounts payables		(51,476)	473,112
Decrease in retirement benefits obligation		(45,699)	(8,139)
Increase in taxes payable		4,605	24,789
Cash generated from operations		1,188,786	(7,804)
Interest paid		(139,905)	(89,278)
Income taxes paid		(157,726)	(189,529)
Net cash generated by/(used in) operating activities		891,155	(286,611)
Cash flows from investing activities			
Proceeds from sale of short-term investments, net		-	2,923
Acquisition of Dr. Scheller, net of cash acquired	13	-	(473,309)
Payments for additional shares in Dr. Scheller	13	(446,187)	-
Proceeds from part disposal of investment in Kit-Capital		27,140	14,888
Payments for property, plant and equipment		(434,188)	(884,343)
Proceeds from disposal of property, plant and equipment		1,969	1,141
Net cash used in investing activities		(851,266)	(1,338,700)
Cash flows from financing activities			
Proceeds from borrowings		2,274,001	2,919,925
Repayment of borrowings		(2,049,556)	(1,971,977)
Repayment of capital lease obligations		(41,223)	(56,095)
Dividends		(210,065)	(144,237)
Net cash used in/(generated by) financing activities		(26,843)	747,616
Net decrease in cash and cash equivalents		(35,290)	(926,951)
Cash and cash equivalents at the beginning of the financial year		**193,365**	**1,120,316**
Effects of exchange rate changes on the balance of cash held in foreign currencies		(48,336)	(49,256)
Cash and cash equivalents at the end of the financial year	**24**	**158,075**	**193,365**

1. GENERAL INFORMATION

OJSC Concern “Kalina” (hereinafter the “Company”), a Russian Open Joint Stock Company, was incorporated on December 12, 1992 as OJSC “Uralskiye Samotsveti” under the laws of the Russian Federation and renamed OAO Concern “Kalina” on November 30, 1999. The consolidated financial statements presented herein include the financial statements of the Company and its subsidiaries (hereinafter referred to jointly as “Operating Subsidiaries” or separately as “Operating Subsidiary” and, together with the Company, the “Group”).

Operating subsidiary	**Share of ownership**	**Place of incorporation**	**Principal Activity**
LLC Pallada Ukraina	100%	Ukraine	Trading
Kalina Overseas Holding B.V.	100%	Netherlands	Trading
Kalina International	100%	Switzerland	Management
Kalina Beauty	100%	Switzerland	Management
Kosmetik und Rasierwaren Solingen GmbH	100%	Germany	Trading
Dr. Scheller Cosmetics AG	87.55%	Germany	Trading
Dr. Scheller DuroDont GmbH	87.55%	Germany	Trading
Lady Manhattan Cosmetics GmbH	87.55%	Germany	Trading
Apotheker Scheller Naturmittel GmbH	87.55%	Germany	Trading
Premium Cosmetics GmbH	87.55%	Germany	Trading
Lady Manhattan Cosmetics GmbH	87.55%	Austria	Trading
Dr. Scheller Cosmetics Polska Sp. zo.o.	87.55%	Poland	Trading
Lady Manhattan Ltd.	87.55%	UK	Trading

The Company and its Operating Subsidiaries (collectively referred to as the “Group”) manufacture and sell a wide range of perfume, cosmetics and household products, primarily for the countries forming part of the Commonwealth of Independent States (“CIS”), and Germany.

As discussed in Note 13, the Group completed in April 2005 the acquisition of a controlling interest in Dr. Scheller Cosmetics AG Group (Dr. Scheller), a German perfume manufacturer and distributor. In June 2006 and December 2006, the Group further purchased 1,209,416 and 685,424 of 6,500,000 outstanding ordinary shares of that company respectively. At December 31, 2006, the Group owned 87.55% of Dr Scheller’s ordinary shares.

As discussed in Note 22, the Group disposed of its wholly owned subsidiary LLC Novoplast in 2006. The subsidiary was engaged in the production of plastic packaging for the Group.

As discussed in Note 22, in 2006 the Group disposed of its wholly owned subsidiary LLC Pallada Vostok, which had previously been identified as held for sale.

In December 2006 the Group management decided to dispose of its detergents manufacturing plant in Omsk (Russian Federation). The Manufacturing plant ceased production in June 2006. Net assets related to the Omsk manufacturing plant, property and equipment and inventory with a carrying value of RUB 153,335 thousand are separately disclosed as “Held For Sale” at December, 31 2006 (Note 9).

2. SIGNIFICANT ACCOUNTING POLICIES

The financial statements have been prepared in accordance with International Financial Reporting Standards. The financial statements have been prepared on the historical cost basis. The principal accounting policies are set out below.

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

The results of subsidiaries acquired or disposed of during the year are included in the consolidated income statement from the effective date of acquisition or up to the effective date of disposal, as appropriate.

