Open Joint Stock Company Concern "Kalina" and subsidiaries

Consolidated Financial Statements
Year Ended December 31, 2005

OPEN JOINT STOCK COMPANY CONCERN “KALINA” AND SUBSIDIARIES

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CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED DECEMBER 31, 2005
(in Roubles and in thousands)

	Notes	2005 ‘000 RUR	2004 ‘000 RUR
REVENUE		8,150,535	5,237,636
COST OF SALES		(4,336,697)	(2,583,641)
GROSS PROFIT		3,813,838	2,653,995
Selling, general and administrative expenses	14	(2,908,280)	(1,871,900)
OPERATING PROFIT		905,558	782,095
Finance costs, net		(89,278)	(3,368)
Investment income		21,561	9,676
Other expense		(3,632)	(4,739)
Foreign exchange differences		(42,605)	21,602
PROFIT BEFORE INCOME TAX AND MINORITY INTEREST		791,604	805,266
INCOME TAX	15	(85,704)	(230,667)
PROFIT FROM CONTINUING OPERATIONS AFTER INCOME TAX AND BEFORE MINORITY INTEREST		**705,900**	**574,599**
Loss for the period from discontinued operations		**(39,616)**	**(44,399)**
PROFIT for the year		**666,284**	**530,200**
Attributable to:			
EQUITY holders of the parent		648,843	530,200
Minority interest		17,411	-

See notes to the consolidated financial statements on pages 8-23.

OJSC "KALINA" AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET
AT DECEMBER 31, 2005
(in Roubles and in thousands)

	Notes	2005 '000 RUR	2004 '000 RUR
ASSETS			
NON-CURRENT ASSETS:			
Property, plant and equipment, net	9	2,692,380	852,380
Goodwill, net		71,062	-
Intangible assets	13	363,646	12,561
Investments in associates	8	72,018	79,420
ASSETS RELATED TO A DISPOSAL GROUP		143,991	166,533
DEFERRED TAX ASSETS, NET	15	121,830	47,370
CURRENT ASSETS:			
Inventories	6	2,410,314	1,148,120
Trade accounts receivable, net	5	1,125,336	366,847
Value added tax and other taxes receivable	7	515,997	315,628
Advances paid	6	323,964	446,197
Other receivables, net	5	84,568	32,967
Short-term investments		-	2,923
Cash and cash equivalents	4	193,365	1,120,316
TOTAL ASSETS		**8,118,471**	**4,591,261**
SHAREHOLDERS' EQUITY AND LIABILITIES			
SHAREHOLDERS' EQUITY:			
Share capital		851,842	851,842
Translation reserve		(49,588)	-
Retained earnings		2,752,012	2,245,640
Minority interest		345,573	-
LIABILITIES RELATED TO A DISPOSAL GROUP		324,169	316,243
DEFERRED TAX LIABILITIES, NET	15	306,667	55,719
NON-CURRENT LIABILITIES:			
Long-term bank loans	12	472,853	217,530
Retirement benefits obligations		173,694	-
Long-term obligations under finance lease	12	35,894	1,009

OJSC "KALINA" AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET
AT DECEMBER 31, 2005 (continued)
(in Roubles and in thousands)

	Notes	2005 '000 RUR	2004 '000 RUR
CURRENT LIABILITIES:			
Trade accounts payable	10	1,001,415	558,013
Other payables and accrued expenses		520,113	78,333
Tax liability	7	103,480	126,548
Short-term obligations under finance lease		34,269	7,306
Short-term bank loans	11	1,246,079	133,081
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		**8,118,471**	**4,591,261**

See notes to the consolidated financial statements on pages 8-23.

OJSC CONCERN “KALINA” AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS’ EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2005
(in Roubles and in thousands)

	Capital Stock	Additional Paid In Capital	Translation reserve	Retained Earnings	Total Stockholders’ Equity
	‘000 RUR	**‘000 RUR**	**‘000 RUR**	**‘000 RUR**	**‘000 RUR**
Balance December 31, 2003	**93,345**	**-**	**-**	**1,798,018**	**1,891,363**
Net income	-	-	-	530,200	530,200
New stock issue	-	758,497	-	-	758,497
Dividends declared	-	-	-	(82,578)	(82,578)
Balance December 31, 2004	**93,345**	**758,497**	**-**	**2,245,640**	**3,097,481**
Translation adjustment	-	-	(49,588)	-	(49,588)
Net income	-	-	-	648,843	648,843
CPT reversal	-	-	-	1,767	1,767
Dividends declared	-	-	-	(144,237)	(144,237)
Balance December 31, 2005	**93,345**	**758,497**	**(49,588)**	**2,752,012**	**3,554,266**

See notes to the consolidated financial statements on pages 8-23.

