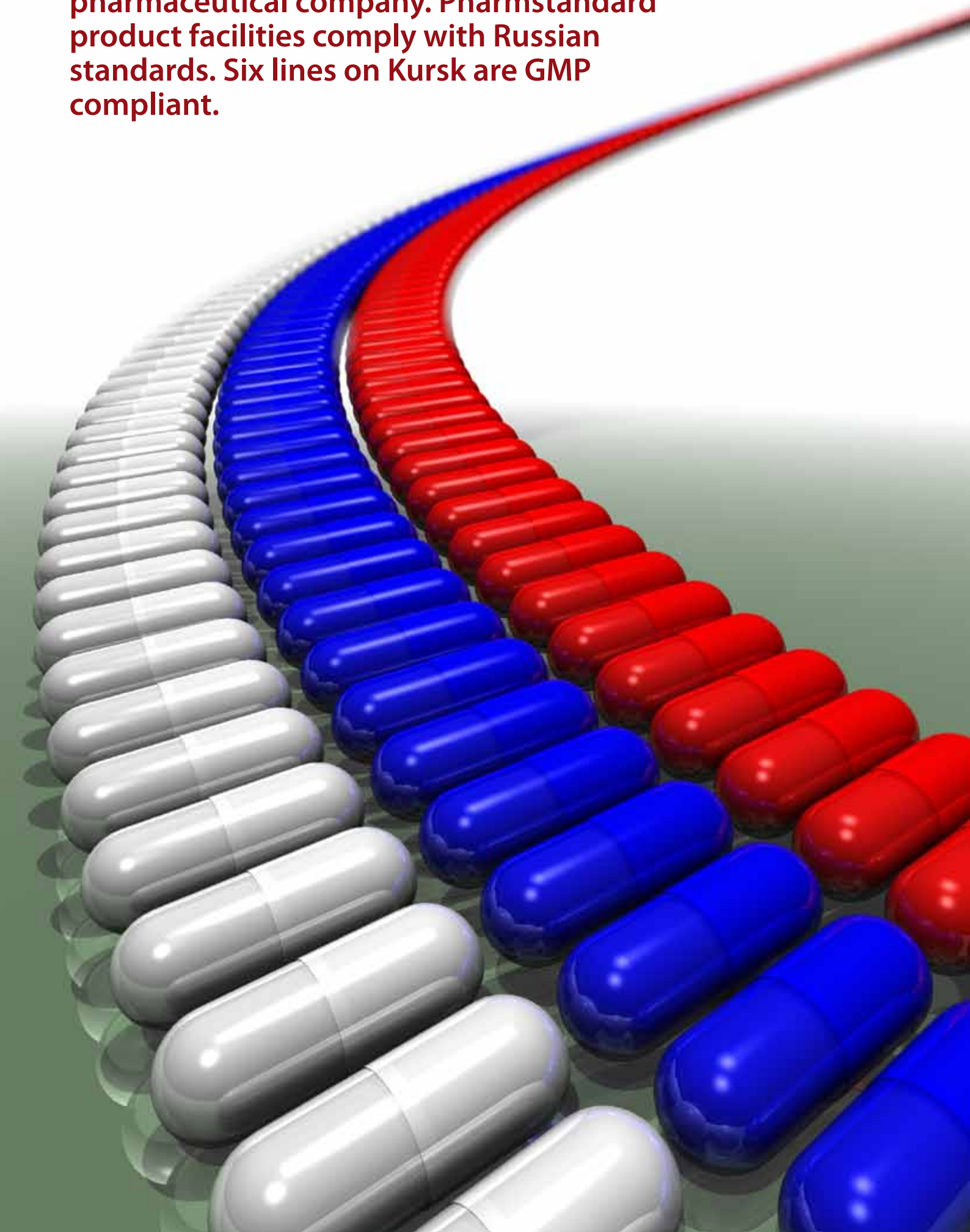
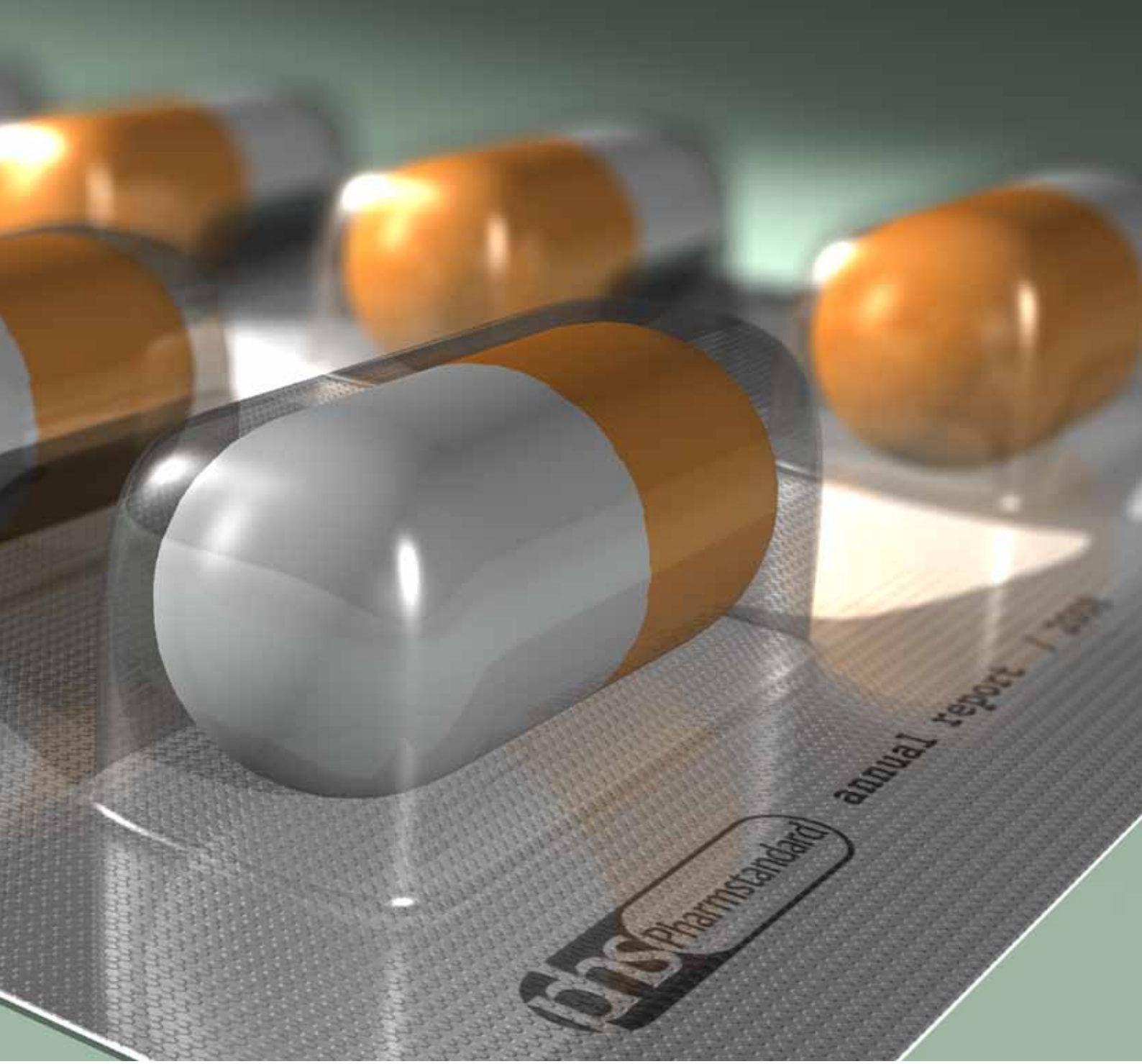

Pharmstandard
2008
ANNUAL REPORT

Pharmstandard is the leading Russian pharmaceutical company. Pharmstandard product facilities comply with Russian standards. Six lines on Kursk are GMP compliant.



Annual report 2008

- Pharmstandard is included into the list of the top 100 fastest growing European companies published by BusinessWeek



01 Introduction

CEO STATEMENT

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I am delighted to provide you with the Pharmstandard annual report on performance in 2008. Like for many companies in the world the year has been difficult but interesting.

The main point is that we achieved the objectives of 2008 and implemented the projects for the year following our strategy. We are ranked the second in the Russian pharmaceutical market and remain among Russian leading manufacturers. We reached high rates of sale and earn high profit in business.

Growth of pharmaceutical product sale revenues reached 36% due to promotion of own brands, sales of new 14 preparations and implementation of joint projects with other pharmaceutical companies.

Acquisition of original Afobazol antianxiety drug appeared to be the next step in our portfolio development. The deal was funded from the current operations and avoided external borrowings.

We continued reorganization and development of our production floors, opened new facilities for production of liquid and solid drug formulations in our factory of OJSC Pharmstandard-Tomskhimpharm and expanded production of liquid drug formulations in the facility of OJSC Pharmstandard-Ufavita.

European inspectors recognized compliance of 6 production lines in the facility of OJSC Pharmstandard-Leksredstva with EU GMP requirements which makes expansion of production and sales for European countries a challenge.

In 2008 Pharmstandard became one of the Russian backbone companies including other 295 companies from various industries. We regard this as recognition of the domestic pharmaceutical production and strategic area for the Russian state and economy.

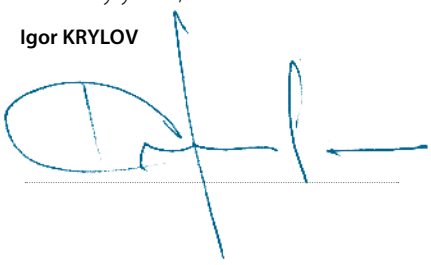
Despite the economic recession, we are planning to implement projects in 2009 to retain leading positions in the market, cooperate with international companies and substitute imports.

We shall strengthen control over expenses and raise efficiency of business processes both in production and marketing and promotion.

For and on behalf
of the Board of Directors

Sincerely yours,

Igor KRYLOV



STATEMENT OF RESPONSIBILITIES

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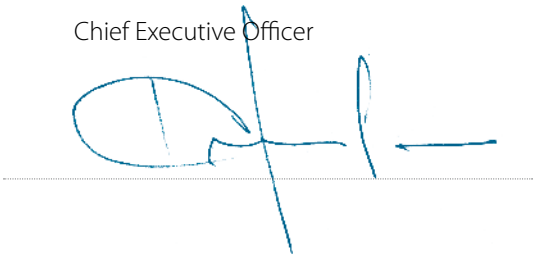
The Management Board members are responsible for preparing this Annual Report of JSC Pharmstandard ("Pharmstandard" or "the Company"), including financial statements in accordance with applicable law and regulations. Each of the current Management Board members, whose names and functions are listed in the Corporate governance section of the Annual Report 2008 confirms that, to the best of his or her knowledge:

- the Company's financial statements, which have been prepared in accordance with IFRS, give a true and fair view of the assets, liabilities, financial position and profit of the Company; and
- the Business Report section contained in the Annual Report includes a fair review of the development and performance of the business and the position of the Company, together with a description of the principal risks and uncertainties that it faces.

Chief Executive Officer



2008 HIGHLIGHTS

Pharmstandard becomes #2 pharmaceutical company in Russia

>> Major Events & Achievements

Company

- Pharmstandard becomes No 1 in the Russian pharmaceutical commercial segment;
- Pharmstandard becomes No 2 in the Russian pharmaceutical market;
- Pharmstandard is included into the list of strategic companies issued by the Government of the Russian Federation;
- Pharmstandard is included into the list of the top 100 fastest growing European companies published by BusinessWeek1;
- Pharmstandard – Leksredstva JSC receives a visit from Russia Prime Minister Vladimir Putin, who came to Kursk to hold a session of the RF Government dedicated to the development of pharmaceutical industry.

Financials

- Revenue growth +26%; total revenue 14,336 mln RUR
- Gross profit growth +28%; gross profit 8,759 mln RUR or 61% of sales
- EBITDA2 growth +24%; EBIDTA 6,049 mln RUR or 42% of sales
- Net profit growth + 7%; net profit 3,503 mln RUR or 24% of sales

Products

- Arbidol® becomes the best selling over-the-counter product of the retail pharmaceutical segment
- Direct antiviral effect of Arbidol® is confirmed in major scientific peer-review journals
- Pentalgin® is announced winner of NARODNAYA MARKA (People's Brand)/RUSSIA'S BRAND No1 Award in Painkillers Category according to the results of nationwide opinion polls
- Pharmstandard's gene-engineering product sales results show noticeable progress. The sales of Biosulin® grew by 36% and reached 164 mln RUR

1 *http://www.businessweek.com/globalbiz/europe/special_reports/20081113europeshot.htm*
2 *EBITDA is defined as profit for the accounting period before finance costs, income tax expense and depreciation and amortization and excluding foreign exchange gain or loss*

Rastan® and Arbidol®
Winners of "Platinum Ounce" awards in 2007

- 3 Pharmstandard brands are named among the top 20 best selling brands in Russia
- Company launches 14 new products, whose share in the sales revenue at the year-end reaches 212 mln RUR. Products launched in 2007 contributed 437 mln RUR

Facilities

- Pharmstandard receives international EU GMP certificates for six Pharmstandard – Leksredstva JSC production lines
- The total output of medicines exceeds 640 million packages (over four packages per each Russian resident)

Long-term projects and Acquisitions

- Pharmstandard acquires the Afobazol® trade mark from Donelle Company Limited financing the transaction entirely from own funds. Afobazol® is a new original selective anxiolytic for anxiety disorders treatment. The product is patent-protected until 2019. Pharmstandard's sales of Afobazol® started in August 2008 and reached 218 mln RUR
- In February 2008, Pharmstandard and Grindeks (Latvia) sign a long-term cooperation agreement for exclusive distribution and promotion of Mildronate® preparation in the Russian Federation. The Mildronate® project developed and implemented in cooperation with Grindeks proves to be a success.
- Pharmstandard announces successful development of SOLMIR project. According to the agreement with Solvay Pharmaceuticals (France), Pharmstandard will produce 2 immunomodulating products – IRS19® and Imudon®. The sales of IRS19® started early in December 2008
- In 2008, the Company's management approved a plan to acquire minority interests in several subsidiaries. As a result, the Company acquired the remaining minority interests in OJSC "Pharmstandard-Ufavita", OJSC "Pharmstandard-Octyabr", OJSC "Pharmstandard-Leksredstva" and OJSC "TZMOI" and became the sole shareholder in all those entities

2008 HIGHLIGHTS

Pharmstandard in figures

Highlights

	2004	2005	2006	2007	2008	CAGR, %
Revenue, RUR mln	3,946	5,685	8,523	11,371	14,336	
growth, %		*44%*	*50%*	*33%*	*26%*	*38%*
Gross Profit, RUR mln	1,726	3,178	4,942	6,852	8,759	
growth, %		*84%*	*56%*	*39%*	*28%*	*50%*
EBITDA, RUR mln	583	1,720	3,255	4,882	6,049	
growth, %		*195%*	*89%*	*50%*	*24%*	*79%*
Net Profit, RUR mln	320	1,019	2,036	3,263	3,503	
growth, %		*218%*	*100%*	*60%*	*7%*	*82%*

Chart #1. Main indictors

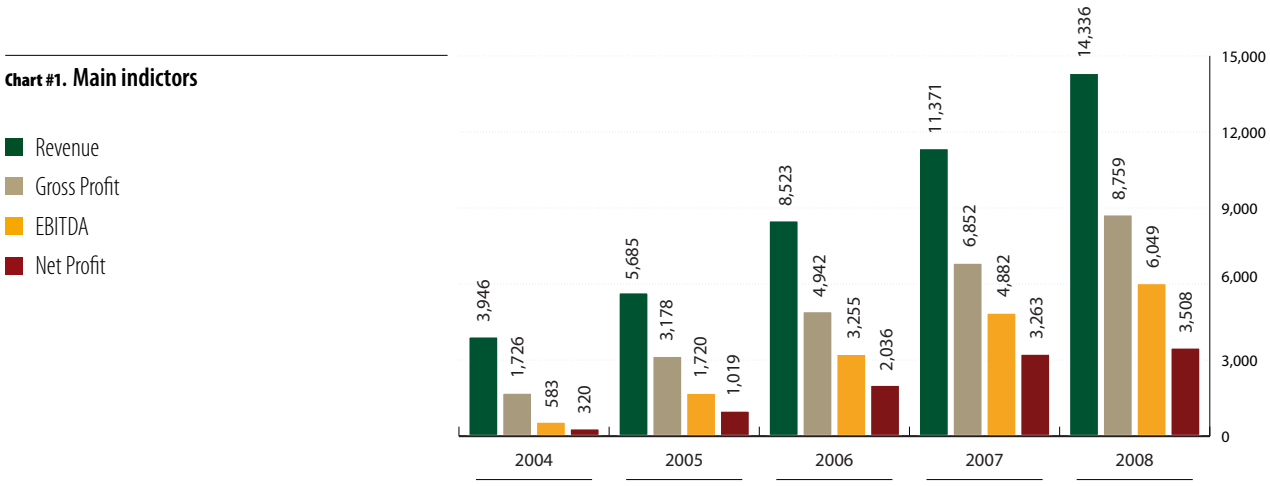
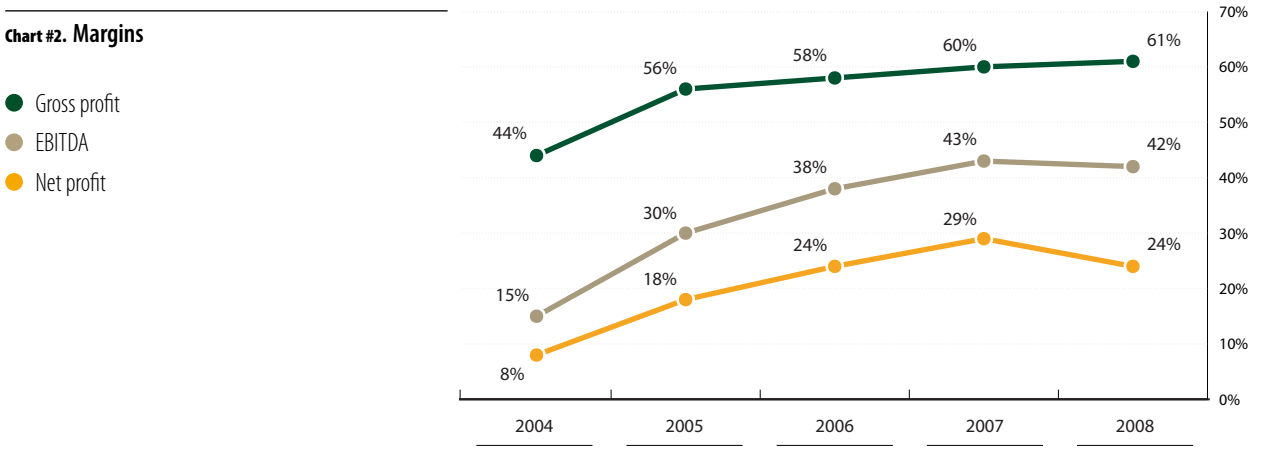


Chart #2. Margins



SHAREHOLDERS STRUCTURE

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Pharmstandard became a public company in 2007 by offering to the public 25.0% of its share capital in the form of GDR during the Initial Public Offering (IPO) on the London Stock Exchange (LSE) and 18.3% of its share capital in the form of ordinary shares on two local stock exchanges (RTS, MICEX).