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

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

Minority interests in the net assets (excluding goodwill) of consolidated subsidiaries are identified separately from the Group’s equity therein. Minority interests consist of the amount of those interests at the date of the original business combination (see below) and the minority’s share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority’s interest in the subsidiary’s equity are allocated against the interests of the Group except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

Business combinations – Acquisitions of subsidiaries and businesses are accounted for using the purchase method. The cost of the business combination is measured as the aggregate of the fair values (at the date of exchange) of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for control of the acquiree, plus any costs directly attributable to the business combination. The acquiree’s identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 Business Combinations are recognized at their fair values at the acquisition date, except for non-current assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations, which are recognized and measured at fair value less costs to sell.

Goodwill arising on acquisition is recognized as an asset and initially measured at cost, being the excess of the cost of the business combination over the Group’s interest in the net fair value of the identifiable assets, liabilities and contingent liabilities recognized. If, after reassessment, the Group’s interest in the net fair value of the acquiree’s identifiable assets, liabilities and contingent liabilities exceeds the cost of the business combination, the excess is recognized immediately in profit or loss.

The interest of minority shareholders in the acquiree is initially measured at the minority’s proportion of the net fair value of the assets, liabilities and contingent liabilities recognized.

Additional equity interests in subsidiaries – Acquisitions of additional equity interest in entities that are already controlled are accounted for using the purchase method. At each date when additional equity interest is acquired, the cost of the shares acquired is measured as the cumulative aggregate of the fair values (at the date(s) of exchange) of assets given, liabilities incurred or assumed, and equity instruments issued by the Group in exchange for additional equity shares of subsidiary, plus any costs directly attributable to the transaction.

At the date of each purchase, the Group recognizes increase\decrease in the value of the subsidiary's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 Business Combinations attributable to additional equity interest acquired and based on the fair values of these assets and liabilities as of the date of the transaction, except for non-current assets (or disposal groups) that are classified as held for sale in accordance with IFRS 5 Non-current Assets Held for Sale and Discontinued Operations, which are recognized and measured at fair value less costs to sell.

The difference between the excess of the cost of consideration paid over the Group's additional interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of subsidiary's recognized as goodwill.

Goodwill – Goodwill arising on the acquisition of a subsidiary or a jointly controlled entity represents the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary or jointly controlled entity recognized at the date of acquisition. Goodwill is initially recognized as an asset at cost and is subsequently measured at cost less any accumulated impairment losses.

For the purpose of impairment testing, goodwill is allocated to each of the Group's cash-generating units expected to benefit from the synergies of the combination. Cash-generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognized for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary or a jointly controlled entity, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Non-current assets held for sale – Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable and the asset (or disposal group) is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within one year from the date of classification.

Non-current assets (and disposal groups) classified as held for sale are measured at the lower of their previous carrying amount and fair value less costs to sell.

Revenue recognition – Revenue is measured at the fair value of the consideration received or receivable. Revenue is reduced for estimated customer returns, rebates and other similar allowances.

Sale of goods – revenue from the sale of goods is recognized when all the following conditions are satisfied:

- The Group has transferred to the buyer the significant risks and rewards of ownership of the goods;
- The Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to the entity; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

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

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

The Group as lessee – Assets held under finance leases are initially recognized as assets of the Group at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalized. Contingent rentals are recognized as expenses in the periods in which they are incurred.

Foreign currencies – The individual financial statements of each group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each entity are expressed in Russian Rubles ('RUB'), which is the functional currency of the Company and the presentation currency for the consolidated financial statements.

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

Exchange differences are recognized in profit or loss in the period in which they arise except for exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur, which form part of the net investment in a foreign operation, and which are recognized in the foreign currency translation reserve and recognized in profit or loss on disposal of the net investment.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are expressed in RUB using exchange rates prevailing at the balance sheet date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuated significantly during that period, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any, are classified as equity and transferred to the Group's translation reserve. Such exchange differences are recognized in profit or loss in the period in which the foreign operation is disposed of.

Goodwill and fair value adjustments arising on the acquisition of a foreign operation are treated as assets and liabilities of the foreign operation and translated at the closing rate.

Retirement benefit costs – Contributions to defined contribution retirement benefit plans are recognized as an expense when employees have rendered service entitling them to the contributions.

For defined benefit retirement benefit plans, the cost of providing benefits is determined using the Projected Unit Credit Method, with actuarial valuations being carried out at each balance sheet date. Actuarial gains and losses that exceed 10 per cent of the greater of the present value of the Group's defined benefit obligation and the fair value of plan assets are amortized over the expected average remaining working lives of the participating employees. Past service cost is recognized immediately to the extent that the benefits are already vested, and otherwise is amortized on a straight-line basis over the average period until the benefits become vested.