OJSC OCNCERN “KALINA” AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED DECEMBER 31, 2005
(in US dollars and in thousands)

	2005 ‘000 RUR	2004 ‘000 RUR
CASH FLOWS FROM OPERATING ACTIVITIES:		
Profit before income tax	791,604	805,266
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation property, plant and equipment	241,842	57,656
Amortization of intangible assets	-	2,542
Loss on disposal of property, plant and equipment	-	6,455
Gain on disposal of long-term investment	(4,626)	-
Finance costs, net	89,278	(1,153)
Discontinued operations, net effect on P&L	30,468	64,735
Operating cash flow before movements in working capital	1,148,566	935,501
Increase in trade accounts receivable	(435,896)	(51,175)
Decrease in other receivables and prepaid expenses	129,376	62,489
Increase in inventories	(905,424)	(86,204)
Increase in trade accounts payable	400,563	121,805
Decrease in PBO	(8,139)	-
Decrease in taxes payable (other than income tax)	(19,201)	(110,390)
Decrease (increase) in taxes recoverable (other than income tax)	(2,435)	26,250
Net cash provided by (used in) operations:	307,410	898,276
Income tax paid	(197,935)	(186,606)
Interest paid, net	(68,035)	(2,813)
Net cash provided by operating activities	41,440	708,857
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, plant, equipment and intangible assets	(882,440)	(104,368)
Proceeds from disposal of property, plant and equipment	1,347	1,959
Purchase of intangible assets	(11,080)	
Purchase of long-term investments in Dr. Scheller	(609,428)	(106,270)
Proceeds from disposal of long-term investments	14,888	
Purchase of short-term investments	(9,259)	
Proceeds from disposal of short-term investments	12,182	
Net cash used in investing activities	(1,483,790)	(208,679)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock		758,497
Dividends paid	(144,237)	(129,206)
Proceeds from/(principal payments on) short-term borrowings, net	810,360	(524,144)
Proceeds from long-term borrowings	262,228	331,372
Principal payments on long-term borrowings	(258,835)	(19,220)
Principal payments on capital lease obligations	(56,095)	(10,804)
Net cash provided by/(used in) financing activities	613,421	406,495
EFFECT OF FOREIGN EXCHANGE RATES ON CASH AND CASH EQUIVALENTS	(98,022)	(13,657)

NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS	(828,929)	906,673
CASH AND CASH EQUIVALENTS, beginning of period	1,120,316	227,300
CASH AND CASH EQUIVALENTS, end of period	193,365	1,120,316

See notes to the consolidated financial statements on pages 8-23.

1. DESCRIPTION OF BUSINESS

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

Operating subsidiary	Share of ownership	Place of incorporation	Principal activity
LLC Pallada Vostok	100%	Uzbekistan	Manufacturing
JSC Lola Atir Upa	56%	Uzbekistan	Manufacturing
LLC Pallada Ukraina	100%	Ukraine	Trading
LLC Zavod Novoplast	100%	Russia	Manufacturing
Kalina Overseas Holding B.V.	100%	Netherlands	Trading
Kosmetik und Rasierwaren Solingen GmbH	61.37%	Germany	Trading
Dr. Scheller DuroDont GmbH	61.37%	Germany	Trading
Lady Manhattan Cosmetics GmbH	61.37%	Germany	Trading
Apotheker Scheller Naturmittel GmbH	61.37%	Germany	Trading
Premium Cosmetics GmbH	61.37%	Germany	Trading
Lady Manhattan Cosmetics GmbH	61.37%	Austria	Trading
Dr. Scheller Cosmetics Polska Sp. zo.o.	61.37%	Poland	Trading
Lady Manhattan Ltd.	61.37%	UK	Trading

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

In June and December 2003 the Group management made a decision to dispose of its 65% share in JSC Alye Parusa (Ukraine) and its wholly owned subsidiary LLC Pallada Vostok (Uzbekistan) respectively, therefore their assets, liabilities as well as cash flows and financial results for the reporting period ended December 31, 2005 are presented as assets, liabilities, cash flows and financial results associated with discontinued operations (Notes 16).

2. PRESENTATION OF FINANCIAL STATEMENTS

***Basis of Presentation* –** The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). Russian statutory accounting principals and procedures differ substantially from those generally accepted under IFRS. Accordingly, the consolidated financial statements, which have been prepared from the Group's Russian statutory accounting records, reflect adjustments necessary for such financial statements to be presented in accordance with IFRS.