In May 2008, the major Pharmstandard shareholder, Augment Investments Limited, placed 2.5% of JSC Pharmstandard share capital in the form of GDR at the market price.

The following table provides information about Pharmstandard shares ownership.

As of 31 December	2008	2007
Augment Investments Limited	54.2%	56.7%
Free Float	45.8%	43.3%
GDR	27.5%	25.0%
Local shares	18.3%	18.3%

Dividends

The Board of Directors recommends not paying dividends for the financial year ended December 31, 2007. Like in 2007, no dividends on ordinary shares will be paid out of 2008 earnings. The Company will retain earnings for possible M&A deals.

CORPORATE GOVERNANCE

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JSC Pharmstandard is subject to applicable corporate governance regulations. In 2008, the Company continued its efforts to advance adoption of international corporate governance standards. Throughout 2008, the Company fully complied with international ethical standards and requirements set forward by the London Stock Exchange.

The major developments during the year were establishment of a new governing body –Management Board, and changes in the composition of the Board of Directors.

Corporate Code

The Corporate Code sets out internal control procedures for Pharmstandard financial and business operations. In particular, it specifies:

- procedures for the internal controls over our financial and business operations,
- procedures for the internal audit of compliance with internal controls.

In addition, the Corporate Code regulates the use of insider information by Pharmstandard's management and employees. Thus, the Corporate Code provides that members of the Company's Board of Directors, Chief Executive Officer and internal auditors shall use insider information (within the meaning specified by the Corporate Code) only for the benefit of the Company, pursuant to applicable law and in accordance with the Corporate Code. The Corporate Code also provides for certain procedures implemented to ensure that all relevant individuals observe regulations set forward by this document.

The Corporate Code also establishes a requirement for the members of the Company's Board of Directors and the General Director to disclose any trading in the Company shares.

The updated version of the Corporate Code was approved by the Company's Board of Directors on 1 October 2008 to reflect the changes connected with the establishment of the new governing body – the Company's Management Board.

Arbidol®

Our product portfolio includes market-leading brands

The Company's governing bodies are:

- Annual General Meeting
- Board of Directors
- Board of Directors Committees
- Management Board

Annual General Meeting

The Annual General Meeting attended by all shareholders is the Company's highest decision-making body. The Company will announce the date and location of 2008 Annual General Meeting in a special press release.

CORPORATE GOVERNANCE

Board of Directors

The Board of Directors principal goal has always been to represent the interests of Pharmstandard's shareholders and other stakeholders. The Board of Directors consists of 11 members; 3 of them are independent.

The Board of Directors comprises:

Viktor KHARITONIN	Chairman of Board of Directors	Mr. Kharitonin has served as Chairman of our Board of Directors since May 2006. Mr. Kharitonin graduated from Novosibirsk State University.
Igor KRYLOV	Board Member, Chief Executive Officer	Mr. Krylov serves as our Chief Executive Officer since 2003 and member of Board of Directors since May 2006. He has more than 15 years experience working in the pharmaceutical industry. Previously, Mr. Krylov held positions with Eli Lilly and Sanofi-Aventis. He graduated with honours from Kirov Military Medical Academy.
Elena ARKHANGELSKAYA	Board Member, Chief Financial Officer	Ms. Arkhangelskaya has served as our Chief Financial Officer since 2003 and member of board of Directors since June 2008. She has 12 years experience working in the pharmaceutical industry. Previously, she held senior positions at Eli Lilly. Ms. Arkhangelskaya graduated from the State Financial Academy and obtained a master of business administration (MBA) degree.
Yegor KULKOV	Board Member	Mr. Kulkov has served as a member of our Board of Directors since May 2006. Mr. Kulkov has held a number of senior financial positions in various companies, and currently serves as Head of the Operational Department at Commercial Bank Aresbank and as General Director of both Gloverton LLC and Mellot Intertrade Corporation companies. He graduated from Novosibirsk State University.
Pavel MILEYKO	Board Member	Mr. Mileyko has served as a member of our Board of Directors and Management Board since May 2006. Mr. Mileyko graduated from Novosibirsk State University.
Sergey DUSHELIKHINSKY	Board Member, Chief Commercial Officer	Mr. Dushelikhinsky has served as our Chief Commercial Officer since 2003 and member of Board of Directors since June 2008. He has 12 years experience in sales. Previously, Mr. Dushelikhinsky worked for CJSC Veropharm and FTK Vremya. Mr. Dushelikhinsky graduated from Moscow Technical University.

Viktor FEDLYUK	Board Member, Head of Legal Department	Mr. Fedlyuk has served as our Head of Legal Department since 2003 and member of Board of Directors since June 2008. He has 10 years of experience in the legal profession, and worked for JSC Sibneft from 1996 to 2003. Mr. Fedlyuk graduated from the National Law Academy of Ukraine.
Olga POKROVSKAYA	Board Member	Ms. Pokrovskaya has served as a member of our Board of Directors since October 2006. She also serves as a member of Evraz Group S.A Board of Directors. Ms. Pokrovskaya has more than 15 years of financial experience. Ms. Pokrovskaya graduated from the State Financial Academy and is a certified public accountant.
Roman GORYUNOV	Independent Board Member	Mr. Goryunov has been a Board Member since June 2008. Previously, he held executive positions at NP RTS Stock Exchange. Currently, Mr. Goryunov is Chairman of RTS JSC Management Board. He graduated from St. Petersburg Technical University Department of Economics and Management with a degree in Economics and Information Systems.
Alexandr PEVZNER	Independent Board Member	Mr. Pevzner has served as a member of our Board of Directors since June 2008. Previously, he held various executive positions in a number of business corporations. Currently, Mr. Pevzner holds the position of Adviser to the General Director of JSC Wholesale Power Market Sixth Generating Company.
Ivan TYRYSHKIN	Independent Board Member	Mr. Tyryshkin has served as an independent member of our Board of Directors since October 2006. He also serves as a member of OJSC RTS Board of Directors. He previously served as President of NP RTS from 2001 to 2003 and as President of CJSC Russkoye Zerno from 2003 to 2004. Since 2006, he has served as both Managing Director and General Director of LLC ATON. Mr. Tyryshkin graduated from the Russian Academy of Economics.

CORPORATE GOVERNANCE

Board of Directors Committees

The Board of Directors has the following committees

- Audit Committee
- Remuneration and Nomination Committee

The committees play an important role in detailed analysis and development of well-grounded, independent professional recommendations to the Board of Directors on specific issues.

Audit Committee

The following table provides information about the members of the Audit Committee. All members of Audit Committee are independent members.

Ivan TYRYSHKIN	Committee Chairman
Roman GORYUNOV	Committee Member
Alexandr PEVZNER	Committee Member

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

- Evaluating and selecting the external auditors to be nominated for election at an Annual General Meeting;
- Reviewing the external auditors' terms of engagement;
- Determining the scope and the review of the results of external and internal audits;
- Review our financial statements and analyze changes in accounting policies, as well as any material adjustments introduced as a result of audit;
- Report internal control and accounting issues to the Board of Directors.

Remuneration and Nomination Committee

The following table provides information about the members of the Remuneration and Nomination Committee.

Ivan TYRYSHKIN	Committee Chairman
Olga POKROVSKAYA	Committee Member
Yegor KULKOV	Committee Member

The Remuneration and Nomination Committee contributes to building a sustainable, highly professional and motivated executive team. It is authorized to:

- Assist the Board of Directors in the development of our remuneration and benefits policies;
- Develop a remuneration system for the members of the Board of Directors and Chief Executive Officer;
- Select and interview potential nominees to the Board of Directors and CEO position; and
- Prepare recommendations for the Board of Directors with respect to these matters.

Management Board

The Board has delegated to the Management Board the coordination of the Company's day-to-day business operations. The Management Board is headed by the Chief Executive Officer and also includes the following members:

Igor KRYLOV	Chief Executive Officer	Mr. Krylov serves as our Chief Executive Officer since 2003.
Pavel MILEIKO	Executive Director	Mr. Mileyko has served as a member of our Board of Directors since May 2006.
Olga MEDNIKOVA	Chief Sales & Marketing Officer	Ms. Mednikova has served as our Chief Sales and Marketing Officer since 2003. She has 13 years experience working in the healthcare industry. Previously, Ms. Mednikova held senior management positions in marketing and promotion at Glaxo Welcome and IVAX. Ms. Mednikova graduated from Samara State Medical University and holds an MD PhD degree.

02 Business report

Overall market volume trend looks optimistic and does not reflect recessionary developments

MISSION

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At Pharmstandard, we are dedicated to the development and production of advanced pharmaceutical products, which meet healthcare requirements and patients' expectations.
The company is committed to the following guiding principles:

- **Innovation** – speedy implementation of cutting-edge scientific developments in medicine and pharmacology in close cooperation with Russian and international scientists

- **Efficiency** – implementation of business process management procedures based on an efficient and balanced combination of technical and scientific innovations with a vast practical experience acquired over the years of extensive involvement in pharmaceutical market

- **Responsibility** – the use of international administrative and technological standards as part of the company's responsible consumer policy. Compliance with ecological standards and commitment to the reduction of industrial effect on the environment in the context of the company's responsibility to future generations

STRATEGY

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We strongly believe that our achievements depend on successful implementation of the Company Strategy. Our goal is to further strengthen our leading position in the Russian pharmaceutical market. The key elements of our strategy are as follows:

- **Promote our market-leading brands to drive sales growth and profitability.** We intend to strengthen our market position in Russia by continuing to leverage our strong brand loyalty and brand awareness through effective sales and marketing of our market-leading brands. We will continue promoting these brands by introducing line extensions of trusted and established products, such as our well-known branded product ranges Pentalgin®, Codelac®, Complivit®, Arbidol® and Fluco-stat®. We will also continue to focus on promoting higher value added brands – Afobazol®, Neupomax®, Biosulin®, Rastan®.

We intend to complement our organic growth by acquisitions. In August 2008 we acquired new original product – Afobazol®.

- **Launch new pharmaceutical products in a timely manner to capture market share.** We intend to maintain strong growth and capture market share by leveraging the brand loyalty and brand awareness of our market-leading brands to develop and launch new products in our Core Therapeutic Segments. We also intend to develop and launch new products in potential for our growth new therapeutic segment. Specifically, we intend to:
  - focus on the timely identification and development of new products, including the development of line-extensions of current brands;
  - focus on the timely identification and development of new products that complement our Core Therapeutic Segments and develop new products to penetrate new therapeutic areas;
  - launch these new pharmaceutical products in a timely manner to capture significant market share;
  - leverage our sales and marketing infrastructure to promote new product launches and achieve leading market positions for new branded products

- **Maintain our focus on cost control.** Our focus and ability to control costs is an important element of both our operating and financial performance. We will continue to evaluate and respond to manufacturing and distribution cost inefficiencies. We also plan to further rationalize our manufacturing costs in order to keep gross profit margins by managing our product mix on the basis of the demand for our pharmaceutical products.

- **Expand our sales and marketing capabilities.** Our sales team has more than doubled in the last two years and amounted to 448 sales people by the end of 2008. We also intend to promote further specialization of the Company sales force by therapeutic areas and expect our more specialized sales and marketing team to facilitate our increased calling efforts on medical practitioners, regional and national distributors and other customers. This measure will help to increase customer awareness of our product portfolio and drive further sales growth.

STRATEGY

- **Grow through acquisitions and realize synergies.** We intend to complement our organic growth through the assessment and use of acquisition opportunities, including opportunities for specific brands, trademarks and patents. In August 2008, we acquired Afobazol® trade mark. The sales of this product in 2008 reached 218 mln RUR. The synergy effect will be achieved by switching Afobazol® manufacturing from third-party facilities to Pharmstandard's own efficient modern facility in Kursk.

- **Cooperation with leading pharmaceutical companies.** We intend to complement our organic growth through cooperation with leading pharmaceutical companies based on co-manufacturing or exclusive marketing and promotion of their most successful pharmaceutical products. Together with Solvay Pharmaceuticals (France), we have successfully launched SOLMIR Project for the manufacturing of two immunomodulating products – IRS19® and Imudon®. In 2008 we established cooperation with Grindeks (Latvia) for exclusive marketing, promotion and distribution of Mildronate® on the Russian pharmaceutical market.

- **Exploit opportunities arising from government funding of healthcare.** We believe that we are well positioned to benefit from potential changes in the Federal Reimbursement Programme (FRP), which are expected to increase the participation of local producers. We plan further participation in the Federal Reimbursement Programme (FRP), namely in the Federal Programme for 7 costly diseases with our GNA product Rastan (somatotropin), and in the ONLC Programme with our insulin product Biosulin® and some other Rx products (both programmes are parts of FRP). In addition, we expect growth in sterilizing machines market, where, we believe our products to have a cost-competitive advantage. This growth is expected within the framework of the National Priority Health Project ("NPHP"), which aims, among other things, to provide Russian hospitals with modern equipment.

OPERATING ENVIRONMENT

Total volume of the Russian pharmaceutical market reached 388.5 billion RUR, which is equivalent to 15.7 billion USD, showing the growth of 27% and 31% respectively.

>> Russian Pharmaceutical Market

In 2008, the Russian pharmaceutical market continued the upward trend in per capita consumption of pharmaceutical products in monetary terms. It also sustained the trend for the bias in the consumption structure towards higher market share of more expensive pharmaceutical products over the year.

The overall market volume trend looks optimistic and does not reflect recessionary developments[1].

In 2008, the total volume of the Russian pharmaceutical market reached 388.5 billion RUR, which is equivalent to 15.7 billion USD, showing the growth of 27% and 31% respectively as compared to 2007[1]. The total volume of the Russian pharmaceutical market in terms of volume remained largely the same as in 2007 with an insignificant downward trend (-1%) over the year. The above downward trend in pharmaceutical product consumption (-5%), which was observed only in the 3rd and 4th quarters of 2008, eventually caused the above insignificant decrease in the annual sales measured by volume[1].

Whereas in 2007, we observed a decrease in the total volume of drugs dispensed under FRP, in 2008 this segment demonstrated an upward trend and achieved the 48% and 54% growth in RUR and USD respectively as compared to the same period of 2007. At the same time, the physical volume of this market segment showed an insignificant decrease (-6%) as compared to 2007. It is most likely that this fact reflects the shift in the procurement structure with regard to the drugs purchased under the programme and increase in the imported drugs share [1].

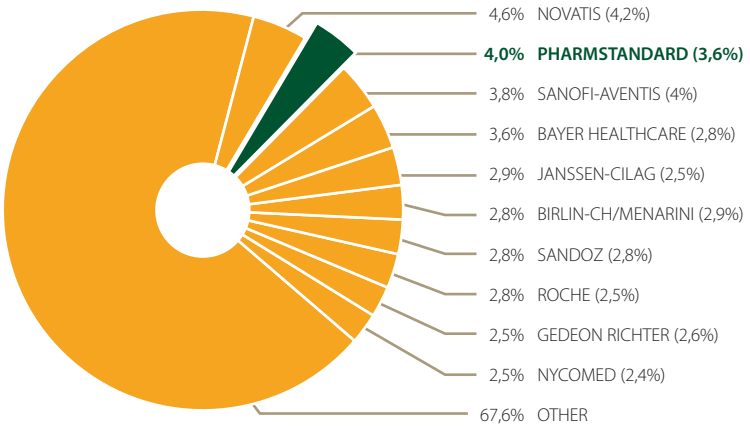
In 2008, the weighted average price of pharmaceutical products in RUR demonstrated a 29% growth throughout the market. This exceeds the annual weighted average price growth in 2007 by 16%. The weighted average price growth in 2008 was largely caused by the price rise in the retail segment observed in the 3rd and 4th quarters of 2008 and by the growth of average prices of the drugs purchased under the FRP programme[1].

1 *Pharmexpert Market Research Centre (MRC), preliminary figures*

OPERATING ENVIRONMENT

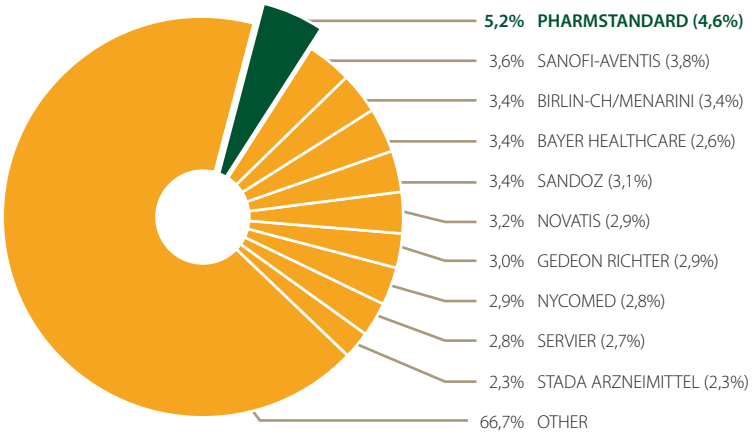
In 2008, there were changes in the distribution of the major players' market shares[1]. Pharmstandard moved up from the third to the second position in the national pharmaceutical market and increased its market share from 3.6% in 2007 to 4.0% in 2008 (excluding retail Mildronate® sales).

Chart #3. Shares of the Leading Companies in the Russian Pharmaceutical Market



Pharmstandard has been the leader of the Russian pharmaceutical market retail segment for two years running. Over this period, its share in the retail segment grew from 4.6% in 2007 to 5.2% in 2008 (excluding retail Mildronate® sales).

Chart #4. Shares of the Leading Companies in the Russian Pharmaceutical Market Retail Segment



For the pharmaceutical sector, 2008 was marked by a number of important events. The Ministry of Industry and Trade of the Russian Federation completed and presented the draft of the Russian Federa-

1 *Pharmexpert Market Research Centre (MRC), preliminary figures*

tion Pharmaceutical Sector Development Strategy for the Period to 2020. This document outlines the guidelines for the adoption of the GMP standards and implementation of the import substitution programme. According to the programme, by 2020, the share of local products in the Russian market shall reach 50%. In December 2008, The Ministry of Industry and Trade of the Russian Federation issued Order No 427 "On the Conditions for the Admission of Foreign Goods with a View to Placing Orders for the Supply of Goods for State and Municipal Needs". Pursuant to this order, foreign manufacturers can supply goods under a government contract only on the condition that they offer a price quotation, which is at least 15% lower than that of a competing local producer. Preferences to Russian manufacturers granted by the order will remain in force until 31 December 2010.