The retirement benefit obligation recognized in the balance sheet represents the present value of the defined benefit obligation as adjusted for unrecognized actuarial gains and losses and unrecognized past service cost, and as reduced by the fair value of plan assets. Any asset resulting from this calculation is limited to unrecognized actuarial losses and past service cost, plus the present value of available refunds and reductions in future contributions to the plan.

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

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

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

Deferred tax liabilities are recognized for taxable temporary differences associated with investments in subsidiaries and associates, and interests in joint ventures, except where the Group is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments and interests are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the liability is settled or the asset realized, based on tax rates (and tax laws) that have been enacted or substantively enacted by the balance sheet date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax for the period – Current and deferred tax are recognized as an expense or income in profit or loss, except when they relate to items credited or debited directly to equity, in which case the tax is also recognized directly in equity, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is taken into account in calculating goodwill or determining the excess of the acquirer's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities over cost.

Property, plant and equipment – Properties, plant and equipment are carried at cost, less any recognized impairment loss. Cost includes professional fees and, for qualifying assets, borrowing costs capitalized in accordance with the Group's accounting policy. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Fixtures and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses.

Depreciation is charged so as to write off the cost or valuation of assets, other than land and properties under construction, over their estimated useful lives, using the straight-line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

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

The overall useful economic lives of the assets for depreciation purposes are as follows:

Description	**Useful Life (years)**
Buildings	50
Machinery and equipment	10-15
Office equipment and other assets	5

Intangible assets

Intangible assets acquired separately – Intangible assets acquired separately are reported at cost less accumulated amortization and accumulated impairment losses. Amortization is charged on a straight-line basis over their estimated useful lives of 10 years for trademarks and licensed software. As described in note 11, intangible assets include trademarks with indefinite useful life. Amortization of intangible assets is included into other administrative expenses. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

Intangible assets acquired in a business combination – Intangible assets acquired in a business combination are identified and recognized separately from goodwill where they satisfy the definition of an intangible asset and their fair values can be measured reliably. The cost of such intangible assets is their fair value at the acquisition date.

Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortization and accumulated impairment losses, on the same basis as intangible assets acquired separately.

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

Intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually, and whenever there is an indication that the asset may be impaired.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in profit or loss.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognized immediately in profit or loss.

Inventories – Inventories are stated at the lower of cost and net realizable value. Costs, including an appropriate portion of fixed and variable overhead expenses, are assigned to inventories held by the method most appropriate to the particular class of inventory, with the majority being valued on a first-in-first-out basis. Net realizable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

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

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

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

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

Financial liabilities and equity instruments issued by the Group

Classification as debt or equity – Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments – An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments are recorded at the proceeds received, net of direct issue costs.

Other financial liabilities – Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

3. BUSINESS AND GEOGRAPHICAL SEGMENTS

Business segments

Products and services within each business segment – For management purposes, the Group is organized into four major operating divisions – cosmetics, tooth-paste, household chemical goods and other. These divisions are the basis on which the Group reports its primary segment information.

Segment revenues

	External sales		**Inter-segment**		**Total**	
	Year ended 31/12/06	**Year ended 31/12/05**	**Year ended 31/12/06**	**Year ended 31/12/05**	**Year ended 31/12/06**	**Year ended 31/12/05**
	RUB'000	**RUB'000**	**RUB'000**	**RUB'000**	**RUB'000**	**RUB'000**
Cosmetics	7,551,793	5,966,522	431,319	502,706	7,983,112	6,469,228
Tooth-paste	892,327	1,075,647	22,623	20,128	914,950	1,095,775
Household chemical goods	822,676	1,029,922	277,993	247,334	1,100,669	1,277,256
Other	71,904	78,444	8,148	14,438	80,052	92,882
Total of all segments	**9,338,700**	**8,150,535**	**740,083**	**784,606**	**10,078,783**	**8,935,141**

Segment result

	Year ended 31/12/06	**Year ended 31/12/05**
	RUB'000	**RUB'000**
Continuing operations		
Cosmetics	3,707,335	3,066,226
Tooth-paste	462,403	582,898
Household chemical goods	114,839	137,272
Other	104,751	27,442
Unallocated central overheads	(3,846,872)	(3,020,497)
Profit before tax	542,456	793,341
Income tax expense	(157,726)	(85,704)
Profit for the year from continuing operations	**384,730**	**707,637**

Segment assets

	Segment assets		Acquisition of segment assets	
	Year ended 31/12/06	Year ended 31/12/05	Year ended 31/12/06	Year ended 31/12/05
	RUB'000	RUB'000	RUB'000	RUB'000
Cosmetics	5,353,682	5,275,094	343,665	603,846
Tooth-paste	696,336	869,529	25,089	85,190
Household chemical goods	217,477	276,102	7,836	27,050
Other	340,422	409,374	12,266	40,107
Total of all segments	6,607,917	6,830,099	388,856	756,193
Unallocated assets	1,163,316	1,288,372	41,915	126,224
Consolidated	**7,771,233**	**8,118,471**	**430,771**	**882,417**

Geographical segments – The Group's four divisions operate in three principal geographical areas – CIS, Europe (primarily Germany) and Others (primarily Mongolia).