The consolidated financial statements of the Group are prepared on the historical cost basis, except for:

- valuation of property, plant and equipment in accordance with both IAS No. 16 “Property, Plant and Equipment” (“IAS 16”);
- valuation of financial instruments in accordance with IAS No. 39 “Financial Instruments: Recognition and Measurement” (“IAS 39”) (more fully described in Note 3);

Use of Estimates and Assumptions – The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. Due to the inherent uncertainty in making those estimates, actual results reported in future periods could differ from such estimates.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Intangible Non-Current Assets – Intangible assets are carried out at a revalued amount, being its fair value at the date of the revaluation less any subsequent accumulated amortization and any subsequent accumulated impairment losses. The fair value is determined by reference to an active market. Revaluations is made with such regularity that at the balance sheet date the carrying amount of the asset does not differ materially from its fair value. At each balance sheet date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is impossible to estimate the recoverable amount of an individual asset, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs. Recoverable amount is the higher of an asset’s net selling price and its value in use, which is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life.

Intangible assets are primarily comprised of trademarks, which have arisen following the acquisition of Dr Scheller AG and were included at fair value on acquisition of Dr Scheller, as at 31/03/05.

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

Assets held under finance leases are recognized as assets of the Group at their fair value at the date of acquisition. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation. Finance costs which represent the difference between the total leasing commitments and the fair value of the assets acquired, are charged to the income statement over the term of the relevant lease so as to produce a constant periodic rate of charge on the remaining balance of the obligations for each accounting period.

Leased assets are depreciated over their estimated useful economic lives or over the term of the lease, if shorter. If there is reasonable certainty that the lessee will obtain ownership by the end of the lease term, the period of expected use is the useful life of the asset. Rents paid under operating leases are charged to the income statement as incurred.

Income taxes – Income taxes payable have been computed in accordance with the laws of the Russian Federation, Ukraine, Uzbekistan and Germany. The Group accounts for deferred taxes on income using the asset and liability method wherein material deferred tax assets and liabilities are recognized based on the future consequences of temporary differences between the financial reporting carrying amounts and tax bases of assets and liabilities using the current enacted income tax rates.

Deferred tax adjustments resulting from the elimination of unrealised profit on intercompany transactions are calculated by reference to the statutory tax rates in place in the country of the selling entity.

Basis of Consolidation – The consolidated financial statements include the accounts of the Company and its operating subsidiaries after the elimination of significant intercompany transactions and balances.

All significant intercompany transactions, balances and unrealized gains (losses) on transactions are eliminated on consolidation.

Business Combinations – For business combinations that have been accounted for under the purchase method of accounting, the financial statements of the Company include the results of operations of the acquired businesses from the date of acquisition. The excess of the fair value of identifiable tangible and intangible net assets acquired over the purchase price (negative goodwill) is used to reduce the fair value of long-term non-monetary assets acquired.

Concentration of Credit Risk – Financial instruments that potentially expose the Group to concentration of credit risk consist primarily of cash, cash equivalents and accounts receivable.

The carrying amount of financial instruments, including cash and cash equivalents and short-term obligations, approximates fair value due to the short-term maturity of the instruments.

Cash and Cash Equivalents – Cash include petty cash and cash held on current bank accounts.

Accounts Receivable – Accounts receivable are stated at their net realizable value after deducting a provision for doubtful accounts. Such provision reflects either specific cases or estimates based on evidence of recoverability.

Inventories – Inventories are stated at the lower of cost, determined by the first-in first-out method for raw materials and weighted average for finished goods, or market value.

Property, Plant and Equipment – Property, plant and equipment is carried at cost less accumulated depreciation. Depreciation is charged using the straight-line method over the asset's estimated useful lives. When assets are retired or otherwise disposed of, the cost and the accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in the statement of operations. The cost of maintenance and repairs is charged to the statement of operations as incurred. Significant renewals and betterment, that extend an asset's estimated useful life, are capitalized.

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

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

Property, plant and equipment held and used by the Group are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of assets may have been impaired. Management considers that no impairment has occurred relating to the Group's investments in property, plant and equipment as of December 31, 2005.

Impairment of tangible and intangible assets – At each balance sheet date, the Company (Group) reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is impossible to estimate the recoverable amount of an individual asset, the Company (Group) estimates the recoverable amount of the cash-generating unit to which the asset belongs.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. Impairment losses are recognized as an expense immediately, unless the relevant asset is land, buildings, other than investment property, or equipment, carried at a revalued amount, in which case the impairment loss is treated as decrease in revaluation reserve.