In 2008, the authorized Government Commission included Pharmstandard and 295 other Russian manufacturers (from different segments) into the list of strategic companies.

OPERATING ENVIRONMENT

The Impact of the Global Financial Crisis on the Development of the Russian Pharmaceutical Market

The global financial crisis of 2008 had the most serious impact on the sectors and companies with the most financial leverage. Obviously, macroeconomic changes will influence further market development, particularly the development of the pharmaceutical market, whose progress will largely depend on the management of the current market situation and on the measures taken to reduce the above influence in future. The fact that demand for pharmaceuticals is based on the necessity to treat a large number of patients for numerous diseases on an ongoing basis makes pharmaceutical market less vulnerable to the recession. Experts expect decrease in the consumption of occasional medicines and non-medicinal products. However, it is difficult to predict the developments of the Russian pharmaceutical market in 2009. Market experts expect that the key factors determining the accuracy of the forecast may include the price rise, shifts in the pharmaceutical product mix and variety reduction, shifts in the distribution network structure and erosion of the consumer purchasing power. According to the RF Ministry of Public Health and Social Development, in 2009, there will be no reduction of free medication expenses. Increase in the share of local pharmaceutical products purchased under the Federal Reimbursement Programme (FRP) will remain a priority within the framework of the national budget optimization scheme. Local pharmaceutical products are more affordable than similar imported drugs. As the current financial crisis has affected all pharmaceuticals manufacturers without exception, we can expect that the above trend will continue in 2009. Given the above, market experts predict that in the context of the ongoing recession, in 2009, the total market value will remain at the same level as in 2008 or show an insignificant increase, while in terms of packages it will continue to decline.

Biosulin®, Phosphogliv®, Rastan®

Our product portfolio includes rDNA (gene-engineering) pharmaceutical products

Pharmaceutical Market Structure

The Russian pharmaceutical market consists of three segments: commercial segment (consumer spending), FRP segment (ONLS + 7 costly diseases), and hospital segment. The market structure is shown in Table N. According to the 2008 preliminary results, the retail segment remains the most significant element of the Russian pharmaceutical market structure and accounts for 74% of the total market monetary value, i.e. 1% less than in 2007. The aggregate volume of the retail segment in 2008 amounted to 289 billion RUR. Insignificant decrease in the retail segment market share observed in 2008 was caused by a considerable increase in the FRP segment market share monetary value (+48%). In 2008, the FRP segment share increased by 2% and amounted to 18%, or to 70.7 billion RUR in sale prices. The same reason accounts for the decrease in the share of the hospital segment from 9% to 7%. The monetary value of the hospital segment in 2008 was equal to 28.9 billion RUR[1].

1 *Pharmexpert Market Research Centre (MRC), preliminary figures*

OPERATING ENVIRONMENT

In 2008, the FRP segment had the highest growth rate as compared to 2007[1]. However, if we analyze the FRP segment trends over the period of 2006-2007, we can see that in 2007 this segment slumped by 24% as compared to 2006. The slump was largely caused by the sales of pharmaceuticals in considerable excess of the quantities planned under the programme followed by the reduction in the product mix offered within its framework. In this way, the growth observed within this segment in 2008, in fact, ensured its recovery to the volume of 2006 and a small excess of 12% as compared to the level of 2006. The retail segment grew by 26% as compared to the level of 2007, whereas the hospital segment growth rate dropped from 10% in 2007 to 4% in 2008.

Table #1. Russian Pharmaceutical Market Segment Trends over the Period of 2006–2008

Seqment	2006	2007, RUR billion	qrowth, %	2008, RUR billion	qrowth, %
Commercial	181,4	230	27%	289	26%
FRP	63,3	47,9	-24%	70,7	48%
Hospital	25,4	27,9	10%	28,9	4%
Total	**270,1**	**305,8**	**13%**	**388,6**	**27%**

In 2008, proportions between the volumes of local and imported pharmaceuticals, as well as between prescription and over-the-counter drugs in the Russian pharmaceutical market remained the same as in 2007.

Retail Segment (Consumer spending)

In 2008, the retail segment showed a 26% growth as compared to 27% in 2007 in monetary value (See Table N). Absolute growth in 2008 was equal to 59 billion RUR as compared to the growth of 49 billion RUR in 2007.

In 2008, the retail segment maintained the positive trend, showed a stable growth rate and retained the largest market share (74%)[1]. In addition it is important to mention that unlike FRP and hospital segment, the retail segment retained its volume in terms of packages as compared to the level of 2007, while the other two segments

1 *Pharmexpert Market Research Centre (MRC), preliminary figures*

continued the downward trend in physical market volume, which became apparent in 2006.

The proportion of imported and local products within the retail segment was very much the same as in 2007, reflecting the strong trend in imported product dominance in terms of monetary value and local product dominance in terms of packages, which has been observed over the last 5 years.

Chart #5. Proportion of Imported and Local Products in the Russian Pharmaceutical Market Retail Segment (RUR, %)

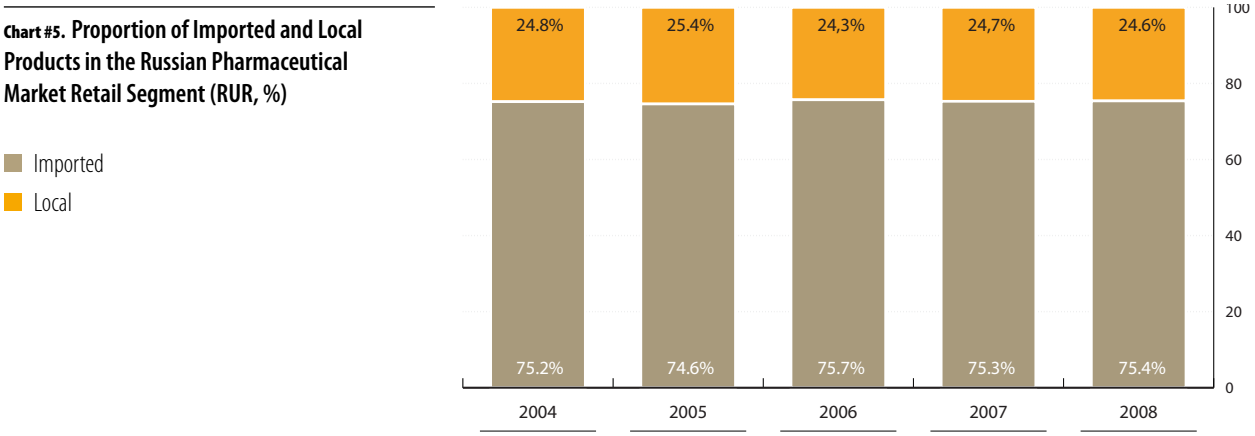
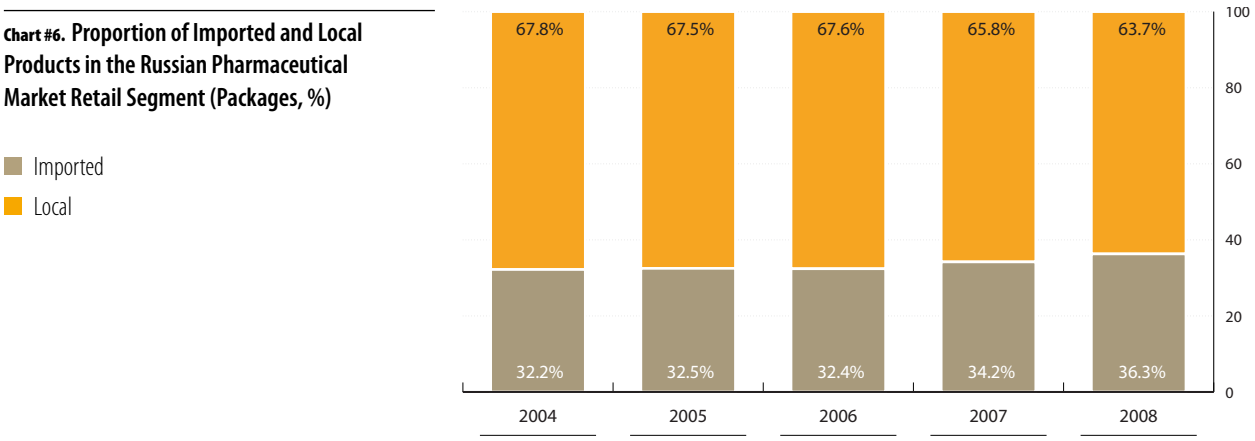


Chart #6. Proportion of Imported and Local Products in the Russian Pharmaceutical Market Retail Segment (Packages, %)



Like in the previous periods, OTC products had a larger share in terms of packages, while prescription drugs led in terms of absolute monetary value. The proportion between prescription and OTC products in the retail segment depends on further development of the reimbursement system and on the number of patients receiving free medication under various national schemes. However, despite the implementation of the Federal Reimbursement Programme (FRP), the

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share of prescription pharmaceuticals in the retail segment did not undergo any significant changes either in terms of physical volume or absolute monetary value.

On the one hand, this fact demonstrates that the volume of free medication is still insufficient and does not cover all categories of patients who need it. On the other hand, the current consumption of some prescription drugs in the retail segment is also inadequate as many patients do not seek medical advice until the very last. As a result, patients of the active working age do not use enough prescription drugs at the early stages of the disease.

The charts below show the proportion of prescription (Rx) and OTC drugs, as well as of imported and local drugs in the retail segment of the Russian pharmaceutical market.

Chart #7. Proportion of Prescription and OTC Products in the Russian Pharmaceutical Market Retail Segment (RUR, %)

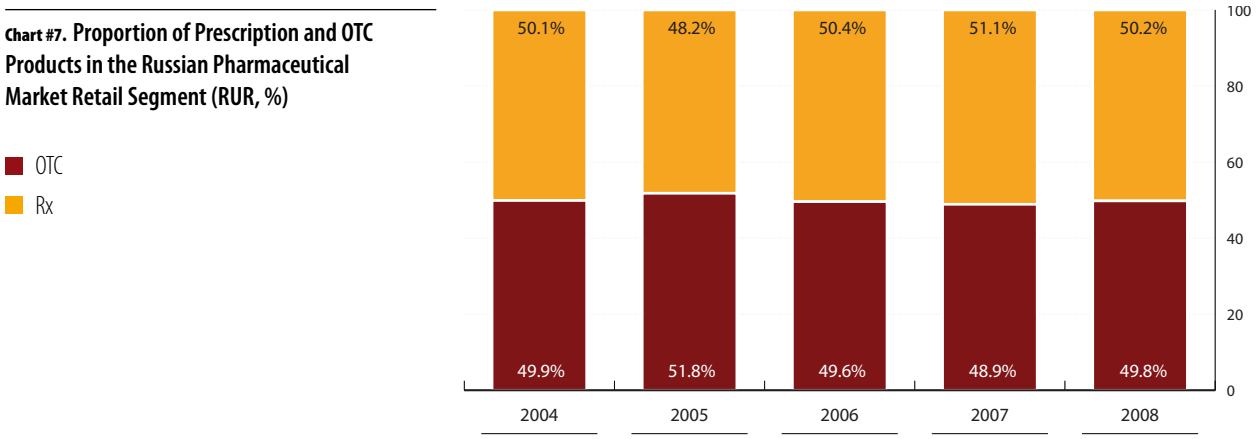
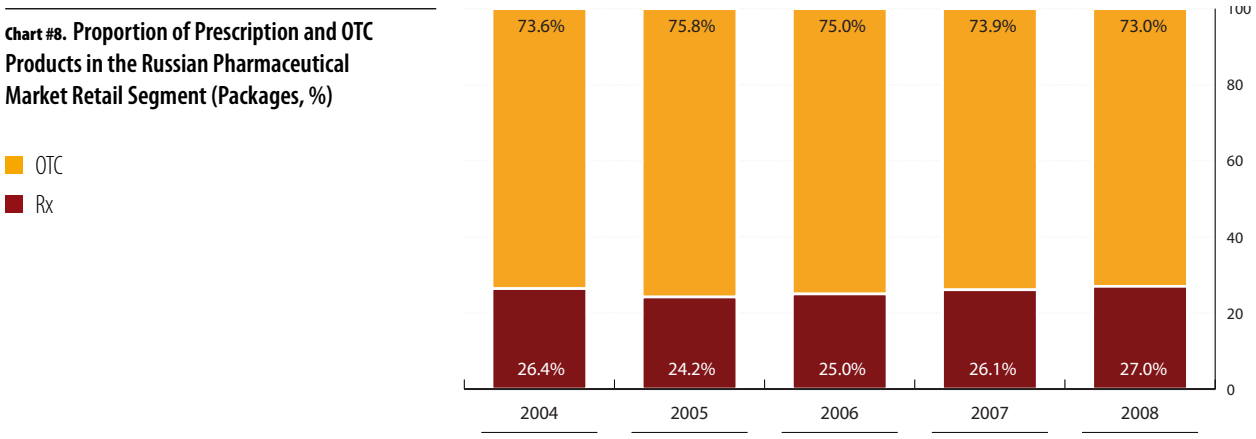


Chart #8. Proportion of Prescription and OTC Products in the Russian Pharmaceutical Market Retail Segment (Packages, %)



Pentalgin®-N®, Pentalgin® Plus®
Our product portfolio includes market-leading brands

Market Trends

We believe that Russian pharmaceutical market has been, and will continue to be, driven by the following trends:

- **Continued improvement in health awareness and modernization of healthcare system.** Development of healthcare insurance and focus on primary care and preventive treatment will increase the quality of healthcare, while continued improvement in health awareness and modernization of diagnostic facilities will ensure greater utilization of preventive and curative pharmaceutical products, and, consequently, greater healthcare expenditures.
- **Broadening availability of generic products and changes in pharmaceutical products consumption patterns.** Both public and private healthcare entities in Russia are looking for ways to reduce or keep down healthcare costs. The broadening availability of generic products, which are typically priced lower than original products, allows increasing demand for affordable pharmaceutical products.
- **Aging Population.** Russia, along with the rest of Europe, has an aging population. The percentage of Russians aged 60 or over will grow from 18.4% in 2000 to 31.7% in 2050 (according to the World Population Prospects: The 2008 Revision issued by the UN Department of Economic and Social Affairs Population Division). We expect that health problems associated with popula-

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tion aging will help drive demand for curative pharmaceutical products and medical technologies, and thus lead to greater healthcare expenditures.

- **Increasing market share of local producers.** We believe that the Russian Government will continue to focus on increasing the share of local products dispensed under the FRP programme through the replacement of some costly imported drugs by local analogues.
- **New trends in pharmacotherapy.** New trends in pharmacotherapy include the discovery of additional therapeutic effects of existing generic pharmaceutical products and increased access to new generations of pharmaceutical substances.

Federal Reimbursement Programme

The Federal Reimbursement Programme (FRP) for Russian citizens was launched in 2005 and became one of the key market drivers. The programme stipulates free medication for certain social groups, such as disabled people and veterans. Initially it also included expenses covering medication of costly chronic conditions and diseases, including AIDS, viral hepatitis, tuberculosis and diabetes. In 2005, the total expenditure under the Federal Reimbursement Programme amounted to 39.6 billion RUR or 78% of the planned budget of 50.8 billion RUR. In 2006, the monetary value of drugs provided within the framework of the Programme increased to 67.9 billion RUR against the planned 34 billion RUR budget. This situation resulted in indebtedness to pharmaceutical suppliers and manufacturers. Consequently, implementation of the Programme was hampered and it became necessary to revise the basic principles for the selection of drugs to be included in the FRP list and monitoring of the state funds allocated for the Programme implementation. The list of essential drugs was revised and cut down. The debts incurred in 2006 were fully repaid only by the end of 2007.

The total expenditure under the Programme in 2007 amounted to 51.2 billion RUR. Further steps to optimize Federal Reimbursement Programme were taken at the end of 2007. The Programme was divided into 2 parts. The first part is a reimbursement programme, which provides medication to patients suffering from 7 costly diseases

(malignant neoplasms of lymphoid, blood-forming and related tissues, haemophilia, cystic fibrosis, pituitary dwarfism or growth hormone deficit, Gaucher disease, multiple sclerosis and postoperative treatment after organ/tissue transplantation). This programme is carried out at the federal level.

The second part is a reimbursement programme, which provides essential medication for population groups entitled to benefits (ONLS Programme). The list of population groups entitled to benefits under the FRP Programme was expanded to include children, pregnant women and pensioners, as well as the disabled and veterans. This programme is carried out at the regional level.

The total expenditure under the Programme in 2008 amounted to 60 billion RUR. 27 billion RUR were spent under ONLS Programme and the remaining budget covered medication of patients suffering from the 7 costly diseases. The approved FRP 2009 budget amounts to 76.9 billion RUR. 28.3 billion RUR will be spent under ONLS Programme; 12.2 billion RUR will form an additional ONLS Programme reserve and 36.4 billion RUR will cover the expenses under the 7 Diseases Programme.

The share of locally produced drugs distributed under the FRP programme was the largest in 2005 (15% in terms of monetary value). In subsequent periods it did not exceed 10%. In 2008, according to preliminary figures presented by Pharmexpert MRC, it was 5.4%. The above figures show that the share of locally produced drugs distributed under the FRP programme remains low. However, the Russian Government is planning measures to increase it. According to the RF Minister for Public Health and Social Development Tatiana Golikova, in the second half of 2009, "public procurement of drugs will be carried out with the focus on the maximum involvement of local manufacturers".

>> Pharmaceutical products

The Company offers over 200 pharmaceutical products in several therapeutic categories supplied in various dosage forms, including three original formulations: Arbidol®, Phosphogliv® and Afobazol®. Pharmstandard's portfolio is formed with a focus on six strategic therapeutic segments with the highest market capacity. They include antivirals, cough and cold preparations, analgesics, vitamins and antifungal agents, which, in 2008, collectively accounted for 61% of the Company's sales in the Russian pharmaceutical market. In 2008, the group of traditional market leaders was extended by the cardiac drugs segment due to the Company's right to exclusive distribution, marketing and promotion of Mildronate® (produced by Grindeks) in the Russian Federation.