The Group's revenue from external customers and information about its segment assets by geographical location are detailed below:

	Revenue from external customers		Segment assets		Acquisition of segment assets	
	Year ended 31/12/06	Year ended 31/12/05	Year ended 31/12/06	Year ended 31/12/05	Year ended 31/12/06	Year ended 31/12/05
	RUB'000	RUB'000	RUB'000	RUB'000	RUB'000	RUB'000
CIS	7,138,069	6,138,115	6,014,193	6,383,705	280,001	795,382
Europe (primarily Germany)	2,200,631	1,787,507	1,757,040	1,734,766	150,770	87,035
Other (primarily Mongolia)	-	224,913	-	-	-	-
Total	**9,338,700**	**8,150,535**	**7,771,233**	**8,118,471**	**430,771**	**882,417**

Due to disposal of Uzbekistan subsidiary LLC Pallada Vostok, there are no sales to Mongolia in 2006.

4. COST OF SALES

Cost of sales includes salary expenses of RUB 748,199 thousands (2005: RUB 731,591 thousands) and raw materials of RUB 4,116,027 thousands (2005: RUB 3,367,504 thousands).

5. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Advertising expenses	1,349,066	1,154,923
Salaries and related taxes	1,029,612	818,161
Transportation expenses	430,009	215,607
Depreciation charge	204,050	161,181
Raw materials obsolescence expenses	154,663	167,951
Taxes, other than income tax	141,691	39,291
Warehouse expenses	77,004	34,596
Consulting expenses	18,676	41,021
Loss on disposal of fixed assets	1,476	42,980
Other	72,305	232,569
Total	**3,478,552**	**2,908,280**

6. FINANCE COSTS

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Interest expense	139,905	89,278
Interest income	(2,270)	(16,936)
Other	3,574	(4,625)
Total	**141,209**	**67,717**

7. INCOME TAXES

Income tax recognized in profit or loss

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Tax expense/(income) comprises:		
Current tax expense/(income)	188,599	157,823
Deferred tax income	(30,873)	(72,119)
Total tax expense	**157,726**	**85,704**

The total charge for the year can be reconciled to the accounting profit as follows:

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Income tax expense at the Company's statutory rates	121,110	190,402
Effect of different tax rates of subsidiaries operating in other jurisdictions	(3,120)	(4,017)
Other permanent differences	39,736	(100,681)
Income tax expense recognized in profit or loss	**157,726**	**85,704**

The Group provides for current taxes based on statutory financial statements maintained and prepared in local currencies and in accordance with local statutory regulations which differ significantly from IFRS. The Group was subject to a tax rate of 24% in Russia, 25% in Ukraine, and 38% in Germany in 2006 and 2005.

Deferred tax balances – Deferred tax balances are presented in the balance sheet as follows:

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Non-current deferred tax assets:		
Accrued expenses	154,749	88,008
Valuation of investments	38,608	33,822
Deferred tax assets	**193,357**	**121,830**
Non-current deferred tax liability:		
Valuation of non-current assets	(233,577)	(180,644)
Depreciation of PPE	(104,621)	(126,023)
Deferred tax liabilities	**(338,198)**	**(306,667)**

8. EARNINGS PER SHARE

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Basic and diluted earnings per share		
From continuing operations	384,730	707,637
From discontinued operations	32,463	(39,616)
Profit for the year	**417,193**	**668,021**

Basic and diluted earnings per share – The earnings and weighted average number of ordinary shares used in the calculation of basic and diluted earnings per share are as follows:

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Profit for the year attributable to equity holders of the parent	417,193	668,021

	Year ended 31/12/06 Shares	Year ended 31/12/05 Shares
Weighted average number of ordinary shares for the purposes of basic and diluted earnings per share (all measures)	9,752,311	9,752,311

9. NON-CURRENT ASSETS CLASSIFIED AS HELD FOR SALE

In December 2006 the Group management decided to dispose of its detergents manufacturing plant in Omsk (Russian Federation). The Manufacturing plant ceased production in June 2006. Net assets related to the Omsk manufacturing plant, property and equipment and inventory with a carrying value of RUB 153,335 thousand are separately disclosed as "Held For Sale" at December 31, 2006.

As of December 31, 2005 LLC Pallada Vostok, which was disposed in 2006, is separately disclosed as discontinued operations with net liabilities of RUB 180,178 thousand.