Sales recognition – Sales are recognized when it is probable that the economic benefits associated with the transaction will flow to the enterprise and the amount of revenue can be measured reliably. Sales are recognized net of value added tax. No sales returns are expected after reporting date.

Borrowing Costs – Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. All other borrowing costs are recognized as an expense in the period in which they are incurred.

4. CASH AND CASH EQUIVALENTS

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

	2005 '000 RUR	2004 '000 RUR
Cash on hand – RUR	370	236
Cash in bank – RUR accounts	84,093	46,115
Cash in bank – USD accounts	23,092	5,969
Bank deposits – RUR accounts	0	0
Bank deposit – EUR accounts	0	1,032,228
Restricted cash – USD accounts	78,871	30,302
Other – EUR euro, UAH, UZS accounts	6,939	5,466
Total	**193,365**	**1,120,316**

The restricted cash is presented by the amounts reserved on Citibank accounts accordingly to loan agreement between the Company and European Bank for Reconstruction and Development for interest and principal debt repayments.

5. ACCOUNTS RECEIVABLE, NET

Accounts receivable consisted of the following at December 31, 2005:

	2005 '000 RUR	2004 '000 RUR
Accounts receivable – trade	1,247,042	489,991
Other accounts receivable	84,568	32,968
Bad debt allowance	(121,706)	(123,144)
Total	**1,209,904**	**399,815**

6. ADVANCES TO SUPPLIERS AND PREPAID EXPENSES

Advances to suppliers and prepaid expenses consisted of the following at December 31, 2005:

	2005	2004
	'000 RUR	**'000 RUR**
Advances to suppliers	389,642	481,208
Bad debt allowance	(72,266)	(37,975)
Prepaid expenses	6,588	2,964
Total	**323,964**	**446,197**

6. INVENTORIES, NET

Inventories consisted of the following at December 31, 2005:

	2005	2004
	'000 RUR	**'000 RUR**
Raw materials	1,116,728	735,869
Work in process	75,553	21,068
Finished goods	1,361,069	524,504
Allowance for obsolescence	(143,036)	(133,321)
Total	**2,410,314**	**1,148,120**

7. TAXES RECOVERABLE AND PAYABLE

Current taxes recoverable consisted of the following at December 31, 2005:

	2005	2004
	'000 RUR	**'000 RUR**
VAT	485,500	296,410
VAT allowance for non-recoverable VAT	(8,830)	
Other taxes	39,327	19,218
Total	**515,997**	**315,628**

Current taxes payable consisted of the following at December 31, 2005:

	2005	2004
	'000 RUR	**'000 RUR**
Income tax	0	1,768
Advertising tax	0	11,639
VAT	54,831	14,607
Provision for roads users tax	0	48,224
Other taxes	48,649	50,310
Total	**103,480**	**126,548**

8. INVESTMENTS

Investments consisted of the following at December 31, 2005:

	2005 '000 RUR	2004 '000 RUR
Investments in LLC Kit-Capital - 10.59% (2004 : 12.17%)	69,158	79,420
Other short-term investments (promissory notes)	2,860	0
Total	**72,018**	**79,420**

KIT-Capital is a construction site development company. Share of 1.57% was disposed while January – March 2005.

9. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment consisted of the following at December 31, 2005:

	2005 '000 RUR	2004 '000 RUR
Land	17,288	17,288
Buildings	2,053,042	647,303
Machinery and equipment	2,165,201	776,850
Office equipment and other assets	168,802	89,461
Construction in progress	90,129	82,962
Less: accumulated depreciation	(1,802,082)	(761,484)
Total	**2,692,380**	**852,380**

10. ACCOUNTS PAYABLE

Accounts payable consisted of the following at December 31, 2005:

	2005 '000 RUR	2004 '000 RUR
Accounts payable – trade	1,001,415	558,013
Accrued interest	21,244	9,934
ST land lease payables	34,269	7,305
Other payables	498,868	68,399
Total	**1,555,796**	**643,651**

11. SHORT-TERM LOANS

Outstanding short-term credit facilities of the Group as of December 31, 2005 consisted of the following:

	Interest rate	2005 '000 RUR	2004 '000 RUR
EBRD loan (USD)	LIBOR+4.75%	147,853	83,080
Citibank loan (RUR)	23%	-	-
Raiffeisenbank Austria loan (USD)	LIBOR+4%	428,000	50,001
MMB loan (RUR)	7%-9.5%	427,000	-
Dresdner Bank Göppingen	EONIA + 0,75% margin	80,950	-

