Open Joint Stock Company “Company M.video” and subsidiaries (the “Group”)

Special Purpose
Independent Auditors’ Report

Preliminary Consolidated
Financial Statements
Year Ended 31 December 2006

OJSC “COMPANY M.VIDEO” AND SUBSIDIARIES

TABLE OF CONTENTS

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

The following statement, which should be read in conjunction with the independent auditors' responsibilities stated in the independent auditors' report set out on pages 2 and 3, is made with a view of distinguishing the respective responsibilities of the management and those of the independent auditors in relation to the preliminary consolidated financial statements of OJSC "Company M.video" and subsidiaries (the "Group").

Management is responsible for the preparation of the preliminary consolidated International Financial Reporting Standards ("IFRS") financial statements that present fairly the preliminary consolidated financial position of the Group as at 31 December 2006 and the preliminary consolidated results of its operations, cash flows and changes in shareholders' equity for the year then ended, in compliance with the basis of accounting set out in Note 2 of the accompanying financial statements.

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

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

Management is also responsible for:

- Designing, implementing and maintaining an effective and sound system of internal controls throughout the Group;
- Maintaining proper accounting records that disclose, with reasonable accuracy at any time, the financial position of the Group, and which enable them to ensure that the preliminary consolidated financial statements of the Group comply with the basis of accounting in Note 2;
- Maintaining statutory accounting records in compliance with local legislation and accounting standards in the respective jurisdictions in which the Group operates;
- Taking such steps as are reasonably available to them to safeguard the assets of the Group; and
- Preventing and detecting fraud and other irregularities.

The preliminary consolidated financial statements for the year ended 31 December 2006 were approved on 4 October 2007 by:

A. Tynkovan	**C. Parks**
Chief Executive Officer	Chief Financial Officer

Deloitte.

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SPECIAL PURPOSE INDEPENDENT AUDITORS' REPORT ON THE PRELIMINARY IFRS CONSOLIDATED FINANCIAL STATEMENTS

To the Shareholders of Open Joint Stock Company "Company M.video":

We have audited the accompanying preliminary consolidated balance sheet of Open Joint Stock Company "Company M.video" and its subsidiaries (collectively, the "Group") as at 31 December 2006 and the related preliminary consolidated statements of operations, changes in shareholders' equity and cash flows for the year then ended (the "financial statements"). The financial statements have been prepared as part of the Group's conversion to International Financial Reporting Standards ("IFRS").

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting described in Note 2 to the accompanying financial statements. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the preliminary consolidated balance sheet of the Group as of 31 December 2006, the preliminary consolidated statements of operations, changes in equity and cash flows for the year then ended have been prepared, in all material respects, in accordance with the basis set out in Note 2, which describes how IFRS have been applied under IFRS 1, including the assumptions management has made about the standards and interpretations expected to be effective, and the policies expected to be adopted, when management prepares its first complete set of IFRS financial statements as at 31 December 2007.

Emphasis of matter

Without qualifying our opinion, we draw attention to Note 2 in the preliminary consolidated financial statements which explains why there is a possibility that the preliminary financial statements for the year ended 31 December 2006 may require adjustment. Moreover, we draw attention to the fact that, under IFRS, only a complete set of financial statements comprising a balance sheet, statement of operations, statement of changes in equity, and cash flow statement, together with comparative financial information and explanatory notes, can provide a fair presentation of the company's financial position, results of operations, and cash flows in accordance with IFRS.

Deloitte & Touche

4 October 2007

PRELIMINARY CONSOLIDATED BALANCE SHEET
AS AT 31 DECEMBER 2006
(in millions of Russian Rubles)

	Notes	2006	2005
ASSETS			
NON-CURRENT ASSETS:			
Property, plant and equipment	6	3,424	636
Construction in process		35	6
Intangible assets	7	33	17
Long term loans and notes receivable	8	37	24
Deferred tax assets	16	378	162
Deferred costs		9	-
Advances paid for property, plant and equipment		14	77
Total non-current assets		3,930	922
CURRENT ASSETS:			
Available for sale investment at cost	34(c)	28	-
Inventories	9	6,961	5,299
Trade accounts receivable	10	667	66
Other accounts receivable and prepaid expenses	11	1,307	239
Value added tax recoverable and other taxes receivable	12	1,666	1,166
Income tax receivable		15	3
Short-term loans and notes receivable	13	102	65
Deferred costs		8	-
Cash and cash equivalents	14	932	738
Total current assets		11,686	7,576
TOTAL ASSETS		**15,616**	**8,498**

PRELIMINARY CONSOLIDATED BALANCE SHEET (CONTINUED)
AS AT 31 DECEMBER 2006
(in millions of Russian Rubles)

	Notes	2006	2005
SHAREHOLDERS' EQUITY/(DEFICIT) AND LIABILITIES			
SHAREHOLDERS' EQUITY/(DEFICIT):			
Issued capital	15	1,498	1
Accumulated deficit		(403)	(523)
Total shareholders' equity/(deficit)		1,095	(522)
NON-CURRENT LIABILITIES:			
Long-term loans and borrowings	17	2,053	650
Forward exchange contract		15	-
Deferred tax liabilities	16	470	1
Deferred revenue		73	-
Warranty provision		3	3
Total non-current liabilities		2,614	654
CURRENT LIABILITIES:			
Trade accounts payable	19	5,809	7,329
Other payables and accrued expenses	20	391	57
Advances received from customers		149	48
Bonds payable	18	2,000	-
Short-term loans and borrowings	22	2,985	882
Value added tax and other taxes payable	21	155	35
Income tax payable		342	11
Deferred revenue		69	-
Warranty provision		7	4
Total current liabilities		11,907	8,366
Total liabilities		14,521	9,020
TOTAL SHAREHOLDERS' EQUITY/(DEFICIT) AND LIABILITIES		**15,616**	**8,498**

The notes on pages 9 to 44 form an integral part of these financial statements. The Independent Auditors' Report is presented on pages 2 and 3.

Signed on behalf of the Board of Directors: 4 October 2007

A. Tynkovan
Chief Executive Officer

C. Parks
Chief Financial Officer

PRELIMINARY CONSOLIDATED INCOME STATEMENT
FOR THE YEAR ENDED 31 DECEMBER 2006
(in millions of Russian Rubles)

	Notes	2006
REVENUES	23	36,258
COST OF GOODS SOLD	24	(28,642)
GROSS PROFIT		7,616
Selling, general and administrative expenses	25	(6,688)
Other operating income	26	414
Other operating expenses	27	(195)
OPERATING PROFIT		1,147
Finance costs, net	28	(411)
PROFIT BEFORE INCOME TAX		736
INCOME TAX	16	(338)
NET PROFIT		**398**
WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES FOR BASIC AND DILUTED EARNINGS PER SHARE (in millions)		2,607
BASIC AND DILUTED EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT (in RUR)		0.1527

The notes on pages 9 to 44 form an integral part of these financial statements. The Independent Auditors' Report is presented on pages 2 and 3.

PRELIMINARY CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS’ EQUITY/(DEFICIT) FOR THE YEAR ENDED 31 DECEMBER 2006

(In millions of Russian Rubles)

	Share capital	Accumulated deficit	Total
Balance at 31 December 2005	**1**	**(523)**	**(522)**
Issuance of shares (Note 15)	1,497	-	1,497
Net profit for the year	-	398	398
Difference arising on transaction with shareholders (Note 6)	-	(278)	(278)
Balance at 31 December 2006	**1,498**	**(403)**	**1,095**

The notes on pages 9 to 44 form an integral part of these financial statements. The Independent Auditors’ Report is presented on pages 2 and 3.

PRELIMINARY CONSOLIDATED STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 DECEMBER 2006

(In millions of Russian Rubles)

	2006
OPERATING ACTIVITIES:	
Profit for the year	398
Adjustments for:	
Income tax expense recognized in profit or loss	338
Interest expense on loans	375
Coupon yield expense	21
Loss on sale or disposal of property, plant and equipment	8
Depreciation and amortization	299
Foreign exchange loss	(28)
Change in fair value of forward contracts	15
Change in provision for goods returned	10
Change in provision for obsolete and slow moving goods	206
Operating cash flows before movements in working capital	1,642
Increase in inventories	(1,868)
Increase in trade receivables	(611)
Increase in other accounts receivable and prepaid expenses	(1,070)
Increase in value added tax recoverable and other taxes receivable	(500)
Increase in deferred cost	(17)
Decrease in trade payables	(1,520)
Increase in other payables and accrued expenses	312
Increase in advances from customers	101
Increase in warranty provision	3
Increase in value added tax and other taxes payable	120
Increase in deferred revenues	142
Cash used in operations	(3,266)
Income tax paid	(322)
Interest paid	(142)
Net cash used in operating activities	**(3,730)**
INVESTING ACTIVITIES:	
Purchases of property, plant and equipment (including construction in progress)	(925)
Decrease in advances paid for property, plant and equipment	63
Purchases of intangible assets	(20)
Receipts from settlements of loans and notes receivable	48
Cash invested in loans and notes receivable	(105)
Net cash used in investing activities	**(939)**
FINANCING ACTIVITIES:	
Proceeds from sale of equity shares	5
Proceeds from borrowings	16,785
Repayment of borrowings	(11,927)
Net cash from financing activities	**4,863**
NET INCREASE IN CASH AND CASH EQUIVALENTS	194
CASH AND CASH EQUIVALENTS, beginning of year	738
CASH AND CASH EQUIVALENTS, end of year	932

Non-cash transactions: For details of property and equipment acquired in exchange for issue of shares see Notes 6 and 15.