Table #2. Company Sales Structure Broken Down into ATC Categories

ATC4 code	ATC2	ATC4	Sales, mln RUR		Sales 08/07, mln RUR	Sales 08/07, %
			2008	2007		
J05B0	J05-ANTIVIRALS FOR SYSTEMIC USE	J05B0-ANTIVIRALS, EXCLUDING ANTI-HIV PRODUCTS	2,730.5	2,317.2	413.3	18%
R05D2	R05-COUGH AND COLD PREPARATIONS	R05D2-ANTITUSSIVES IN COMBINATIONS	2,275.3	1,789.3	485.9	27%
N02B0	N02-ANALGESICS	N02B0-NON-NARCOTICS AND ANTI-PYRETICS	1,958.4	1,591.0	367.4	23%
C01D0*	C01-CARDIAC THERAPY*	C01D0-CORONARY THERAPY EXCLUDING CALCIUM ANTAGONISTS AND NITRITES*	1,149.4	–	–	–
A11A4	A11-VITAMINS	A11A4-OTHER MULTIVITAMINS WITH MINERALS	697.5	587.3	110.2	19%
J02A0	J02-SYSTEMIC AGENTS FOR FUNGAL INFECTIONS	J02A0-SYSTEMIC AGENTS FOR FUNGAL INFECTIONS	579.7	517.1	62.5	12%
A05B0	A05-CHOLAGOGUES AND HEPATIC PROTECTORS	A05B0-HEPATIC PROTECTORS, LIPOTROPICS	428.3	356.5	71.8	20%
J05B9	J05-ANTIVIRALS FOR SYSTEMIC USE	J05B9-ANTIVIRALS, OTHERS	337.3	246.6	90.7	37%
R02A0	R02-THROAT PREPARATIONS	R02A0-THROAT PREPARATIONS	261.7	138.4	123.3	89%
N05B4	N05-PSYCHOLEPTICS	N05B4-BARBITURATES, COMBINATIONS	236.3	154.7	81.6	53%

* *Mildronate®*

The Company's product portfolio includes five brands, which are market leader in their respective sectors. They are Arbidol® (antiviral), Terpincod® (cough and cold), Pentalgin® (analgesic), Complivit® (vitamin + mineral) and Flucostat (antifungal agent). These products have retained leadership in their respective market sectors for the past few years. They demonstrate strong growth; make the main contribution in the revenue increase and play the role of the strategic focus in the realization of the Company's growth strategy. The seventh position in the ATC sales rating is taken by the hepatoprotector segment, which includes the original prescription drug Phosphogliv® (hepatoprotector).

Arbidol® has been the leader of the Russian pharmaceutical market retail segment sales for the past three years in terms of monetary value (according to preliminary figures presented by Pharmexpert MRS)

According to the results of FY 2008, three Pharmstandard's formulations – Arbidol®, Pentalgin® and Terpincod® – were included in the list of the retail segment top-20 brands.

In 2008, eight Pharmstandard products were included in the list of the top-20 leading brands of the Russian manufacturers segment against six products in 2007. They were Arbidol® (antiviral), Terpincod® (cough and cold), Pentalgin® (analgesic), Complivit® (vitamin + mineral), Flucostat (antifungal agent) and Codelac® (cough and cold). The two additional products included in the top-20 list in 2008 were Amixin® (immunostimulator) and Phosphogliv® (hepatoprotector).

In addition to the six core segments, the Company is expanding into other potentially promising therapeutic segments, such as drugs used in the treatment of endocrine disorders (Biosulin® and Rastan), hepatoprotectors (Phosphogliv®), drugs used in the treatment of infectious diseases, cardiovascular diseases and diseases, which affect the immune and the nervous systems.

The Company pays serious attention to the new products portfolio formation and development realizing an efficient strategy for the expansion into the five key segments. This strategy is based on the launch of new sub-brands derived from the leading brands and on the launch of its products into new potentially promising therapeutic segments. Thus, in 2008, the company successfully launched 14 new products.

Successful implementation of the initially developed strategy enables the Company to conclude new transactions for the purchase of brands and carry out joint projects for the promotion of pharma-

PRODUCTS

ceuticals in the Russian market in partnership with other companies. In 2008, the Pharmstandard acquired the original Afobazol® formulation. Afobazol® is an anxiolytic used in the treatment of anxiety disorders and has a significant growth potential. In 2008, Pharmstandard successfully launched the project for exclusive distribution, marketing and promotion of Mildronate® (produced by Grindeks JSC) in the Russian Federation. Mildronate® is a cardiac drug. It is a metabolic corrector used in the complex treatment of acute and chronic ischemic blood circulation disorders. Mildronate® project was included into Pharmstandard's marketing activities in line with the Company's portfolio strategy of product promotion. In combination with other cardiac drugs under active targeted promotion the project enabled the Company to employ the existing medical representatives and marketing funds and improve their efficiency.

In 2008, Pharmstandard's year-end sales results showed the revenue growth of 36%. It was more than the general market trend (+27%), and exceeded the 34% revenue growth achieved by the Company in 2007. The OTC drug sales grew by 24% and the sales of prescription drugs – by 122% in terms of monetary value.

Table #3. Sales structure – FY 2008, RUR mln.

Year	2008	2007	Difference	Difference, %
Pharmaceutical products	13,260	9,763	3,498	36%
OTC products	10,553	8,520	2,034	24%
Afobazol®	218	0	218	–
IRS-19	17	0	17	–
Prescription products	2,638	1,188	1,449	122%
Mildronate®	1,149	0	1,149	–
Other sales	69	55	15	27%
Medical equipment and disposables	1,076	1,609	-533	-33%
TOTAL SALES	**14,336**	**11,371**	**2,965**	**26%**

The organic growth of the total revenue received from the sales of pharmaceutical products amounted to 24%, including the 24% organic growth from the sales of OTC products and the 25% organic growth received from the sales of prescription products.

2008 year-end sales results of the market leaders included in the top-10 brands list, which accounted for 76% of the total Com-

pany's sales, were higher than in 2007. Arbidol® was the absolute sales leader in 2008. Its share in the total company sales amounted to 20% and grew by 18% as compared to the level of 2007.

Table #4. 10 Best Selling Brands in 2008

№	BRAND	2008			2007			Volume 08/07		Sales 08/07	
		Volume (mln packs)	Sales (mln RUR)	% of total sales	Volume (mln packs)	Sales (mln RUR)	% of total sales	Change	%	Change	%
1	Arbidol®	26.35	2,731	21%	25.06	2,316	24%	1.29	5%	415	18%
2	Terpincod®	15.72	1,606	12%	18.92	1,322	14%	-3.21	-17%	284	21%
3	Pentalgin®	31.96	1,582	12%	28.76	1,314	14%	3.21	11%	268	20%
4	Mildronate®	5.56	1,149	9%	0	0	0%	5.56	–	1,149	–
5	Complivit®	10.32	673	5%	11.38	623	6%	-1.06	-9%	50	8%
6	Codelac®	10.33	670	5%	9.15	468	5%	1.18	13%	202	43%
7	Flukostat®	4.97	561	4%	4.57	502	5%	0.4	9%	58	12%
8	Phosphogliv®	1.32	424	3%	1.11	356	4%	0.21	19%	68	19%
9	Amixin®	0.79	337	3%	0.58	247	3%	0.21	37%	91	37%
10	Corvalol	53.82	236	2%	41.40	155	2%	12.42	30%	82	53%
	Other brands	487.10	3,223	24%	480.74	2,407	25%	6.37	1%	816	34%
	TOTAL SALES	**648.24**	**13,191**	**100%**	**621.67**	**9,708**	**100%**	**26.58**	**4%**	**3,483**	**36%**

PRODUCTS

Main Groups of Pharmaceutical Products

In compliance with the product registration status and existing retail drug-dispensing practices, our product portfolio is divided into over-the-counter drugs (OTC) and prescription drugs (Rx). Besides it includes products sold under trade names and international non-proprietary names (INN).

In 2008, OTC products accounted for 80% of the total sales volume. In 2007, the share of OTC products was equal to 87% of the total sales volume. The share of prescription pharmaceutical products in the total sales volume increased from 12% in 2007 to 20% in 2008. Among the products, which contributed to the prescription group share gain are Mildronate® (cardiac drug), Phosphogliv® (hepatoprotector), Biosulin® (Insulin), Azitrox® (Azitromicine) and Liptonorm® (Atorvastatin).

Over-the-Counter Products (OTC)

Since the OTC portfolio includes all the five leading brands, it dominates in the total Company's sales. In 2008, OTC products showed a 24% growth, whereas their organic growth (excluding Afobazol®) amounted to 22%. Further promotion of the leading brands is the key element of the Company's strategy, which ensures expansion and increase in returns. OTC products were and will remain in the focus of priority marketing and promotion, as they belong to the most potentially promising retail segment categories, enjoy high demand and are characterized by high levels of awareness and consumption.

Arbidol®, whose sales in 2008 showed an 18% growth, is the indisputable leader of sales within the OTC group. Afobazol®, another OTC product, made a considerable contribution into the OTC group sales growth and accounted for 2% of the total OTC group revenue in 2008. It was included in the list of 2008 ten top products.

Table #5.

№	BRAND	2008			2007			Volume 08/07		Sales 08/07	
		Volume (mln packs)	Sales (mln RUR)	% of total sales	Volume (mln packs)	Sales (mln RUR)	% of total sales	Change	%	Change	%
1	Arbidol®	26.35	2,731	26%	25.06	2,316	27%	1.29	5%	415	18%
2	Terpincod®	15.72	1,606	15%	18.92	1,322	16%	-3.21	-17%	284	21%
3	Pentalgin®	31.96	1,582	15%	28.76	1,314	15%	3.21	11%	268	20%
4	Complivit®	10.32	673	6%	11.38	623	7%	-1.06	-9%	50	8%
5	Codelac®	10.33	670	6%	9.15	468	5%	1.18	13%	202	43%
6	Flukostat® (tablets)	4.93	555	5%	4.52	495	6%	0.41	9%	59	12%
7	Amixin® (125mg)	0.73	317	3%	0.51	226	3%	0.22	42%	91	40%
8	Corvalol	53.82	236	2%	41.40	155	2%	12.42	30%	82	53%
9	Afobazol®	1.50	218	2%	0	0	0%	1.50	–	218	–
10	Activated charcoal	65.53	162	2%	51.12	60	1%	14.42	28%	102	170%
	Other brands	389.95	1,805	17%	382.16	1,542	18%	7.78	2%	263	17%
	TOTAL SALES	**611.14**	**10,553**	**100%**	**572.98**	**8,520**	**100%**	**38.16**	**7%**	**2,034**	**24%**

PRODUCTS

Prescription Products (Rx)

In 2008, Pharmstandard's prescription products portfolio showed a 122% growth with the organic growth of 25%. This growth was largely possible due to the launch of Mildronate®, which was the leader of the top 10 prescription brands. A number of Pharmstandard's branded prescription products are distributed under the FRP Programme. However, depending on their category, the promotion of the branded drugs can be successfully carried out in the retail segment. Thus, Phosphogliv® sales in the retail segment by far exceed its share in the FRP segment sales. At the same time, Biosulin® is mainly distributed under the FRP Programme. In 2008, the sales of these two products grew by 19% and 36% accordingly. Increase in the share of prescription products in the total level of pharmaceutical sales is currently one of the Company's priorities. However for the majority of prescription drugs the growth potential can be realized only under the condition of the FRP Programme optimization with regard to locally produced pharmaceuticals.

Table #6.

№	BRAND	2008			2007			Volume 08/07		Sales 08/07	
		Volume (mln packs)	Sales (mln RUR)	% of total sales	Volume (mln packs)	Sales (mln RUR)	% of total sales	Change	%	Change	%
1	Mildronate®	5.56	1,149	44%	0	0	0%	5.56	–	1,149	–
2	Phosphogliv®	1.32	424	16%	1.11	356	30%	0.21	19%	68	19%
3	Biosulin®	0.37	164	6%	0.24	120	10%	0.13	53%	44	36%
4	Reduxin®	0.13	113	4%	0	0	0%	0.13	–	113	–
5	Cyclodol®	2.39	83	3%	0.96	29	2%	1.43	149%	53	184%
6	Pikamilon®	3.19	61	2%	2.54	45	4%	0.65	26%	16	35%
7	Renipril®	1.75	60	2%	1.95	68	6%	-0.21	-10%	-8	-11%
8	Azitrox®	0.38	57	2%	0.26	37	3%	0.12	47%	20	52%
9	Sulfokamfokain®	1.63	42	2%	1.84	34	3%	-0.22	-12%	8	23%
10	Liptonorm®	0.15	41	2%	0.08	21	2%	0.07	87%	19	91%
	Other brands	20.23	444	17%	39.69	477	40%	-19.46	-49%	-33	-7%
	TOTAL SALES	**37.10**	**2,638**	**100%**	**48.67**	**1,188**	**100%**	**-11.59**	**-24%**	**1,449**	**122%**

Medical Equipment

We develop, manufacture, market and sell medical equipment such as sterilizing and distilling machines, and disposables, such as syringes, at our Tyumen manufacturing facility. Medical equipment and disposables accounted for 7% of our sales in 2008.

The following table shows the results of the core medical equipment and disposables sales over the specified periods.

Table #7.

	2008, mln Rur	2007, mln Rur	Difference, %
Medical Equipment	746	1,211	-38%
Syringes & Disposables	267	319	-16%
Spare Parts	30	29	4%
Other	33	50	-32%
Total	**1,076**	**1,609**	**-33%**

Although our medical equipment business significantly depends on government tenders, whose absence largely accounted for a 33% decline in sales in 2008, Pharmstandard's retail sales to hospitals over the same period stayed on the level of 2007

The following table shows the results of the medical equipment sales broken down by the sales channels.

Table #8.

	2008, mln Rur	2007, mln Rur	Difference, %
Retail Segment	859	858	0%
Export	109	178	-39%
Tenders	87	530	-84%
Others	21	42	-47%
Total	**1,076**	**1,609**	**-33%**

PRODUCTS

Product Development & Research

Pharmstandard creates new products and introduces line extensions of its well-known brands. Every year, the company launches at least 10 new formulations. Pharmstandard portfolio expansion is based on the production of high quality generics at affordable prices and development of innovative formulations in close cooperation with the leading Russian research centres. In 2004-2008, the company launched more than 35 new preparations.

The Company carries out comprehensive research activities aimed at the development of innovative products. All new formulations undergo rigorous preclinical and clinical studies in compliance with the requirements of applicable international and national regulations.

Pharmstandard provides all kinds of support for medical research centres and supplies practicing doctors with reliable scientific information and teaching materials required for the improvement of the healthcare quality.

In 2008 we have introduced 14 new pharmaceutical products (9 OTC products and 5 prescription products) including rDNA product Neupomax® (colony-stimulating factors) for the treatment of neutropenia in oncology patients.

The following table provides certain information about our registration applications broken down by therapeutic segments for both prescription and OTC products as of 31 December 2008.

Table #9.

Product		Date	Description (Therapeutic Segment)	Sales Value, RUR mln	ATC value, 2008, RUR mln
OTC	Influnorm®	Jul08	R05A – cold preparation without anti-infectives	24	5,136
	Pentalgin® Plus	Mar08	N02B – non-narcotics analgesics and antipyretic	65	7,001
	Complivit® Ophtalmo	Jul08	A11A – multivitamins with minerals	20	4,740
	Complivit® Se	Aug08	A11A – multivitamins with minerals	4	4,740
	Complivit® Fe	Aug08	A11A – multivitamins with minerals	4	4,740
	Complivit® Mg	Sep08	A11A – multivitamins with minerals	3	4,740
	Neurocomplit®	Feb08	A11D – B1 vitamin and combinations	7	1,430
	Lactazar®	Sep08	A15A – appetite stimulants	<1	23
	Neosmectine®	Jan08	A07B – intestinal absorbent antidiarrhoeals	29	1,520
Rx	Combilipen®	Feb08	A11D3 – (injections) – B1 vitamin and combinations	39	977
	Octolipen®	May08	A05B0 – hapatic protectors	3	6,200
	Neupomax®	Jun08	L03A1 – colony-stimulating factors	6	335
	Formetin®	Sep08	A10B2 – biguanide antidiabetics	<1	789
	Bloctran®	Mar08	C09C0 – antgiotensine-2 antagonists plain	8	774

In 2008, new products contributed 212 million RUR to the Company's revenue. Products launched in 2007 demonstrated noticeable sales dynamics and contributed 437 million RUR in 2008. The following table provides information about the sales dynamics of the products launched in 2007.

Table #10.

Product launch		ATC	Sales value	
			2008, RUR mln	2007, RUR mln
OTC	Maxicold®	R05A0 – Cold Preparations without Anti-Infectives	57	50
	Passifit®	N05B5-Herbal Hypnotics/ Sedatives	18	24
	Immunex®	L03A0 – Immunostimulating Agents Excluding Interferons	3	10
	Complivit® Ca D3	A12A- calcium products	42	28
	Complivit® 365	A11A- Multivitamins, combinations	85	17
Rx	Biosulin®	A10C2-Human Insulins and Analogues	164	120
	Rastan®	H04C0-Growth Hormones	36	53
	Artrozan®	M01A1-Anti-Rheumatics, Non-Steroidal Plain	21	16
	Benfolipen®	A11D (tablets) – vitamin B1 and combinations	11	2

PRODUCTS

Following our strategic intentions, in 2009, we are going to launch 10 OTC and 2 prescription products, including extensions for our Complivit® and Codelac® umbrella brands and a new topical anti-psoriasis product Zinocap®.

Table #11.

Product		Date	Description	ATC value, RUR mln
OTC	Complivit® Anti-stress	Jun09	A11A – multivitamins with minerals	4,740
	Complivit® Siyanie	Jun09	A11A – multivitamins with minerals	4,740
	Complivit® Diabetes	Jun09	A11A – multivitamins with minerals	4,740
	Complivit® Woman 45+	Nov09	A11A – multivitamins with minerals	4,740
	Complivit® Active (Chewing), 3-10 years	Nov09	A11A – multivitamins with minerals	4,740
	Codelac® Broncho, syrup	Dec09	R05D – antitussives	2,774
	Codelac® Broncho, tablets	Jun09	R05D – antitussives	2,774
	Magnelis B6	Apr09	A12C – other mineral supplement	878
	Zinocap®, aerosol	Sep09	D05A – topical antipsoriasis product	523
	Zinocap®, cream	Sep09	D05A – topical antipsoriasis product	523
Rx	Mildronate®, ampules	Aug09	C01D – coronary therapy excluding calcium antagonists and nitrites	2,896
	Traneksam	Sep09	B02A – antifibrinolytics	81

BUSINESS OVERVIEW

>> Sales & Marketing

Expansion of marketing and promotion capabilities is a strategic key to the Company's success. In 2008, optimization of our Sales & Marketing (S&M) Service was carried out on the basis of the following key principles:

- Implementation of proficiency criteria for the purposes of S&M staff formation (a degree in Medicine or Pharmaceutical Science and pharmaceutical experience);
- Promotion of employee's specialization and targeted expertise in terms of different product groups;
- Headcount optimization and product portfolio synergy career advancement system used to ensure maximum coverage of target audiences and preserve/increase profitability per resource unit (full time equivalent medical representative);
- Development of performance indicators/deliverables appropriate for regular analysis

In 2008, the S&M structure reflected business specialization and included three business units:

- prescription products, products for outpatients and hospitals (Rx);
- non-prescription (OTC) products;
- endocrinology products

As of 31 December 2008, S&M had 448 employees, who provided efficient interaction with medical specialists and retail pharmacists all over Russia. According to our estimates, we have one of the largest S&M Services among local pharmaceutical manufacturers.