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Property, plant and equipment	99,475	97,444
Inventories	53,860	39,321
Trade and other receivables	-	6,203
Cash and cash equivalents	-	1,023
Assets classified as held for sale	**153,335**	**143,991**
Accounts payable	-	(303,770)
Short-term debt	-	(20,399)
Liabilities classified as held for sale	**-**	**(324,169)**
Net assets/(liabilities) classified as held for sale	**153,335**	**(180,178)**

10. PROPERTY, PLANT AND EQUIPMENT

	Construction in progress	Land	Buildings	Machinery & Equipment	Fixtures & Fittings	Total
	RUB'000	RUB'000	RUB'000	RUB'000	RUB'000	RUB'000
Cost						
Balance at January 1, 2005	**55,709**	**17,288**	**647,303**	**804,103**	**89,461**	**1,613,864**
Additions to CIP	881,646	-	-	-	-	881,646
Transfers from CIP	(847,211)	-	320,858	442,830	83,523	-
Acquisition of subsidiary	-	-	839,565	1,156,725	4,786	2,001,076
Disposals	-	-	(4,184)	(258,838)	(6,404)	(269,426)
Balance at January 1, 2006	**90,144**	**17,288**	**1,803,542**	**2,144,820**	**171,366**	**4,227,160**
Additions to CIP	430,771	-	-	-	-	430,771
Transfers from CIP	(446,093)	-	111,616	257,694	76,783	-
Disposals	-	-	(137)	(8,043)	(3,925)	(12,105)
Balance at December 31, 2006	**74,822**	**17,288**	**1,915,021**	**2,394,471**	**244,224**	**4,645,826**

Accumulated depreciation

	Construction in progress	Land	Buildings	Machinery & Equipment	Fixtures & Fittings	Total
	RUB'000	RUB'000	RUB'000	RUB'000	RUB'000	RUB'000
Balance at January 1, 2005	**-**	**-**	**180,158**	**531,896**	**49,430**	**761,484**
Charge for the year	-	-	47,016	109,367	24,920	181,303
Acquisition of subsidiary	-	-	87,502	757,585	-	845,087
Disposals	-	-	(38,270)	(209,698)	(5,126)	(253,094)
Balance at January 1, 2006	**-**	**-**	**276,406**	**1,189,150**	**69,224**	**1,534,780**
Charge for the year	-	-	49,787	207,336	49,401	306,524
Disposals	-	-	(19)	(8,043)	(3,576)	(11,638)
Balance at December 31, 2006	**-**	**-**	**326,174**	**1,388,443**	**115,049**	**1,829,666**
Carrying amount						
As at December 31, 2005	**90,144**	**17,288**	**1,527,136**	**955,670**	**102,142**	**2,692,380**
As at December 31, 2006	**74,822**	**17,288**	**1,588,847**	**1,006,028**	**129,175**	**2,816,160**

11. OTHER INTANGIBLE ASSETS

	Trademarks and other intangible assets	Licensed software	Total
	RUB’000	RUB’000	RUB’000
Cost			
Balance at January 1, 2005	**3,119**	**13,036**	**16,155**
Additions	9,308	2,147	11,455
Disposals	(120)	-	(120)
Acquired on acquisition of subsidiary	342,602	-	342,602
Balance at January 1, 2006	**354,909**	**15,183**	**370,092**
Additions	5,496	-	5,496
Disposals	(3)	-	(3)
Balance at December 31, 2006	**360,402**	**15,183**	**375,585**
Accumulated amortization			
Balance at January 1, 2005	**761**	**2,833**	**3,594**
Amortization expense	832	2,031	2,863
Disposals	(11)	-	(11)
Balance at January 1, 2006	**1,582**	**4,864**	**6,446**
Amortization expense	8,226	1,518	9,744
Disposals	-	-	-
Balance at December 31, 2006	**9,808**	**6,382**	**16,190**
Carrying amount			
Balance at January 1, 2006	**353,327**	**10,319**	**363,646**
Balance at December 31, 2006	**350,594**	**8,801**	**359,395**

The useful life for Dr. Scheller trademarks (carrying value of trademarks “Mankhattan” as of December 31, 2006 is RUB 324,763 thousands) is currently assessed as indefinite, and the carrying amount of trademarks is subject to annual impairment review.

12. GOODWILL

	Year ended 31/12/06	Year ended 31/12/05
	RUB’000	RUB’000
Balance at beginning of year	71,062	-
Increase in equity interest in Dr. Scheller	148,740	71,062
Effect of foreign currency exchange differences	(2,681)	-
At the end of the year	**217,121**	**71,062**

13. ACQUISITION OF DR. SCHELLER

During April 2005, the Group completed the acquisition of 61% of the outstanding shares of Dr. Scheller Cosmetics AG (Dr. Scheller) for a purchase price of RUB 609,428 thousand in cash. Dr. Scheller is a German perfume manufacturer and distributor.