The notes on pages 9 to 44 form an integral part of these financial statements. The Independent Auditors’ Report is presented on pages 2 and 3.

(In millions of Russian Rubles)

1. GENERAL INFORMATION

The preliminary consolidated financial statements of OJSC “Company M.video” (the “Company”) and subsidiaries (the “Group”) as at and for the year ended 31 December 2006 were authorized for issue in accordance with a resolution of the Board of Directors on 4 October 2007. The Company and its subsidiaries (refer listing below) are incorporated in the Russian Federation.

LLC “Company M.video” was incorporated on 3 December 2003. The reorganization of the Group’s operational activities occurred over the period to December 2005, with the full trading operations commencing on 1 January 2006. As part of the reorganization prior to 1 January 2006 the Group acquired substantially all of its merchandise inventory from a related party of the Group (refer to Note 29). On 25 September 2006 the Company was reorganized from a Limited Liability Company to an Open Joint Stock Company (refer to Note 15).

The Group is the owner of a chain of consumer electronic stores operating in the Russian Federation. The Group specializes in the sale of TV, audio, video, Hi-Fi, home appliances, digital equipment as well as related services.

The Group operates in two sectors: retail and wholesale. The retail sector is comprised of a chain of owned and leased stores and two online internet stores that sell to end users. The wholesale sector is comprised of sales to other retailers.

The following are subsidiaries of the Company as of 31 December 2006:

Name of subsidiary	Nature of business	Proportion of ownership interest and voting power held, % 2006	Proportion of ownership interest and voting power held, % 2005
LLC “M.video Management”	Trading	100	100
LLC “M.video Torg”	Equipment	100	100
LLC “M.video Trade”	Trading	100	100
LLC “M.video – Voronezh”	Trading	100	100
LLC “M.video – Ekaterinburg”	Trading	100	100
LLC “M.video – Kazan”	Trading	100	100
LLC “M.video – Krasnodar”	Trading	100	100
LLC “M.video – Nizhny Novgorod”	Trading	100	100
LLC “M.video – Oblast”	Trading	100	100
LLC “M.video – Perm”	Trading	100	100
LLC “M.video – Petersburg”	Trading	100	100
LLC “M.video – Rostov on Don”	Trading	100	100
LLC “M.video – Samara”	Trading	100	100
LLC “M.video – Saratov”	Trading	100	100
LLC “M.video – Ufa”	Trading	100	100
LLC “M.video – Center”	Trading	100	100
LLC “M.video – Chelyabinsk”	Trading	100	100
LLC “Nivo”	Trading	100	100
LLC “Techno-smart”	Trading	100	100
LLC “Triumph MV”	Trading	100	100
LLC “Universopt”	Trading	100	100
LLC “Electrosteal”	Trading	100	100

(In millions of Russian Rubles)

Name of subsidiary	Nature of business	Proportion of ownership interest and voting power held, % 2006	Proportion of ownership interest and voting power held, % 2005
LLC "Sphera Invest"	Real Estate	100	-
LLC "Standard Invest"	Real Estate	100	-
LLC "M.video Finance"	Finance	100	-

Refer to Note 34 "Events after the balance sheet date" below for changes in the Group structure.

Shareholders

As at and for the year ended 31 December 2006, the registered shareholders of OJSC "Company M.video" and their respective ownership and voting interests were as follows:

Svece Limited	99.597%
M.video Holding (Cyprus) Limited	0.402%
Non-commerical partnership M.video	0.001%

Holders of ordinary shares possess the right to vote.

Ultimate Shareholders

M.video Investment Ltd., a company incorporated in the British Virgin Islands controls 100% of the voting and ordinary shares of M.video Holding (Cyprus) Limited and Svece Limited.

Mr. Alexander Tynkovan, a citizen of the Russian Federation, has a controlling interest in M.video Investment Ltd. (BVI).

2. PRESENTATION OF FINANCIAL STATEMENTS

Basis of Preparation

For the year ended 31 December 2007, the Group will be preparing its first complete set of financial statements in accordance with International Financial Reporting Standards ("IFRS"). IFRS include standards and interpretations approved by the International Financial Reporting Standards Board ("IASB") including International Accounting Standards ("IAS") and interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC"). The rules for the first time adoption of IFRS are described in IFRS 1 "First-time Adoption of International Financial Reporting Standards" ("IFRS 1"). IFRS 1 states that companies should use the same accounting policies in their opening IFRS balance sheet and for all periods presented as comparative information in their first complete set of IFRS financial statements. The accompanying preliminary consolidated balance sheet as at 31 December 2006, consolidated income statement, statement of cash flows and changes in equity for the year then ended together with related notes (the "preliminary consolidated financial statements") will be included in the Group's first complete set of IFRS consolidated financial statements for the year ending 31 December 2007.

In preparing the preliminary IFRS consolidated financial statements, management has used the existing standards and interpretations which have been in issue up to 30 June 2007 to make assumptions about the accounting policies expected to be adopted when the first IFRS consolidated annual financial statements are prepared for the year ending 31 December 2007.

The Group cannot be certain that the accounting policies applied in preparing the preliminary consolidated balance sheet will be the same policies that will be applied to the final balance sheet and the first complete set of IFRS financial statements prepared for the year ending 31 December 2007, due to:

- Any changes in existing standards;
- Changes in the interpretations of existing standards by the IASB;
- New standards may be issued by the IASB, which, although not mandatory for 2007, may be permitted for earlier adoption;
- Further development in industry interpretation and application of existing standards; and
- Management's future decision to adopt alternative accounting policies which may differ from those originally selected.

However, based on new or revised pronouncements issued by the IASB and IFRIC to the date of approval of these preliminary consolidated financial statements and the announcement by the IASB made on 24 July 2006 that no major new standards would be issued or become effective before 2009, management believes that the effect of any possible changes in accounting policies in the Group's first complete set of IFRS financial statements for the year ending 31 December 2007 is not expected to be significant. Further, management has committed not to make voluntary changes to accounting policies.

The Group's transition date to IFRS was 1 January 2006. The Group did not previously prepare consolidated financial statements under IFRS or another internationally recognized accounting framework.

All companies within the Group maintain their accounting records in accordance with Russian Accounting Standards ("RAS"). RAS differs substantially from those standards generally accepted under IFRS. Accordingly, the preliminary consolidated financial statements, which have been prepared based on the Russian statutory accounting records, reflect those adjustments necessary for such preliminary consolidated financial statements to be presented in accordance with IFRS.

The disclosures required by IFRS 1 "First-time adoption of International Financial Reporting Standards" for the transition from Russian Accounting Standards to IFRS are provided in Note 33.

The preliminary consolidated financial statements have been prepared on the historical cost basis except for the valuation of financial instruments in accordance with IAS No. 39 "Financial Instruments: Recognition and Measurement" ("IAS 39") and valuation of items of property, plant and equipment at the date of transition to IFRS to arrive at deemed cost as allowed by IFRS 1 (more fully described in Note 3).

Functional and presentation currency – The Group uses the Russian Ruble ("RUR") as its functional and presentation currency. Management has selected the RUR as the Group's functional currency because the majority of the Group's transactions are denominated in RUR.

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

The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies.

Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

All intra-group transactions, balances, income and expenses and profits and losses resulting from intra-group transactions that are recognized in assets are eliminated in full on consolidation.

Business and geographic segments – The Group has only one reportable business and geographic segment thus segment reporting information as required by IAS 14 "Segment Reporting" has not been provided.

Going concern – These preliminary IFRS consolidated financial statements are prepared on the going concern basis. As of 31 December 2006 the year end, the Group is in a net current liability position. This has arisen principally due to the redemption option available to the holders of ruble bonds which is exercisable in certain circumstances, thus requiring their classification as current liabilities. Management has evaluated the Group's ability to continue as a going concern and believes that the Group will continue to trade as a going concern within the foreseeable future. In addition, management believes that should it be necessary, it will be able to draw down on facilities which are currently uncommitted.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing at the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are translated at the rates prevailing at the balance sheet date.