All S&M employees have a degree in Pharmaceutical Science or in Medicine, as well as experience of working at other pharmaceutical companies (including multinational organizations).

All S&M employees have regular in-house career-development training. In 2008, each medical representative attended at least 2 training sessions, while a manager attended 4 training sessions on the average.

In 2008, over 60% of S&M employees were awarded bonuses under a bonus scheme successfully implemented by the Company Management to improve the employees' performance and motivation.

In 2008, we continued efficient implementation of the electronic territory management system (ETMS) to provide optimization of performance monitoring. Besides, the Company implies the system of regular reports, which contain information about market and mar-

BUSINESS OVERVIEW

keting indicators (awareness, consumption and loyalty) and monthly profitability of each promoted brand.

The above initiatives enabled us to achieve impressive results with regard to cost management and improved the efficiency of tactical decisions.

Product Facilities

Pharmaceuticals

The following table provides information about the Company's pharmaceutical manufacturing facilities.

Table #12.

Factory	Approximate size, m²	Land own/ lease	Dosage form	Shifts	Capacity 000's 2008	Utilisation, 2008	Date of new capacity launch
LEKSREDSTVA (KURSK)	14'900	lease	Syrops & liquid forms	3	65,887	86%	Apr08
			Tablets	3	693,586	49%	
			Sprays	3	13,100	87%	
			Powders	3	6,730	42%	Jun08
			Capsules	3	37,930	60%	May08
UFAVITA (UFA)	5'850	lease	Ampules	3	12,442	61%	
			Frozen-dried preparation	3	4,166	50%	Jul08
			Syrops & liquid forms	3	9,053	28%	
			Tablets	3	145,288	43%	
			Vitamin bars (ferrohematogen)	3	35,700	51%	Aug08
			Insulin	3	14,400	3%	
PHYTOFARM (N. NOVGOROD)	1'200	lease	Ointments	3	744	23%	Jan08
			Powders	3	–	0%	
			Syrops & liquid forms	3	–	0%	
			Tablets	3	–	0%	
TOMSKHIMPHARM (TOMSK)	29'000	own	Syrops & liquid forms	3	5,400	5%	
			Tablets	3	273,239	28%	Mar09
			Sprays	3	2,880	27%	Oct08

Leksredstva In 2008, the Company increased its liquid forms production capacity through modernization of the Corvalol line process equipment. Launch of new production lines helped to increase capsule and sachet forms production capacity. In 2008, the total production capacity of the factory increased by 14% as compared to the level of 2007. Leksredstva receives international EU GMP certificates for six production lines.

Ufavita In 2008, the Company increased its ampules production capacity through the improvement of the equipment capacity. Optimization of the existing lines drying schedule and launch of a new frozen-dried preparations line (Phosphogliv®, Rastan) increased frozen-dried preparations production capacity.

Phitofarm In 2008, the Company shut down the production of low-margin liquid forms, ointments, powders and syrups and launched the production of highly profitable formulations (Termicon cream) at Phytofarm Tomsk branch. The production of tablet forms will be relocated to the Tomskhimfarm facilities.

BUSINESS OVERVIEW

Two warehouses for pharmaceutical products in Kursk and Ufa are under construction.

Tomskhimfarm In 2008, Tomskhimfarm launched a new line for the production of sprays with the annual capacity of 4.32 mln package units. The line is now used for the production of a new spray formulation based on bacterial lysates (IRS-19). The line for the production of low-margin formulations was stopped and the process equipment was removed to be replaced by new modern lines for the production of highly profitable pharmaceuticals, including Amixin®, Arbidol® and Imudon. The new lines with the annual production capacity of 29.8 mln package units will be launched in April 2009.

After the launch of new lines for the production of tablet forms at Pharmstandard- Tomskhimfarm in April 2009, the aggregate Pharmstandard Group capacity will increase to 1.35 billion package units per year. It is by 14.8 mln package units more than in 2007.

In 2008, the aggregate capacity utilization of the Company pharmaceutical manufacturing facilities was equal to 69%.

Medical Equipment

The following table provides information about the Company's medical equipment capacities.

Table #13.

Production Form	Capacity[1] As at 31 December 2008
Syringes	276 milion
Needles for syringes	0
Sterilising machines (up to 100 liters)	9,600
Sterilising machines (greater than 100 liters)	428
Distiling machines	7,200

In 2008, the Company shut down the production of syringes following the slump in sales caused by fierce competition with Chinese syringe manufacturers in 2007. The production capacity of the single remaining facility was sufficient to meet the sales targets for 2008. In 2008, the sales of syringes amounted to 244 mln units.

1 Based on one, two or three daily shifts (8 hours each) and 5 working days per week.

Pharmstandard product facilities comply with Russian standards. Six lines on Kursk are GMP compliant. JSC «Pharmstandard-Leksredstva» is the first Russian pharmaceutical plant included in EudraGMP database.

The production of syringe needles was shut down for the reason of its low profitability. Currently, we buy needles from the Japanese company NIPRO, which is one of leading global needle manufacturers. We have increased sterilizing and distilling machines production capacities through the installation of modern equipment (Hyundai turning machine and Fronius automatic welder).

In 2008, the aggregate capacity utilization of the Company's medical equipment manufacturing facilities was equal to 62%.

Distribution

The Company sells products under direct contracts with wholesalers. As of the end of 2008, products were sold under 40 contracts. In 2008 5 top distributors accounted for 69% of sales as compared to 2007 with 11% share growth.

Since autumn 2008 flows of goods have shown a tendency towards re-distribution among wholesalers both in the pharmaceutical market and the Company's sales structure. This occurred due to economic recession and ruble devaluation which increased accounts receivable for imported drugs, made credits more expensive, caused lack of access to new credit lines and failure of prolongation due to change in requirements for collaterals.

Pharmstandard strengthened control over lending and collateral of credit limits to distributors and computerized the process of approval of orders for products based on accounts receivable. Decisions on lending and extension of credit limits are made by the Credit Committee which includes the Company's top managers and is headed by the CEO. In 2008 sales growth reached 26%, while accounts receivable increased only by 13% (4,761 mln rubles in 2008 and 4,176 mln rubles in 2007). Periods of payment deferal remained the same: 90–120 days in Russia and 180 days for exports.

In the second half of 2008 the structure of distributors in sales changed which was reflected in 2008 final figures.

BUSINESS OVERVIEW

Table #14.

Distributor	2008 (% of sales)	2007 (% of sales)
Katren	20%	15%
Protek	14%	10%
SIA International	14%	9%
Genesis	13%	19%
ROSTA	8%	6%
	69%	**58%**

Due to management going concern problems, shipments to Genesis Ltd. have been reduced in the second half of 2008. Therefore, the company's share in sales reduced from 19% down to 13% (excluding Genisis Ltd., top 4 distributors represent about 50% of sales). In December 2008 Genesis Ltd. declared a voluntary bankruptcy. As of 31 December 2008, Genesis Ltd. accounts receivable reached 476.1 mln rubles. An allowance for total accounts receivable is accrued for as sales & distribution expense.

The average stock is equal to 60 days product sales neglecting the out of stock situation.

Procurement

Pharmstandard procures a lot of materials and supplies, including raw materials, auxiliary materials and packaging, to carry out pharmaceutical production.

The following table shows our procurement structure.

Table #15.

	Share, %
Raw materials	76%
API	66%
Others	10%
Auxiliary materials	1%
Packaging	23%
Total materials & supplies	**100%**

The majority of the materials are procured from a variety of external sources, primarily through brokers. As of 31 December 2008, we used around 500 materials & supplies, about 50% of which we procured from our top-10 suppliers. We import the majority of raw materials used in pharmaceutical production since certain types of raw materials are either not produced in Russia, fail to meet quality standards or are in short supply. We import raw materials from several European countries, China and India.

The following table shows a breakdown of procurement contracts per currency.

Table #16.

Currency	Share %
EUR	16%
USD	41%
RUR	43%
Total materials & supplies	**100%**

Over 70% of materials and components for our medical equipment and disposables are supplied by 20 primary contractors.

Employees

As of 31 December 2008, we had 5,001 full-time employees, of whom 54 % were trade union members. So far, we have not experienced any business interruption resulting from labour disputes and we believe our relationship with the employees to be good.

The following table shows our headcount as of 31.12.2007 and 31.12.2008.

Table #17.

As of 31 December	2008	2007	Difference, %
Production/Logistics	3,503	3,949	-11%
Research and Development	133	140	-5%
Marketing and Promotion	667	600	11%
Management and Administrative	698	767	-9%
Total	**5,001**	**5,456**	**-8%**

The following table shows the headcount at each of our manufacturing facilities and at the Company's Head Office in Moscow as of 31 December 2008.

Table #18.

	Kursk	Ufa	Tomsk	N.Novgorod	Tyumen	St.Petersburg	HO
Production/Logistics	1,184	980	375	21	942	1	0
Research and Development	40	28	19	0	8	0	38
Marketing and Promotion	0	0	0	0	0	0	667
Management and Administrative	85	165	102	22	130	18	176
Total	**1,309**	**1,173**	**496**	**43**	**1,080**	**19**	**881**

In 2008 we reduced the staff by 8% to 5001 employees. This reduction was achieved through enhancement of productivity at TZMOI and continued Phitofarm restructuring. Increase in the Marketing and Promotion was caused by the expansion of the promotion units staff.

Flucostat®

Our product portfolio includes market-leading brands

Social Policy

Pharmstandard JSC, the undisputed leader of the Russian pharmaceutical industry, guarantees the highest quality of all its products.

The underlying principles of Pharmstandard's social policy have been brought into line with Russia's national policy in the sphere of medical supplies, which stipulates for the replacement of expensive imported medicines with affordable local products manufactured in compliance with the highest international standards. Pharmstandard is known for its commitment to product safety and consumer health. To meet these challenges, Pharmstandard has organized a rigorous internal system of pharmacovigilance focused on the collection and analysis of information about side effects and interaction of different pharmaceutical products. Another task solved by the system is to ensure efficient interaction with respective regulatory authorities.

Pharmstandard is a socially responsible company, which provides target support to the most vulnerable social groups and social welfare institutions on a regular basis. The Company puts high value on the doctors and patients' confidence in its products and keeps investing in the development of new formulations and improvement of production processes.

Regulatory Issues

State Registration of Pharmaceutical Products

Prior to being manufactured, sold or imported to Russia, pharmaceutical products, including substances, are subject to registration by the Federal Service on Surveillance in Healthcare and Social Development (ROSZDRAVNADZOR). Manufactures are required to register all pharmaceutical products, including new forms of earlier registered pharmaceutical products, products with new dosage or products with a different composition of auxiliary substances, as well as generic versions of original pharmaceutical products.

Registration requirements for pharmaceutical products are complex and include pre-clinical and clinical studies.

Pre-clinical studies, which are mandatory for all pharmaceutical products, are conducted either by pharmaceutical products developers or by organizations specializing in pre-clinical studies. The Federal Service maintains a list of such organizations. Our pre-clinical studies are traditionally conducted by third party organizations included in this list.

During the registration process a pharmaceutical product and its dossier undergo pharmaceutical review by a specialized federal expertise organization – Scientific Center for Expertise of Medical Products.

Subject to the Federal Law on Pharmaceutical Products, clinical trials are required for most products undergoing registration. The Federal Law on Pharmaceutical Products requires that organizations conducting clinical trials should be approved and accredited by ROSZDRAVNADZOR.

Clinical trials are conducted to prove the efficacy and safety of pharmaceutical products for humans and to obtain information on their possible side effects. Relying on the results of clinical trials, ROSZDRAVNADZOR decides whether the product should be recommended for medical use. If the product is not recommended for medical use, it cannot be registered with ROSZDRAVNADZOR. In our experience, the trial period takes from several months to several years depending on the pharmaceutical product being tested.

The statutory limit for the review of registration documents required for State Registration of pharmaceutical products is six months upon the completion of all expertise, pre-clinical and clinical studies.

Generic versions of original products that were previously registered in Russia are subject to accelerated State Registration procedure. Generic versions of branded pharmaceutical products require a special bioequivalence study. This study compares bioavailability of the original and generic products and usually takes several months.

The statutory limit for the review of registration documents required for accelerated State Registration procedure is three months upon the completion of all expertise, pre-clinical and bioequivalent studies. The generic version of an existing product may not be registered prior to expiration of the original product patent rights.

On receiving State Registration, the product is included into the State Register of Pharmaceutical Products, and the applicant receives a registration certificate, official standards for the product formula, components and characteristics, including packing, transportation and safety, other indicators and methods of quality control for the registered pharmaceutical product, as well as usage instructions.

Manufacturing Licenses

Pharmaceutical products, including substances and certain plasters, may not be manufactured without a respective production license issued by ROSZDRAVNADZOR. To obtain a manufacturing license, the applicant must have qualified specialists responsible for the manufacture, quality control and marking of pharmaceutical products under license requirements, whose qualifications can be proved by appropriate supporting documents.

Pharmstandard has all necessary manufacturing licenses.

Risk Management

category	category specification	definition	possible risks for Pharmstandard Group	regulation methods	risk probability for Pharmstandard Group
FINANCIAL	INFLATION RISK	a possibility that relative value of assets (in monetary terms), expected income and profit may decrease	risk of increase in raw material and supplies prices; lack of balanced mechanisms for establishing correlation between prices of raw material and supplies and prices of marketed products	changeover to shorter-term contractual obligations (conclusion of spot-contracts) with regard to the purchase of raw materials and supplies; appropriate pricing policy; shortening of the time interval used for cost estimation	high
			risk of marketed products overpricing (fixing non-competitive prices)	appropriate marketing policy and market monitoring	low
	TRADE MARKS IMPAIRMENT	a possibility that others may attack our brand trough developing, using or selling products that are similar or functionally equivalent to our products	potential impairment of intangible assets, including major brands	regular monitoring of primary current costs evaluation carried out for the purposes of taking preventive measures	medium
	FOREIGN EXCHANGE RISKS	a risk of currency losses resulting from the change of the currency price rate with regard to the currency of payment in the period between the conclusion of a foreign trade, foreign economic or credit agreement and effecting of payments under such agreement	risks related to foreign currency loans and outstanding payments to raw materials suppliers	conclusion of contracts at a "budgeting rate"; additional assessment of the transaction	high
	LIQUIDITY RISK	a possibility of losses on securities conversion or other commodities disposal resulting from the revision of their quality rating and utilization value; scarcity of funds required for punctual settlement of liabilities	risk of scarcity of funds required for timely settlement of own liabilities (discharge of taxes, payment of wages and salaries, repayment and servicing of loans)	an organized system for the planning and management of the scarcity of funds; the company has introduced new credit control standards to reduce the risk of overdue receivables	low
			risk of losses on financial derivatives resulting from changes in their fair value	priority to the use of debt instruments issued by the government or by financial institutions with a substantial government interest (Savings Bank); reduction of portfolio diversification level; pessimistic forecasting	low
	CREDIT RISKS	risk of failure to collect receivables due under settlements with buyers and customers	risk of losses related to creation of reserves and subsequent violation of payment discipline	the company has introduced daily monitoring of the correlation between shipment and payment; tightened the measures for the changeover to delayed payment delivery system; developed reconciliation database and introduced weekly monitoring of receivables cash flow	high

category	category specification	definition	possible risks for Pharmstandard Group	regulation methods	risk probability for Pharmstandard Group
OPERATIONAL	PERSONNEL RISK	risk of improper discharge of duties/ rules/procedures	risk of material errors and malpractices	enhancement of internal control measures	medium
		risk of inefficient corporate structure	risk of inefficient delegation of authority; creation of additional bureaucratic barriers, loss of operational efficiency of information flows established between distant enterprises	use of appropriate evaluation instruments for the existing business processes evaluation; organization of training sessions for the company personnel	low
		risk of key managers and specialists loss	risk of key managers and specialists loss	adequate compensation package	low
		risk of qualified personnel shortage	risk of qualified personnel shortage	an increased offer of qualified personnel caused by the current economic recession enables the company "to pick and choose" specialists	medium
	PROCESSES RISK	risk of incorrect organization of processes schedules and procedures	risk of incorrect organization of processes schedules and procedures	qualified personnel; a system of internal standards and procedures compliance control	low
		lack (inadequacy) of the information security system and/or information access procedure	information security system inadequacy	creation of information access control; implementation of regular measures for identification and elimination of risk factors	medium
	IT SYSTEMS RISK	technological risk of hardware or software failure	technological risk of hardware or software failure	creation of reserve database storage facilities/servers; qualified technical staff formation	low
	EXTERNAL FACTOR RISKS	risk of unrecorded competitive expansion	risk of competition within the pharmaceutical industry	development of R&D capabilities; analysis of the new pharmaceutical products market; portfolio diversification; expansion into new market segments through participation in government-sponsored schemes; support of import substitution strategy	low
		risk of inefficient acquisition	risk of losses resulting from the integration of acquired assets combined with the risk of weakened financial performance	thorough preliminary analysis; development of new methods	medium
		risk of participation in government-sponsored schemes	risk of overdue receivables (reserve) resulting from the sales of products under the FRP Programme	collection of information; control of compliance with contractual terms and conditions; control of receivables structure and adequate diversification	low
	RISK OF DIRECT FINANCIAL LOSSES	stock exchange risk	non-compliance with capital requirements or other legal (stock exchange) requirements	timely updating of information; distribution of responsibility areas among the corporate internal services; regular monitoring	low

+26% REVENUE GROWTH, total revenue 14,336 mln RUR

+28% GROSS PROFIT GROWTH
gross profit 8,759 mln RUR or 61% of sales

+24% EBITDA GROWTH
EBIDTA 6,049 mln RUR or 42% of sales

+ 7% NET PROFIT GROWTH
net profit 3,503 mln RUR or 24% of sales

03 Management's Discussion and Analysis

of Financial Condition and Results Of Operations Development

INTRODUCTION

>>

Further discussion of our financial situation and performance results should be based on the Group's Consolidated Financial Statement, notes thereto and other information conveyed in this annual report.