	Book value	Fair value adjustments	Fair value
	RUB'000	RUB'000	RUB'000
Net assets acquired			
Current assets	756,028	-	756,028
Purchased plant and equipment	1,056,750	259,558	1,316,308
Intangible assets	24,067	318,535	342,602
Deferred tax liability	(24,134)	(215,629)	(239,763)
Current liabilities	(625,015)	-	(625,015)
Non-current liabilities	(672,962)	-	(672,962)
	514,734	**362,464**	**877,198**
Goodwill			71,062
Total consideration satisfied by cash			609,428
Net cash outflow arising on acquisition:			
Cash consideration			609,428
Cash and cash equivalents acquired			(136,119)
Total consideration net of cash acquired			**473,309**

During June and December 2006, the Group acquired additional 1,894,840 shares of Dr. Scheller Cosmetics AG (Scheller), 26% for a combined purchase price of RUB 446,187 thousand in cash. The acquisition took place as follows:

- in June 2006 the Group acquired 1,209,416 shares for a purchase price of RUB 285,461 thousand in cash;
- in December 2006 the Group acquired 685,424 shares for a purchase price of RUB 160,726 thousand in cash.

The transaction was accounted for under the purchase accounting method:

- in June 2006 fair value of Scheller net assets was RUB 1,021,124 thousand and additional goodwill recognized RUB 95,467 thousand;
- in December 2006 fair value of Scheller net assets was RUB 1,019,000 thousand and additional goodwill recognized RUB 53,273 thousand.

The total number of shares of Dr. Scheller outstanding at December 31, 2006 was 6,500,000. The total number of shares owned by the Group was 5,690,580 at December 31, 2006.

14. TAXES RECOVERABLE AND PAYABLE

Taxes recoverable consisted of the following at December 31, 2006 and 2005:

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Value Added Tax ("VAT")	436,557	485,500
Allowance for non-recoverable VAT	(43,745)	(8,830)
Other taxes	39,310	39,327
Total	**432,122**	**515,997**

Taxes payable consisted of the following at December 31, 2006 and 2005:

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
VAT	36,750	54,831
Other taxes	71,335	48,649
Total	**108,085**	**103,480**

15. INVENTORIES

Inventories consisted of the following at December 31, 2006 and 2005:

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Finished goods	1,084,008	1,361,069
Raw materials	837,599	1,116,728
Work in progress	67,244	75,553
Allowance for obsolescence	(154,663)	(143,036)
Total	**1,834,188**	**2,410,314**

16. TRADE AND OTHER RECEIVABLES

	Year ended 31/12/06 RUB'000	Year ended 31/12/05 RUB'000
Trade receivables	1,541,702	1,331,610
Allowance for doubtful debts	(147,428)	(121,706)
Total	**1,394,274**	**1,209,904**

17. BORROWINGS

	Annual interest rate	Current		Non-current	
		Year ended 31/12/06	Year ended 31/12/05	Year ended 31/12/06	Year ended 31/12/05
		RUB'000	RUB'000	RUB'000	RUB'000
Long-term loans					
EBRD loan (USD)	LIBOR*+4.75 %	135,260	147,853	135,260	295,706
Black Sea Trade bank loan (USD)	LIBOR*+4.5 %	-	-	157,987	-
Badden-Wurttembergische bank loan (EUR)	3.9-4.4%	-	-	161,859	177,147
Total		**135,260**	**147,853**	**455,106**	**472,853**
Short-term loans					
Raiffeisenbank Austria loan (USD)	LIBOR*+4%	372,916	428,000	-	-
MMB loan (RUB)	7-9.5%	341,000	427,000	-	-
Citibank loan (USD)	7%	105,000	-	-	-
Dresdner Bank Göppingen	EONIA**+0.75%	157,730	80,950	-	-
Deutsche bank – Money market loan	3,85%	69,394	68,370	-	-
Other loans in RUB, USD, EUR, UAH	19-23%	283,470	93,906	-	-
Total		**1,329,510**	**1,098,226**	**-**	**-**

* LIBOR = London Interbank Offered Rate
** EONIA = Euro Overnight Index Average.

Long-term loans as of December 31, 2006 and 2005 are repayable as follows:

	Year ended 31/12/06	Year ended 31/12/05
	RUB'000	RUB'000
Within one year	135,260	147,853
In the second year	234,241	147,853
In the third to fifth years inclusive	220,865	325,000
Total	**590,366**	**620,706**

18. TRADE AND OTHER PAYABLES

	Year ended 31/12/2006	Year ended 31/12/2005
	RUB'000	RUB'000
Trade payables	908,961	1,001,415
Other payable	518,937	498,868
Accrued interest	12,399	21,244
Total	**1,440,297**	**1,521,527**