Exchange differences are recognized in profit or loss in the period in which they arise.

Property, plant and equipment – Property, plant and equipment are stated at historical cost less subsequent depreciation and impairment. Deemed cost of the items of property, plant and equipment existing as at 1 January 2006, the date of transition to IFRS, was determined on the basis of fair values determined by independent appraisers as allowed by the provisions of IFRS 1. Fair value of properties was determined with reference to market prices, while fair value of the other items, including the Group's trade equipment, was predominantly based on the estimates of depreciated replacement costs. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Major replacements or modernizations are capitalized and depreciated over their estimated useful lives. All other repair and maintenance expenditure is charged to the income statement during the financial period in which it is incurred.

Depreciation is charged so as to write off the cost or valuation of assets, over their estimated useful lives, using the straight line method, on the following bases:

Buildings	20-30 years
Leasehold improvements	2-7 years
Trade equipment	5 years
Security equipment	3 years
Other fixed assets	3-5 years

For leasehold improvements the depreciation period includes the period when the Group has the possibility to extend the period of the lease, taking into account the legal provisions relating to lease terms, and its intention to seek a long term presence in the various retail locations in which it operates. This is relevant for leases of retail space which, on a portfolio basis, have a history of successful renewal. All other leasehold improvements are depreciated over the shorter of useful life and the related lease term.

Trade equipment is depreciated over the estimated useful life specified above unless there is a plan to fully renovate the store prior to reaching the predetermined estimated useful life. In this situation, the net book value of trade equipment will be depreciated over the remaining estimated useful life being the period of time up to the planned renovation works.

The assets' residual value and useful lives are reviewed, and adjusted, if appropriate, at each balance sheet date. Where there are indicators that an asset's or cash generating unit's carrying amount is greater than its estimated recoverable amount, it is written down to its recoverable amount.

The gain or loss arising on the disposal or retirement of an asset is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in income.

Construction in process comprises the cost of equipment in the process of installation and other costs directly related to the construction of property, plant and equipment including an appropriate allocation of directly attributable variable overheads that are incurred in construction. Depreciation of these assets, on the same basis as for other property assets, commences when the assets are ready for their intended use.

Intangible assets – Intangible assets acquired separately are reported at cost less accumulated amortization and accumulated impairment losses. Amortization is charged on a straight-line basis over their useful lives. The estimated useful life and amortization method are reviewed at the end of each annual reporting period, with the effect of any changes in estimate being accounted for on a prospective basis.

The estimated useful lives per class of intangible asset are as follows:

Software licenses	5 to 10 years

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

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

Current tax

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.

The Group's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax

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

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

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

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

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

Current and deferred tax for the period

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

Fair value – The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investment where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arms length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis or other valuation models.

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

Financial assets are classified into the following specified categories: financial assets as ‘at fair value through profit or loss’ (“FVTPL”), ‘held-to-maturity investments’, ‘available-for-sale’ (“AFS”) financial assets and ‘loans and receivables’. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Effective interest method

The effective interest method is a method of calculating the amortized cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset, or, where appropriate, a shorter period.

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

Financial assets at FVTPL

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

A financial asset is classified as held for trading if:

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

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

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

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognized in profit or loss. The net gain or loss recognized in profit or loss incorporates any dividend or interest earned on the financial asset. Fair value is determined in the manner described in Note 3 above.

Held-to-maturity investments

Held-to-maturity investments are recorded at amortized cost using the effective interest method less impairment, with revenue recognized on an effective yield method.

Loans and receivables

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

Available for sale

Available for sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified in any of the three preceding categories. After initial measurement, available for sale financial assets are measured at fair value with unrealized gains or losses being recognized directly in equity in the net unrealized gains reserve. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognized in the income statement. Interest earned or paid on the investments is reported as interest income or expense using the effective interest rate. Dividends earned on investments are recognized in the income statement as 'Dividends received' when the right or payment has been established.

For available for sale investments for which there is no reliable market information to determine fair value, the investments are carried at cost.

Impairment of financial assets

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

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

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

In respect of AFS equity securities, any increase in fair value subsequent to an impairment loss is recognized directly in equity.

Financial liabilities and equity instruments issued by the Group

Classification as debt or equity

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

Financial guarantee contract liabilities

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

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

Financial liabilities

Financial liabilities are classified as either financial liabilities at FVTPL or other financial liabilities.

Financial liabilities at FVTPL

Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if:

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

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

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

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognized in profit or loss. The net gain or loss recognized in profit or loss incorporates any interest paid on the financial liability. Fair value is determined in the manner described in Note 3 above.

Other financial liabilities

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

Derivative financial instruments – The Group enters into derivative financial instruments to manage its exposure to foreign exchange rate risk on its foreign currency denominated debt, namely foreign exchange forward contracts. The Group does not use hedge accounting for these derivatives. As a result, such derivative financial instruments are treated as other financial assets and liabilities at FVTPL. Gains and losses are recognized for the changes in fair value of forward contracts and presented as part of finance costs of the Group.

The fair value of forward exchange contracts is calculated by reference to current forward exchange rates for contracts with similar maturity profiles.

Inventories – Inventories are recorded at the lower of average cost or net realizable value. In-bound freight related costs from our suppliers are included as part of the net cost of merchandise inventories. Also included in the cost of inventory are certain supplier bonuses that are not reimbursement of specific, incremental and identifiable costs to promote a supplier's products. Other costs associated with storing and transporting merchandise inventories to our retail stores are expensed as incurred and included in selling, general and administrative expenses.

Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale.

Cash and cash equivalents – Cash and short term deposits in the balance sheet comprise cash at banks, in transit and on hand in stores and short term deposits with an original maturity of three months or less.

Borrowing costs – Borrowing costs are recognized in the income statement in the period in which they are incurred.

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

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the balance sheet date, taking into account the risks and uncertainties surrounding the obligation.

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

Warranties

Warranties are generally covered by the brand owner directly or through their authorized agents in Russia.

When a supplier is unable to offer warranty services for their products in the Russian Federation, the Group makes a provision for warranty costs. These costs are recognized at the date of sale of the relevant products, at management's best estimate of the expenditure required to settle the Group's obligations.

Revenue recognition – Revenue is measured at the fair value of the consideration received or receivable. Revenue is reduced for estimated customer returns, rebates, discounts and value added tax. Inter-company revenues are eliminated. The following specific recognition criteria must also be met before revenue is recognized:

Sale of goods

Revenue from the sale of goods is recognized when all the following conditions are satisfied:

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

The Group has two categories of goods for resale: retail and wholesale.

Retail revenues – revenue is recognized at the point of sale or when the delivery is complete, if later. Retail sales are transacted by either cash or credit card. The recognized revenue includes credit card fees payable for the transaction. Such costs are presented in operating expenses.

Wholesale revenues – revenue is recognized when the customer has collected the goods from the warehouse or when goods are delivered and accepted at the customer's warehouse and after satisfying the criteria outlined above.

Revenue from services

Revenues from services are recognized in the period in which the services have been rendered, by reference to stage of completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided. The criteria outlined in the "Sale of goods" section above are also considered.

Agents

The Group recognizes as revenue any sales performed as an agent at net amounts. Such fees include sales of telephone service contracts, service and installation fees.

Additional service agreements

Revenues for the sales of additional service agreements are recognized over the life of the agreement using a straight line method. Cash received in advance of services provided is presented as deferred revenue. Costs directly associated with the sale of additional service agreements, such as sales bonuses paid to shop assistants, are also deferred and subsequently recognized in the income statement on the same basis as related revenue (refer to Note 34(d)).

Gift cards

The Group sells gift cards to its customers in its retail stores and through its website. The gift cards have an expiration date and are required to be used during specified periods of time. The Group recognizes income from gift cards when: (i) the gift card is redeemed by the customer; or (ii) when the gift cards expire.

Supplier bonuses – The Group receives bonuses from suppliers. All supplier bonuses are treated as volume allowances unless they are subject to a separate agreement which is specific, incremental and identifiable. Supplier bonuses which are earned by achieving certain volume purchases are recorded when it is reasonably assured the Group will reach these volumes. Supplier bonuses based on volume are recorded as a reduction of the carrying cost of the inventory to which they relate. Supplier bonuses provided as a reimbursement of specific, incremental and identifiable costs incurred to promote a supplier's products are included as an expense (or asset cost) reduction when the cost is incurred.

Leases – The Group has not entered into any finance leases, although it does have a significant number of operating leases.

Operating lease payments are recognized as an expense on a straight line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognized as an expense in the period in which they are incurred. The impact of lease escalation clauses are recognized in expenses in the period in which they are activated.

Any benefits received from the landlord as an incentive to enter into an operating lease are spread over the lease term on a straight line basis.

