Management's discussion and analysis of financial condition and results of operations for the years 2007, 2006 and 2005 and for the six months ended 30 June 2008 and 2007

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The following discussion and analysis of the Polyus Group's financial condition and results of operations should be read in conjunction with the Polyus Group's consolidated financial statements. The information on oil and steel prices has been extracted from Bloomberg and the "Western Europe free on board Amsterdam-Rotterdam-Antwerp" measure respectively. The information on gold sales in troy ounces in the domestic market and for export, weighted-average gold selling price, average evening fixing price in London and excess of weighted-average selling price over average evening fixing price have been extracted from the statistics of the LBMA.

The Polyus Group's consolidated financial statements have been prepared in accordance with IFRS and under existing Polyus Group accounting policies. References to "restatements" of such financial information in the Operating and Financial Review are explained in the notes to the financial statements. The individual financial statements of the Polyus Group entities operating in the Russian Federation are presented in roubles, their functional currency. The Polyus Group has chosen to present its consolidated financial statements in US dollars, as management believes it is a more convenient presentation currency for international users of the consolidated financial statements of the Group.

The Polyus Group is the largest gold producer in the Russian Federation and among the largest gold mining companies in the world, based on mineral resources and production volumes. The Polyus Group mines gold and performs geological exploration in four major gold-producing regions of the Russian Federation, including Krasnoyarsk, Irkutsk, Magadan and the Republic of Sakha (Yakutia).

Polyus Gold Shares are traded on the leading Russian stock exchanges, MICEX and RTS. Polyus Gold's ADRs are listed on the main market of the London Stock Exchange and traded on the over-the-counter markets in the United States. Polyus Gold Shares are included in the key Russian stock exchange indices of MICEX and RTS, and international stock exchange indices such as FTSE Gold Mines and MSCI Emerging Markets. The Polyus Group produced 1.2 million troy ounces of gold in 2007.

The following discussion and analysis of financial condition and results of operations for the years 2007, 2006 and 2005 and for the six months ended 30 June 2008 and 2007 represents the management's opinion in relation to the Polyus Group's operating and financial results, including discussions of:

- key performance indicators of certain business units and subsidiaries;
- financial positions as at 30 June 2008, 31 December 2007, 31 December 2006 and 31 December 2005;
- the Polyus Group's liquidity, solvency and capital sources; and
- significant events affecting the Polyus Group's operating performance for these periods.

1. The Polyus Group's operating results

1.1 External market factors affecting the Polyus Group's financial results

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

The Polyus Group's revenues are denominated in USD, whereas up to 80% of the Polyus Group's expenses are denominated in RUB, which means that movements in the RUB/USD exchange rate impact on the Polyus Group. Many costs included in the Polyus Group's cost of sales are also directly or indirectly impacted by the prices of oil and steel. Changes in oil prices impact the prices of diesel fuel, gasoline and lubricants for mining and construction equipment. Steel forms the basis for the price of all rolled metal products, pipes, machinery and vehicles.

In the periods under discussion, prices for these products, and the RUB/USD exchange rate, saw significant movements, which influenced the Polyus Group's financial results:

Average price/ rate	2007	2006	2005	Six months ended 30 June 2008	Six months ended 30 June 2007
Oil (Brent brand) (USD per barrel)[1]	72.5	65.1	54.5	102.7	62.5
Steel (hot rolled) (USD per tonne)[2]	563	499	477	760	535
Average USD/RUB rate	25.58	27.19	28.29	23.94	26.08
Period end USD/RUB rate	24.55	26.33	28.78	23.46	25.82

1. Bloomberg.
2. Spot price as set according to the "Western Europe free on board Amsterdam-Rotterdam-Antwerp" measure.

Summary of performance results

The following table shows the results of the Polyus Group's operations in 2007, 2006 and 2005:

USD' 000	Years ended December 31			2007 against 2006	2006 against 2005
	2007 (restated)	2006 (restated)	2005 (restated)	%	%
Gold sales	849,023	734,559	473,184	15.6	55.2
Other sales	18,096	18,127	17,700	(0.2)	2.4
Cost of gold sales	(449,216)	(426,527)	(260,030)	5.3	64.0
Cost of other sales	(25,866)	(18,816)	(19,750)	37.5	(4.7)
Gross profit	392,037	307,343	211,104	27.6	45.6
Gross profit on gold sales	399,807	308,032	213,154	29.8	44.5
Gross profit margin	45.2%	40.8%	43.0%	10.7	(5.1)
Profit before income tax	177,107	1,228,391	191,478	(85.6)	541.5
Pre-tax margin	20.4%	167.2%	39.0%	–	–
Income tax expense	(85,299)	(73,080)	(53,899)	16.7	35.6
Profit for the year	91,808	1,155,311	137,579	(92.1)	739.7
Net profit/(loss) attributable to minority interest	5,999	(414)	17	–	–
Net profit attributable to shareholders of Polyus Gold	85,809	1,155,725	137,562	(92.6)	740.1
Net profit margin	10.6%	157.3%	28.0%	–	–
Earnings per share – basic and diluted (USD)	0.49	0.75	–	–	–

The following table shows the results of the Polyus Group's operations for the six months ended 30 June 2008 compared to the six months ended 30 June 2007:

USD' 000	Six months ended 30 June 2008 (restated)	Six months ended 30 June 2007 (restated)	Change, %
Gold sales	505,730	309,360	63.5
Other sales	13,179	8,689	51.7
Cost of gold sales	(243,644)	(192,261)	26.7
Costs of other sales	(13,230)	(7,964)	66.1
Gross profit	262,035	117,824	122.4
Gross profit on gold sales	262,086	117,099	123.8
Gross profit margin	50.5%	37.0%	36.3
Gross profit margin on gold sales	51.8%	37.9%	36.9
Profit/(loss) before income tax	213,050	(43,399)	–
Pre-tax margin	41.1%	(13.6%)	–
Income tax expense	(52,163)	(22,463)	132.2
Net profit/(loss) for the period	160,887	(65,862)	–
Net (loss)/profit attributable to minority interest	(312)	650	–
Net profit/(loss) attributable to shareholders of Polyus Gold	161,199	(66,512)	–
Net profit/(loss) margin	31.0%	(20.7%)	–
Earnings/(loss) per share – basic and diluted (USD)	0.90	(0.38)	–

1.2 **Gold sales**

The following table shows the results of the Polyus Group's gold sales for the years ended 2007, 2006 and 2005:

	Years ended 31 December				
	2007 (restated)	2006 (restated)	2005 (restated)	2007 against 2006 %	2006 against 2005 %
Gold sales (USD thousands)	849,023	734,559	473,184	15.6	55.2
Gold sales (thousand troy ounces)	1,210	1,216	1,049	(0.5)	15.9
In the domestic market (thousand troy ounces)	1,050	875	588	20.0	48.8
For export (thousand troy ounces)	160	341	461	(53.1)	(26.0)
Average gold selling price (USD per troy ounce)	701.7	604.1	451.1	16.2	33.9
Average evening fixing price in London (USD per troy ounce)(1)	695.4	603.5	444.4	15.2	35.8
Excess of average selling price over average evening fixing price (USD per troy ounce)	6.3	0.6	6.7	950	(91)

1. Source: LBMA

The following table shows the results of the Polyus Group's gold sales for the six months ended 30 June 2008 compared to the six months ended 30 June 2007:

	Six months ended 30 June		
	2008 (restated)	2007 (restated)	Change, %
Gold sales (USD thousands)	505,730	309,360	63.5
Gold sales (thousand troy ounces) ...	559	470	18.9
In the domestic market (thousand troy ounces)	559	453	23.4
For export (thousand troy ounces) ...	–	17	(100.0)
Average gold selling price (USD per troy ounce)	904.7	658.2	37.4
Average evening fixing price in London (USD per troy ounce) [(1)]...	910.9	658.1	38.4
Excess/(deficit) of weighted-average selling price over/(under) average evening fixing price (USD per troy ounce)..	(6.2)	0.1	–

1. Source: LBMA

The Polyus Group generally sells more gold in the second half of any given reporting year, because the Polyus Group is usually only able to conduct its alluvial operations from May to November (inclusive) because the rivers in the Irkutsk region tend to be frozen for the remainder of the year. As gold prices increased during each of 2005, 2006, 2007 and 2008, the weighted-average selling price calculated for the relevant full reporting year exceeded the average evening fixing price. These excesses are not usually reflected in the figures for the six months periods because, as indicated, the Polyus Group does not generally produce or sell as much gold in the first half of each year in comparison to the second half.

2007 compared to 2006

In 2007, the Polyus Group's revenue from gold sales reached a historical high and was USD 849,023 thousand, an increase of 15.6% as compared to 2006.

The increase in revenue resulted primarily from favourable gold prices, as production and sales volumes remained relatively consistent between the two years. In 2007, the Polyus Group produced 1,214 thousand troy ounces (37.8 tonnes) of refined gold, almost the same as in 2006 when it produced 1,215 thousand troy ounces. The Polyus Group sold 1,210 thousand troy ounces in 2007, which is comparable to the 1,216 thousand troy ounces sold in 2006.

During 2007, the global price of gold increased by more than 30% between the start of the year and the end of the year. On 2 January 2007, the first business day in the market, the gold price was USD 639.75 per troy ounce, and on 28 December 2007, the last business day in the market, the gold price was USD 833.75 per troy ounce.

The Polyus Group's policy of selling gold at spot market prices (without using any type of hedging instruments) made it possible to realise the benefit of an increasing gold price in the financial results for 2007. The average selling price in 2007 was USD 701.7 per troy ounce as compared to USD 604.1 per troy ounce in 2006. In 2007, the achieved average selling price exceeded the average London fixing for the year by USD 6.3, reflecting the Polyus Group's efficiency in managing its sales.

In 2007, the sales structure continued to change significantly from export sales to domestic market sales. Whereas in 2006 export accounted for almost 30% of sales in USD terms, in 2007 gold was largely sold in the domestic market to Russian banks (87% of sales). The increase of sales in the domestic market was primarily due to more favourable contracts terms negotiated with Russian banks.

The increase in exports in the second half of 2007 compared to the first half of 2007 (from 17 thousand troy ounces to 143 thousand troy ounces) is related to the seasonal distribution of supplies.

2006 compared to 2005

In 2006, gold sales increased to USD 734,559 thousand, an increase of USD 261,375 thousand (or 55%) from 2005. The increase in gold sales resulted from a 34% increase in the average gold selling price and a 16% increase in physical sales volume. The increase in volumes reflected a full year of production and sales from the acquisitions in 2005 of OJSC “Aldanzoloto GRK” and OJSC “South-Verkhoyansk Mining Company”.

The Polyus Group increased the proportion of tonnes of gold sold in the Russian Federation from 56% in 2005 to 72% in 2006, primarily due to higher domestic demand for gold and the improvement of gold purchase terms with domestic customers.

The export sales by the Polyus Group in 2006 were made on the basis of a new export contract and decreased by 26%. Deliveries of gold bullion in accordance with the standards of the London Bullion Market Association were made directly to the buyer’s vault. Sales were at prices determined on the basis of London pricing plus an agreed upon premium.