The following important events took place in 2008:

- **Acquisition of Afobazol® trademark**
  In August 2008, the Company signed an agreement with Donelle Company Limited (Cyprus) shareholders for the purchase of Afobazol® trademark by buying out all Donelle's shares. By the end of the year, the volume of Afobazol® sales amounted to 217.5 mln RUR, which was equal to 1% of the total volume of sales or 2% of the OTC products sales in 2008.

- **Buying out minority interests in the Company's subsidiaries**
  In 2008, the Company's management approved a plan to acquire minority interests in several subsidiaries. As a result, the Company acquired the remaining minority interests in OJSC "Pharmstandard-Ufavita", OJSC "Pharmstandard-Octyabr", OJSC "Pharmstandard-Leksredstva" and OJSC "TZMOI" and became the sole shareholder in all those entities.

- **Mildronate®: Pharmstandard-Grindeks (Latvia) joint project**
  In February 2008, the Company signed a contract with Grindeks (Latvia) for exclusive distribution and promotion of a Grindeks product Mildronate® in Russia. Subject to the contract, Mildronate® is partly imported by Pharmstandard and partly purchased from a Grindeks Russian affiliate. In 2008, the volume of Mildronate® sales amounted to 1,149.0 mln RUR.

This section contains forward-looking statements that involve risks and uncertainties. Under the influence of various factors, actual results may differ materially from those mentioned in such forward-looking statements.

RESULTS OF OPERATIONS

>> The table featured in this section shows the key figures, which reflect the Company results as of 31 December 2008 and 2007 in absolute values and as sales percentage ratio (the exchange rate gain and losses are recorded in the Group's financial reporting documents).

In Russia, classification of pharmaceuticals as prescription products (Rx) or non-prescription over-the-counter products (OTC) is regulated by the government and is periodically re-visited. The recent re-visiting of OTC and Rx products classification introduced in 2008 had a significant influence on the Company's product portfolio structure. For the purposes of comparative analysis, the prior year figures were restated accordingly. The above changes in the Company portfolio structure do not affect the sales results.

Year ended 31 December	2008		2007	
	mln,RUR	%	mln, RUR	%
Sales of goods	**14,335.9**	**100**	**11,371.3**	**100**
Pharmaceutical products	13,260.2	92	9,762.6	86
OTC products	10,553,4	74	8,519.9	75
Branded	9,087,1	63	7.427.5	65
Non-branded	1,466,3	10	1.092.4	10
Prescription products	2,637,6	18	1,188.2	10
Branded	2,349,2	16	938.0	8
Non-branded	288,4	2	250.2	2
Other sales	69,3	0	54.6	0
Medical equipment and disposables	1,075.7	8	1,608.7	14
Cost of sales	-5,577.5	39	-4,519,7	-40
Gross profit	**8,758.4**	**61**	**6,851.6**	**60**
Selling and distribution costs	-2,466.8	17	-1,626,0	14
General and administrative expenses	-656.2	5	-570,5	5
Other expenses, net	-715.2	5	-41,4	0
Interest income	22.6	0	28,7	0
Interest expense	-255.2	2	-320,4	3
Profit before income tax			4,321.9	38
Income tax expense	-1,184.4	8	-1,058.7	9
Profit for the period	**3,503.1**	**24**	**3,263.2**	**29**
Attributable to participants of the Company	3,504.0		3,227.9	
Attributable to minority shareholders' stakes	-0.9		35.3	

RESULTS OF OPERATIONS

Product Distribution

The Company's core activities include manufacturing and distribution of finished pharmaceutical products, medical equipment and disposables. The sales of pharmaceuticals amount to 92.5% of its total sales volume, while the sales of medical equipment account for the remaining 7.5%. The sales of pharmaceuticals and medical equipment are for the most part carried out under direct contracts signed with wholesale distributors and/or medical institutions. The total volume of sales in 2008 amounted to 14,335.9 mln RUR, which is by 29% more than in 2007 (11,371.3 mln RUR).

In 2008, the increase in the sales of pharmaceuticals was equal to 36%, including a 24% increase in the sales of own products (organic growth excluding the sales of Mildronate®).

The project for the distribution of a branded prescription product Mildronate® carried out together with Grindeks (Latvia), which was launched in 2008, had a major impact on the increase in the sales of pharmaceuticals. As of the end of 2008, the sales of Mildronate®) amounted to 1,149.0 mln RUR, which is equal to 43% of the total sales of prescription products and/or 8% of the total sales of pharmaceuticals (these figures reflect the fact that some product series were withdrawn from the market [1]).

Pharmaceutical Products

The sales of OTC products grew by 2,033.1 mln RUR or by 24% – from 8,519.9 mln RUR in 2007 to 10,553.4 mln RUR in 2008. This increase was achieved largely due to implementation of an active promotion strategy. The main contribution can be attributed to the following products: Arbidol®, Terpincod®, Pentalgin® and Codelac®. The sales of Arbidol® in 2008 grew by 414.7 mln RUR or by 18% as compared to 2007. There was a considerable growth in the sales of Terpincod® – 284 mln RUR, Pentalgin® – 268.3 mln RUR and Codelac® – 201.9 mln RUR, which corresponds to 21%, 20% and 43% respectively. The sales of Afobazol® over the 5 months of 2008 (the trademark, was acquired by Pharmstandard in 2008) achieved an impressive result of 217.5 mln

1 *Series withdrawal: on 24 March 2009, the Federal Service on Surveillance in Healthcare and Social Development issued an order for the withdrawal of certain Mildronate series packaged in ampules in connection with a process error discovered in February 2009. A detailed description of this fact is given in the Company's Consolidated Financial Statements Note 28.*

RUR in absolute figures securing this drug a position in the list of the top-10 OTC portfolio products.

The sales of prescription products (Rx) increased by 1,449.4 mln RUR or by122% – from 1,188.2 mln RUR in 2007 to 2,637.6 mln RUR in 2008. This increase was largely achieved due to the sales of Mildronate®. The organic sales growth in the OTC products segment (excluding Mildronate®) was equal to 300.3 mln RUR or 25.2%. The organic growth of OTC products sales volume was materially influenced by the sales of Phosphogliv® – 68.0 mln RUR, Cyclodol – 53.5 mln RUR and Biosulin® – 43.9 mln RUR, which corresponds to 19%, 184% and 36% respectively.

Medical Equipment & Disposables

In 2008, the sales of medical equipment and disposables dropped by 553.0 mln RUR or by 33% and amounted to 1,075.6 mln RUR against 1,608.7 mln RUR in 2007. This decrease, however, cannot be interpreted as critical, since the high sales figures of 2007 were achieved mainly due to the fact that the Company was awarded a major government contract for sterilizers from the Directorate of the Federal Agency for the RF State Reserves. No similar tenders were held in 2008. Therefore, the analysis of the medical equipment segment trend over the period of 2007–2008 excluding the figures related to the above tender shows that the absolute decrease in the sales of medical equipment was equal to 79.1 mln RUR or 7%.

This trend is mainly a result of the global recession, which lessened effective demand for high-priced equipment.

Cost of Sales

The cost of sales includes the cost of raw materials and supplies, goods for resale, production overheads, direct labour costs, and expenses related to amortization and depreciation of trademarks and fixed assets.

In 2008, the cost of goods sold by the Company increased by 1,057.7 mln RUR or by 23% as compared to 2007 and amounted to 5,577.5 mln RUR against 4,519.7 mln RUR in 2007.

The main item of cost of sales is Raw Materials, Supplies and Goods for Resale (73%). In 2008, those expenditures increased by 1,104.8 mln RUR or 37% and amounted to 4.102.2 mln RUR against

RESULTS OF OPERATIONS

2,997.5 mln RUR in 2007. The increase was caused by the planned growth in pharmaceutical production volume and purchase of Mildronate® for resale.

Depreciation and amortization expenses in 2008 amounted to 535.6 mln RUR (9.6% of the total costs), which is by 54.3 mln RUR or by 11% more than in 2007. The main factors resulting in increase of those expenses were the launch of new production facilities (JSC Pharmstandard-Leksredstva and JSC Pharmstandard-UfaVITA) and additional amortization of Afobazol® trademark purchased in August 2008.

In 2008, percentage of cost of sales in relation to total sales dropped to 38.9% against 39.7% in 2007 due to a considerable reduction of production overheads (by 10% or by 80.6 mln RUR) achieved through the transfer of Masterlek products manufacturing to Pharmstandard own production facilities. Another factor that had a material effect on the reduction of the total cost was the reduction of direct labour costs (by 9% or by 20.7 mln RUR), which resulted from the closure of the production of needles for disposable medical items at the Company's TZMOI manufacturing facility.

Gross Profit

Due to the above factors, the Company recorded a 1,906.8 mln RUR or a 28% gross profit growth – from 6,851.6 mln RUR in 2007 to 8,758.4 mln RUR in 2008.

The main gross profit growth factors include:

- synergy effect achieved from the transfer of Arbidol®, Flukostat® and Phosphogliv® production to Pharmstandard own production facilities;
- increased sales of highly cost-effective products

In 2008, gross profit from the Company's pharmaceutical business segment amounted to 8,405.4 mln RUR or 63.4% of the total sales. Gross profit from the sales of medical equipment was equal to 353.0 mln RUR or 32.8% of the total segment sales.

Operating Expenses

Operating expenses increased by 926.5 mln RUR or by 42% – from 2,196.5 mln RUR in 2007 to 3,123.1 mln RUR in 2008. The operating expenses to sales ratio increased from 19.3% in 2007 to 21.8% in 2008.

In 2008, operating expenses related to sales and distribution (S&D) increased by 840.8 mln RUR (52%) and amounted to 2,466.8 mln RUR against 1,626.0 mln RUR in 2007, i.e. comprised 17.2% and 14.3% of total sales, respectively. This relative increase occurred due to the accrual for a bad debt allowance for a one of the Company's distributors CJSC Genesis receivables in the amount of 476.1 mln RUR in connection with the initiation of a bankruptcy procedure against that distributor.

In 2008, marketing, advertising and promotion costs (43% of the total S&D expenses) increased by 308.2 mln RUR, or by 41%. Increased advertising costs, including advertising expenses related to the promotion of Arbidol®, Pentalgin® and new Afobazol® and Neosmektin products. In 2008 marketing, advertising and promotion costs amounted to 1,061.8 mln RUR against 753.6 mln RUR in 2007.

In 2008, labour costs (19.3% of S&D) grew by 79.9 mln RUR or by 20% as compared to 2007. It happened mainly due to the increased number of medical representatives (up to 350 medical representatives by 31 December 2008) and to the existing staff salaries inflation increase.

Other expenses (18.3% of S&D) dropped by 23.5 mln RUR or by 5% primarily due to the termination of license fee payments in connection with the expiration of Arbidol® trademark patent protection period in December 2007.

In 2008, general and administrative expenses (G&A) increased by 85.7 mln RUR or by 15% and amounted to 656.2 mln RUR against 570.5 mln RUR in 2007. Labour costs are the major item of general and administrative expenses (61.4% of G&A). They increased by 46.6 mln RUR (13%) from 356.5 mln RUR in 2007 to 403.1 mln RUR in 2008 primarily by salaries inflation increase and overtime payments.

In 2008, the cost of utilities and services amounted to 63.0 mln RUR or 9.6% of G&A. Over the year the expenses increased by 14.9 mln RUR due to the growth of utility rates, as well as the growth of the consumed services volume and price.

Other administrative expenses amounted to 190.1mln RUR or 29% of the G&A. In 2008, these expenses increased in line with the increase in the services provided by third parties (shipping, insurance services, etc.).

RESULTS OF OPERATIONS

Operating Profit

Due to the above factors, operating profit[1] in 2008 grew by 980.3 mln RUR or by 21% – from 4,655.0 mln RUR in 2007 to 5,635.3 mln RUR in 2008 – and amounted to 39.3% of the total sales volume against 40.9% in 2007. This decrease in profitability is related to the accrual for bad debt allowance in respect of Genesis distributor receivable in connection with the initiation of a bankruptcy procedure against the said distributor. Unadjusted for the above reserve, operating profit to the sales ratio in 2008 would be equal to 42.6%.

Other Expenses, net

Other expenses in 2008 amounted to 715.2 mln RUR or 5% of the total sales. Foreign exchange loss equal to 524.8 mln RUR was the most significant item (3.7% of the total sales). The loss was caused by a considerable increase in the US dollar-rouble exchange rate in the fourth quarter 2008, resulting from the global recession. An additional component of the other expenses item in 2008 was impairment of Afobazol® trademark amounting to 140.5 mln RUR as of 31 December 2008. This impairment mainly resulted from increase of the discount rate applied in the trade mark valuation model from 13% to 18.1% for the first years of the trademark's life cycle and 15% thereafter. This increase in discount rate was a direct result of the current global recession.

At the same time, this item shows the positive balance resulting from reimbursement of 107.2 mln RUR promotional expenses primarily related to the Mildronate® Project.

Interest Expenses, net

In 2008, our interest expenses, net dropped by 59 mln RUR or by 20% – from 291.6 mln RUR in 2007 to 232.6 mln RUR in 2008 – due to the scheduled repayment of debts under the syndicated loan contract signed with the Citibank in December 2006. The contract stipulates full repayment of the debt in 2011.

Corporate Income Tax

In 2007 and 2008, corporate tax rate in Russia was equal to 24%. The Company's tax expenses in 2008 were equal to 1,184.4 mln RUR

1 *Operating profit is defined as profit before income tax and before the deduction of other expenses, net and financial expenses, net.*

and effective tax rate was 25.3% against 1,058.7 mln RUR and 24.5%, respectively, in 2007. In 2007 and 2008, the Company incurred certain amount of non-deductible expenses.

In November 2008, the Russian lawmakers enacted a law reducing the corporate income tax rate from 24% to 20% starting from 1 January, 2009. The Company recalculated its deferred tax balances as of 31 December 2008 applying the updated tax rate in accordance with IFRS. As a result of such re-calculation deferred tax credit of 116.4 mln RUR was recorded in the Company's consolidated income statement for 2008.

Net Profit

In 2008, the Company's net profit increased by 239.9 mln RUR or by 7% and amounted to 3,503.1 mln RUR against 3,263.3 mln RUR in 2007, i.e. 24.4% and 28.7% to total sales, respectively. Net profit attributable to equity holders of the parent was 3,504.0 mln RUR. Net loss attributable to minority shareholders was 0.9 mln RUR.

LIQUIDITY AND CAPITAL RESOURCES

>> Overview

Our liquidity requirements arise primarily from the need to increase the Company's working capital, finance its capital expenditure program and expand its product portfolio through selective acquisitions of subsidiaries and intangible assets. During the periods covered by the Company's Consolidated Financial Statements, we primarily financed our operations and investments through free cash flow and short-term borrowings from banks and related parties. In future, we also intend to fund acquisitions, if any, through free cash flow and borrowings.

The following table summarizes our cash flows in 2007 and 2008.

Cash flows	Year ended 31 December 2008, mln RUR	Year ended 31 December 2007, mln RUR
Net cash flow from operating activities	3,836.9	2,081.4
Net cash used in investing activities	(2,709.8)	(1,729.8)
Net cash used in financing activities	(1,332.8)	(352.0)
Cash and cash equivalents at the end of the period, net of bank overdraft	**(13.2)**	**192.6**

Net cash from operating activities

Substantially, all our cash flows from operating activities for the periods covered by the Company's Consolidated Financial Statements were generated from sales of pharmaceutical products and medical devices. Standard commercial contracts that we sign with distributors provide for 90–120 day credit period, and we offer individual credit conditions to each distributor. In 2007 and 2008, net cash from operating activities was 3,837 mln RUR and 2,081 mln RUR respectively. The increase in the net cash flow from the Company's primary activities recorded in 2008 was generated due to the reduction of overdue receivables achieved through the collection of balances outstanding from the FRP program in 2007 and 2006, and, furthermore, through the reduction of the VAT Recoverable items in the Company's Balance Sheet. Furthermore, the growth of operating profits relating to the sales of high-margin products and the launch of the Mildronate® distribution project, gave rise to the inflow of economic benefits, which resulted in an incremental increase in net cash flow.

Net cash used in investing activities

In 2007 and 2008 the net cash used in investing activities amounted to 1,730 mln RUR and 2,710 mln RUR respectively. Within the above periods, our most significant investment activities included acquisition of property, manufacturing facilities, equipment and intangible assets; sale of non-current assets classified as held for sale; operations with financial assets; acquisition of minority interests and purchase of TZMOI shares in 2005. In 2007 and 2008, we paid 521.6 mln RUR and 661.1 mln RUR respectively for the acquisition of property, manufacturing facilities and equipment. These acquisitions were primarily made within the framework of capital investments in the development of the Company's production capacities, including modernization of the existing and the launch of new lines for the production of tablets, Phosphogliv® capsules and sacheted powders at the Company's manufacturing facility in Kursk; the launch of new lines for the production of solutions, ampoules and tablets in Ufa; and the launch of new lines for the production of Amixin®, Arbidol® and other tableted pharmaceuticals in Tomsk. In 2008, the Company paid 1,993.6 mln RUR for the acquisition of intangible assets, i.e. Afobazol® trademark (against 165.2 mln RUR in 2007, including 160.0 mln RUR for Neosmektin trademark). In 1st quarter of 2008, Pharmstandard Management approved a plan for the purchase of the stakes held by minority shareholders in several Company subsidiaries. The total consideration paid on this acquisition amounted to 501.7 mln RUR.

Meanwhile, the Company also sold certain assets. In accordance with the Company Strategy, in 2008, the Company sold part of its medical equipment business segment "TMK" LLC for a cash consideration of 122.1mln RUR. Besides, in December 2007, the Company acquired 19.88% of "Dipaka Trading Limited" for a cash consideration of 245.3 mln RUR. In the fourth quarter of 2008, Pharmstandard's share in Dipaka Trading Limited was sold for 268.9 mln RUR.

Net cash used in financing activities

In 2007 and 2008, net cash used in financing activities amounted to 352.0 mln RUR and 1,332.8 mln RUR respectively. These amounts primarily covered scheduled repayments of the Citibank Loan received in 2006.

LIQUIDITY AND CAPITAL RESOURCES

Contractual obligations and other commitments

As of 31 December 2008, the total amount of 235.0 mln RUR was still payable to the former Donelle shareholders. Donelle is the sole shareholder of CJSC Aphopharm, whereas the latter is the holder of Afobazol® trademark, which is its only asset. An addendum to the original contract with the former Donelle shareholders was concluded on 12 March, 2009. As of 31 December 2008, we had no material contractual obligations other than capital expenditure and certain liabilities incurred in the ordinary course of business, such as trade payables, wages and tax expenses. We are not engaged in any significant off balance sheet financing.