Deutsche Bank - Money market loan	3,85%	68,370	-
Other loans in RUR, USD, EUR, SUM, UAH	19-23%	93,906	-
Financial lease			
Current portions of liability on financial lease (RUR)	13%	34,269	7,306
Total		**1,280,348**	**140,386**

12. LONG-TERM DEBT

Long-term debt consisted of the following as of December 31, 2005:

	2005	2004
	'000 RUR	**'000 RUR**
Long-term bank loans		
EBRD loan (USD)	295,706	217,530
Baden-Wurttembergische bank	177,147	
Financial lease		
Long-term portion of financial lease liability (RUR)	35,894	1,009
Total long-term debt	**508,747**	**218,539**

In 2003, the Group entered into a long-term credit line agreement with a related party (Note 16) – the European Bank for Reconstruction and Development (EBRD). The total amount of credit line facilities to be provided under the contract is 20 mln. US dollars with an annual interest rate of LIBOR plus 4.75%. The facilities are collateralized by pledge of equipment with approximate carrying value of 15,528 thousand US dollars and deposit of 2,740 thousand US dollars in Citibank (Note 4) as of December 31, 2005.

In the second half of 2002 the Company entered into a financial lease agreement of production equipment.

Future minimum lease payments due under non-cancelable leases at December 31, 2005 were:

Financial lease commitments as lessee:		
Due within 12 months	$	34,269
Due during the second year		35,894
Total minimum lease payments:		70,163
Less amount, representing interest		
Present value of minimum lease payments	**$**	**70,163**

13. INTANGIBLE ASSETS

	Patents and trademarks	Licensed software	Total
	'000 RUR	**'000 RUR**	**'000 RUR**
Cost			
At 1 January 2005	3,119	13,036	16,155
Additions	9,307	2,147	11,454
Disposals	(120)	-	(120)
Acquired on acquisition of subsidiary	342,602	-	342,602
At 31 December 2005	354,908	15,183	370,091
Amortization			
At 1 January 2005	760	2,833	3,594

Charge for the year	832	2,030	2,862
Disposals	(11)	-	(11)
At 31 December 2005	1,581	4,864	6,445
Carrying amount			
At 31 December 2004	2,358	10,203	12,561
At 31 December 2005	353,326	10,320	363,646

Useful life for Dr. Scheller trademarks is indefinite, trademarks should be subject to annual impairment review.

14. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Total selling, general and administrative expenses consisted of the following at December 31, 2005:

	2005 '000 RUR	2004 '000 RUR
Advertising expenses	1,154,923	537,457
Salaries	733,635	353,065
Consulting expenses	41,021	94,430
Transportation expenses	215,607	177,084
Raw materials obsolescense expenses	167,951	156,690
Social taxes on salaries	84,526	74,946
Depreciation charge	161,181	16,719
Other taxes	39,291	46,439
Loss on securities floatation	4,802	86,575
Other	374,351	484,878
Total	**2,908,281**	**1,871,900**

15. TAXES

Total tax expense consisted of the following at December 31, 2005:

	2005 '000 RUR	2004 '000 RUR
Current tax expense	189,529	202,036
Deferred tax (benefit) expense	(103,824)	28,631
Total	**85,704**	**230,667**

The Group provides for current taxes based on statutory financial statements maintained and prepared in local currencies and in accordance with local statutory regulations which differ significantly from IFRS. The Group was subject to a tax rate of 24% in Russia, 25% in Ukraine, 26% in Uzbekistan and 38% in Germany in 2005 and 2004.

The provision for income taxes is different from that which would be obtained by applying the statutory income tax rates to income before income taxes. Below is a reconciliation of theoretical income tax to the actual amount of tax expense recorded in the Group's statement of operations:

	2005 '000 RUR	2004 '000 RUR

Income tax expense at statutory rates		
Adjustments due to:	187,105	190,384
Tax penalties		
Discontinued operations	-	-
Other permanent differences	2,424	11,652
Income tax expense	**189,529**	**202,036**

The tax effects of temporary differences that give rise to deferred tax assets and liabilities at December 31, 2005 are as follows:

	2005 '000 RUR	2004 '000 RUR
Non-current deferred tax assets:		
Accrued expenses	88,008	55,497
Valuation of investments	33,823	
Valuation of closing stock of work in progress and finished goods		(8,128)
	121,830	**47,370**
Non-current deferred tax liabilities:		
Provisions and allowances	-	55
Valuation of non-current assets	180,644	
Depreciation of PPE	126,023	55,664
	306,667	**55,719**

16. DISCONTINUED OPERATIONS

Pallada Vostok (Uzbekistan)

In December 2003 Group management made a decision to dispose of its wholly owned subsidiary LLC Pallada Vostok based in Uzbekistan. The subsidiary was engaged in the production of a wide range of cosmetic brands sold on the Uzbekistan market.