Six months ended 30 June 2008 compared to six months ended 30 June 2007

In the first six months of 2008, the Polyus Group’s revenue from gold sales was USD 505,730 thousand, an increase of 63.5% as compared to the first six months of 2007. The increase in revenue primarily resulted from significant growth in gold output (18.9%) and from greater average selling prices.

In the first six months of 2008, the Polyus Group produced 559 thousand troy ounces (17.4 tonnes) of refined gold, compared to 470 thousand troy ounces (14.6 tonnes) during the same period in the previous year. The growth in production resulted from increased output at the Olimpiada mine, which became possible after the commissioning of Mill No. 3 at the mine and additional volumes of oxidised ores, which were previously extracted from Vostochny Pit and from the Olenye deposit.

During the first half of 2008, the gold price on the global market increased 9.9%. On 2 January 2008, the first business day of the reporting period, the gold price was USD 846.8 per troy ounce. On 30 June 2008, the last business day of the second quarter 2008, the gold price was USD 930.3 per troy ounce.

The Polyus Group’s policy of selling gold at spot market prices (without any type of hedging instruments) made it possible to realise the benefit of an increasing gold price in full in its financial results in the first half of 2008. The weighted average gold price increased to USD 904.7 per troy ounce in the first half of 2008, compared to USD 658.2 per troy ounce in the first half of 2007.

In the first half of 2008, the Polyus Group sold gold on the domestic market only, having decided not to continue working under export contracts because of the more attractive contractual terms with Russian banks.

1.3 Cost of gold sales

The following table shows the results of the Polyus Group's cash operating costs for the years ended 2007, 2006 and 2005:

USD' 000	Years ended 31 December			2007 against 2006	2006 against 2005
	2007 (restated)	2006 (restated)	2005 (restated)	%	%
Cash operating costs..	442,224	348,212	232,373	27.0	49.9
Materials and spares	137,956	103,617	74,950	33.1	38.2
Labour..................	144,008	104,358	69,378	38.0	50.4
Fuel	62,645	49,237	28,920	27.2	70.3
Power	12,660	14,617	10,477	(13.4)	39.5
Tax on mining.......	51,138	42,361	29,742	20.7	42.4
Other cash operating costs	33,817	34,022	18,906	(0.6)	80.0
Amortisation and depreciation of operating assets.....	87,196	73,718	45,251	18.3	62.9
Change in deferred stripping costs..........	(68,065)	5,230	(9,565)	n/a	n/a
Change in gold-in-process and refined gold	(12,621)	(7,951)	(10,117)	58.7	21.4
Change in provision for land restoration.......	482	7,318	2,088	93.4	250.5
Cost of gold sales.....	449,216	426,527	260,030	5.3	64.0

2007 compared to 2006

In 2007, cost of gold sales increased by USD 22,689 thousand to USD 449,216 thousand.

Cash operating costs

The principal reason for the increase in cost of gold sales was the increase in cash operating costs within all the Polyus Group's production entities. During 2007, cash operating costs included in cost of sales were USD 442,224 thousand.

The largest item included in cash operating costs in 2006 and 2007 was payroll expenses. Whereas in 2006 the payroll expenses for production staff were USD 104,358 thousand (including USD 77,808 thousand for mining staff payroll and USD 26,550 thousand for concentration and smelting staff payroll), in 2007 these expenses increased to USD 144,008 thousand.

The 38% increase is higher than the increase in labour costs across Russia (approximately 20% in 2007) because all the Polyus Group's production entities are located in the Far North regions or the regions which are equivalent to the Far North, requiring the Polyus Group to pay additional compensation. Moreover, in 2007 the employees of the Olimpiada mine received bonuses for early commissioning of Mill No. 3.

The second largest item included in cash operating costs was materials and spare parts used during the mining, concentration and smelting processes. The materials and spare parts which the Polyus Group procures consist of spare parts for mining and construction machines, fuel, lubricants, rolled metal products, cables, and technological materials for the gold mill.

The cost of materials and spare parts consumed in 2007 was USD 137,956 thousand as compared to USD 103,617 thousand in 2006, an increase of 33%. The growth was primarily due to additional purchases to support the increase in ore volumes processed, which was made possible by commissioning Mill No. 3. The biggest increase of approximately 40% was registered at the Polyus Group's largest mine, the Olimpiada mine, which accounted for more than 60% of the Polyus Group's cost of materials and spare parts in 2007 and 2006. In addition, the cost of some materials and spare parts which the Polyus Group procured in the reporting year also increased, primarily due to world-wide changes in underlying commodity prices.

Due to the increase in the gold price, applied to a similar sales volume, the Polyus Group paid USD 51,138 thousand in mining taxes on mining, which was USD 8,777 thousand more than in 2006. In accordance with Chapter 26 of the Tax Code of the Russian Federation, the tax on mining base includes concentrate or any other semi-product containing precious metal obtained by extraction of this metal from ore, alluvial or industrial deposits, such as the gold produced by the Polyus Group. Concentrates and other semi-products containing gold are subject to the tax at the rate equal to 6% of the cost of these semi-products. The cost is determined based on selling prices for the relevant tax period.

Amortisation and depreciation of operating assets

Amortisation and depreciation of operating assets included in cost of sales increased by 18% from USD 73,718 thousand to USD 87,196 thousand. This amount included depreciation (USD 71,016 thousand) and amortisation of the mineral rights (USD 16,180 thousand). The increase resulted mainly from commissioning of new mining and metallurgical facilities, including Mill No. 3.

2006 compared to 2005

In 2006, the cost of gold sales increased by USD 166,497 thousand (an increase of 64%) to USD 426,527 thousand compared to USD 260,030 thousand in 2005. Key reasons for the increase of cost of gold sales in 2006 are as follows:

- inclusion of the full year effect of the production costs of OJSC Aldanzoloto GRK and OJSC SVMC in 2006, totalling USD 82 million compared to USD 13 million from the date of acquisition in September 2005 to the year end;
- a 4% rise in the sulphide ore share in the total quantity of ore processed. The processing of sulphide ore requires twice as much reagents and materials as oxidised ore; and
- increased energy costs.

Cash operating costs

In 2006, cash operating costs increased by USD 115,839 thousand (an increase of 50%) to USD 348,212 thousand, compared to USD 232,373 thousand in 2005.

In 2006, the largest component of cash operating costs was labour. In 2006, labour costs increased by USD 34,980 thousand (an increase of 50%) to USD 104,358 thousand. The increase was mainly due to the full year effect of labour costs of OJSC Aldanzoloto GRK and OJSC SVMC, which were USD 12 million in 2006 compared to USD 2 million in 2005 after the date of acquisition in September 2005; a USD 15 million increase of wages in OJSC Lenzoloto and LLC LZRK to bring them in line with the average payroll rates in the Irkutsk region; and a USD 10 million increase of labour costs at CJSC Polyus.

The second largest item included in cash operating costs in 2006 was materials and spare parts used during the mining, concentration and smelting processes, including spare parts for mining and construction machines, fuel, lubricants, rolled metal products, cables, and technological materials for the gold mill. In 2006, materials and spares used in production were USD 103,617 thousand compared to USD 74,950 thousand in 2005. This increase resulted mostly from the 4% rise in the sulphide ore share in the total quantity of ore processed at Polyus and the full year effect of consumables and spares of Aldanzoloto and SVMC. Sulphide ore requires approximately twice as much reagents and materials as oxidised ore.

In 2006, mining tax expense increased by 42.4% compared to 2005, to USD 42,361 thousand, principally due to a 33.9% increase in average gold selling price.

The 70.3% increase in fuel expenses in 2006 was mainly a result of a growth in fuel prices of between 14 and 20% (depending on the fuel in question) and the full year effect of the consolidation of OJSC Aldanzoloto GRK acquired in September 2005.

Amortisation and depreciation of operating assets

Amortisation and depreciation of operating assets included in cost of sales increased by 63% from USD 45,251 thousand to USD 73,718 thousand. The increase was mainly due to the full year effect of the acquisition and consolidation of OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC.

Six months ended 30 June 2008 compared to six months ended 30 June 2007

In the first six months of 2008, the cost of gold sales increased by USD 51,383 thousand from the first six months of 2007 and was USD 243,644 thousand.

The following table shows the results of the Polyus Group's cash operating costs breakdown in the first six months of 2008 compared to the first six months of 2007:

	Six months ended 30 June		
USD'000	**2008 (restated)**	**2007 (restated)**	**Change, %**
Cash operating costs................	246,435	177,318	39.0
Materials and spares.............	68,608	48,338	41.9
Labour	84,946	63,616	33.5
Fuel......................................	36,912	25,821	43.0
Power	7,787	6,489	20.0
Tax on mining	34,209	20,209	69.3
Other cash operating costs ...	13,973	12,845	8.8
Amortisation and depreciation of operating assets	52,805	48,457	9.0
Change in deferred stripping costs...................................... ..	(57,817)	(17,266)	234.9
Change in gold-in-process and refined gold.........................	1,603	(16,797)	n/a
Change in provision for land restoration............................	618	549	12.6
Cost of gold sales	243,644	192,261	26.7

Cash operating costs

The principal reason of the increase in cost of sales was the increase of cash operating costs within all the Polyus Group's production entities. In the first six months of 2008, cash operating costs included in cost of sales were USD 246,435 thousand, compared to USD 177,318 thousand in the first six months of 2007.

In the first six months of 2008, payroll expenses were the largest item in cash operating costs. In the first six months of 2007, the payroll expenses for production staff were USD 63,616 thousand, whereas in the first six months of 2008 those expenses grew to USD 84,946 thousand. The 33.5% increase approximately equals the overall labour costs increase in Russia for the 12 months period ended 30 June 2008.

The second largest item included in cash operating costs for the first six months of 2008 was expenses on spare parts for trucks and excavators, and for construction machinery, expenses on rolled metal products and cables, technological materials for plants and other materials and spares, used in mining, smelting and concentrating. In the first six months of 2008, the cost of materials and spares were USD 68,608 thousand, compared to USD 48,338 thousand in the first six months of 2007 (representing an increase of 41.9%). The increase was primarily the result of the growth in ore processing. The major contributor of the increase in ore processing was the Olimpiada mine. The cost of a number of materials and spares, purchased by the Polyus Group in the reporting period also increased, primarily due to world-wide changes in underlying commodity prices.

A significant portion of cash operating costs is fuel, mainly diesel oil, fuels and lubricants for trucks and excavators and for an oil-fired power plant operating at the Nezhdaninskoye deposit. Expenses on fuel grew 43.0% from the first six months of 2007 to USD 36,912 thousand in the first six months of 2008.

Due to increased gold production and growth in the gold price the Polyus Group paid USD 34,209 thousand in tax on mining in the first six months of 2008, which is USD 14,000 thousand more than in the first six months of 2007.