QUALITATIVE AND QUANTITATIVE DISCLOSURES ABOUT MARKET RISKS

>> *Operating environment*

The Russian economy is vulnerable to the global market downturns and economic slowdowns. In Russia, the ongoing global financial crisis has resulted in capital markets instability, significant deterioration of liquidity in the banking sector, and tighter credit conditions. While the Russian Government has introduced a range of stabilization measures to provide liquidity to Russian banks and companies and support their debt refinancing efforts, there is still no certainty regarding access to capital and the cost of capital for the Pharmstandard Group and its counterparties. This situation can affect our financial position, performance and business prospects. We are exposed to market risks primarily related to foreign currency exchange rates, interest rates, fluctuations in the prices of raw materials and creditworthiness of the counterparties from whom we would expect payments under normal commercial conditions. In compliance with our treasury policies, we centrally manage and monitor our risk exposure by seeking to minimize external financial risks.

Credit risk

Our principal credit risk arises from the distributors' possible failure to fulfil their payment obligations under a sales contract. In compliance with the Group's general principles for doing business, all of our sales are made on credit. The credit terms depend on our credit and marketing practices with respect to a particular customer. We manage credit risk by relying on the policies which ensure that the products are sold to customers with appropriate credit histories. Moreover, we carry out daily monitoring of sales and receivables with the help of effective internal control procedures. Our credit committee composed of the Company CEO, CFO and Director of Commercial Operations sets the Company Credit Policy, which is revised in response to particular circumstances. According to the Company Credit Policy, customers are generally divided into three categories: those with a maximum credit limit, those for whom the credit committee will set a credit limit and those who are required to make prepayments. The majority of our sales contracts are concluded with the customers who fall under the first category (in 2008, approximately 55% of the sales were made to our five major customers). The carrying amount of the accounts receivable, net of provisions, represents the maximum amount of exposure to the

QUALITATIVE AND QUANTITATIVE DISCLOSURES ABOUT MARKET RISKS

credit risk at the end of each quarter. We believe that, other than the concentration with the five major customers, we have no significant concentrations of credit risk. Although collection of receivables can be influenced by various economic factors, the Company's Management Team believes that there is no significant risk of loss beyond the provisions stipulated by respective contracts.

Currency Risk

A certain amount of our purchases is denominated in currencies other than the rouble (the functional and reporting currency used in our Consolidated Financial Statements). We incur currency risk whenever we enter into transactions denominated in a currency other than our functional currency. Generally, our foreign currency transactions, which account for a substantial proportion of the Company's purchases of raw materials, as well as to borrowings and related interest payments thereon, are settled in roubles. However, they are linked to US dollar or Euro. Therefore, our cost of sales, operating costs and expenses presented in our Consolidated Financial Statements, as well as payables and borrowings shown in the Company's Balance Sheet can be influenced by the foreign exchange rate fluctuations. Our principal method for minimizing currency risks is to avoid exposure to currency fluctuations by maintaining a certain proportion of rouble-denominated transactions. At the beginning of 2009, the Russian rouble was devalued with regard to some currencies (primarily US dollar and Euro). On the date when the Company's Consolidated Financial Statements were authorized for issue, the Central Bank of Russia set the official Russian rouble-US dollar exchange rate equal to approximately 33.4 RUR for 1 USD, which means a 13.4% reduction in the value of the Russian rouble with regard to the US Dollar since 31 December 2008. We hope that in 2009 the US dollar-rouble exchange rate will not change significantly with regard to its current value as of the date of the Company's Consolidated Financial Statements issuance.

Interest rate risk

We are exposed to interest rate risk through interest cash flow and market value fluctuations, since the majority of interest rates on our long-term borrowings are floating and based on LIBOR. In September 2007, when LIBOR rate was approximately 5.7%, we entered into an

Interest Rate Swap Agreement covering all interest payments on the Citibank loan, basically swapping the LIBOR rate interest obligations into a fixed rate of 4.932% per annum. In this manner, the Company protects itself against LIBOR rate fluctuations.

Liquidity risk

Our policy is to maintain sufficient cash and cash equivalents or have available funding through an adequate amount of committed credit facilities to meet our operating and financial commitments. We perform continuous monitoring of cash deficit risks, as well as of the scheduled liability repayments accuracy. Moreover, we perform daily planning and control of the cash flow.

Capital Risk Management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and maintain an optimal capital structure, which ensures the reduction of the cost of capital. The Company manages and adjusts its capital structure depending on external economic conditions. To maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt (strictly observing the terms and conditions set by the Loan Agreement with the Citibank).

Commodity price risk

We beleive that the Company is not subject to any material risk resulting from fluctuations in the prices of materials and supplies used in our production processes because we do not rely on any specific commodity to a significant extent and because there is no significant correlation between the rise and fall of the prices of different raw materials and supplies procured by the Company.

■ The Company's financial statements prepared in accordance with IFRS give a true and fair view of the assets, liabilities, financial position and profit of the Company

04 Consolidated Financial Statements

For the year ended 31 December 2008

INDEPENDENT AUDITORS' REPORT

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To the Shareholders and Management of OJSC "Pharmstandard"

We have audited the accompanying consolidated financial statements of OJSC "Pharmstandard" and its subsidiaries ("the Group"), which comprise the consolidated balance sheet as at 31 December 2008, and the consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of consolidated 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 consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated 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 auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2008, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young LLC

15 April 2009

A member firm of Ernst & Young Global Limited

Consolidated Balance Sheet

at 31 December 2008

(in thousands of Russian Roubles)

	Notes	2008	2007
ASSETS			
Non-current assets			
Property, plant and equipment	8	3,917,109	3,691,266
Intangible assets	9	6,347,141	4,468,477
Long-term financial assets at fair value through profit or loss	14	–	245,398
		10,264,250	**8,405,141**
Current assets			
Inventories	11	2,484,910	1,760,195
Trade receivables	12	4,761,359	4,176,200
VAT recoverable		326,208	358,767
Prepayments		73,544	130,479
Short-term financial assets at fair value through profit or loss	14	113,995	111,899
Cash and cash equivalents	13	186,066	192,589
		7,946,082	**6,730,129**
Non-current assets classified as held for sale	10	–	158,855
Total assets		**18,210,332**	**15,294,125**
EQUITY AND LIABILITIES			
Equity attributable to equity holders of the parent			
Share capital	18	37,793	37,793
Retained earnings		12,413,396	9,004,021
		12,451,189	**9,041,814**
Minority interest		163,203	560,879
Total equity		**12,614,392**	**9,602,693**

(in thousands of Russian Roubles)

	Notes	2008	2007
Non-current liabilities			
Long-term borrowings and loans	15	760,512	1,954,576
Deferred tax liability	25	739,186	1,047,799
Derivative financial instruments	15, 27	89,087	44,598
Other non-current liabilities		34,048	36,826
		1,622,833	**3,083,799**
Current liabilities			
Trade and other payables and accruals	17	1,707,544	1,046,520
Current portion of long-term borrowings	15	1,582,722	1,310,374
Income tax payable		144,292	37,934
Other taxes payable	16	339,307	212,806
Bank overdraft	13	199,242	-
		3,973,107	**2,607,633**
Total liabilities		**5,595,940**	**5,691,432**
Total equity and liabilities		**18,210,332**	**15,294,125**

Signed and authorised for release on behalf of the Board of Directors of OJSC PHARMSTANDARD

General Director ..... **I. K. Krylov**

Chief Financial Officer ..... **E. V. Arkhangelskaya**

15 April 2009

The accompanying notes on pages 83–125 are an integral part of these consolidated financial statements.

Consolidated Income Statement

For the Year Ended 31 December 2008

(in thousands of Russian Roubles)

	Notes	2008	2007
Revenue	19	14,335,867	11,371,345
Cost of sales	20	(5,577,468)	(4,519,749)
Gross profit		**8,758,399**	**6,851,596**
Selling and distribution costs	21	(2,466,841)	(1,626,041)
General and administrative expenses	22	(656,248)	(570,519)
Other income	23	149,762	274,142
Other expenses	23	(864,963)	(315,591)
Financial income	24	22,569	28,729
Financial expense	24	(255,189)	(320,367)
Profit before income tax		**4,687,489**	**4,321,949**
Income tax expense	25	(1,184,381)	(1,058,709)
Profit for the year		**3,503,108**	**3,263,240**
Attributable to:			
Equity holders of the Parent		3,504,046	3,227,895
Minority interests		(938)	35,345
		3,503,108	**3,263,240**
Earnings per share (in Russian roubles)			
- basic and diluted, for profit of the year attributable to equity holders of the parent	18	92.72	85.41

Signed and authorised for release on behalf of the Board of Directors of OJSC PHARMSTANDARD

General Director **I. K. Krylov**

Chief Financial Officer **E. V. Arkhangelskaya**

15 April 2009

The accompanying notes on pages 83–125 are an integral part of these consolidated financial statements.

Consolidated Statement of Cash Flows

For the Year Ended 31 December 2008

(in thousands of Russian Roubles)

	Notes	2008	2007
Cash flows from operating activities:			
Profit before income tax		4,687,489	4,321,949
Adjustments for:			
Depreciation and amortisation	8,9	604,204	527,600
Allowances for impairment of inventories and financial assets	11, 12, 23	427,259	152,364
Loss recognised on sale of non-current assets classified as held for sale	23	13,891	24,101
Impairment charge – property, plant and equipment and intangible assets	8, 9, 23	199,749	42,403
Gain from disposal of property, plant and equipment and investments property and non-current assets classified as held for sale	23	(18,996)	(15,044)
Foreign exchange loss (gain)	23	524,842	(259,098)
Gain from disposal of long-term financial assets	14	(23,546)	--
Financial income	24	(22,569)	(28,729)
Financial expense	24	255,189	320,367
Operating cash flows before working capital changes		**6,647,512**	**5,085,913**
Increase in trade receivables	12	(1,047,408)	(892,491)
Increase in inventories	11	(718,039)	(385,398)
Decrease (increase) in VAT recoverable		32,559	(136,091)
Decrease in prepayments		56,936	38,753
Increase (decrease) in trade payables, other payables and accruals and advances received	17	273,368	(184,189)
Increase in taxes payable other than income tax		126,501	64,346
Cash generated from operations		**5,371,429**	**3,590,843**
Income tax paid	25	(1,351,703)	(1,237,928)
Interest paid		(195,680)	(282,917)
Interest received		12,815	11,361
Net cash from operating activities		**3,836,861**	**2,081,359**

Consolidated Statement of Cash Flows

(continued)

For the Year Ended 31 December 2007

(in thousands of Russian Roubles)

	Notes	2008	2007
Cash flows from investing activities:			
Purchase of property, plant and equipment	8	(661,068)	(521,582)
Purchase of intangible assets	9	(1,993,637)	(165,220)
Cash received from sale of long-term financial assets	14	268,944	-
Cash paid for long-term financial assets	14	-	(245,398)
Cash paid for acquisition of minority interests		(501,740)	(910)
Cash paid to settle the obligation for OJSC "TZMOI" shares acquired in 2005	7	-	(824,723)
Cash received from sale of investment property and property, plant and equipment	8	51,573	17,574
Cash received from sale of short-term financial assets	14	84,220	32,513
Cash paid for short-term financial assets	14	(104,300)	(81,300)
Cash received from sale of non-current assets classified as held for sale	10	141,086	34,133
Loans repaid by related parties	7	5,121	25,153
Net cash used in investing activities		**(2,709,801)**	**(1,729,760)**
Cash flows from financing activities:			
Proceeds from loans and borrowings	15	4,407	–
Repayment of loans and borrowings	15	(1,337,232)	(351,976)
Net cash used in financing activities		**(1,332,825)**	**(351,976)**
Net decrease in cash and cash equivalents overdraft		**(205,765)**	**(377)**
Cash and cash equivalents at the beginning of the year	13	**192,589**	**192,966**
Cash and cash equivalents at the end of the year, net of bank overdraft	13	**(13,176)**	**192,589**

The accompanying notes on pages 83–125 are an integral part of these consolidated financial statements.

Consolidated Statement of Changes in Equity

For the Year Ended 31 December 2007

(in thousands of Russian Roubles)

	Equity attributable to equity holders of the parent			Minority interests	Total equity
	Share capital	Retained earnings	Total		
Balance at 31 December 2006	**37,793**	**5,838,906**	**5,876,699**	**463,664**	**6,340,363**
Profit for the year	–	3,227,895	3,227,895	35,345	3,263,240
Disposal of part of an ownership interests in subsidiaries	–	(66,476)	(66,476)	66,476	–
Effect of acquisition of minority interests	–	3,696	3,696	(4,606)	(910)
Balance at 31 December 2007	**37,793**	**9,004,021**	**9,041,814**	**560,879**	**9,602,693**
Effect from change in profit tax rate (Note 25)	–	34,937	34,937	–	34,937
Net income for the year recognized directly in equity	–	**34,937**	**34,937**	**–**	**34,937**
Profit for the year	–	3,504,046	3,504,046	(938)	3,503,108
Total income and expense for the year	–	**3,538,983**	**3,538,983**	**(938)**	**3,538,045**
Effect of de-recognition of minority interests (Note 5.2)	–	(493)	(493)	(24,113)	(24,606)
Effect of acquisition of minority interests (Note 5.2)	–	(129,115)	(129,115)	(372,625)	(501,740)
Balance at 31 December 2008	**37,793**	**12,413,396**	**12,451,189**	**163,203**	**12,614,392**

The accompanying notes on pages 83–125 are an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

For the Year Ended 31 December 2008

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

1. Corporate Information

OJSC "Pharmstandard" ("the Company") and its subsidiaries ("the Group") principal activities are production and wholesale distribution of pharmaceutical and medical products. The Company is incorporated in the Russian Federation. Prior to 5 May 2006, the Company was registered as a limited liability company under the name of "Biovit". In May 2006, the Company was renamed as "Pharmstandard" and reorganised into an open joint stock company. Since May 2007, the Company's shares are publicly traded (Note 18). The Group's corporate office is in Dolgoprudny, Likhachevsky proezd, 5B, Moscow region, Russian Federation and its manufacturing facilities are based in Kursk, Tomsk, Ufa, Nizhny Novgorod and Tyumen. The Company held shares of voting interests in the following major subsidiaries consolidated within the Group as at 31 December 2008 and 2007, respectively:

Entity	Country of incorporation	Activity	2008 % share	2007 % share
"Pharmstandard" LLC	Russian Federation	Central procurement	100	100
"Pharmstandard-Leksredstva" OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	99
"Pharmstandard-Tomskhimpharm" OJSC	Russian Federation	Manufacturing of pharmaceutical products	91	91
"Pharmstandard-Ufavita" OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	94
"Pharmstandard-Octyabr" OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	93
"Pharmstandard-Phitofarm-NN" LLC	Russian Federation	Manufacturing of pharmaceutical products	99	99
"TZMOI" OJSC	Russian Federation	Manufacturing of medical equipment	100	89
"TMK" LLC*	Russian Federation	Manufacturing of medical equipment	–	100
"Masterlek" CJSC	Russian Federation	Manufacturing pharmaceutical products	100	100
"Black Bird Investment Enterprises Corp"	British Virgin Islands	Finance and holding Company**	100	100
Donelle Company Limited	Cyprus	Finance and holding Company**	100	–
Aphopharm CJSC	Russian Federation	Finance and holding Company**	100	–

* *TMK LLC was sold during the first quarter of 2008 (Note 10).*

** *Finance and holding companies do not conduct any business activities.*

These consolidated financial statements were authorised for issue by the Board of Directors of OJSC "Pharmstandard" on 10 April 2009.

2. *Basis of Preparation of the Financial Statements*

Statement of compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

Basis of accounting

The Group's Russian entities maintain their accounting records in Russian Roubles ("RR") and prepare their statutory financial statements in accordance with the Regulations on Accounting and Reporting of the Russian Federation. The statutory financial statements have been adjusted to present these consolidated financial statements in accordance with IFRS. These adjustments principally relate to valuation and depreciation of property, plant and equipment, valuation and amortisation of intangible assets, certain valuation allowances, using fair values for certain assets and derivative instruments, purchase accounting for business combinations and the resulting income tax effects and also to consolidation.

The consolidated financial statements have been prepared under the historical cost convention except as disclosed in the accounting policies below. For example, derivative instruments and certain short-term assets are recorded at fair value and non-current assets classified as held for sale are recorded at the lower of carrying amount and fair value less costs to sell.

Changes in Accounting Policies

The accounting policies adopted are consistent with those of the previous financial period except that the Group has adopted the following new and amended IFRS and IFRIC interpretations as of 1 January 2008.

- IFRIC 11 "IFRS 2 – Group and Treasury Share Transactions";
- IFRIC 12 "Service Concession Arrangements";
- IFRIC 14 IAS 19 "The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction";
- Amendments to IAS 39 and IFRS 7 "Reclassification of Financial Assets";

IFRIC 11 "IFRS 2 – Group and Treasury Share Transactions" requires arrangements whereby an employee is granted rights to an entity's equity instruments to be accounted for as an equity-settled scheme, even if the entity buys the instruments from another party, or the shareholders provide the equity instruments needed.

IFRIC 12 "Service Concession Arrangements" applies to service concession operators and explain how to account for the obligations undertaken and rights received in service concession arrangements.

IFRIC 14 "The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction" provides guidance on how to access the limit on the amount of surplus in a defined benefit scheme that can be recognised as an asset under IAS 1 Employee Benefits.

Amendments to IAS 39 and IFRS 7 "Reclassification of Financial Assets" are the latest in a series of steps that the IASB has undertaken to respond to the credit crisis. These amendments permit the reclassification of some financial instruments

There were no significant effects of these changes in accounting policies on these consolidated financial statements.