Pre-opening expenses – Expenses incurred in the process of opening new stores which do not meet capitalization criteria under IAS 16 "Property, plant and equipment" are expensed as incurred. Such expenses include rent, utilities and other operating expenses.

Employee benefits – The Group contributes to the Russian Federation state pension, medical and social insurance and employment funds on behalf of all its current employees by paying unified social tax ("UST"). Any related expenses are recognized in the income statement as they become due. The Group does not operate any employer sponsored pension plans.

4. CHANGES IN IFRS STANDARDS AND THEIR ADOPTION BY THE GROUP

The following new or revised standards and interpretations issued by IASB and IFRIC have been published at the date of authorization of the Group's preliminary consolidated financial statements for the year ended 31 December 2006, but are not yet effective and will be mandatory for adoption in the Group's financial statements for periods ending after 31 December 2007:

- IAS 23 (revised) "Borrowing costs" effective for annual periods beginning on or after 1 January 2009. The revision to IAS 23 removes the option of immediately recognizing as an expense borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset. A qualifying asset is one that takes a substantial period of time to get ready for use or sale. An entity is, therefore, required to capitalize such borrowing costs as part of the cost of the asset. Currently, borrowing costs are recognized by the Group as an expense when incurred. The Group has significant borrowing costs and is currently evaluating the potential impact of IAS 23 (revised) on the financial statements presentation.
- IFRS 8 "Operating segments" effective for annual periods beginning on or after 1 January 2009. The standard requires the disclosure of information about the operating segments of the Group, the products and services provided by the segments, the geographical areas in which the Group operates, and revenues from the Group's major customers. This standard will supersede IAS 14 "Segment Reporting". The Group is currently evaluating the potential impact of IFRS 8 on the presentation of segmental information.

- IFRIC 11 "IFRS 2 – Group and treasury share transactions" effective for annual periods beginning on or after 1 March 2007. Management is currently assessing the impact of this interpretation but believes that this interpretation should not have a significant impact on the Group.
- IFRIC 12 "Service concession arrangements" effective for the annual periods beginning on or after 1 January 2008. Service concession arrangements are arrangements whereby a government or other body grants contracts for the supply of government services to private operators. Management believes that this interpretation is not relevant to the Group.
- IFRIC 13 "Customer loyalty programmes" effective annual periods beginning on or after 1 July 2008. This interpretation addresses accounting by entities that grant loyalty award credits to customers who buy other goods and services. Specifically, it explains how such entities should account for their obligations to provide free or discounted goods or services to customers who redeem award credits. Management is currently assessing the impact of this interpretation but believes that this interpretation should not have a significant impact on the Group.
- IFRIC 14 "IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" effective for annual periods beginning on or after 1 January 2008. In many countries, laws or contractual terms require employers to make minimum funding payments for their pension or other employee benefit plans. Management is currently assessing the impact of this interpretation but believes that this interpretation should not have a significant impact on the Group.

5. CRITICAL ACCOUNTING JUDGEMENTS AND KEY SOURCES OF ESTIMATION UNCERTAINTY

In the application of the Group's accounting policies, which have been described in Note 3, management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant, including, but not limited to, the uncertainties and ambiguities of the Russian legal and taxation systems and the difficulties in securing your rights as defined in contracts. Actual results may differ from these estimates.

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

Inventory valuation

Inventories are valued at the lower of weighted average cost and net realizable value. Management reviews the inventory balances to determine if inventories can be sold at amounts greater than or equal to their carrying amounts. This review includes identification of slow moving inventories, obsolete inventories, and partially or fully damaged inventories. The identification process includes historical performance of the inventory, current operational plans for the inventory, as well as industry and customer specific trends. Damaged stock is either provided for or written off depending on the extent of damage. Management makes a provision for any items considered to be obsolete. The provision represents the difference between the cost of inventory and its estimated net realizable value.

The net realizable value provision was calculated using the following methodology:

(a) Stock held for resale – comparison of expected selling price versus the carrying value on a stock keeping unit basis;
(b) Damaged goods – examination of historical data relating to discounts associated with damaged goods and compared to book value at the balance sheet date;
(c) Stock held at service centers – applied a provision in the amount of 70% of the carrying value of the inventory.

If our actual results differ from our expectations with respect to the selling of our inventories at amounts equal to or less than their carrying amounts, we would be required to adjust our inventory.

Supplier bonuses

Management has determined that substantially all supplier bonuses received or receivable in respect of promotional activities should be treated as volume based, effectively reducing the cost of goods purchased from the suppliers. Had those bonuses been treated as a reduction of marketing expenses, inventories would increase by 121 million RUR, cost of goods sold would increase by 249 million RUR, and selling, general and administrative expenses would decrease by 370 million RUR.

Allowances for doubtful accounts

Allowance for doubtful accounts is established if there is objective evidence that the Group will not be able to collect the amounts due according to original contractual terms and reduces accounts receivable to the amounts expected to be collected. In estimating uncollectible amounts, management considers factors such as current overall economic conditions, historical customer performance and anticipated customer performance. The Group's provisions cover individual balances where there is evidence that losses are probable as at the balance sheet date. Management uses significant judgment in estimating uncollectible amounts. While management believes its processes effectively address the exposure for doubtful accounts, changes in the economy, industry or specific customer conditions may require adjustments to the allowance for doubtful accounts recorded in the Group's preliminary consolidated financial statements.

Tax and customs provisions and contingencies

The Group is subject to various taxes arising in the Russian Federation. The majority of its merchandise is imported into Russia and is therefore also subject to the Russian customs regulations. Significant judgment is required in determining the provision for income taxes and other taxes. The Group recognizes liabilities for anticipated tax issues based on estimates of whether additional taxes will be due. Refer to Note 31 for further discussion.

(In millions of Russian Rubles)

6. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment as at 31 December 2006 and 2005 consisted of the following:

	Buildings	Leasehold improvements	Trade equipment	Security equipment	Other	Total
Cost						
At 31 December 2005	-	63	267	115	191	636
Additions	2,205	464	143	82	198	3,092
Disposals	-	-	-	-	(9)	(9)
At 31 December 2006	2,205	527	410	197	380	3,719
Accumulated Depreciation						
At 31 December 2005	-	-	-	-	-	-
Charge for the year	9	42	89	66	90	296
Disposals	-	-	-	-	(1)	(1)
At 31 December 2006	9	42	89	66	89	295
Net Book Value						
At 31 December 2006	**2,196**	**485**	**321**	**131**	**291**	**3,424**
At 31 December 2005	**-**	**63**	**267**	**115**	**191**	**636**

During December 2006 the Group acquired a 100% interest in LLC "Sphera Invest" and LLC "Standard Invest" in exchange for 29,833 million ordinary shares issued by the Company. Prior to these acquisitions, these entities were under common control. The transactions were treated as acquisitions of assets. The total cost of property, plant and equipment acquired was 2,196 million RUR.

The net assets of LLC "Sphera Invest" and LLC "Standard Invest" as at the date of acquisition can be categorized as follows:

	million RUR
Buildings	2,182
Security equipment	4
Other property, plant and equipment	10
	2,196
Other assets	190
Deferred tax liability	(370)
Other liabilities	(802)
Net assets	1,214
Consideration	(1,492)
Charged to equity	**(278)**

The number of shares issued for property, plant and equipment received was based on an external valuation report. The difference between the nominal value of the shares issued and the fair value of property and equipment and other related assets and liabilities acquired was treated as an adjustment to equity, net of tax effect.

At 31 December 2006, property, plant and equipment with a carrying amount of 320 million RUR was collateralized against a portion of loans provided to the Group by banks (refer to Notes 17 and 22).

At 31 December 2006, there were no commitments for the acquisition of property, plant or equipment.

(In millions of Russian Rubles)

7. INTANGIBLE ASSETS

Intangible assets as of 31 December 2006 and 2005 consisted of the following:

	Software licenses	Trade marks	Total
Cost			
At 31 December 2005	17	-	17
Additions	17	3	20
Disposals	-	(1)	(1)
At 31 December 2006	34	2	36
Accumulated amortization			
At 31 December 2005	-	-	-
Charge for the period	3	-	3
At 31 December 2006	3	-	3
Net book value			
At 31 December 2006	**31**	**2**	**33**
At 31 December 2005	**17**	**-**	**17**

The amortization expense has been included in selling, general and administrative expenses.

At 31 December 2006, the Group had commitments for the acquisition of software licenses (refer to Note 31).

8. LONG TERM LOANS AND NOTES RECEIVABLE

Long term loans receivable as of 31 December 2006 and 2005 consisted of the following:

	Maturity	2006	2005
Promissory notes from a third party	March 2008	33	24
Unsecured RUR loans given to third parties	March 2008	3	-
Unsecured RUR loans given to related parties	December 2008 to May 2009	1	-
Total		**37**	**24**

Promissory notes from a third party represent the promissory note received from the company DVI Volga. The promissory notes are unsecured and not interest bearing.