1.4 Selling, general and administrative expenses

The following table sets forth the selling, general and administrative expenses of the Polyus Group for the years ended 2007, 2006 and 2005:

USD' 000	**Years ended 31 December 2007 (restated)**	**2006 (restated)**	**2005 (restated)**	**2007 against 2006 %**	**2006 against 2005 %**
Share option plan	132,548	–	–	–	–
Salaries	76,291	44,019	30,739	73.3	43.2
Taxes other than mining and income taxes	20,724	11,322	4,685	83.0	141.7
Professional services	8,288	6,820	3,389	21.5	101.2
Depreciation	3,969	4,759	5,742	(16.6)	(17.1)
Rent expenses	1,799	1,379	1,671	30.5	(17.5)
Repair and maintenance	1,734	1,025	3,128	69.2	(67.2)
Communication services	1,278	1,415	761	(9.7)	85.9
Bank charges	1,224	1,548	917	(20.9)	68.8
Other	13,921	7,391	4,124	88.4	79.2
Total	**261,776**	**79,678**	**55,156**	**228.5**	**44.5**

2007 compared to 2006

During 2007, the Polyus Group's selling, general and administrative expenses increased by 229% from USD 79,678 thousand in 2006, primarily due to the costs of the share option plan.

Salaries

Payroll for administrative staff increased by USD 32,272 thousand to USD 76,291 thousand in 2007. All of the Polyus Group's entities had an increase in administrative staff payroll. The Krasnoyarsk business unit (the Olimpiada mine) accounted for 46% of these expenses with a 43% increase, whilst the Irkutsk hard rock business unit (Zapadnoye mine) had a 17% increase in administrative staff payroll costs. The increase in the administrative payroll was also a result of acquisition of several companies in 2006, which expenses had been consolidated in full only starting from 2007. Moreover, the Polyus Group established its headquarters in Moscow in 2006.

Share option plan

In April 2007, the Board of Polyus Gold passed a resolution to implement a share option plan. As at 31 December 2007, 4,575,065 shares had been issued to management, representing 2.40% of Polyus Gold's issued share capital. In 2007, the fair value of the options granted was USD 132,548 thousand.

Taxes, other than mining and income taxes

In addition to tax on mining and income taxes, the Polyus Group pays property tax, VAT (which for the purpose of this item only includes non-recoverable VAT), unified social tax and other taxes. In 2007, the Polyus Group paid USD 20,724 thousand in federal and regional tax payments other than tax on mining and income tax, approximately 83% more than in 2006, primarily due to an increase of non-recoverable VAT. The amount of non-recoverable VAT increased significantly at CJSC Polyus (Krasnoyarsk business unit), which made contributions to the share capital of new subsidiaries in non-monetary form, which resulted in a write-off of VAT of a total amount of USD 2,895 thousand.

The following table shows the components of taxes, other than mining and income taxes, for 2007, 2006 and 2005:

USD '000	**Years ended 31 December**			**2007 against 2006**	**2006 against 2005**
	2007 (restated)	**2006 (restated)**	**2005 (restated)**	**%**	**%**
Taxes, other than mining and income taxes	20,724	11,322	4,685	83.0	141.7
VAT	10,092	3,378	1,170	198.8	188.7
Property tax...........	8,231	5,135	3,145	60.3	63.3
Other taxes	2,401	2,809	370	(14.5)	659.2

Other selling, general and administrative expenses

Other selling, general and administrative expenses include rental and communication costs, professional and banking service fees, repair and maintenance costs, depreciation and other costs. Other selling, general and administrative expenses increased by USD 7,876 thousand in 2006 to USD 32,213 thousand in 2007. This increase was mainly due to product selling costs, including the costs for transportation of finished products, which increased more than 5 times to USD 1,027 thousand. The Polyus Group's expenses for professional service fees of auditors, lawyers and consultants also increased by 21.5% and were USD 8,288 thousand in 2007.

2006 compared to 2005

In 2006, selling, general and administrative expenses increased by USD 24,522 thousand (an increase of 44%) to USD 79,678 thousand.

Salaries

Payroll expenses in 2006 were USD 44,019 thousand, and increased by USD 13,280 thousand from 2005, principally attributable to the growth in business activities of the Polyus Group's head office. The weighted average number of head office employees was 22% higher in 2006 compared to 2005, leading to a corresponding increase in salaries expense. The increase also reflected the full-year effect of OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC since they were acquired in September 2005.

Taxes, other than mining and income taxes

The increase in taxes, other than mining and income taxes from USD 4,685 thousand in 2005 to USD 11,322 thousand in 2006 was primarily the result of the full year effect of taxes paid by OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC and to the acquisition of property, plant and equipment, resulting in increased property tax.

Other selling, general and administrative expense

Other selling, general and administrative expenses (including rental and communication costs, professional and banking service fees, and repair and maintenance costs, depreciation and other costs) increased in 2006 and amounted to USD 24,337 thousand, compared to USD 19,732 in 2005. One of the largest contributors to the growth was the substantial increase (from USD 3,389 thousand in 2005 to USD 6,820 thousand in 2006) in professional services, including audit, legal and other consulting fees due to the spin-off from Norilsk Nickel and the listing of Polyus Gold's ADRs on the London Stock Exchange. The increase was also caused by the full year effect of expenses of OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC.

Six months ended 30 June 2008 compared to six months ended 30 June 2007

The following table sets forth the selling, general and administrative expenses of the Polyus Group for the six months ended 30 June 2008 and 2007:

	Six months ended June 30		
USD' 000	**2008 (restated)**	**2007 (restated)**	**Change, %**
Salaries	31,265	28,051	11.5
Taxes other than mining and income taxes	9,711	5,237	85.4
Professional services	5,938	2,442	143.2
Bank charges	5,699	3,923	45.3
Rent expenses	2,434	139	1,651.1
Depreciation	2,103	2,163	(2.8)
Repair and maintenance	810	439	84.5
Communication services	589	565	4.2
Share option plan	–	132,548	–
Other	6,405	5,535	15.7
Total	**64,954**	**181,042**	**(64.1)**

During the first six months of 2008 selling, general and administrative expenses decreased by USD 116,088 thousand from USD 181,042 thousand in the first half of 2007. This was mainly a result of the expenses relating to the exercise of the share option plan, reflected in the first half of 2007 administrative expenses, more than offsetting increases in other costs.

Salaries

The payroll for administrative staff did not change significantly compared to the first half of 2007, and amounted to USD 31,265 thousand.

Taxes, other than mining and income taxes

In addition to mining tax and income tax the Polyus Group pays property tax, VAT, unified social tax and other taxes. In the first half of 2008 the Polyus Group paid USD 9,711 thousand in federal and regional tax payments other than mining tax and income tax, 85.4% higher than in the first half of 2007, primarily due to an increase of non-recoverable VAT. The amount of non-recoverable VAT increased significantly at CJSC Polyus (Krasnoyarsk business unit), primarily as a result of the contribution of assets to various new subsidiaries. The input VAT on assets contributed is non-recoverable under the tax code of the Russian Federation. In addition, due to the growing volumes of construction and exploration works the property tax increased.

The following table sets forth the components of taxes, other than mining tax and income tax, for the six months ended 30 June 2008 and 2007:

	Six months ended 30 June		
USD'000	**2008 (restated)**	**2007 (restated)**	**Change, %**
Taxes, other than mining tax and income tax	9,711	5,237	85.4
VAT	2,314	762	203.7
Property tax	5,858	3,151	85.9
Other taxes	1,539	1,324	16.2

Other selling, general and administrative expenses

Other selling, general and administrative expenses (which include rental and communication costs, professional and banking service fees, repair and maintenance costs, depreciation and other costs) increased by USD 8,772 thousand to USD 23,978 thousand in the first half of 2008. This increase was mainly due to professional and banking services, which grew 82.8% to USD 11,637 thousand. This one-time increase in these expenses was primarily due to consulting services provided on a proposal to spin-off the exploration assets into another entity.

1.5 Research and exploration expenses

In 2007, research and exploration costs decreased by USD 1,357 thousand to USD 6,217 thousand. The decrease was mainly due to the decrease of exploration costs throughout the Polyus Group. In 2006, the increase in exploration works in all regions of operations of the Polyus Group led to a substantial increase in research and exploration expenses from USD 1,886 thousand in 2005 to USD 7,574 thousand in 2006.

In the six months ended 30 June 2008 research and exploration costs increased by USD 1,005 thousand from the six months ended 30 June 2007, to USD 4,430 thousand, mainly due to the increased exploration activity in the Krasnoyarsk and Irkutsk alluvial business units.

1.6 Other operating income and expenses

2007 compared to 2006

During 2007, other operating income was USD 7,696 thousand, or USD 5,602 thousand more than in 2006. The increase was primarily due to changes in the allowance for reimbursable VAT (representing an increase of USD 3,641 thousand). In 2007, the Polyus Group reached an amicable settlement with one of its creditors, as a result of which it was released from payment of interest on a loan totalling USD 4,055 thousand.

Other operating expenses increased by 27.8% to USD 18,025 thousand in 2007 due to an increase in the losses arising from the disposal of property, plant and equipment of USD 6,421 thousand, and increased charity contributions to USD 3,868 thousand.

2006 compared to 2005

During 2006, other operating income was USD 2,094 thousand as a result of a release of decommissioning liability.

In 2006, other operating expenses decreased to USD 14,108 thousand, compared to USD 26,506 thousand in 2005 due to the following items:

- a reduction in impairment of property, plant and equipment from USD 11,613 thousand in 2005 to USD 383 thousand in 2006. In 2005, the impairment of assets in the amount of USD 5,572 thousand was in OJSC Matrosov Mine, and a write-off was made of construction-in-progress in OJSC Lenzoloto in the amount of USD 5,355 thousand; and
- a decrease in losses from disposal of property, plant and equipment from USD 4,848 thousand in 2005 to USD 1,494 thousand in 2006, the main contributors in 2005 being CJSC Polyus, with losses of USD 2 299 thousand and OJSC Lenzoloto, with losses totalling USD 1,077 thousand.

Six months ended 30 June 2008 compared to six months ended 30 June 2007

Other operating income in the first half of 2008 amounted to USD 4,841 thousand, which is USD 3,704 thousand higher than in the first half of 2007. The increase was primarily a result of the profit on disposal of property, plant and equipment.

Other operating expenses reduced significantly and amounted to USD 7,444 thousand in the first half of 2008, compared to USD 16,656 thousand in the first half of 2007. During the first half of 2008, the Polyus Group disposed of fixed assets with a profit, compared to the loss on disposal of fixed assets for the sum of USD 5,564 thousand in the first half of 2007.

1.7 **Finance costs, income from investments and foreign exchange gain/(loss)**

The following table sets forth the components of financial and investment activity in 2007, 2006 and 2005:

USD' 000	Years ended 31 December			2007 against 2006	2006 against 2005
	2007 (restated)	2006 (restated)	2005 (restated)	%	%
Finance costs	(6,629)	(6,453)	(3,586)	2.7	79.9
Income from investments....................	61,537	1,102,111	52,012	(94.4)	n/a
Foreign exchange gain/(loss)	8,484	(75,344)	(250)	–	n/a

2007 compared to 2006

In 2007, finance expenses did not change significantly from 2006 and amounted to USD 6,629 thousand.

Income from investments in 2007 was USD 61,537 thousand, which is two times lower than the investment income for 2006 in the amount of USD 121,649 thousand, after adjustment for the recognition of income arising from the sale of Gold Fields shares in the amount of USD 980,462 thousand. The decrease of income from investing activity related primarily to a reduction of income from interest on bank deposits and a reduction of the effective yield on money placed in asset management. At the year-end 2007, bank deposits were USD 443,653 thousand as compared to USD 608,957 thousand at the end of 2006.