The contract on sales was signed, title transfers to the customer after 100% payment of the contract sum, but the customer just paid 50% of the contract sum. Negotiations on the sales of the subsidiary are in process.

Major assets and liabilities of the subsidiary as of December 31, 2004 and 2003 were as follows:

	2005 '000 RUR	2004 '000 RUR
Assets associated with discontinued operations:		
Cash and cash equivalents	1,023	489
Accounts receivable, net	983	384
Advances to suppliers and prepaid expenses	5,219	5,999
Inventories	39,321	54,237
Taxes recoverable	-	2,791
Investments	-	703
Property, plant and equipment, net	97,444	101,929
Total assets associated with discontinued operations	**143,991**	**166,532**
Liabilities associated with discontinued operations:		
Accounts payable	303,770	274,060
Short-term debt	20,398	8,346
Taxes payable	-	11,024
Long-term debt	-	22,812
Total liabilities associated with discontinued operations:	**324,169**	**316,242**

At December 31, 2005 LLC Pallada Vostok was indebted to the rest of the Group in the amount of 149,453 thousand RUR, represented by 44,797 thousand RUR in trade payables and 104,656 RUR received as advances from the rest of the Group.

Revenues and (net loss) of LLC Pallada Vostok for the years 2005 and 2004 were 11.5m and (39.6m) RUR and 86.1m and (44.4m) RUR, respectively.

17. CAPITAL STOCK

As of December 31, 2005 the Group had 9,752,311 authorised and issued ordinary shares at RUR 70 per share (2004: 9,752,311 authorised and issued ordinary shares at 70 RUR per share).

In April 2004 the Group issued 1,387,403 new common shares at a par value of 70 RUR per share. Shares were placed at 525 RUR against shareholders pre-emptive rights and 550.62 RUR per share through a public offering.

As of December 31, 2005 dividends for the second half of 2004 in the amount of 83,967 thousand RUR were declared and paid in full.

In 2005 interim dividends for the first 6 months were declared in the amount of 60,269 thousand RUR. The interim dividends per share were 6.18 RUR (0.22 US dollars).

The Company is owned 30% by Mr Timur Rafkatovich Goryaev (Chief Executive Officer of the Group), 12.93% by Deutsche Bank Trust Company Americas, USA, 6.58% by Skandinaviska Enskilda Banken AB, Sweden, 6.63% by State Street Bank and Trust Company, USA, 4.55% by the Bank of New York, USA and 39.31% by other shareholders.

18. RELATED PARTY TRANSACTIONS

Trading transactions

The Group has one party related by means of common control – LLC "Soyuzspezstroy".

Advances to related parties as of December 31, 2005 were as follows:

	2005	2004
	'000 RUR	**'000 RUR**
LLC "Soyuzspezstroy"	37,530	37,031
Total		

Purchases from related parties for the years ended December 31, 2005 were as follows:

	2005	2004
	'000 RUR	**'000 RUR**
LLC "Soyuzspezstroy"		
Purchase of services	93,644	11,966
Total	**93,664**	**11,966**

Advance to LLC "Soyuzspecstroy" is the advance for building services.

19. REMUNERATION OF KEY MANAGEMENT PERSONNEL

	2005	2004
	'000 RUR	'000 RUR
Short-term employee benefits	50,206	37,649
Total		

20. POST RETIREMENT BENEFITS

Employees of the Group are generally beneficiaries of state-administered defined contribution pension programs. The Group remits a required percentage of the aggregate employees' salaries to the statutory Pension Funds.

In addition, a number of employees of the Dr. Scheller subsidiary are enrolled in an unfunded defined benefit pension plan.

Dr. Scheller utilizes actuarial methods to account for the pension plan. Inherent in the application of these actuarial methods are the following key assumptions:

Discount rate	4% per annum
Expected rate of salary increases	1.5% per annum
Pension increase	1.5% per annum
	Valuation at
	31/12/2005
Discount rate	4%
Expected rate of salary increases	1,5%
Future pension increases	1,5%

The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at 31/12/2005 by Kern&Mauch Kollegen Gmh (the Firm of actuaries, registered in Germany). The present value of the defined benefit obligation, the related current service cost and past service cost were measured using the projected unit credit method.