For additional information relating to related party loans receivable, refer to Note 29.

(In millions of Russian Rubles)

9. INVENTORIES

Inventories as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
Goods for resale	7,682	5,826
Other inventories	13	1
Less: provision for obsolete and slow moving goods	(734)	(528)
Total	**6,961**	**5,299**

At 31 December 2006, the value of inventory pledged as collateral for borrowings from banks was 5,001 million RUR.

No inventory was collateralized for the year ended 31 December 2005.

10. TRADE ACCOUNTS RECEIVABLE

Trade accounts receivable as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
Trade receivables from third parties	709	24
Receivables from related parties	1	75
Provision for goods returns	(43)	(33)
Total	**667**	**66**

For details relating to related party receivables, refer to Note 29.

Trade receivables are non interest bearing and are generally on 7-30 day terms.

As at 31 December 2006 the trade receivables were neither past due nor impaired.

Refer to Note 32 for discussion of concentration of credit risk.

11. OTHER ACCOUNTS RECEIVABLE AND PREPAID EXPENSES

Other accounts receivable and prepaid expenses as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
Advances paid to suppliers and prepaid expenses	756	207
Other receivables from third parties	543	34
Other receivables from related parties	13	2
Advances paid to related parties	1	-
Less: Allowance for doubtful debts	(6)	(4)
Total	**1,307**	**239**

For details relating to other receivables due from related parties, refer to Note 29.

(In millions of Russian Rubles)

12. VALUE ADDED TAX RECOVERABLE AND OTHER TAXES RECEIVABLE

Value added tax recoverable and other taxes receivable as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
VAT recoverable	1,653	1,160
Other taxes receivable	13	6
Total	**1,666**	**1,166**

13. SHORT TERM LOANS AND NOTES RECEIVABLE

Short term loans and notes receivable of 31 December 2006 and 2005 consisted of the following:

	Interest rate %	Maturity	2006	2005
Promissory notes from third parties	-	December 2007	72	59
Unsecured RUR loans given to related parties	8%	August 2007	30	6
Total			**102**	**65**

Promissory notes from third party represent a promissory note from the Company DVI Izhevsk. The promissory notes are unsecured and not interest bearing.

For additional information relating to related party loans receivable, refer to Note 29.

14. CASH AND CASH EQUIVALENTS

Cash and cash equivalents as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
Petty cash and cash in stores	44	32
Cash at banks	140	315
Cash in transit	748	391
Total	**932**	**738**

At 31 December 2006, the fair value of cash and cash equivalents is equal to their carrying value.

Cash in transit represents cash collected from the Group's stores and not yet deposited into the bank account as of the relevant period end.

(In millions of Russian Rubles)

15. ISSUED CAPITAL

During the year the Company was reorganized from a Limited Liability Company to an Open Joint Stock Company. Before the reorganization, the Company increased its share capital by 5 million RUR. During reorganization the Company split into 120,705,400 ordinary shares with a par value of 0.05 RUR.

In December 2006, the Company issued an additional 29,832,940,000 ordinary shares with a par value of 0.05 RUR in exchange for issued share capital of LLC "Standard Invest" and LLC "Sphera Invest" (refer to Note 6).

The Company had 30,120,705,400 authorized ordinary shares as of 31 December 2006. The par value of ordinary shares is 0.05 RUR per share.

16. INCOME TAX

The Group's income taxes for the year ended 31 December 2006 was as follows:

	2006
Current tax expense	(455)
Deferred tax benefit	117
Total income tax expense	**(338)**
Deferred tax charged to equity (refer to Note 6)	**(370)**

The tax effect on the major temporary differences that give rise to the deferred tax assets and liabilities as at 31 December 2006 and 2005 is presented below:

	2006	2005
Deferred tax assets		
Difference in depreciable value of property, plant and equipment	35	1
Provision for obsolete and slow-moving inventory	176	127
Adjustment on unrealized profit	27	-
Warranty provision	2	2
Accrual for unused vacation	7	3
Provision for goods return	10	8
Deferred revenue	35	-
Fair market adjustment on forward exchange contract	4	-
Salary-related accruals	2	-
Adjustments on prepaid expenses	12	-
Write off of accounts receivable	5	-
Loss carry forward	29	17
Other adjustments	34	4
Total	**378**	**162**

(In millions of Russian Rubles)

	2006	2005
Deferred tax liabilities		
Difference in depreciable value of property, plant and equipment	394	1
Adjustment on supplier allowances and other adjustments on payables	66	-
Deferred cost	4	-
Other adjustments	6	-
Total	**470**	**1**

The Group has tax losses (refer to table above) that are available indefinitely for offset against future taxable profits of the companies in which they arose. Deferred tax assets have been recognized in respect of these losses as they have arisen in subsidiaries that are expected to be profitable in future periods.

The statutory tax rate effective in the Russian Federation was 24%. The taxation charge for the year is different from that which would be obtained by applying the statutory income tax rate to the net income before income tax. Below is a reconciliation of theoretical income tax at 24% to the actual expense recorded in the Group's income statement:

	2006
Income before income tax	736
Theoretical income tax expense at statutory rate of 24%	(177)
Adjustments due to:	
Non-deductible expenses, net	(129)
Income tax provisions	(32)
Income tax expense	**(338)**

Taxable temporary differences in relation to investments in subsidiaries for which deferred tax liabilities have not been recognized as of 31 December 2006 amounted to 454 million RUR.

17. LONG-TERM LOANS AND BORROWINGS

Long-term loans and borrowings as of 31 December 2006 and 2005 consisted of the following:

	Interest rate	Maturity	2006	2005
Secured third parties loans (banks) – 59 million EUR	EURIBOR(1m) and (3m) + 2.74% to 4.5%	January 2009	2,053	-
Unsecured loans from related parties	12%	June 2007	-	650
Total			**2,053**	**650**

The secured loans and borrowings have been secured by the Group's property, plant and equipment and inventory (refer to Notes 6 and 9).

(In millions of Russian Rubles)

18. BONDS PAYABLE

Bonds payable as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
Corporate bonds	**2,000**	**-**

In November 2006, the Group issued RUR non-collateralized bonds with gross proceeds amounting to 2,000 million RUR (the "Bonds"). Direct issue costs of these bonds were not significant. The maximum term of these bonds is 3 years with the maturity date being 18 November 2009. The coupon interest rate of these bonds is 10% for the first year. Interest is paid semi-annually in arrears. The bonds are listed on the Moscow Inter-bank Currency Exchange ("MICEX").

The interest rate paid on the bonds is fixed for the first year only. After the first anniversary, the Group can set a new coupon interest rate. The revised rate comes into effect on 18 November annually and would be fixed for another year. After the new rate is set, the bondholders have the option to either retain or redeem bonds held. The par value of individual bonds is 1,000 RUR.

Due to the redemption option described above, the bonds have been classified as current liabilities.

19. TRADE ACCOUNTS PAYABLE

Trade accounts payable as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
Trade payables to third parties	5,723	175
Trade payables to related parties	86	7,154
Total	**5,809**	**7,329**

Trade payables are non-interest bearing and are normally settled between 30 and 90 days, depending on individual supplier terms.

For terms and conditions relating to related party payables, refer to Note 29.

(In millions of Russian Rubles)

20. OTHER PAYABLES AND ACCRUED EXPENSES

Other payables and accrued expenses as of 31 December 2006 and 2005 consisted of the following:

	2006	2005
Interest payable to related parties	118	19
Other current liabilities to third parties	97	14
Accrued salaries	55	2
Accounts payable for property, plant and equipment	42	-
Accrued unused vacation	30	14
Bond coupon yield payable	21	-
Other accrued expenses	16	-
Other current liabilities to related parties	10	8
Interest payable to third parties	2	-
Total	**391**	**57**

Interest is settled periodically depending on the terms of the loan agreement.

Interest payable on the Bonds is settled semi-annually (refer to Note 18).

21. VALUE ADDED TAX AND OTHER TAXES PAYABLE

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

	2006	2005
VAT payable	102	6
Other taxes payable	53	29
Total	**155**	**35**

22. SHORT-TERM LOANS AND BORROWINGS

Short-term loans and borrowings as of 31 December 2006 and 2005 consisted of the following:

	Interest rate %	Maturity	2006	2005
Unsecured bank overdraft – RUR	8%	January 2007	31	-
Loans from third parties (Banks)				
Secured loan (RUR)	7.5 to 7.6%	January 2007 to April 2007	1,552	-
Secured loan (EUR)	7-8%	January 2006	-	106
Secured loan (EUR)	EURIBOR +4.4%	March 2006	-	770
Total short-term loans from third parties			**1,552**	**876**
Unsecured RUR loans from related parties	11% to 15%	June 2007	1,402	6
Total			**2,985**	**882**

The secured loans referred to in the table above have been secured by the Group's property, plant and equipment and inventory (refer to Notes 6 and 9).