During 2007, the Polyus Group recognised a foreign exchange gain of USD 8,484 thousand, as compared to a loss of USD 75,344 thousand in 2006. During 2006, the net foreign exchange loss arose primarily from investing activities of foreign subsidiaries of the Polyus Group during a period of depreciation of the USD.

2006 compared to 2005

In 2006, finance costs increased to USD 6,453 thousand, compared to USD 3,586 thousand in 2005. This was due to the unwinding of the discount of the decommissioning obligation increased to USD 3,579 thousand as a result of acquisition of Yakut mining companies, which was partially off-set by a gain on the revaluation of borrowings denominated in foreign currency of USD 1,122 thousand.

In 2006, net income from investments increased to USD 1,102,111 thousand, compared to USD 52,012 thousand in 2005, mostly due to the realised gain on the sale of investment in Gold Fields in the amount of USD 980,462 thousand.

The net increase in interest income in 2006 was USD 64,233 thousand, which was primarily the result of the increase of bank deposits with original maturity from three to twelve months of USD 357,441 thousand.

Six months ended 30 June 2008 compared to 30 June 2007

The following table sets forth the components of financial and investment activity in the first six months of 2008 and 2007:

USD'000	Six months ended 30 June 2008 (restated)	Six months ended 30 June 2007 (restated)	Change, %
Finance costs	(2,335)	(2,667)	(12.4)
Income from investments..........................	25,047	34,801	(28.0)
Foreign exchange gain	290	6,629	(95.6)

Finance costs, income from investments and foreign exchange gain in the first six months were USD 23,002 thousand, a decrease of USD 15,761 thousand from USD 38,763 thousand in the first six months of 2007.

1.8 Income tax

2007 compared to 2006

During 2007, the Polyus Group accrued USD 85,299 thousand in income tax. The effective income tax rate (ratio of current and deferred tax expense to IFRS income before tax) in 2007 was 48%, whereas the statutory income tax rate in Russia established in 2007 was 24%. The difference in the effective tax rate was mainly because the Polyus Group had subsidiaries in other jurisdictions with higher effective tax rates and because of significant non-deductible items for tax purposes, primarily stock options. The effective tax rate in 2006 was 6%. This was primarily due to gains on the disposal of investments in Gold Fields, which was taxed in lower tax rate jurisdictions.

2006 compared to 2005

In 2006, the current income tax expense increased by USD 19,181 thousand (an increase of 36%) to USD 73,080 thousand, as compared to 2005. The effective rates in 2006 and 2005 were 6% and 28% respectively. The low effective income tax rate in 2006 was due to a significant portion of profits (realised gains on disposal of investments in Gold Fields Ltd.) being taxed in low tax rate jurisdictions, which offset the effects of disallowable items and taxable losses of subsidiaries not carried forward.

Six months ended 30 June 2008 compared to six months ended 30 June 2007

In the first half of 2008, the Polyus Group accrued USD 52,163 thousand as income tax, compared to USD 22,463 thousand in the same period for 2007. The effective income tax rate (ratio of current and deferred tax to profit before income tax and minority interest) in the first half of 2008 was 24%. In the first half of 2007 there was an income tax expense of USD 22,463 despite a pre-tax loss of USD 43,399. The first half of 2007 expense was due to a comparatively high amount of disallowable items and losses of subsidiaries not eligible for carry forward.

1.9 Other sales and cost of other sales

2007 compared to 2006

Revenues received by the Polyus Group from the sale of products other than gold and services did not change significantly from 2006 and amounted to USD 18,096 thousand. This revenue includes sales of electricity, revenue from transportation, handling and warehousing services, and other revenues. In 2007, the cost of sales of other products and services was higher than the revenue from their sale and amounted to USD 25,866 thousand. Sale of electricity to third parties accounted for USD 8,066 thousand in 2007, compared to USD 6,890 in 2006. Other cost of sales also included materials and payroll costs.

2006 compared to 2005

In 2006, revenues from other sales were USD 18,127 thousand, compared to USD 17,700 in 2005. Costs of other sales in 2006 were USD 18,816 thousand, compared to USD 19,750 thousand in the previous year.

Six months ended 30 June 2008 compared to six months ended 30 June 2007

Revenues received by the Polyus Group in the first half of 2008 from the sale of products other than gold and services increased by 51.7% compared to the first half of 2007 to USD 13,179 thousand.

In the first half of 2008 the cost of sales of other products and services was higher than the revenue from their sale and amounted to USD 13,230 million.

Other revenues include sales of power, transportation and loading services, and storage services.

Sale of electricity to third parties accounted for a significant portion of other revenues, representing USD 5,941 thousand in the first half of 2008. The majority of the sales were made by CJSC Vitimenergosbyt, a Polyus Group subsidiary located in Bodaibo district of Irkutsk region.

2. Non-GAAP financial measures

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

2.1 Adjusted EBITDA

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

The following table sets forth the Polyus Group's Adjusted EBITDA for the years ended 31 December 2007, 2006 and 2005:

	Years Ended December 31		
USD'000	**2007 (restated)**	**2006 (restated)**	**2005 (restated)**
Profit for the year	91,808	1,155,311	137,579
+ Income tax charged	85,299	73,080	53,899
+ Depreciation and amortisation for the year	92,495	79,025	50,993
+ Interest expense	6,629	6,453	3,586
– Interest payable written off	(4,055)	–	–
– Interest income	(51,493)	(107,616)	(43,383)
– Income on disposal of investments	(9,898)	(987,696)	(2,607)
+ Foreign exchange loss	–	75,344	250
– Foreign exchange gain	(8,484)	–	–
+ Loss from disposal of property, plant and equipment and work-in-progress	6,421	1,494	4,848
+ Impairment of property, plant and equipment	313	383	11,613
+ Reversal of environmental obligations	–	2,094	–
+ Change of provision for VAT receivable	–	2,814	1,340
+ Charge from stock option plan obligations	132,548	–	–
– Excess of the Group's share in the fair value of net assets acquired over the cost of acquisition	–	–	(15,746)
– Non-monetary changes in excessive stripping works[1]	(10,210)	785	(1,435)
Adjusted EBITDA	**331,373**	**301,471**	**200,937**

1. "Non-monetary changes in excessive stripping works" is a calculation made by Polyus Gold which estimates the non-cash portion of costs included in the costs attributable to deferred stripping costs, primarily representing depreciation and amortisation.

2007 compared to 2006

The Polyus Group's Adjusted EBITDA in 2007 was USD 331,373 thousand, which is USD 29,902 thousand or 9.9% more than in 2006, which is a reflection of increased gold prices, and the effects of an increase in cost structure.

2006 compared to 2005

In 2006, Adjusted EBITDA was USD 301,471 thousand compared to USD 200,937 thousand in 2005 as a result of an average price increase of more than 33% and increase in production and sales of greater than 20%.

The following table sets forth the Polyus Group's Adjusted EBITDA for the six months ended 2008 compared to the six months ended 2007:

	Six months ended 30 June	
USD'000	**2008 (restated)**	**2007 (restated)**
Profit/(loss) for the period	160,887	(65,862)
+ Income tax charged	52,163	22,463
+ Depreciation and amortisation for the period	55,633	50,620
+ Interest expenses	2,335	2,667
– Interest income	(10,494)	(30,264)
– Income on disposal of investments	(14,553)	(2,109)
– Foreign exchange gain	(290)	(6,629)
–/+ (Gain) / Loss from disposal of property, plant and equipment	(1,951)	5,564
+ Impairment of property, plant and equipment	–	68
+ Change of provision for VAT receivable	–	3
+ Change from stock option plan obligations	–	132,548
– Non-monetary changes in excessive stripping works[(1)]	(8,673)	(2,590)
Adjusted EBITDA	**235,057**	**106,479**

1. "Non-monetary changes in excessive stripping works" is a calculation made by Polyus Gold which estimates the non-cash portion of costs included in the costs attributable to deferred stripping costs, primarily representing depreciation and amortisation.

The Polyus Group's Adjusted EBITDA in the first half of 2008 was USD 235,057 thousand, which is USD 128,578 thousand more than in the first half of 2007 (an increase of 121%) reflecting increased gold prices.

2.2 Total Cash Costs

The Polyus Group calculates and presents the financial items TCC and "total cash costs per troy ounce" in accordance with industry practice. These items are not IFRS measures. An investor should not consider these items in isolation or as alternatives to cost of sales, profit for the year attributable to shareholders of Polyus Gold, net cash generated from operating activities or any other measure of financial performance presented in accordance with IFRS. The calculation of total cash costs may vary significantly among gold mining companies, and by themselves do not necessarily provide a basis for comparison with other gold mining companies.

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

The following table shows the Polyus Group's TCC for the years ended 31 December 2007, 2006 and 2005:

	Years Ended December 31			2007 against 2006	2006 against 2005
	2007 (restated)	2006 (restated)	2005 (restated)	%	%
Cost of gold sales (USD thousand)	449,216	426,527	260,030	5.3	64.0
– property, plant and equipment depreciation (USD thousand)	(87,196)	(73,718)	(45,251)	18.3	62.9
– provision for annual vacation payment (USD thousand)	(4,190)	(2,663)	–	57.3	–
– provision for land rehabilitation (USD thousand)	(482)	(7,318)	(2,088)	(93.4)	250.5
+ non-monetary changes in inventories[1] (USD thousand)	2,383	1,349	1,695	76.6	(20.4)
+ non-monetary changes in excessive stripping works[2] (USD thousand)	10,210	(785)	1,435	–	–
TCC (USD thousand)	369,941	343,393	215,820	7.7	59.1
Gold sales, thousand troy ounces	1,210	1,216	1,049	(0.5)	15.9
TCC, USD/oz	306	282	206	8.5	36.9
TCC, RUB/oz	7,820	7,677	5,820	1.9	31.9

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

2007 compared to 2006

In 2007, TCC per troy ounce in RUB grew by 1.9% and by 8.5% on a USD basis.

The increase in TCC was mainly due to the fact that cash operating costs increased by 27% for the period under review, while the volume of sales accounted for on the basis of troy ounces remained constant. See paragraph 1.4 above ("Cost of gold sales").

2006 compared to 2005

In 2006, TCC increased by 31.9% in RUB per troy ounce and by 36.9% in USD per troy ounce). This is mainly due to the acquisition of the Kuranakh mine, leading to both cash operating costs increasing by 50% in 2006 compared to 2005, and a 15.9% per cent increase in sales volumes. See paragraph 1.4 above ("Cost of gold sales").

The table below shows the Polyus Group's TCC for the six months ended 2008 compared to the six months ended 2007:

USD' 000	Six months ended 30 June 2008 (restated)	2007 (restated)	Change, %
Cost of gold sales (USD thousand)	243,644	192,261	26.7
- property, plant and equipment depreciation (USD thousand)	(52,805)	(48,457)	9.0
- provision for annual vacation payment (USD thousand)	(7,116)	(1,667)	326.9
- provision for land rehabilitation (USD thousand)	(618)	(549)	12.6
-/+ non-monetary changes in inventories[1] (USD thousand)	(350)	3,893	–
+ non-monetary changes in excessive stripping works[2] (USD thousand)	8,673	2,590	234.9
TCC (USD thousand)	191,428	148,071	29.3
Gold sales, thousand troy ounces	559	470	18.9
TCC, USD/oz	342	315	8.6
TCC, RUB/oz	8,200	8,217	(0.2)

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

For the six months ended 30 June 2008, TCC in RUB declined by 0.2%, while in USD it increased by 8.6% above the level of the previous period. The main reason for the growth of TCC in USD terms was that, in the first half of 2008, cash operating costs increased by 39% compared to the first half of 2007, combined with a 19% increase in volumes sold.