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

	Year ended 2005 '000 RUR
Current service cost	2,377
Interest cost	7,327

The amount included in the balance sheet arising from the Group's obligations in respect of its defined benefit retirement benefit schemes is as follows:

	Year ended 2005 '000 RUR	**Year ended 2004 '000 RUR**
Present value of defined benefit obligations	181,104	-
Fair value of scheme assets	-	-
Deficit in scheme	181,104	-

Unrecognised loss	(7,411)	-
Liability recognized in the balance sheet	173,693	-

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

	2005	2004
	‘000 RUR	**‘000 RUR**
Acquisition of Dr. Scheller	180,379	-
Service cost	1,835	-
Interest cost	9,035	-
Actuarial loss	8,901	-
Benefits paid	(9330)	-
Effect of exchange rate movements	(9,716)	
At 31 December	181,104	-

The present value of fair value of scheme assets in the current period was RUR NIL as of December 31, 2005 (2004: RUR NIL).

Other than the defined benefit scheme liability outlined above, the Group was not liable for any supplementary pensions, post retirement health care, insurance benefits, or retirement indemnities to its current or former employees, as at December 31, 2005 and 2004.

21. COMMITMENTS AND CONTINGENCIES

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

Tax Environment – Due to the presence in Russian, Ukrainian and Uzbek commercial legislation, and tax legislation in particular, of provisions allowing more than one interpretation, and also due to the practice developed in a generally unstable environment by the tax authorities of making arbitrary judgment on business activities, if a particular treatment based on Management’s judgment of the Group’s business activities was to be challenged by the tax authorities, the Group may be assessed additional taxes, penalties and interest. Tax years remain open to review by the tax authorities for three years.

22. ACQUISITION NOTE

During April 2005, the Group completed the acquisition of 61.37% shares (as a percentage of the number of shares outstanding) of Dr. Scheller Cosmetics AG (Scheller) for a purchase price of 21.96 million US dollars in cash. Dr. Scheller Cosmetics AG is a German perfume manufacturer and distributor.

Total number of shares as at 31/03/2005 was 6,500,000; number of treasury shares as at 31/03/2005 was 315,319; number of shares outstanding as at 31/03/2005 was 6,184,681. Number of shares acquired by Group is 3,795,740.

Percentage of shares held by the Group as a proportion of all shares, including treasury shares is 58.4%; Percentage of shares held by the Group as a proportion of all shares outstanding is 61.37%.

The acquisition was accounted for under the purchase accounting method, and accordingly, Scheller's results of operations have been included in these consolidated financial statements, April 2005. At the date of issuing this report, the purchase price allocation had not been finalized. The only fair value adjustment made was in respect of recognition of trademark intangibles.

Preliminary price allocation is as follows:

Current assets	'000 RUR	756,028
Non-current assets	'000 RUR	1,227,495
Intangible assets adjusted for FV	'000 RUR	431,415
Deferred tax asset	'000 RUR	-
Current liabilities	'000 RUR	(625,015)
Non-current liabilities	'000 RUR	(780,811)
Deferred tax liability	'000 RUR	(131,914)
Purchase price	'000 RUR	609,427

23. SEGMENT REPORTING

Primary

	Cosmetics	**Tooth-paste**	**Household chemical goods**	**Other**	**Consolida-ted**
	Year ended 31/12/05	Year ended 31/12/05	Year ended 31/12/05	Year ended 31/12/05	Year ended 31/12/05
	'000 RUR	'000 RUR	'000 RUR	'000 RUR	'000 RUR
Revenue					
External sales	5,533,272	1,065,378	716,431	835,454	8,150,535
Inter-segment sales					
Total revenue from continuing operations	5,533,272	1,065,378	716,431	835,454	8,150,535
Result					
Segment result from continuing operations	2,851,769	542,129	127,671	292,270	3,813,838
Unallocated corporate expense					(2,908,280)
Operating profit from continuing operations					905,558
Investment revenues					21,561
Other gains and losses					(46,237)

Finance costs	(89,278)
Profit before tax	791,604
Income taxes expense	(85,704)
Profit for the year from continuing operations	705,900
Segment result from discontinued operations	(39,616)
Profit	**666,284**