(In millions of Russian Rubles)

23. REVENUES

Revenues for the year ended 31 December 2006 consisted of the following:

	2006
Sale of goods – retail (including internet)	31,402
Sale of goods – wholesale	4,831
Other	25
Total	**36,258**

Other revenue relates to the sale of additional service agreements and commissions from the sale of mobile phone contracts.

24. COST OF GOODS SOLD

Cost of goods sold for the year ended 31 December 2006 consisted of the following:

	2006
Cost of goods sold	29,593
Inventory losses	192
Change in provision for obsolete and slow moving inventory	206
Supplier bonuses	(1,349)
Total	**28,642**

25. SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

Selling, general and administrative expenses for the year ended 31 December 2006 consisted of the following:

	2006
Payroll and related taxes	1,630
Lease expense	1,351
Advertising and promotional expenses	1,281
Transportation	559
Warehouse services	428
Depreciation and amortization	299
Utilities expense	165
Repairs and maintenance	155
Service centre	146
Security	125
Bank charges	92
Consulting services	77
Travel	59
Communication	54
Office expenses	51
Packaging and raw materials	41
Legal and audit expenses	37
Training	37

(In millions of Russian Rubles)

	2006
Insurance	23
Taxes other than income tax	17
Commissions	8
Bad debt expense	6
Other	47
Total	**6,688**

Payroll and related taxes includes a 284 million RUR contribution to the state pension plan.

26. OTHER OPERATING INCOME

Other operating income for the year ended 31 December 2006 consisted of the following:

	2006
Income from supplier advertising	209
Other	205
Total	**414**

Other includes commissions received from banks on loans provided to customers, goods delivery and other individually insignificant items.

27. OTHER OPERATING EXPENSES

Other operating expenses for the year ended 31 December 2006 mainly consisted of loss on currency sales in the amount of 18 million RUR, loss on disposal of property, plant and equipment in the amount of 8 million RUR and other individually insignificant items.

28. FINANCE COSTS, NET

Finance costs for the year ended 31 December 2006 consisted of the following:

	2006
Interest on bank loans	187
Interest on non-bank loans	118
Coupon yield on corporate bonds	21
Change in fair value of derivatives	15
Other	70
Total	**411**

(In millions of Russian Rubles)

29. RELATED PARTIES

Related parties include shareholders, key management, entities under common ownership and control, and entities over which the Group has significant influence.

The preliminary consolidated financial statements include the financial statements of OJSC "Company M.video" and its subsidiaries which are listed in Note 1 under "General Information".

The following table provides the total amount of transactions, which have been entered into with related parties for the relevant financial year (for information regarding outstanding balances at 31 December 2006 and 2005, also refer to Notes 8, 10, 11, 13, 17, 19, 20, 22):

Sales/purchases from related party	2006	2006	31 December 2006		31 December 2005	
	Sales to related parties	Purchases from related parties	Amounts owed by related parties	Amounts owed to related parties	Amounts owed by related parties	Amounts owed to related parties
Entities under common control						
LLC "Sphera Invest"*	-	89	-	-	-	-
LLC "Standard Invest"*	1	72	-	-	-	-
LLC "ElectroAreal"	-	(2)	12	-	75	7,154
LLC "KMV"	-	18	-	80	-	-
LLC "Olga-Alternativa"	-	2	-	1	-	-
LLC "Anzhela"	-	5	1	-	1	-
LLC "Polet-ZM"	-	1	-	26	-	-
LLC "Bars"	-	19	-	-	-	-
LLC "Private Security Agency Bars-SB"	-	35	-	-	-	-
LLC "Noviy Format"	-	21	2	-	-	-
Transservice Group of Companies	16	77	-	2	-	1
LLC "Transfert"	-	1	-	-	-	1
LLC "Avtoritet"	-	8	-	-	1	-
LLC "Avto-Express"	-	65	-	6	-	-
LLC "PSK Logistic Service"	-	717	-	-	-	-
LLC "TIC BE Sokol"	-	118	-	-	-	-

* – These entities became part of the Group during the year ended 31 December 2006 (refer to Note 6).

Loans from/to related party			31 December 2006		31 December 2005	
	Interest income	Interest expense	Amounts owed by related parties	Amounts owed to related parties	Amounts owed by related parties	Amounts owed to related parties
Entities under common control:						
Goodhall Ltd	-	88	-	891	-	669
Velga Ltd	-	3	-	630	-	-
LLC "ElectroAreal"	-	-	-	-	-	6
LLC "Noviy Format"	-	-	25	-	-	-
LLC "Transservice-95"	-	-	3	-	-	-
LLC "Avto-Express"	-	-	2	-	-	-
LLC "Anzhela"	-	-	-	-	5	-
LLC "Apeks Plus"	-	-	-	-	1	-

The ultimate parent

M.video Investment Ltd. (BVI)

There were no transactions between the Group and the ultimate parent during the year ended 31 December 2006.

Immediate parent entity

Svece Ltd owns 99.597% of the ordinary shares of OJSC "Company M.video".

Refer to Notes 1 and 15.

Terms and conditions of transactions with related parties

Related parties may enter into transactions, which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties. Outstanding balances at the year end are unsecured and settlement occurs in cash. There have been no guarantees provided or received for any related party receivables or payables with the exception of what is disclosed in Note 31. For the year ended 31 December 2006, the Group has not recorded any impairment of receivables relating to amounts owed by related parties (2005: nil). This assessment is undertaken each financial year through examining the financial position of the related party and the market in which the related party operates.

Transactions with other related parties

The nature of transactions with related parties is as follows:

- LLC "Sphera Invest" – rented property to the Group up to the time the properties were purchased by the Group. Refer to Notes 6 and 15;
- LLC "Standard Invest" – rented property to the Group up to the time the properties were purchased by the Group. Refer to Notes 6 and 15;
- LLC "KMV", LLC "Olga Alternativa", LLC "Anzela", LLC "Nadezhda Yg", LLC "Polet ZM", LLC "Noviy Format" – relates to the purchase of properties by LLC "Sphera Invest" and LLC "Standard Invest";
- LLC "ElectroAreal" – the Group acquired inventory held as at 1 January 2006 from this entity;
- LLC "Bars" – provided courier services to the Group;
- LLC "Private Security Agency Bars – SB" – provided store and head office security services;
- LLC "Transservice 95" – provided after sale and other servicing of the Group's merchandise;
- LLC "Transfert" – provided logistics and home delivery services;
- LLC "Avtoritet" – provided the brand name "Smart-on" to the Group under a license agreement and two trading premises in Moscow under a lease agreement;
- LLC "Avto-Express" – provided a car leasing service to the Group and logistic services;
- LLC "TIC BE Sokol" – sells private label merchandise to the Group;
- Goodhall Ltd – provided financing to the Group;
- Velga Ltd – provided financing to the Group.

(In millions of Russian Rubles)

Compensation of key management personnel of the Group

Key management personnel as at 31 December 2006 are as follows:

EXECUTIVES	Title
Alexander Tynkovan	President and Chief Executive Officer
Alexander Zayonts	Vice-President
Mikhail Tynkovan	Director
Christopher Parks	Chief Financial Officer – Appointed 2 October 2006
Pavel Breev	General / Expansion Director
Janusz Lella	Retail Director
Michael Kuchment	Commercial Director
Georges Correia	IT Director
Natalya Muravieva	Logistics Director
Olga Vasiliskova	Human Resources Director
Martina Frieser	Marketing Director – Appointed 1st November 2006
Oleg Lunin	Chief Financial Officer – Resigned 30th June 2006
Victor Schipin	Marketing Director – Resigned 31 August 2006.

Compensation of key management personnel for the period ended 31 December 2006 comprised of only short term benefits including salaries, bonuses, relocation, annual leave, schooling and medical insurance expenses and amounted to 62 million RUR.

The Group did not provide any post employment, termination or share based benefits to key management personnel during the period other than contributions to state pension fund and the social funds as a part of payments of unified social tax on salaries and bonuses. Unified social tax paid relating to compensation of key management personnel is included in the amount stated above.

30. OPERATING LEASE ARRANGEMENTS

The Group has entered into commercial leases for the rental of retail properties, warehouses and office space. These leases have terms ranging between 1 and 10 years. The majority of the lease contracts contain escalation clauses. The Group does not have an option to purchase the leased premises at the expiration of the lease period.