2.3 Adjusted net profit and other profitability indicators

Polyus Gold defines adjusted net profit as net profit attributable to its shareholders -adjusted for the charge in respect of its share option plan obligations in 2007 and the gain on its disposal of Gold Fields shares in 2006. Adjusted return on assets is calculated as the adjusted net profit divided by the average assets for the year. Adjusted return on equity is calculated as the adjusted net profit divided by the average equity attributable to shareholders of Polyus Gold for the year. Adjusted return on invested capital is calculated as the adjusted net profit divided by the sum of the average equity attributable to shareholders of Polyus Gold and average non-current and current loans and borrowings for the year.

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

The following table shows the Polyus Group's calculation of adjusted net profit, adjusted return on assets, adjusted return on equity and adjusted return on invested capital for the years ended 31 December 2007, 2006 and 2005:

USD'000, unless otherwise indicated	Years Ended 31 December 2007 (restated)	2006 (restated)	2005 (restated)	2007 against 2006 %	2006 against 2005 %
Net profit attributable to shareholders of Polyus Gold	85,809	1,155,725	137,562	n/a	n/a
+ Charge from stock option plan obligations(1)	132,548	–	–	–	–
- Gain on disposal of Gold Fields shares	–	(980,462)	–	–	–
Adjusted net profit	218,357	175,263	137,562	24.6	27.4
Assets (average for the year)	3,527,817	3,452,244	2,375,492	2.2	45.3
Equity attributable to shareholders of the parent (average for the year)	3,043,901	2,979,152	2,012,256	2.2	48.1
Non-current and current loans and borrowings (average for the year)	17,995	20,544	32,369	(12.4)	(36.5)
Adjusted return on assets(2), %	6.19	5.08	5.79	21.9	(12.3)
Adjusted return on equity(3), %	7.17	5.88	6.84	21.9	(14.0)
Adjusted return on invested capital(4), %	7.13	5.84	6.73	22.1	(13.2)

1. In 2007, net profit was adjusted for the cost of the share option plan and in 2006 for the amount of the gain on disposal of Gold Fields shares.
2. Adjusted return on assets is calculated as the adjusted net profit divided by the assets (average for the year).
3. Adjusted return on equity is calculated as the adjusted net profit divided by the equity attributable to shareholders of the parent (average for the year).
4. Adjusted return on invested capital is calculated as the adjusted net profit divided by the sum of equity attributable to shareholders of the parent (average for the year) and non-current and current loans and borrowings (average for the year).

2007 compared to 2006

Adjusted return on assets increased by 1.11 percentage points, adjusted return on equity increased by 1.29 percentage points and adjusted return on invested capital increased by 1.29 percentage points. The asset base of the Polyus Group increased significantly following the acquisition of the Kuranakh mine and the construction of Mill No. 3. Benefits are expected to accrue in the long term. As those assets are depreciated, the rates of return in an individual year may be expected to increase even higher.

2006 compared to 2005

In 2006, the Polyus Group's adjusted profitability indicators decreased. Adjusted return on assets declined by 0.71 percentage points to 5.08 %, adjusted return on equity declined by 0.96 percentage points and adjusted return on invested capital declined by 0.89 percentage points.

The following table shows the Polyus Group's analysis of adjusted net profit, adjusted return on assets, adjusted return on equity and adjusted return on invested capital for the six months ended 2008 compared to the six months ended 2007:

	Six months ended 30 June		
USD'000, unless otherwise indicated	**2008 (restated)**	**2007 (restated)**	**Change, %**
Net profit/(loss) attributable to shareholders of Polyus Gold	161,199	(66,512)	–
+ Charge from stock option plan[1]	–	132,548	–
Adjusted net profit	161,199	66,036	144.1
Assets (average for the period)	3,923,817	3,283,723	19.5
Equity attributable to shareholders of the parent (average for the period)	3,384,629	2,829,422	19.6
Non-current and current loans and borrowings (average for the period)	10,455	13,102	(20.2)
Adjusted return on assets[2], %	4.11	2.01	104.5
Adjusted return on equity[3], %	4.76	2.33	104.3
Adjusted return on invested capital[4], %	4.75	2.32	104.7

1. Net profit for the six months ended 30 June 2007 was adjusted for the cost of the share option plan.
2. Adjusted return on assets is calculated as the adjusted net profit divided by the assets (average for the year).
3. Adjusted return on equity is calculated as the adjusted net profit divided by the equity attributable to shareholders of the parent (average for the year).
4. Adjusted return on invested capital is calculated as the adjusted net profit divided by the sum of equity attributable to shareholders of the parent (average for the year) and non-current and current loans and borrowings (average for the period).

Profitability of both assets and equity and invested capital improved significantly. This improvement was mainly due to the fact that gross profit almost doubled and gross margin increased from 37.0% to 50.5% due to favourable gold price movements during the first six months of 2008 while the amount of assets and equity grew insignificantly. In the first half of 2008, loans and borrowing were redeemed which resulted in an improvement of invested capital profitability.

3. Summary table of performance results by business units

The following table shows the Polyus Group's performance results by business units for the years ended 31 December 2007, 2006 and 2005:

	2007			**2006**			**2005**		
	Revenue USD '000	**Production 000 oz**	**Sales 000 oz**	**Revenue USD '000**	**Production 000 oz**	**Sales 000 oz**	**Revenue USD '000**	**Production 000 oz**	**Sales 000 oz**
Krasnoyarsk business unit	603,649	861	856	516,076	854	855	357,767	783	795
Irkutsk hard rock business unit	23,231	32	33	18,517	32	31	6,623	15	15
Irkutsk alluvial business unit	124,111	179	179	103,984	172	172	94,230	212	211
Yakutia business unit	98,032	142	142	95,982	157	158	14,564[1]	28[1]	28[1]
Group total	**849,023**	**1,214**	**1,210**	**734,559**	**1,215**	**1,216**	**473,184**	**1,038**	**1,049**

1. The Polyus Group acquired the Yakutia business unit as a going concern in the fourth quarter of 2005.

3.1 Krasnoyarsk business unit (Olimpiada mine)

The Krasnoyarsk business unit is the Polyus Group's leading mining operation. In addition, the Krasnoyarsk business unit (CJSC Polyus) acts as a distributing agent and sells its own gold and that of its subsidiaries on the basis of agency agreements.

In 2007, gold sales of the Krasnoyarsk business unit were USD 603,649 thousand. In 2007, the entity sold 856 thousand troy ounces of gold from 861 thousand troy ounces of gold produced during the year. Between 2005 and 2007, the volume of production grew by 9.9%, the volume of sales grew by 7.7% and revenue increased by 68.7%.

Currently the mine is in transition to sulphide ores processing. Whereas in 2006 sulphide ores represented 67% of the total volume of ores processed, in 2007 this figure increased to 73%. Polyus Group expects that in 2009 the Olimpiada mine will completely convert to the processing of sulphide ores.

3.2 Irkutsk hard rock business unit (Zapadnoye mine)

In 2007, the Zapadnoye mine's gold sales were USD 23,231 thousand, which is 25.5% more than in 2006. The volume of production did not change significantly from 2006 levels. However, in 2006 gold production at the mine doubled and reached 32 thousand troy ounces compared to 15 thousand troy ounces in 2005. The significant growth in gold production by Zapadnoye mine was enabled by the improvement of mining technologies, and ore processing and recovery technologies.

In 2007, the volume of production was 213% of 2005 levels, the volume of sales was 220% of 2005 levels, and revenue increased by 251% as compared to 2005 levels.

3.3 Irkutsk alluvial gold business unit (Alluvial deposits)

In 2007, gold sales of the Irkutsk alluvial gold business unit were USD 124,111 thousand. In 2007, the total gold production from the alluvial deposits was 179 thousand troy ounces compared to 172 thousand troy ounces in 2006. In 2007, the Irkutsk alluvial gold business unit sold 178.9 thousand troy ounces of gold from 179 thousand troy ounces of gold produced within the year. In 2006, the total gold production from the Polyus Group's alluvial deposits was 18.9% lower than in 2005. The decrease in production in 2006 was mainly due to the depletion of the prepared ore, decline in grades of the sands washed, and the unfavourable weather conditions compared to those of the previous years.

In 2007, the volume of production and sales decreased by 15.6% and 15.2% respectively, while revenue increased by 31.7% as compared to 2005 levels. The Polyus Group believes that organisational improvements and an increase in exploration on the alluvial deposits should lead to a yield higher gold output in the coming years.

3.4 Yakutia business unit (Kuranakh mine)

In 2007, revenue of the Yakutia business unit totalled USD 98,032 thousand compared to USD 95,982 thousand in 2006. The revenue growth was due solely to the growth of the selling price, as the physical production of refined gold by the Kuranakh mine in 2007 reduced to 142 thousand troy ounces compared to 157 thousand troy ounces in 2006. The decrease of gold production by Kuranakh mine related primarily to deterioration of the average gold grade of the processed ore. In 2007, the Yakutia business unit sold 141.8 thousand troy ounces of gold from 142 thousand troy ounces of gold produced within the reporting period. Major steps were taken in 2006 to improve mine operations and to enable a consistent growth of gold output at Kuranakh mine in the future.

The Kuranakh mill was commissioned in 1965 and is one of the oldest enterprises in the industry and its obsolete production facilities have resulted in a gradual reduction of profitability. In 2007 and 2008, the Polyus Group implemented a modernisation programme which is expected to result in a gradual increase in profitability and production. The Polyus Group also plans to increase the mill's capacity from 3.6 million tonnes of ore per year to 4.5 million tonnes of ore per year.

The following table shows the Polyus Group's performance results by business units for six months ended 30 June 2008 compared to six months ended 30 June 2007:

	Six months ended 30 June					
	2008			2007		
	Revenue USD '000	Production 000 oz	Sales 000 oz	Revenue USD '000	Production 000 oz	Sales 000 oz
Krasnoyarsk business unit...	405,901	449	449	228,668	347	347
Irkutsk hard rock business unit	10,561	11	11	10,288	15	16
Irkutsk alluvial business unit...	26,861	31	31	24,108	37	37
Yakutia business unit...	62,407	68	68	46,296	69	71
Group total....	**505,730**	**559**	**559**	**309,360**	**469**	**471**

Krasnoyarsk business unit (Olimpiada mine)

Refined gold output at the Polyus Group's key production unit, Olimpiada Mine in Krasnoyarsk region, was 14.0 tonnes (449 thousand troy ounces) in the first half of 2008, compared to 10.8 tonnes (347 thousand troy ounces) for the same period in the previous year. Enhanced production at Olimpiada mine is related to the commissioning of a new sulphide ore processing plant, Mill No. 3. Mill No. 3 is the largest sulphide ore processing plant in Russia with a capacity of 5 million tonnes of ore per annum, was commissioned in July 2007. The increase in production was also achieved by putting into processing additional oxide ore, which was obtained as a result of additional exploration in the Vostochny pit of Olimpiada mine, and by putting into processing ore from Olenye deposit, which was mined in 2007. The enhanced production and sales volumes, coupled with increased gold prices, led to a 77.5% increase in revenues in the Krasnoyarsk business unit.