19. OBLIGATIONS UNDER FINANCE LEASES

Finance lease liabilities

	Minimum lease payments		Present value of minimum lease payments	
	Year ended 31/12/06	Year ended 31/12/05	Year ended 31/12/06	Year ended 31/12/05
	RUB'000	RUB'000	RUB'000	RUB'000
No later than 1 year	26,043	34,269	23,408	34,065
Later than 1 year and not later than 5 years	29,620	35,894	28,116	35,894
Later than five years	-	-	-	-
Present value of minimum lease payments	**55,663**	**70,163**	**51,524**	**69,959**
Included in the financial statements as:				
Current borrowings			26,043	34,269
Non-current borrowings			29,620	35,894
Total			**55,663**	**70,163**

20. RETIREMENT BENEFIT OBLIGATIONS

Employees of the Group in Russia, Ukraine are generally beneficiaries of state-administered defined contribution pension programs. The Group remits a required percentage of the aggregate employees' salaries to the statutory pension Funds. The granting of a pension requires the fulfillment of a waiting period of 15 years of pensionable time of service.

Dr. Scheller maintains a defined benefit plan and utilizes actuarial methods to account for the related pension obligations. Inherent in the application of these actuarial methods are the following key assumptions:

Discount rate	4.5% per annum
Expected rate of salary increases	1.5% per annum
Pension increase	1.5% per annum
Return on plan assets	3.2% per annum

The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at December 31, 2006 by Kern Mauch & Kollegen GmbH (the Firm of actuaries, registered in Germany). The present value of the defined benefit obligation, the related current service cost and past service cost was measured using the projected unit credit method.

Amounts recognized in income in respect of these defined benefit schemes are as follows:

	Year ended 31/12/2006	Year ended 31/12/2005
	RUB'000	RUB'000
Current service cost	2,325	2,377
Interest cost	7,182	7,327

The amount included in the balance sheet arising from the entity's obligation in respect of its defined benefit plans is as follows:

	Year ended 31/12/2006 RUB'000	**Year ended 31/12/2005 RUB'000**
Present value of funded defined benefit obligation	175,529	181,105
Fair value of plan assets	(48,263)	-
Deficit in scheme	127,266	181,105
Unrecorded gain/(loss)	729	(7,411)
Liability recognized in the balance sheet	**127,995**	**173,694**

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

	Year ended 31/12/2006 RUB'000	**Year ended 31/12/2005 RUB'000**
Opening defined benefit obligation	181,105	-
Acquisition of Dr. Sheller	-	180,379
Service cost	2,325	1,835
Interest cost	7,182	9,035
Actuarial loss	729	8,901
Benefits paid	(9,542)	(9,330)
Fair value of plan assets	(48,263)	-
Effect of exchange rate movements	(6,270)	(9,715)
Closing defined benefit obligation	**127,266**	**181,105**

Movement in fair value of plan assets is as follows:

	Year ended 31/12/2006 RUB'000
At January 1, 2006	-
Contribution to plan assets	48,749
Additional expense of reinsurance	(486)
At December 31, 2006	48,263

Other than the defined benefit scheme liability outlined above, the Group was not liable for any supplementary pensions, post retirement health care, insurance benefits, or retirement indemnities to its current or former employees, as at December 31, 2006 and 2005.

21. RELATED PARTY TRANSACTIONS

Trading transactions The group has one party related by means of common ownership – LLC “Soyuzspezstroy”. Advances for construction to related parties as of December 31, 2006 and 2005 were as follows:

	Purchases of services		Advances to related parties	
	Year ended 31/12/06	Year ended 31/12/05	Year ended 31/12/06	Year ended 31/12/05
	RUB’000	RUB’000	RUB’000	RUB’000
LLC “Soyuzspezstroy”	103,752	93,644	27,875	37,031
Total	**103,752**	**93,644**	**27,875**	**37,031**

Compensation of key management personnel

The remuneration of directors and other members of key management during the year was as follows:

	Year ended 31/12/06	Year ended 31/12/05
	RUB’000	RUB’000
Short-term benefits	48,041	50,206
Total	**48,041**	**50,206**

The remuneration of directors and key executives is determined by the remuneration committee having regard to the performance of individuals and market trends.

22. DISPOSAL OF BUSINESS

Pallada Vostok (Uzbekistan)

In December 2003 Group management made a decision to dispose of its wholly owned subsidiary LLC Pallada Vostok based in Uzbekistan. The subsidiary was engaged in the production of a wide range of cosmetic brands sold on the Uzbekistan market. A Sale and Purchase Agreement (SPA) was agreed with LLC RAMR on May 28, 2004, for an amount of RUB 5,507 thousand. The full proceeds have not yet been received by the Company, due to non-payment by the customer, therefore the legal title to LLC Pallada Vostok remains within the Group. However, the management of the Group consider that the Group has effectively lost control of LLC Pallada Vostok and decided, in accordance with IFRS 3 to write off the assets and liabilities of Pallada Vostok in the consolidated financial statements in respect of the year ended December 31, 2006. A net income of RUB 32,463 thousand was recorded in the financial statements for the year ended December 31, 2006.