Future minimum rentals payable under non-cancelable operating leases for premises occupied as at 31 December 2006 are as follows:

	2006
Within one year	1,511
After one year but not more than five years	4,450
More than five years	3,728
	9,689

(In millions of Russian Rubles)

Future minimum rentals payable under committed, non-cancelable future store operating leases for premises as at 31 December 2006 are as follows:

	2006
Within one year	60
After one year but not more than five years	901
More than five years	1,466
	2,427

31. COMMITMENTS AND CONTINGENCIES

Taxation and regulatory environment

Russian tax, currency and customs legislation is subject to frequent changes and varying interpretations. Management's interpretation of such legislation in applying it to business transactions of the Group may be challenged by the relevant authorities enabled by law to impose fines and penalties. Recent events within the Russian Federation suggest that the tax, customs or other relevant government authorities are taking a more assertive position in their interpretation of the legislation and assessments made and as a result, it is possible that the transactions that have not been challenged in the past may be challenged in the future. Generally, fiscal periods remain open to review by the tax authorities in respect of taxes for the three calendar years preceding the year of tax review. Under certain circumstances reviews may cover longer periods. The Group believes it has provided adequately for all tax liabilities based on its understanding of the tax legislation.

Management reviews the Group's compliance with applicable tax regulations and current interpretations. Furthermore, management regularly assesses the potential financial exposure relating to tax contingencies for which the 3 years tax inspection right has expired but, which, under certain circumstances, may be challenged by regulatory bodies. From time to time potential exposures and contingencies are identified and at any point in time a number of such open tax positions may exist. Management has recorded a provision of 32 million RUR for income tax contingencies in these consolidated financial statements as their best estimate of potential liabilities arising from such contingencies. However, the range of potential exposures and details of individual tax positions are not disclosed to avoid prejudicing the Group's position.

Customs

As is common in the business, the Group or an affiliated party negotiates and confirms with overseas representatives of foreign manufacturers, the quantity, price and attributes of the foreign manufactured goods, but the goods may be procured through parties both affiliated and unaffiliated with the Group.

Subject to the above, during the year ended 31 December 2006, the Group purchased a significant portion of its foreign manufactured goods on the territory of the Russian Federation from Russian legal entities, including Russian wholesalers or resellers, which may or may not have imported the goods into Russia directly. As the Group was not involved in clearing customs for the goods purchased on the territory of Russia, management can not be certain that the entities which imported the goods into Russia were in full compliance with the applicable regulations of the Russian customs code. During the year the relative proportion of direct imports from foreign manufacturers and purchases from the Russian subsidiaries of foreign manufacturers has been increasing and the purchases from Russian wholesalers and resellers decreasing.

As described above in *Taxation and regulatory environment section*, the relevant authorities are taking a more assertive position in their interpretation of the applicable laws. Under Russian law a company in possession of goods that were imported with proven violations of the customs law may be subject to significant administrative or civil penalties and / or confiscation of the goods, if it was involved in, aware of, or should have known that violation of the customs code were occurring. To date, the Group has not been subject to any notification of violations of the customs code.

Management believes that the Group entities were acting in compliance with all applicable tax and legal requirements in respect imported products, were not involved, not aware and could not be expected to know of any significant violations of the applicable customs code by the Russian wholesalers or resellers. Accordingly, management did not recognize any provisions in respect of such contingencies in these preliminary consolidated IFRS financial statements and determined that with current limitations in access to customs clearance documents it is not practicable to estimate the likely potential financial effect, if any, of such contingent liabilities.

License Agreements

At 31 December 2006, the Group had a commitment of 6 million RUR in respect of a SAP software license payable over the next year. The Group uses SAP software for finance and human resources. In addition, the Group had entered into a contract for SAP support which amounted to approximately 300 thousand RUR on an annual basis.

Further, the Group has entered into a 5 year contract with Microsoft for Microsoft Office software rights which commenced in July 2006. This contract is structured in a way that allows the Group to prepay one year at a time. The amount paid during 2006 was 11 million RUR. Based on expected growth rates in the number of users during the remainder of the 5 year contract, the average annual cost for years 2 to 5 should be approximately 23 million RUR. Assuming that the actual number of users is in line with expectations during the remainder of the 5 year contract, this amount is a reasonable approximation of the annual commitment to Microsoft in the subsequent years.

Litigation

In the normal course of business, the Group is subjected to proceedings, lawsuits, and other claims. While such matters are subject to other uncertainties, and outcomes are not predictable with assurance, the management of the Group believes that any financial impact arising from these matters would not be material to its financial position or annual operating results.

Environmental matters

The enforcement of environmental regulation in the Russian Federation is evolving and the enforcement posture of government authorities is continually being reconsidered. The Group periodically evaluates its obligations under environmental obligations. In the current enforcement climate under existing legislation, management believes that there are no significant liabilities for environmental matters.

Guarantees

The Group has guaranteed to an unrelated party the performance of a contract in respect of the supply of goods, entered into by a related party, to a maximum amount of 69 million RUR.

(In millions of Russian Rubles)

32. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Group's principal financial instruments, other than a forward exchange contract, comprise bank loans, overdrafts and trade payables. The main purpose of these financial instruments is to raise finance for the Group's operations. The Group has various financial assets such as trade receivables and cash, which arise directly from its operations.

The Group entered into a forward exchange contract to manage currency risks arising from the Group's sources of finance. It is, and has been throughout 2006, the Group's policy that no trading in derivatives for speculative purposes shall be undertaken.

The main risks arising from the Group's financial instruments are cash flow interest rate risk, liquidity risk, foreign currency risk and credit risk. The shareholders review and agree policies for managing each of these risks which are summarized below:

Interest rate risk

The Group's exposure to the risk of changes in market interest rates relates primarily to the Group's long-term obligations with floating interest rates.

There is also a risk to short-term rates due to economic and political risks associated with working in the Russian Federation with predominantly Russian banks who borrow on international markets.

The following table sets out the carrying amount, by maturity, of the Group's financial instruments that are exposed to interest rate risk:

31 December 2006	**Within 1 year**	**1-2 years**	**2-3 years**	**3-4 years**	**4-5 years**	**More than 5 years**	**Total**
Floating rate							
EURIBOR (1m) and 3m+2.74% to 4.5% Secured bank loans	-	-	2,053	-	-	-	**2,053**

31 December 2005	**Within 1 year**	**1-2 years**	**2-3 years**	**3-4 years**	**4-5 years**	**More than 5 years**	**Total**
Floating rate							
EURIBOR (1m)+4.4% Secured bank loan	770	-	-	-	-	-	**770**

(In millions of Russian Rubles)

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's profit before tax (through the impact on floating rate borrowings). This assumes that year end debt levels are constant over the year. There is no impact on the Group's equity.

	Increase / decrease in basis points	Annualized effect on profit before tax
2006		
Changes in the floating interest rates	25	(5)
	50	(10)
	100	(21)
	(25)	5
	(50)	10
	(100)	21

Additionally, the Group is exposed to changes in interest rates as and when it refinances its short-term borrowings (Notes 18 and 22), including resetting the interest rate payable on the corporate bonds during November 2007 as described in Note 18.

Foreign currency risk

The Group has transactional currency exposures. Such exposures arise from: (1) purchases by an operating unit with delayed credit terms in currencies other than the unit's functional currency. The Group does not attempt to hedge this risk, as individually these amounts are too small to warrant hedges and the payment dates are too frequent to attempt to do a collective hedge; (2) long term loans which are denominated in Euros or United States Dollars. The Group uses forward exchange contracts to eliminate the currency exposures on loan repayments. The forward exchange contracts must be in the same currency as the foreign currency item.

It is the Group's policy not to enter into forward contracts until a firm commitment is in place. The Group does not have transactional currency exposure relating to revenues as sales occur on the territory of the Russian Federation and are denominated in RUR.

No sensitivity analysis has been performed due to the fact that movements in foreign currencies (i.e. 10% or less) will not have a material impact on the Group.

Credit risk

The Group trades only with recognized, creditworthy third parties who are registered in the Russian Federation. It is the Group's policy that all customers who are granted credit terms have a history of purchases from the Group, employ individuals who are known to the Group and can demonstrate they have the financial resources to cover their limits. The Group also requires these customers to provide certain documents such as incorporation documents and financial statements. In addition, receivable balances are monitored on an ongoing basis with the result that the Group's exposure to bad debts is not significant.

During the year ended 31 December 2006, the Group provided a financial guarantee on behalf of a related party (refer to Note 31). With respect to credit risk arising from the financial assets of the Group, the Group's exposure to credit risk arises from default of the counterparty, with a maximum exposure equal to the carrying amount of these instruments.

(In millions of Russian Rubles)

As at 31 December 2006 there was one trade debtor owing to the Group 521 million RUR, representing 78% of total balance. This related to sales to a wholesale customer made during December 2006. This was a one off transaction and the outstanding amount was collected in full during first six month of 2007. There were no other concentrations of credit risk as of 31 December 2006.

Liquidity risk

The Group's treasury department monitors its risk to a shortage of funds using a recurring liquidity planning tool. This tool considers the maturity of both its financial investments and financial assets (e.g. accounts receivable, other financial assets) and projected cash flows from operations.