Irkutsk business unit (Zapadnoye Mine and alluvials)

Refined gold production at Zapadnoye Mine in the first half of 2008 was 0.4 tonnes (11 thousand troy ounces), compared to 0.5 tonnes (15 thousand troy ounces) in the same period in the previous year. Gold production at alluvial deposits in Irkutsk region in the first six months of 2008 was 1.0 tonnes (31 thousand troy ounces) of gold compared to 1.1 tonnes (37 thousand troy ounces) in the same period in the previous year.

Yakutia business unit (Kuranakh mine)

Kuranakh mine in the Sakha Republic (Yakutia) produced 2.1 tonnes (68 thousand troy ounces) of refined gold in the first six months of 2008, compared to 2.1 tonnes (69 thousand troy ounces) for the same period in the previous year. This insignificant reduction in production was caused by lower grades in the ore mined. The Polyus Group is in the process of modernizing its mill at the mine to increase its capacity from 3.6 million tones of ore per annum to 4.5 million tones of ore per annum. Main works on modernisation are expected to be completed in the first quarter of 2009.

4. Review of financial sustainability and solvency

4.1 Analysis of balance sheet items

The table below shows extracts of the Polyus Group's consolidated balance sheet as at 30 June 2008, and as at 31 December 2007, 2006, 2005:

USD '000	30 June 2008 (restated)	2007 (restated)	2006 (restated)	2005 (restated)
ASSETS				
Non-current assets				
Property, plant and equipment	2,049,429	1,783,432	1,395,605	1,107,993
Deferred stripping costs	144,886	82,061	10,382	14,438
Other non-current assets(1)	39,839	13,971	12,940	20,080
Total non-current assets	2,234,154	1,879,464	1,418,927	1,142,511
Current assets				
Inventories	239,272	224,209	169,471	123,056
Investments in securities and other financial assets	752,122	1,270,918	1,238,429	2,230,256
Cash and cash equivalents	672,110	226,174	294,197	28,408
Other current assets(2)	176,525	172,685	161,160	98,073
Total current assets	1,840,029	1,893,986	1,863,257	2,479,793
TOTAL ASSETS	4,074,183	3,773,450	3,282,184	3,622,304
EQUITY AND LIABILITIES				
Equity attributable to shareholders of Polyus Gold	3,507,484	3,261,774	2,826,027	3,132,277
Minority interest	45,335	47,187	32,647	29,762
TOTAL EQUITY	3,552,819	3,308,961	2,858,674	3,162,039
Total non-current liabilities	311,133	281,950	252,175	238,772
Current liabilities				
Short-term borrowings	–	20,909	15,001	26,087
Trade and other payables and accrued expenses	111,705	105,583	70,513	50,329
Other current liabilities(3)	98,526	56,047	85,821	145,077
Total current liabilities	210,231	182,539	171,335	221,493
TOTAL LIABILITIES	521,364	464,489	423,510	460,265
TOTAL EQUITY AND LIABILITIES	4,074,183	3,773,450	3,282,184	3,622,304

1. Other non-current assets consist of investments in securities and other financial assets and the long-term portion of reimbursable value added tax.
2. Other current assets consist of reimbursable value added tax, accounts receivable, advances paid to suppliers, income tax receivable and other current assets.
3. Other current liabilities consist of contingent consideration on acquisition of subsidiaries, dividends payable, minority interest liability, income tax payable and other taxes payable.

4.1.1 Assets

Non-current assets

The table below analyses the Polyus Group's property, plant and equipment at 30 June 2008, and at 31 December 2007, 2006 and 2005:

USD '000	30 June 2008 (restated)	2007 (restated)	2006 (restated)	2005 (restated)
Exploration and evaluation assets	401,949	301,238	133,811	63,176
Mining assets.............................	1,289,046	1,253,565	1,061,939	916,766
Non-mining assets.....................	40,428	41,084	37,350	34,712
Capital construction-in-progress	318,006	187,545	162,505	93,339
Total property, plant and equipment.................................	2,049,429	1,783,432	1,395,605	1,107,993

The Polyus Group's property, plant and equipment grew from USD 1,107,993 thousand at 31 December 2005, to USD 2,049,429 at 30 June 2008. The main reasons were:

- acquisition of the Kuranakh mine and associated assets by stages during 2005 and 2006;
- construction of Mill No. 3 at Olimpiada, mainly during 2007;
- exploration and evaluation of new prospects; and
- ongoing construction at all mines.

2007 compared to 2006

In 2007, the Polyus Group's assets structure did not undergo significant change. Whereas in 2006 non-current assets accounted for 43% of all the assets, in 2007 their share reached 50%. This change was primarily due to additions to property, plant and equipment. In 2007, the Polyus Group was actively involved in geological exploration and construction works, and therefore capitalised expenses for exploration and evaluation works (an increase of 125%) and assets used in construction-in-progress works (an increase of 15%). Additions to the most significant group of assets – mining assets – were 18% of the starting balance. The closing balance of mining assets was USD 1,253,565 thousand as at 31 December 2007.

Deferred stripping costs capitalised in 2007 grew substantially to USD 82,061 thousand, compared to USD 10,382 thousand in 2006. In 2007, the Polyus Group significantly increased its stripping costs at Olimpiada due to the depletion of the oxide ore and the commencement of extensive development of sulphide gold ore bodies in the open pit mine. In order to obtain access to the sulphide ore body the Polyus Group performed a substantial amount of overburden operations, resulting in significant stripping costs.

2006 compared to 2005

In 2006, the share of non-current assets increased in the Polyus Group's assets structure. In 2005, non-current assets accounted for 32% of all the assets, whereas in 2006 their share increased to 43%.

The net book value of property, plant and equipment increased by USD 287,612 thousand (an increase of 26.0%) from USD 1,107,993 as at 31 December 2005 thousand to USD 1,395,605 thousand as at 31 December 2006. The increase in net book value was primarily due to the acquisition of property, plant and equipment, together with construction-in-progress connected with the Mill No.3 construction at Olimpiada mine amounting to USD 270,713 thousand, and the addition of mining assets owned by subsidiaries acquired during the year amounting to USD 6,974 thousand.

In 2006, deferred stripping costs were USD 10,382 thousand, 28.1% lower than in 2005.

30 June 2008 compared to 31 December 2007

In the first six months of 2008, the Polyus Group's assets structure remained relatively constant. At 31 December 2007 non-current assets accounted for 50% of all the assets, while at 30 June 2008 they accounted for 55%.

During the first half of 2008, the Polyus Group continued its geological exploration and construction works. Capitalised expenses for exploration and evaluation works increased by 33.4% and assets used in construction-in-progress works increased by 69.6%. Additions to mining assets were 2.8% of the starting balance. The closing balance of mining assets was USD 1,289,046 thousand at 30 June 2008.

In the first six months of 2008, deferred stripping costs grew by 76.6% to USD 144,886 thousand. This increase was the result of the continued deferral of the stripping costs at Olimpiada in respect of accessing the sulphide ore body.

The long-term portion of reimbursable VAT increased significantly (an increase of 212.7 %) and equalled USD 36,975 thousand at 30 June 2008 as the Polyus Gold Group has paid VAT on capital projects.

Current assets

2007 compared to 2006

In 2007, there was an increase in the most significant groups of current assets, such as investments in securities and other financial assets, inventories and accounts receivable, while cash and cash equivalents decreased. The change was due to revaluation of the assets under trust management, the value of inventories and production growth. In addition, the value of reimbursable VAT increased.

As at 31 December 2007, the value of short-term investments in securities and other financial assets increased by 2.6% from 31 December 2006 and were USD 1,270,918 thousand. This primarily related to loans under repurchase agreements, which grew by USD 90,346 thousand, bank investment deposits and investments in securities available for sale, which also grew significantly. This increase was due to revaluation of the investment deposits under trust management of Rosbank and of Rosfund share.

Cash and cash equivalents on the Polyus Group's accounts decreased by USD 68,023 thousand, to USD 226,174 thousand at 31 December 2007 from USD 294,197 thousand at the end of 2006. This was primarily due to the growth of investments in securities and the effect of the capital expenditure programme, which required significant investments.

The Polyus Group's management pursues a policy of using its own current assets to finance the programme in order to retain the Polyus Group's financial sustainability and to postpone debt financing as long as possible.

Inventories increased by 32% to USD 224,209 thousand as at 31 December 2007. Stores and materials (net of allowance for obsolescence), which accounted for 75% of the total inventories value at 31 December 2007, increased by 31% compared to USD 128,121 thousand as at 31 December 2006. The volumes of diesel fuel, grinding balls and spare parts purchased for mining equipment significantly increased, because there was a several times increase in the volumes of processing at the Olimpiada mine following the commissioning of Mill No. 3. The cost of gold under processing also increased amounting to USD 54,961 thousand as at 31 December 2007 compared to USD 41,348 thousand as at 31 December 2006.

2006 compared to 2005

Investments in securities and other financial assets decreased by USD 991,827 thousand (or 44.5%) to USD 1,238,429 thousand as at 31 December 2006 as compared to USD 2,230,256 thousand as at 31 December 2005. The decrease was mainly due to the sale of the investment in Gold Fields, a USD 299,882 thousand decrease in promissory notes receivable and investment deposit with Rosbank, partly offset by a USD 660,969 thousand increase in bank deposits, loans under repurchase agreements, and equity securities due to the reinvestment of proceeds received on disposal of the stake in Gold Fields. Funds received were used in conjunction with current activities including:

- in a share buyback programme (USD 995,557 thousand);
- to buy out minority interests in some of the Polyus Group's subsidiaries (USD 307,667 thousand); and
- in the ongoing capital expenditure programme.

The total value of inventories consisting of refined gold, gold-in-process and stores and materials (net of allowance for obsolescence) increased by USD 46,415 thousand (or 38%) to USD 169,471 as at 31 December 2006 as compared to USD 123,056 thousand at 31 December 2005. The increase in inventories was due to the increase in work-in-process at Polyus by USD 8,313 thousand and at CJSC Sukhoi Log by USD 2,301 thousand, and an increase in stores and materials at Polyus by USD 23,068 thousand, at OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC by USD 7,872 thousand, and at other subsidiaries by USD 5,682 thousand. A 39.5% increase in stores and materials stock resulted from the purchase of additional spare parts for equipment and machinery acquired in 2006, and a 14-20% increase in fuel prices.

As at 31 December 2006, cash and cash equivalents were USD 294,197 thousand, compared to USD 28,408 thousand at 31 December 2005. This increase was primarily due to the cash proceeds received from the sale of the Gold Fields shares and cash proceeds from Norilsk Nickel in connection with the Polyus Group's spin-off.

As at 31 December 2006, advances to suppliers and other receivables were USD 38,087 thousand compared to USD 25,409 thousand at 31 December 2005. This 50% increase is mainly related to the capital construction-in-progress at CJSC Polyus, and to the increase in advance payments for materials and supplies at CJSC Polyus and LLC LZRK.