	Year ended 31/12/06 RUB'000
Book value of net assets sold	
Current assets	
Cash and cash equivalents	1,023
Trade receivables	10
Other receivables	6,373
Inventories	42,199
Non-current assets	
Property, plant and equipment	97,444
Current liabilities	
Payables	(305,179)
Non-current liabilities	
Borrowings	(20,398)
Net liabilities disposed of	(178,528)
Bad debt related to LLC Pallada Vostok	149,042
Gain on disposal	(32,463)

	Year ended 31/12/06 RUB'000
Consideration received in cash and cash equivalents	2,977
Less cash and cash equivalent balances disposed of	(1,023)
Cash inflow on disposal	**1,954**

Novoplast

The Group disposed of its wholly owned subsidiary LLC Novoplast in 2006. The subsidiary was engaged in the production of plastic packaging for the Group. The Sale and Purchase Agreement (SPA) was signed on December 20, 2006, and the disposal proceeds of RUB 49,805 thousand were received on February 20, 2007. RUB 27,441 thousand profit on disposal was recorded in the IFRS Financial Statements for the year ended December 31, 2006.

	Year ended 31/12/06 RUB'000
Book value of net assets sold	
Current assets	
Cash and cash equivalents	8,726
Trade receivables	7,114
Other receivables	1,468
Inventories	3,953
Non-current assets	
Property, plant and equipment	14,664
Current liabilities	
Payables	(13,337)
Net assets disposed of	22,588
Gain on disposal	(27,441)

	Year ended 31/12/06 RUB'000
Consideration received in cash and cash equivalents	50,029
Less cash and cash equivalent balances disposed of	(8,726)
Cash inflow on disposal	**41,303**

23. RESTRUCTURING COSTS OF DR. SCHELLER

Since January 1, 2007 a significant proportion of Dr. Scheller's production facilities were transferred to the Ekaterinburg manufacturing plant.

As a result of this transfer, the trademark cream “Apotheker Scheller” is now produced in Ekaterinburg from January 9, 2007. Total one-off expenditure of RUB 85,086 thousand was incurred as a result of transferring the production to Ekaterinburg. Such costs consisted primarily of workshop personnel expenses RUB 38,490 thousand; plant, property and equipment write-off RUB 20,509 thousand and RUB 14,541 thousand. It is expected that significant savings in production costs will be achieved from this relocation of production.

As of December 31, 2006 no further obligations, legal or constructive, exist in respect of the restructuring.

24. CASH AND CASH EQUIVALENTS

Cash consisted of the following at December 31, 2006 and 2005:

	Year ended 31/12/2006 RUB'000	Year ended 31/12/2005 RUB'000
Cash on hand – RUB	890	370
Cash in bank – RUB accounts	37,885	84,093
Cash in bank – USD accounts	52,065	23,092
Restricted cash – USD accounts	67,131	78,871
Other – EUR, UAH accounts	104	6,939
Total	**158,075**	**193,365**

25. CONTINGENCIES AND OPERATING ENVIRONMENT

Operating environment – The Group's principal business activities are within the Russian Federation, CIS, and Germany. Laws and regulations affecting businesses operating in the Russian Federation and CIS countries are subject to rapid changes and the Group's assets and operations could be at risk due to negative changes in the political and business environment.

Taxation – Tax laws in Russia are subject to frequent changes and varying interpretations. Management's interpretation of such legislation in applying it to business transactions of the Group may be challenged by the relevant regional and federal authorities enabled by law to impose fines and penalties. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and as a result, it is possible that the transactions that have not been challenged in the past may be challenged. Fiscal periods remain open to review by the tax authorities in respect of taxes for the three calendar years preceding the year of tax review. Under certain circumstances reviews may cover longer periods. While the Group believes it has provided adequately for all tax liabilities based on its understanding of the tax legislation, the above facts may create additional financial risks for the Group.

26. RISK MANAGEMENT POLICIES

Management of risk is an essential element of the Group's operations. The main risks inherent to the Group's operations are those related to credit risk exposures, market movements in interest rates and foreign exchange rates. A description of the Group's risk management policies in relation to those risks follows.

Credit risk – The Group is exposed to credit risk which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss.

The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one customer, or groups of customers. In addition, the ageing of receivables is monitored periodically by Management.

Currency risk – Currency risk is that the financial results of the Group will be adversely impacted by changes in exchange rates to which the Group is exposed. The Group is exposed to currency risk in respect of its loans outstanding, which are denominated in several currencies.

Interest rate risk – The Group is exposed to some interest rate risk since some of its borrowings and bonds provide for variable interest calculations.