The Group's objective is to maintain a continuity of funding and flexibility through the use of bank overdrafts and bank loans. Each year the Group analyzes its funding needs and anticipated cashflows, so that it can determine its funding needs. The seasonality of the business, the store expansion plan and the anticipated working capital requirements form the basis of the evaluation. The Group uses long-term instruments (loans and borrowings) to cover a significant proportion of the base liquidity needs. The Group uses short term loans and bank overdrafts to cover seasonality needs. Every quarter the Group updates its liquidity needs and secures facilities with several banks to ensure that the Group has sufficient amount of approved undrawn borrowing facilities. At 31 December 2006, the Group had available 3.41 billion RUR of uncommitted standby borrowing facilities. The Group can formally apply for additional tranches of debt and the bank will provide additional funding provided all conditions precedent had been met. Additionally, if corporate bonds are not put for redemption until 2009, approximately 58% of the Group's debt will mature in more than one year from December 31 2006.

The table below summarizes the maturity profile of the Group's financial liabilities at 31 December 2006 based on contractual undiscounted payments:

31 December 2006	Less than 3 months	3-12 months	1-5 years	Total
Interest bearing loans and borrowings	1,583	3,402	2,053	7,038
Trade payables	5,809	-	-	5,809
Other payables and accrued expenses	403	21	-	424
Income tax payable	309	-	-	309
Value added tax and other taxes payable	155	-	-	155
Forward exchange contract	-	-	15	15
Total	**8,259**	**3,423**	**2,068**	**13,750**

31 December 2005	Less than 3 months	3-12 months	1-5 years	Total
Interest bearing loans and borrowings	876	6	650	1,532
Trade payables	7,329	-	-	7,329
Other payables and accrued expenses	57	-	-	57
Income tax payable	11	-	-	11
Value added tax and other taxes payable	35	-	-	35
Forward exchange contract	-	-	-	-
Total	**8,308**	**6**	**650**	**8,964**

(In millions of Russian Rubles)

Capital management

The primary objective of the Group's capital management program is to maximize shareholder value while minimizing the risks associated with the loan portfolio. The consumer electronics business is a cyclical business and as such requires short term fluctuations in capital to purchase goods to satisfy the seasonal demand. The Group uses a combination of long-term loans, short term loans and supplier credit terms to meet the seasonal capital needs. The store expansion program adds to the capital needs as the capital and pre-opening costs associated with the new stores puts additional pressure on the Group's financial resources. While the Group has not established any formal policies regarding debt to equity proportions the Group reviews the capital needs of the Group periodically to determine actions to balance its overall capital structure through shareholders' capital contributions or new share issues, return of capital to shareholders as well as the issue of new debt or the redemption of existing debt.

The Group's overall strategy remains unchanged from 2005.

Fair values

Set out below is a comparison by category of carrying amounts and fair values of all of the Group's financial instruments that are carried in the financial statements:

	Carrying amount		Fair value	
	2006	**2005**	**2006**	**2005**
Financial assets				
Cash and cash equivalents	932	738	932	738
Available for sale investment at cost	28	-	28	-
Loans and notes receivable (current)	102	65	102	65
Loans and notes receivable (non-current)	37	24	37	24
Financial liabilities				
Bank overdraft	31	-	31	-
Interest-bearing loans and borrowings:				
Floating rate borrowings	2,053	770	2,053	770
Fixed rate borrowings	4,954	762	4,954	762
Forward exchange contract	15	-	15	-

33. EFFECT OF FIRST-TIME ADOPTION OF IFRS

The first year of application of IFRS was 2006. The transition to IFRS was accounted for according to IFRS 1 "First-time Adoption of International Financial Reporting Standards". 1 January 2006 was the date of transition to IFRS. The effect of transition from RAS to IFRS is as follows:

Reconciliation of shareholders' equity as of 31 December 2006 and 1 January 2006:

	31 December 2006	1 January 2006
Company's equity under RAS reported in standalone basis (unaudited)	**6**	**4**
Other consolidated entities' equity/(deficit) under RAS reported in standalone basis (unaudited)	**672**	**(90)**
Cumulative equity/(deficit) under RAS for all Group entities reported in standalone basis (unaudited)	**678**	**(86)**

(In millions of Russian Rubles)

	31 December 2006	1 January 2006
IFRS adjustments:		
Consolidation of subsidiaries – eliminating entries	(345)	(8)
Provision for obsolete and slow moving inventory and adjustment on supplier bonuses	(595)	(528)
Adjustments to cost and depreciation of property, plant and equipment	21	(5)
Adjustments on amortization of intangible assets	(28)	-
Provision for doubtful accounts receivable	(9)	(4)
Provision on goods return	(42)	-
Expenses accrual	(35)	(10)
Deferred tax	209	161
Deferred revenue	(142)	-
Warranty provision	(10)	(7)
Recognition of forward	(15)	-
Adjustment on share capital	1,492	-
Other adjustments	(84)	(35)
Total adjustments to shareholders' equity/(deficit)	**417**	**(436)**
Shareholders' equity/(deficit) in accordance with IFRS	**1,095**	**(522)**

Reconciliation of net income under RAS and IFRS for the year ended 31 December 2006 is as follows:

	2006
Company's loss under RAS reported on standalone basis (unaudited)	**(2)**
Other consolidated entities' profit under RAS reported on standalone basis (unaudited)	**756**
Cumulative profit under RAS for all Group entities reported on standalone basis (unaudited)	**754**
IFRS adjustments:	
Consolidation of subsidiaries	(286)
Depreciation/amortization of property, plant and equipment and intangible assets	(99)
Change in inventory obsolescence provision and adjustment of cost of inventory for supplier bonuses	161
Deferred tax	48
Deferred revenue	(142)
Change in provision for goods return	(42)
Deferred cost	17
Capitalization of leasehold improvements	88
Consolidation and other adjustments	(101)
Total adjustment to net income	**(356)**
Net income in accordance with IFRS	**398**

34. EVENTS AFTER THE BALANCE SHEET DATE

(a) The following entities were merged into LLC "M.video Management" on 2 April 2007:

Name of subsidiary

LLC "M.video – Voronezh"
LLC "M.video – Ekaterinburg"
LLC "M.video – Kazan"
LLC "M.video – Krasnodar"
LLC "M.video – Nizhny Novgorod"
LLC "M.video – Oblast"
LLC "M.video – Perm"
LLC "M.video – Petersburg"
LLC "M.video – Rostov on Don"
LLC "M.video – Samara"
LLC "M.video – Saratov"
LLC "M.video – Ufa"
LLC "M.video – Center"
LLC "M.video – Chelyabinsk"
LLC "Techno-smart"
LLC "Triumph MV"

(b) Reverse split transaction

On 13 July 2007, the OJSC "Company M.video" Board of Directors approved a reverse share split of 1:200 (in compliance with the decision of OJSC "Company M.video" shareholders on 29 June 2007). On 23 August 2007 the Company registered this change with the appropriate governmental agencies and changed the charter and share register from 29,953,645,400 shares at 0.05 RUR to 149,768,227 shares at 10 RUR.

(c) LLC "Liga Development"

On 16 August 2007, the Group sold its 25% interest in LLC "Liga Development" to a related party for 28 million RUR. The sales price was equal to the carrying value of the asset as at 31 December 2006. The asset is included in the 31 December 2006 preliminary IFRS consolidated financial statements in the line "Available for sale investment at cost".

(d) Service center

On 10 September 2007, LLC "M.video Management" signed a contract to transfer its obligations under the 2, 3 and 5 year additional service agreements ("ASA") to a related party. Under the terms of the contract the related party will be responsible for all costs associated with the rendering of services under the ASA program. In return for assuming this obligation the related party will be paid a percentage of the monies received from the Group's customers. The contract provisions include both past and future sales of the ASA. The related amount of deferred revenue at the date of sale, net of consideration paid to the related party, would be recognized as income by the Group.

(e) Long term incentive plan

On 28 June 2007, the Board of Directors approved the adoption of a Long Term Incentive Plan (LTIP) for selected members of the Group’s management team. In accordance with the terms of the LTIP, one percent (1%) of the Company’s existing shares have been allocated to the LTIP, contingent on the occurrence of Initial Public Offering of the Company’s shares (“IPO”). Between 26 September 2007 and 1 October 2007, 35 persons became members of the plan and 42.37% of the shares designated for the LTIP were committed. Under the terms of the LTIP the vesting period is three (3) years with 33.33% of the shares to vest each April subsequent to the year of the IPO. Participants are able to exercise their 33.33% entitlement within 30 days of each vesting period by paying 10 RUR per share to the operator of the program after the vesting date. The participant must be employed at the anniversary date to exercise his or her right unless the Board of Directors waives this condition.