30 June 2008 compared to 31 December 2007

The value of short-term investments in securities and other financial assets decreased by 40.8% to USD 752,122 thousand as at 30 June 2008 compared to USD 1,270,918 thousand at 31 December 2007. By 30 June 2008 the Polyus Group had redeemed the promissory notes of Rosbank, withdrawn its investments in securities and closed its investment account at Rosbank. These funds were partly used in the capital expenditure programme, and partly distributed to current bank accounts. As a result of this redistribution cash and cash equivalents increased by 197.2% to USD 672,110 thousand at 30 June 2008 compared to USD 226,174 thousand at 31 December 2007.

Inventories increased by 6.7% to USD 239,272 thousand at 30 June 2008 compared to USD 224,209 thousand at 31 December 2007. Stores and materials (net of allowance for obsolescence) grew by 8.3% compared to 2007 and amounted to USD 181,982 thousand at 30 June 2008. The volumes of diesel fuel, grinding balls and spare parts purchased for mining equipment continued to grow. The cost of gold under processing was USD 54,198 thousand at 30 June 2008.

4.1.2 Capital and liabilities

Since 1 January 2005, the Polyus Group has been financed by equity capital and has had no significant bank debt.

4.1.3 Share capital and reserves

2007 compared to 2006

As at 31 December 2007 the share capital and reserves were USD 3,308,961 thousand, compared to USD 2,858,674 thousand at 31 December 2006.

The value of treasury shares at 31 December 2007 were USD 730,450 thousand, which is 27% less than at the end of 2006 (USD 995,557 thousand). During the year the Polyus Group sold 4,575,065 shares out of treasury under the share option plan for a total consideration of USD 64,051 thousand.

The additional paid-in capital decreased and was USD 2,118,165 thousand at 31 December 2007 (compared to USD 2,190,661 thousand at 31 December 2006).

During the period, Polyus Gold paid out dividends based on 2006 results, and the amount of dividends paid was USD 22,664 thousand. Of this, USD 942 thousand related to dividends to minority shareholders in Polyus Group subsidiaries.

The movement in exchange rates resulted in an increase in the translation reserve of USD 163,933 thousand.

2006 compared to 2005

As at 31 December 2006, Polyus Gold's share capital and reserves decreased by 9.6% to USD 2,858,674 thousand at 31 December 2006, compared to USD 3,162,039 thousand at 31 December 2005. The decrease in share capital and reserves was caused partly by the repurchase of 17,146,780 of Polyus Gold's own shares for the total amount of USD 995,557 thousand.

During the period the additional paid-in capital increased by 19.2% from USD 1,837,330 thousand at the end of 2005 to USD 2,190,661 thousand at the end of 2006 due to the issue of new shares.

Retained earnings were impacted by the result for the year and a USD 281,720 thousand reduction due to the acquisition of a non-controlling interest in a subsidiary.

The movement in exchange rates resulted in an increase in the translation reserve of USD 252,718 thousand of which USD 2,775 thousand was attributable to minority shareholders.

30 June 2008 compared to 31 December 2007

As at 30 June 2008, share capital and reserves were USD 3,552,819 thousand compared to USD 3,308,961 thousand at 31 December 2007.

Due to the change in RUB/USD exchange rate, the translation reserve has increased by USD 127,911 thousand. The Polyus Group's retained earnings grew by USD 109,162 thousand, reflecting net profit of USD 160,887 less dividends declared of USD 22,258 thousand (in respect of year 2007 results) and adjustments in connection with the acquisition of minorities and the change in shareholding structure in subsidiaries of USD 29,779 thousand.

4.1.4 Non-current liabilities

2007 compared to 2006

The largest portion of non-current liabilities was deferred tax liabilities, which at 31 December 2007 were USD 200,609 thousand compared to USD 178,860 thousand in the previous year. Environmental obligations increased by USD 9,828 thousand because of the unwinding of the discount and a strengthening of the US dollar.

2006 compared to 2005

Deferred tax liabilities did not change substantially. At the end of 2006 their value was USD 178,860 thousand, compared to USD 172,673 at the end of 2005. The remaining long-term liabilities, including environmental obligations and other non-current liabilities, changed insignificantly.

30 June 2008 compared to 31 December 2007

Deferred tax liabilities at 30 June 2008 were USD 223,095 thousand compared to USD 200,609 thousand at the beginning of the period. Environmental obligations increased by USD 6,697 thousand.

4.1.5 Current liabilities

2007 compared to 2006

The current liabilities structure slightly changed. The significant movement was the payment of contingent consideration on acquisition of subsidiaries of USD 38,228 thousand. The Polyus Group recognised liabilities under the share option plan in the amount of USD 5,357 thousand, which corresponded to the fair value of the option for 0.1% of the shares of the Polyus Group.

Historically the rate of borrowings by the Polyus Group was relatively low. The value of short-term borrowings by the Polyus Group increased from USD 15,001 thousand at 31 December 2006 to USD 20,909 at 31 December 2007. The weighted-average interest rate in 2006 was 12%, and in 2007 it decreased to 10%. This balance is mainly represented by USD-denominated loans from Flemicort Consulting Inc. at the effective interest rate of 8% per annum and RUB-denominated loans from Rosbank Management Company at the effective interest rate of 7% per annum.

Trade payables did not materially change and amounted to USD 21,651 thousand at 31 December 2006. Other payables and accrued expenses as at 31 December 2007 were USD 83,932 thousand, which is 69% more than in the previous year. This relates mainly to an increase in the volumes of property, plant and equipment purchases not paid for at the end of 2007. In addition, the Polyus Group's outstanding amounts on payroll settlements as of the year end were USD 28,069 thousand compared to USD 9,255 thousand as at 31 December 2006, which is mainly due to a delay in transferring funds from Head Office to subsidiaries.

Current tax liabilities as at 2007 were USD 33,850 thousand, which is 31.5% more compared to 31 December 2006. The growth mainly was the result of an increase in income tax payable (an increase of 68.4%) and VAT (an increase of 43.1%) liabilities as a result of increase in gold sales and profits.

2006 compared to 2005

The value of short-term borrowings decreased by 42.5%, to USD 15,001 thousand at 31 December 2006 compared to USD 26,087 thousand at 31 December 2005.

Contingent consideration for the acquisition of subsidiaries was 50.7% lower than in the previous year amounting to USD 60,087 thousand at 31 December 2006, compared to USD 121,904 thousand at 31 December 2005, due to the repayment of contingent consideration made in 2006 of USD 61,817 thousand.

As at 31 December 2006 trade payables increased by 31.2% to USD 20,799 thousand at the end of 2006. The value of other payables and accrued expenses was USD 49,714 at the end of 2006, which is 44.2% more than at the end of 2005. The increase in trade and other payables is due to USD 4,063 thousand increase in wages and salaries payable and USD 4,409 thousand in additional holiday accruals, and payable related to commencing exploration and mining works in OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC. Current tax liabilities increased by 11.1% to USD 25,734 thousand at the end of 2006, while property tax payable more than tripled for this period as a result of increase in the value of property, plant and equipment.

30 June 2008 compared to 31 December 2007

Trade payables were USD 56,713 thousand compared to USD 21,651 thousand at 31 December 2007. Other payables and accrued expenses as at 30 June 2008 were USD 54,992 thousand compared to USD 83,932 thousand as at the beginning of 2008. The unsettled liabilities under the share option plan were partly settled (representing 50% of liabilities), and the remaining 50% expired and was written off through the income statement. At the beginning of the period these liabilities were USD 5,357 thousand, which corresponds to the fair value of the option for 0.1% of the shares of the Polyus Group. In addition, in the first half of 2008 the Polyus Group accrued a dividends payable obligation in the sum of USD 22,721 thousand, following a General Shareholders' meeting on 26 June 2008. Borrowings were all repaid in the first half of 2008, and contingent consideration on acquisition of subsidiaries reduced significantly as a result of payments made of USD 20,069 thousand.

In May 2008, Polyus Gold's subsidiary, CJSC Polyus, completed the purchase of an additional 2.7% of the shares of OJSC Matrosov mine, bringing the total percentage of ownership of Matrosov mine by CJSC Polyus to 97.5%. Under Russian legislation, the Polyus Group has an obligation to make an offer to purchase the remaining shares held by Matrosov mine's minority shareholders. The Polyus Group recognised a liability equal to the fair value of the ultimate cash obligation in its balance sheet as of 30 June 2008, and a decrease in minority interest in respect of this transaction in its condensed consolidated statement of changes in equity in the amount of USD 4,974 thousand for the six months ended 30 June 2008. The difference between the carrying value of the minority interest derecognised in equity and the fair value of the obligation was recognised in the condensed consolidated statement of changes in equity for the six months ended 30 June 2008.

Current income tax liabilities more than doubled to USD 28,579 thousand at 30 June 2008. This was mainly due to a significant growth of the Polyus Group's income as a result of increasing sales partly offset by the growth of operating expenses. At the end of the period other taxes payable equalled to USD 25,405 thousand compared to USD 21,187 thousand as at 31 December 2007. The growth was due to the increase in unified social tax (an increase of 117.9%) and personal income tax (an increase of 127.2%) liabilities. The unified social tax and personal income tax liabilities increased as a result of the growth of wages of production staff.

4.2 Cash flow analysis

The following table shows extracts of the Polyus Group's consolidated cash flow statement for the years ended 31 December 2007, 2006 and 2005 and for the six months ended 30 June 2008 and 2007:

				Six months ended 30 June	
USD '000	**2007 (restated)**	**2006 (restated)**	**2005 (restated)**	**2008 (restated)**	**2007 (restated)**
Operating activities					
Profit before income tax	**177,107**	**1,228,391**	**191,478**	**213,050**	**(43,399)**
Adjustments[(1)]	170,023	(918,134)	6,788	27,879	168,530
Operating profit before working capital changes	**347,130**	**310,257**	**198,266**	**240,929**	**125,131**
Changes in working capital	(40,197)	(69,771)	(90,877)	(25,444)	33,358
Cash flows from operations	**306,933**	**240,486**	**107,389**	**215,485**	**158,489**
Interest paid	(1,671)	(3,552)	(2,438)	(2,527)	(696)
Income tax paid	(50,187)	(89,897)	(45,600)	(27,126)	(27,758)
Net cash generated from operating activities	**255,075**	**147,037**	**59,351**	**185,832**	**130,035**
Investing activities					
Capital expenditures[(2)]	(469,823)	(625,005)	(304,302)	(325,480)	(197,891)
Other investments spendings/ proceeds[(3)]	90,648	1,320,495	(1,010,813)	591,585	189,604
Net cash (used in)/generated from investing activities	**(379,175)**	**695,490**	**(1,315,115)**	**266,105**	**(8,287)**
Net cash generated from/(used in) financing activities	**42,337**	**(632,895)**	**1,269,846**	**(20,835)**	**(2,956)**
Effect of translation to presentation currency	13,740	56,157	1,311	14,834	7,730
Net (decrease)/increase in cash and cash equivalents	**(68,023)**	**265,789**	**15,393**	**445,936**	**126,522**
Cash and cash equivalents at beginning of the year	**294,197**	**28,408**	**13,015**	**226,174**	**294,197**
Cash and cash equivalents at end of the year	**226,174**	**294,197**	**28,408**	**672,110**	**420,719**

1. Adjustments for non-cash items include: the share option plan, amortisation and depreciation, expensed stripping costs, finance costs, loss on disposal of property, plant and equipment, change in allowance for doubtful debts, impairment of advances paid to suppliers (reversed)/recognised, change in provision for land restoration, impairment of property, plant and equipment, change in allowance for reimbursable value added tax, income from investments, foreign exchange (gain)/loss, net and other items.
2. Capital expenditures include purchases of property, plant and equipment, acquisition of shares in subsidiaries, deferred stripping costs capitalised, interest received, proceeds from sale of property, plant and equipment and proceeds from sale of shares in subsidiaries.
3. Other investments spendings/proceeds include repayment of contingent consideration, proceeds from sale of shares in Gold Fields, dividends received, purchase of promissory notes and other financial assets and proceeds from sale of promissory notes and other financial assets.