Other Information

	31/12/05	31/12/05	31/12/05	31/12/05
	'000 RUR	'000 RUR	'000 RUR	'000 RUR
Segment assets	1,673,439	279,611	88,785	2,041,836
Unallocated corporate assets				650,544
Consolidated total assets				**2,692,380**

	Cosmetics	**Tooth-paste**	**Household chemical goods**
	'000 RUR	'000 RUR	'000 RUR
Capital expenditure			
Depreciation	8,119	16,215	5,960
Non-cash expenditure other than depreciation			

Secondary

'000 USD	**Sales Revenue by Geographical Market**		**Carrying Amount of Segment Assets**	**Additions to PPE and Intangible assets**
	2005		'000 RUR	
Russia	4,963,534	Russia	1,531,101	795,382
CIS	1,174,581	Uzbekistan (disc. oper.)	97,444	-
Europe	1,787,507	Ukraine	2,461	-
Other (primarily USA and Mongolia)	224,913	Germany	1,515,250	87,035
	8,150,535		**3,146,256**	**882,417**

24. EXPLAINATION OF TRANSITIONS TO IFRSs

This is the first year that the company has presented its financial statements under IFRS. The following disclosures are required in the year of transaction. The last financial statements under US GAAP were for the year ended 31 December 2004 and the date of transition to IFRS was therefore 1 January 2005.

Reconciliation of equity at 1 January 2005 (date of transition to IFRSs)

Note		US GAAP	Effect of transaction to IFRSs	IFRSs
	Property, plant and equipment	821,207	31,173	852,380
	Goodwill	-	-	-
	Intangible Assets	15,103	(2,542)	12,561
	Financial Assets	2,923	-	2,923
	Total non-current assets	**839,233**	**28,631**	**867,864**
	Trade and other receivables	366,847	-	366,847
	Inventories	1,110,971	37,149	1,148,120
	Other receivables	1,169,895	(81,781)	1,088,115
	Cash and cash equivalents	1,120,316	-	1,120,316
	Total current assets	**3,768,029**	**(44,631)**	**3,723,398**
	Total assets	**4,607,262**	**(16,000)**	**4,591,261**
	Interest bearing loan	350,611	-	350,611
	Trade and other payables	937,458	23,444	960,902
	Employees benefits	-	-	-
	Restructuring provision	-	-	-
	Current tax liabilities	126,548	-	126,548
	Deffered tax liabilities	55,719	-	55,719
	Total liabilities	**1,470,336**	**23,444**	**1,493,780**
	Total assets less total liabilities	**3,136,926**	**(39,444)**	**3,097,481**
	Issued capital	740,530	111,311	851,842
	Revaluation reserve	704,582	(704,582)	-
	[Hedging reserve]	-	-	-
	Retained earnings	1,770,402	475,238	2,245,640
	Other Accumulated Comprehensive Income	(78,589)	78,588	-
	Minority interest	-	-	-
	Total equity	**3,136,925**	**(39,444)**	**3,097,481**

Property, plant and equipment. Up to 2002 year property, plant and equipment was valued in accordance with IAS No. 29 “Financial Reporting in Hyperinflationary Economies” (“IAS 29”), this is different from US GAAP, where PPE was valued based on historical USD exchange rates. Difference between IFRS and GAAP accounting is related to prior years and is posted to retained earnings.

Inventory, other receivables, trade and other payables. These includes reclassifications between different balance sheet lines.

Issued capital. Up to 2002 year issued capital was valued in accordance with IAS No. 29 “Financial Reporting in Hyperinflationary Economies” (“IAS 29”), this is different from US GAAP, where

capital was valued based on historical USD exchange rates. Difference between IFRS and GAAP accounting is related to prior years and is posted to retained earnings.
The nature of revaluation reserve and other accumulated comprehensive income for IFRS is retained earnings, these lines of EQUITY were reclassified to retained earnings.

Reconciliation profit or loss for 2004

Note		US GAAP	Effect of transaction to IFRSs	IFRSs
	Revenue	5,262,013	(24,377)	5,237,636
	Cost of sales	(2,645,167)	61,526	(2,583,641)
	Gross profit	**2,616,845**	**37,149**	**2,653,995**
	Distribution costs			
	Administrative expenses	(1,715,840)	(55,132)	(1,770,972)
	Finance income	4,516	-	4,516
	Finance cost	(3,368)	-	(3,368)
	Other income and expenses	(100,506)	-	(100,506)
	FOREX	21,602		21,602
	Profit before tax	823,249	(17,983)	805,266
	Tax expenses	(230,181)	(486)	(230,667)
	Net profit (loss)	**593,068**	**(18,469)**	**574,599**