2007 compared to 2006

In 2007, net cash provided by operating activities increased by USD 108,038 thousand to USD 255,075 thousand. The increase of net inflow of cash from operations resulted mainly from a USD 114,464 thousand increase in gold sales connected with the increase in gold prices growth and an increase in physical production volumes, together with a USD 39,710 thousand reduction in current income tax paid. The positive changes in cash flow from operations was partly offset by cash outflow caused by the purchase of inventories. The increase of these costs was a result of increased prices on fuel and materials.

During 2007, the Polyus Group used USD 379,175 thousand in investment activities, while in 2006 it received USD 695,490 thousand from investment activities. Total change of net cash flows from investment activities was USD 1,074,665 thousand. This change was primarily due to the fact that in 2006 the Polyus Group received net proceeds in the amount of USD 1,925,402 thousand from disposal of the Polyus Group's stake in Gold Fields, which it acquired in 2005. During 2007, the Polyus Group also actively purchased property, plant and equipment. The total amount spent for these purposes totalled USD 382,802 thousand. In addition, interest income received by the Polyus Group in 2007 included USD 82,382 thousand less than in 2006 and amounted to USD 26,696 thousand.

Cash received from financing activities in the year ended 31 December 2007 totalled USD 42,337 thousand compared to cash used in financing activities in the amount of USD 632,895 thousand in the year ended 31 December 2006. The net cash outflow in 2006 was primarily due to the buyback of Polyus Gold Shares for the total amount of USD 995,557 thousand, partly offset by a USD 360,197 cash contribution by Norilsk Nickel in connection with the spin-off. The major cash flows in 2007 were proceeds from sale of treasury shares of USD 64,051 thousand and dividends paid of USD 21,722 thousand.

2006 compared to 2005

In 2006, net cash inflow from operations more than doubled over the 2005 levels to USD 147,037 thousand. The improvement in net cash inflow from operating activities resulted mainly from an increase of USD 261,375 thousand in gold sales, resulting from gold selling price growth, and an increase in physical production volumes during the year ended 31 December 2005. The positive changes in cash flow from operations was partly offset by cash outflow caused by the purchase of inventories.

Net cash outflow from investing of USD 1,315,115 thousand in the year ended 31 December 2005 was followed by net cash inflow of USD 695,490 thousand in the year ended 31 December 2006.

The overall change in net cash flow from investing activities by USD 2,010,605 thousand was the result of the following:

- In the year ended 31 December 2006, the Polyus Group paid for the shares in acquired subsidiaries in the amount of USD 307,667 thousand (net of cash acquired), compared to USD 153,560 thousand a year before. Included in both years' payments were those for shares in OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC with the total purchase price of USD 236,904 thousand (USD 115,000 thousand was paid in the year 2005, USD 61,817 thousand in 2006, the remainder in 2007). Included in the year 2005 payment were also 74% of the shares in OJSC Pervenets for USD 25,816 thousand, 1% of the shares in OJSC Matrosov Mine for USD 4,265 thousand, 11.2% of the shares in Lenzoloto for USD 8,289 thousand, and 100% of the shares in CJSC Sibzolotorazvedka for USD 727 thousand. During the year 2006 the Polyus Group acquired an additional 50% interest in OJSC SVMC for USD 300,167 million and a 100% interest in LLC GRK BarGold for USD 7,500 thousand.
- During the year ended 31 December 2006, investment in the acquisition of property, plant and equipment was USD 267,551 thousand, an 86% increase compared to the year ended 31 December 2005. This increase was primarily due to the construction of Mill No. 3 at

Olimpiada mine and fixed assets purchases by OJSC Aldanzoloto GRK, OJSC SVMC and OJSC YMC, and to payments for exploration works.

- During the year ended 31 December 2006, the Polyus Group disposed of its stake in Gold Fields acquired in the year ended 31 December 2005, resulting in the recognition of net proceeds in the amount of USD 1,925,402 thousand. The net proceeds received on disposal were reinvested into short-term bank deposits, Rosbank promissory notes and other financial assets in the same period (although some of the Gold Fields proceeds were re-invested in deposits with a less than three months' term and are thus classified as cash and cash equivalents).
- During the year ended 31 December 2006 the Polyus Group received final dividends for 2005 from Gold Fields in the amount of USD 6,420 thousand, and interest income of USD 109,078 thousand, which is USD 76,627 thousand more than in 2005.

Net cash outflow from financing activities in the year ended 31 December 2006 was USD 632,895 thousand, compared to a USD 1,269,846 thousand net cash inflow from financing activities in the year ended 31 December 2005. The net cash inflow in the year 2005 was due to the proceeds of CJSC Polyus shares issue in the amount of USD 1,299,745 thousand, while the net cash outflow in the year 2006 was mostly due to the acquisition by the Polyus Group of the issued shares of Polyus Gold for a total consideration of USD 995,557 thousand in November 2006, partly offset by a USD 360,197 cash contribution by Norilsk Nickel in connection with the spin-off.

30 June 2008 compared to 30 June 2007

In the first half of 2008, the Polyus Group generated income before tax in the amount of USD 213,050 thousand, compared to a loss of USD 43,399 thousand in the first half of 2007. This increase was due to growing revenues, which resulted from the increase in both gold selling prices and physical production volumes. As a result, operating profit before working capital changes was USD 240,929 thousand, which is 92.5% higher than in the first half of 2007. USD 25,444 thousand was used for working capital financing, with the value of current assets and advances to suppliers increasing in the period. In the first half of 2008 net cash generated from operating activities increased by USD 55,797 thousand and totalled USD 185,832 thousand.

During the six months ended 30 June 2008, the Polyus Group substantially increased its capital expenditures by 64.5%. Capital expenditures were USD 325,480 thousand, compared to USD 197,891 thousand in the same period of the previous year. However, while the capital expenditures were high, the Polyus Group had cash inflow from investments, as it closed positions on Rosbank promissory notes, and a number of deposits and trust management contracts for a total amount of USD 574,506 thousand. As a result in the first half of 2008 the Polyus Group received USD 266,105 thousand of net cash generated from investing activities, compared to USD 8,287 thousand spent in the first half of 2007.

In the first half of 2008, the Polyus Group repaid the loan obtained by its associated company OJCS SVMC for the total amount of USD 19,843 thousand. This resulted in increased net financing cash outflow in the sum of USD 20,835 thousand compared to an outflow of USD 2,956 thousand in the first half of 2007.

4.3 Capital expenditures, acquisitions of subsidiaries and deferred stripping costs

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

The following table shows the Polyus Group's capital expenditures, acquisition of subsidiaries and deferred stripping costs for the years ended 31 December 2007, 2006 and 2005:

	Years Ended 31 December		
USD'000	2007 (restated)	2006 (restated)	2005 (restated)
+ Purchase of property, plant and equipment	382,802	267,551	143,946
– Proceeds from sale of property, plant and equipment	(17,952)	(12,030)	(2,876)
Net capital expenditures	**364,850**	**255,521**	**141,070**
Acquisition of subsidiaries, net of cash acquired, and increase of ownership in subsidiaries	–	307,667	153,560
+ Repayment of contingent consideration on acquisition of subsidiaries	38,228	61,817	
– Proceeds from disposal of subsidiary, net of cash disposed of	(1,320)	–	107
Acquisition of subsidiaries, net of adjustments above	**36,908**	**369,484**	**153,667**
+ Deferred stripping costs capitalised	68,065	–	9,565
+ Interest expenses capitalised	–	–	–
Total capital expenditures, acquisition of subsidiaries and deferred stripping costs	**469,823**	**625,005**	**304,302**

2007 compared to 2006

In 2007, the Polyus Group spent USD 469,823 thousand on total capital expenditures, acquisition of subsidiaries and deferred stripping costs. This is less than in 2006 due to the fact that in 2006 a significant amount was expended on the acquisition of subsidiaries (USD 369,484 thousand). In 2007, the Polyus Group spent USD 382,802 thousand on property, plant and equipment, compared to USD 267,551 thousand in 2006, mainly relating to the construction of Mill No. 3 at Olimpiada. In 2007, stripping costs capitalised were USD 68,065 thousand, compared to nil in 2006 due to the costs incurred on deferred stripping relating to the transition of production at Olimpiada mine from oxide ore to sulphide ore.

2006 compared to 2005

In 2006, the Polyus Group substantially expanded its capital expenditures and acquisitions of subsidiaries. The total spent in this area more than doubled in 2006 to USD 625,005 thousand compared to USD 304,302 thousand in 2005. The major reason for the increase was the acquisition of corporate entities in the Yakut region, including OJSC Aldanzoloto, which controls the Kuranakh mine. Purchases of property, plant and equipment increased from USD 143,946 thousand in 2005 to USD 267,551 thousand in 2006.

The following table shows the Polyus Group's capital expenditures, costs of acquisitions of subsidiaries and deferred stripping costs for the six months ended 30 June 2008 compared to the six months ended 30 June 2007:

	Six months ended 30 June	
USD'000	**2008 (restated)**	**2007 (restated)**
+ Purchase of property, plant and equipment	230,101	162,094
- Proceeds from sale of property, plant and equipment	(4,635)	(4,146)
Net capital expenditures	**225,466**	**157,948**
Acquisition of subsidiaries, net of cash acquired, and increase of ownership in subsidiaries................................	22,128	–
+ Repayment of contingent consideration on acquisition of subsidiaries	20,069	22,677
- Proceeds from disposal of subsidiary, net of cash disposed of..	**–**	**–**
Acquistion of subsidiaries, net of adjustments above	42,197	22,677
+ Deferred stripping costs capitalised	57,817	17,266
+ Interest expenses capitalised..	–	–
Total capital expenditures, costs of acquisition of subsidiaries and deferred stripping costs......................	**325,480**	**197,891**

In the first half of 2008, the Polyus Group spent USD 325,480 thousand on capital expenditures, costs of acquisitions of subsidiaries and deferred stripping costs. Approximately 71% of these investments were used for purchase of property, plant and equipment, including equipment for mills under construction, mining and construction equipment and rolled metal products. Stripping expenses capitalised were USD 57,817, while in the same period of the previous year these expenses totalled USD 17,266 thousand due to ongoing stripping at Olimpiada mine.