IFRSs and IFRIC Interpretations not yet effective

The Group has not applied the following IFRSs and IFRIC Interpretations that have been issued, but are not yet effective:

- IFRIC 13 "Customer Loyalty Programmes";
- IFRIC 15 "Agreements for the Construction of Real Estate";
- IFRIC 16 "Hedges of a Net Investment in a Foreign Operation";
- IFRIC 17 "Distributions of Non-cash Assets to Owners"
- IFRIC 18 "Transfers of Assets from Customers";
- IFRS 8 "Operating segments";
- IAS 23 (amended 2007) "Borrowing costs";
- IAS 39 "Financial Instruments: Recognition and Measurement" – Eligible Hedged Items;
- IFRS 2 "Share-based Payments" – Vesting Conditions and Cancellations;
- IFRS 3R "Business Combinations" and IAS 27R "Consolidated and Separate Financial Statements";
- IAS 1 Revised "Presentation of Financial Statements";
- Amendments to IAS 32 and IAS 1 "Puttable Financial Instruments";
- Amendments to IFRS 1 and IAS 27 "Determining the cost of an investment in the separate financial statements";
- "Improvements to IFRSs" — a collection of amendments to IFRSs that will not be included as part of another major project. The following table shows the list of IFRSs where amendments have been made that can result in accounting changes for presentation, recognition or measurement purposes and the topics addressed by these amendments:

IFRS	Subject of amendment
IFRS 5 Non-current Assets Held for Sale and Discontinued Operations	Plan to sell the controlling interest in a Subsidiary
IFRS 7 Financial Instruments: Disclosures"	Removal of the reference to "total interest income" as a component of finance costs
IAS 8 Accounting Policies, Change in Accounting Estimates and Errors	Clarification that only implementation guidance that is an integral part of an IFRS is mandatory when selecting accounting policies
IAS 10 Events after the Reporting Period	Clarification that dividends declared after the end of the reporting period are not obligations

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

IFRS	Subject of amendment
IAS 16 Property, Plant and Equipment	Recoverable amount
	Sale of assets held for rental
IAS 18 Revenue	Replacement of the term "direct costs" with "transaction costs" as defined in IAS 39
IAS 19 Employee Benefits	Curtailments and negative past service cost
	Plan administration costs
	Replacement of term 'fall due'
	Guidance on contingent liabilities
IAS 20 Accounting for Government Grants and Disclosure of Government Assistance	Government loans with a below-market rate of interest
IAS 27 Consolidated and Separate Financial Statements	When a parent entity accounts for a subsidiary at fair value in accordance with IAS 39 in its separate financial statements, this treatment continues when the subsidiary is subsequently classified as held for sale
IAS 28 Investments in Associates	Required disclosures when investments in associates are accounted for at fair value through profit or loss
	Impairment of investment in associate
IAS 34 Interim Financial Reporting	Earnings per share is disclosed in interim financial reports if an entity is within the scope of IAS 33
IAS 31 Interests in Joint Ventures	Required disclosures when interests in jointly controlled entities are accounted for at fair value through profit or loss
IAS 29 Financial Reporting in Hyperinflationary Economies	Description of measurement basis in financial statements
IAS 36 Impairment of Assets	Disclosure of estimates used to determine recoverable amount
IAS 38 Intangible Assets	Advertising and promotional activities
	Units of production method of amortisation
IAS 39 Financial Instruments: Recognition and Measurement	Reclassification of derivatives into or out of the classification of at fair value through profit or loss
	Designating and documenting hedges at the segment level
	Applicable effective interest rate on cessation of fair value hedge accounting
IAS 40 Investment Property	Property under construction or development for future use as investment property
IAS 41 Agriculture	Discount rate for fair value calculations
	Additional biological transformation

The Group expects that the adoption of the pronouncements listed above will have no significant impact on the Group's result of operation and financial positions in the period of initial application.

3. Summary of Significant Accounting Policies

3.1 Principles of Consolidation

Subsidiaries

Subsidiaries, which are those entities in which the Group has an interest of more than 50 percent of the voting rights, or otherwise has power to exercise control over their operations, are consolidated. Subsidiaries are consolidated from the date on which control is transferred to the Group and are no longer consolidated from the date that control ceases. All intercompany transactions, balances and unrealised gains on transactions between Group companies are eliminated; unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Where necessary, accounting policies for subsidiaries have been changed to ensure consistency with the policies adopted by the Group.

Minority interest is the interest in subsidiaries with equity not held by the Group. Minority interest at the balance sheet date represents the minority shareholders' portion of the fair value of the identifiable assets and liabilities of the subsidiary at the acquisition date and the minorities' portion of movements in equity since the date of the combination. Minority interest is presented as an equity item.

Business combinations

The purchase method of accounting is used to account for business combinations by the Group. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest.

The excess of purchase consideration over the fair value of the Group's share of identifiable net assets is recorded as goodwill (Note 3.8). If the cost of the acquisition is less than the fair value of the Group's share of identifiable net assets of the subsidiary acquired the difference is recognised directly in the income statement.

Losses allocated to minority interest do not exceed the minority interest in the equity of the subsidiary unless there is a binding obligation of the minority to fund the losses. The excess, and any further losses applicable to the minority, are allocated against the Group interest.

Increases in ownership interests in subsidiaries

The differences between the carrying values of net assets attributable to interests in subsidiaries acquired and the consideration given for such increases are charged or credited to retained earnings.

Acquisition of productive assets (single asset entities)

Acquisition of a subsidiary that does not constitute a business but a group of productive assets is not considered a business combination and the cost of such acquisition is allocated to the identifiable assets and liabilities in the group based on their relative fair values at the date of acquisition.

3.2 Cash and Cash Equivalents

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

For the purpose of the consolidated cash flow statements cash and cash equivalents consist of cash and short term deposits as defined above, net of outstanding bank overdrafts.

3.3 Value Added Tax

The Russian tax legislation permits settlement of value added tax ("VAT") on a net basis within one legal entity.

VAT is payable upon invoicing and delivery of goods, performing work or rendering services, as well as upon collection of prepayments from customers. VAT on purchases, even if they have not been settled at the balance sheet date, is deducted from the amount of VAT payable.

Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

3.4 Inventories

Inventories are recorded at the lower of cost and net realisable value. Cost is determined on a first in, first out basis. The cost of finished goods and work in progress comprises raw material, direct labour, other direct costs and related production overheads (based on normal operating capacity), but excludes borrowing costs. Net realisable 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.

3.5 Non-current Assets Held for Sale

An item is classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. Non-current assets held for sale are measured at the lower of carrying amount and fair value less costs to sell.

3.6 Property, Plant and Equipment

Property, plant and equipment are stated at cost or deemed cost at the date of transition to IFRS (herein referred to as cost) less accumulated depreciation and impairment losses. Deemed cost was determined for property, plant and equipment at 1 January 2004 by reference to their fair value through valuation by an independent appraisal company. Depreciation is calculated on a straight-line basis. The depreciation periods, which represent the estimated useful economic lives of the respective assets, are as follows:

	Number of years
Buildings	10 to 50
Plant and machinery	5 to 30
Equipment and motor vehicles	3 to 7

The asset's residual values, useful lives and methods are reviewed, and adjusted as appropriate, at each financial year end. Land is not depreciated.

Repair and maintenance expenditure is expensed as incurred. Major renewals and improvements are capitalised, and the assets replaced are derecognised. Gains and losses arising from the retirement of property, plant and equipment are included in the income statement as incurred.

3.7 Goodwill

Goodwill on an acquisition of a subsidiary is included in intangible assets. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses.

Goodwill is reviewed for impairment, annually or more frequently if events or changes in circumstances indicate that the carrying amount may be impaired. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is so allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes.

Impairment is determined by assessing the recoverable amount of the cash-generating unit (group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash-generating unit (group of cash-generating units) is less than the carrying amount, an impairment loss is recognised. Where goodwill forms part of a cash-generating unit (group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

3.8 Other Intangible Assets

Intangible assets acquired separately from business combinations are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination are initially recognised at fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Intangible assets with a finite life are amortised on a straight-line basis over the useful economic lives (for trade marks useful economic life is estimated between 15 and 20 years) and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets are reviewed at least at each financial year-end. Changes in

the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the income statement in the expense category consistent with the function of the intangible asset.

3.9 Investments and Other Financial Assets

Financial assets within the scope of IAS 39 are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, or available-for-sale financial assets, as appropriate. The Group does not have held-to-maturity investments.

When financial assets are recognised initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs. The Group determines the classification of its financial assets on initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end. All regular way purchases and sales of financial assets are recognised on the trade date, which is the date that the Group commits to purchase the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the period generally established by regulation or convention in the market place.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss includes financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit or loss.

Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Derivatives are also classified as held for trading unless they are designated as effective hedging instruments or a financial guarantee contract. Gains or losses on investments held for trading are recognised in profit or loss.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement loans and receivables are carried at amortised cost using the effective interest method less any allowance for impairment. Gains and losses are recognised in the income statement when the loans and receivables are derecognised or impaired, as well as through the amortisation process.

Available-for-sale financial investments

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 unrealised gains or losses recognised directly in equity until the

investment is derecognised or determined to be impaired at which time the cumulative gain or loss previously recorded in equity is recognised in the income statement.

Fair value

The fair value of investments that are actively traded in organised financial markets is determined by reference to quoted market bid prices at the close of business on the balance sheet date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's 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.

Amortised cost

Loans and receivables are measured at amortised cost. This is computed using the effective interest method less any allowance for impairment. The calculation takes into account any premium or discount on acquisition and includes transaction costs and fees that are an integral part of the effective interest rate.

Impairment of financial assets

The Group assesses at each balance sheet date whether a financial asset or group of financial assets is impaired.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on assets carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not been incurred) discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition). The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss shall be recognised in the income statement. 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 recognised, the previously recognised impairment loss is reversed, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date. Any subsequent reversal of an impairment loss is recognised in the income statement. For more information in relation to trade receivables see Note 3.3.

Available-for-sale financial investments

If an available-for-sale asset is impaired, an amount comprising the difference between its cost (net of any principal payment and amortisation) and its current fair value, less any impairment loss previously recognised in the income statement, is transferred from equity to the income statement. Reversals in respect of equity instruments classified as available-for-sale are not recognised in the income statement. Reversals of impairment losses on debt instruments are reversed through the income statement, if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss was recognised in the income statement.

3.10 Borrowings

Borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are measured at amortised cost using the effective interest

method; any difference between the fair value of the consideration received (net of transaction costs) and the unwinding of discount is recognised as an interest expense over the period of the borrowings.

Interest costs on borrowings to finance the construction of property, plant and equipment are capitalised, during the period of time that is required to complete and prepare the asset for its intended use. All other borrowing costs are expensed.

3.11 Income Taxes

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

Deferred income taxes are provided for all temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes, except where the deferred income tax arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

A deferred tax asset is recorded only to the extent that it is probable that taxable profit will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured at tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on tax rates that have been enacted or substantively enacted at the balance sheet date.

Deferred tax assets and deferred tax liabilities can be offset only if: (a) a Group entity has a legally enforceable right to set off current tax assets against current tax liabilities; and (b) the deferred tax assets and the deferred tax liabilities relate to income taxes levied by the same taxation authority on either: (i) the same taxable entity; or (ii) different taxable entities which intend either to settle current tax liabilities and assets on a net basis, or to realise the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, associates and joint ventures, except where the timing of the reversal of the temporary difference can be controlled and it is probable that the temporary difference will not reverse in the foreseeable future.

The effect from a change in tax rates is recognized in income statement except to the extent that it relates to items previously charged or credited to equity. In particular, this policy is applicable to deferred taxes recorded to equity at the date of transition to IFRS for deemed cost of property, plant and equipment.

3.12 Leases

Operating lease payments are recognised as an expense in the income statement on a straight line basis over the lease term.

3.13 Derecognition of Financial Assets and Liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when the rights to receive cash flows from the asset have expired.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the income statement.

3.14 Provisions

Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate of the amount can be made.

Expense relating to any provision is presented in the income statement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects where appropriate the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognised as a finance cost.

3.15 Equity

Share capital

Ordinary shares are classified as equity.

Dividends

Dividends declared by Group subsidiaries are recognised as a liability and deducted from equity at the balance sheet date only if they are declared before or on the balance sheet date. Such dividends are disclosed when they are proposed before the balance sheet date or proposed or declared after the balance sheet date but before the consolidated financial statements are authorised for issue.

3.16 Revenue Recognition

Revenues are recognised when the title passes to the customer, assuming that collection is reasonably assured and sales price to final customers is fixed or determinable. Revenues are measured at the fair value of the consideration received or receivable.

3.17 Employee Benefits

Under provision of the Russian legislation, social contributions are made through a unified social tax ("UST") calculated by the Group by the application of a regressive rate (from 26% to 2%) to the annual gross remuneration of each employee. The Group allocates the UST to three social funds (state pension fund, social and medical insurance funds), where the rate of contributions to the pension fund varies from 20% to 2% depending on the annual gross salary of each employee. The Group's contributions relating to UST are expensed in the year to which they relate. Total contributions for UST amounted to RR 270,770 during the year ended 31 December 2008 (2007: RR 244,179) and they were classified as labour costs in these consolidated financial statements.

3.18 Foreign Currency Transactions

The consolidated financial statements are presented in the national currency of the Russian Federation, Russian Rouble (RR), which is the functional currency of the Company and its Russian subsidiaries. Transactions in foreign currencies are initially recorded in the functional currency at the exchange rate ruling at the date of transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the balance sheet date. All resulting differences are taken to the income statement. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

The functional currency of the foreign operations is the United States dollar (US$). As at the reporting date, the assets and liabilities of that subsidiary are translated into the presentation currency of the Group (the Russian Rouble) at the rate of exchange ruling at the balance sheet date and its income statement is translated at the weighted average exchange rate for the year. The exchange differences arising on the translation are taken directly to a separate component of equity. In 2008 and 2007, the foreign subsidiaries did not perform any operations and held minor assets and liabilities, therefore its translation into the presentation currency had no effect on these consolidated financial statements.

3.19 Impairment of Non-Financial Assets

The Group assesses at each reporting date whether there is any indication that an asset may be impaired. The assets subject to such assessment are primarily property, plant and equipment and trade marks. If any such indication exists, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or group of assets. Where the carrying amount of an asset exceeds its recoverable

amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the assets.

4. Significant Accounting Judgements and Estimates

The key assumptions concerning the future and other key sources of estimation uncertainty at the balance sheet date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Useful life of property, plant and equipment and intangible assets

The Group assesses the remaining useful lives of items of property, plant and equipment and intangible assets at least at each financial year end. If expectations differ from previous estimates, the changes are accounted for as a change in an accounting estimate in accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors". These estimates may have a material impact on the amount of the carrying values of property, plant and equipment and intangible assets and on depreciation and amortization recognised in the income statement.

Impairment of non-financial assets

The determination of impairments involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment. The determination of the recoverable amount of a cash-generating unit involves the use of estimates by management. Methods used to determine the value in use include discounted cash flow-based methods, which require the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. These estimates, including the methodologies used, may have a material impact on the fair value and ultimately the amount of any asset impairment.

The following factors are considered in assessing impairment of major specific assets of the Group:

Property, plant and equipment: changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists.

Trade marks: changes in current competitive conditions, changes in the regulations, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, introduction of alternative products on the market and other changes in circumstances that indicate impairment exists.

Impairment of goodwill

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also

to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2008 and 2007 was RR 1,180,469. More details are provided in Note 9.

Allowance for doubtful accounts

The Group maintains an allowance for doubtful accounts to account for estimated losses resulting from the inability of customers to make required payments. When evaluating the adequacy of an allowance for doubtful accounts, management bases its estimates on the aging of accounts receivable balances and historical write-off experience, customer credit worthiness and changes in customer payment terms. If the financial condition of customers were to deteriorate, actual write-offs might be higher than expected. As at 31 December 2008, allowances for doubtful accounts have been created in the amount of RR 568,676 (2007: RR 167,933). More details are provided in Note 12.

Allowance for obsolete and slow moving inventory

The Group determines the allowance for obsolete or slow moving items of inventories based on their expected future use and realizable value. The net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of sale or distribution. Selling prices and costs to sale are subject to change as new information becomes available. Revisions to the estimates may significantly affect future operating results.

Fair value of derivatives

The fair value of derivatives is determined using valuation techniques. These valuation techniques are based on assumptions such as future interest rate changes and the applicable notional amount. Management believes the estimated fair values resulting from the valuation technique which are recorded in the balance sheet and the related changes in the fair values recorded in the statement of changes in equity are reasonable and the most appropriate at the balance sheet date.

Current taxes

Russian tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group's entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Group's entities may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As of 31 Decem-

ber 2008 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. More details are provided in Note 26.

5. Acquisitions and de-recognition of minority interests and other acquisitions

5.1 Acquisition of Afobazol trade mark

In August 2008, the Company signed contracts with shareholders of Donelle Company Limited (Cyprus) – "Donelle" with the purpose of acquiring the Afobazol trade mark through the purchase of all outstanding Donelle shares. On 10 October 2008 all shares of Donelle were transferred to the Company.

Donelle is the sole shareholder of CJSC Aphopharm – "Aphopharm". Aphopharm is a holder of the Afobazol trade mark being its only asset. The acquisition was accounted for as an acquisition of a productive assets (see note 3.1) and the consideration payable amounting to RR 2,228,620 was allocated fully to the trade mark (see Note 9).

As at 31 December 2008 a total of RR 235,000 was still payable to the former shareholders of Donelle. An addendum to the original contract with the former shareholders of Donelle was concluded on 12 March 2009 (Note 28).

5.2 Acquisitions and de-recognition of minority interests

In 1st quarter 2008, the Company's management approved a plan to acquire minority interests in several subsidiaries. As a result, the Company acquired a further 6% interest in OJSC "Pharmstandard-Ufavita", 4% interest in OJSC "Pharmstandard-Octyabr", 1% interest in OJSC "Pharmstandard-Leksredstva" and 11% interest in OJSC "TZMOI", resulting in an increase in the Company's interests in OJSC "Pharmstandard-Ufavita", OJSC "Pharmstandard-Octyabr", OJSC "Pharmstandard-Leksredstva" and OJSC "TZMOI" to 100%, 97%, 100% and 100%, respectively. Total consideration paid in cash for the acquired minority interests was RR 501,740. The difference of RR 129,115 between the total consideration and the carrying amount of the minority interests acquired of RR 372,625 was debited directly to equity.

In accordance with Russian regulations in respect of joint stock companies with a controlling shareholder interest of more than 95% and in accordance with the approved plan on acquisition of minority interests, the Group derecognised the remaining minority interest of 3% in OJSC "Pharmstandard-Octyabr". At the time of derecognition, the carrying value of the minority interest amounted to RR 24,113 and the liability to minority shareholders amounted to RR 24,606 (Note 17). This liability was measured based on the unconditional shares purchase value offered by the Company to the minority shareholders in accordance with the regulations. The difference of RR 493 between the total unconditional shares purchase value offered to the minority shareholders and the carrying amount of the minority interests derecognised was debited directly to equity.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

6. Segment Information

The Group is organised into two main business segments: (1) production and wholesale of pharmaceutical products and (2) production and wholesale of medical equipment. The second segment arose as a result of the acquisition of OJSC "TZMOI" in 2005 and is entirely represented by OJSC "TZMOI".

Segment assets consist primarily of property, plant and equipment, intangible assets, inventories, receivables and operating cash. There were no assets unallocated to segments as of 31 December 2008 and 2007. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate liabilities. Segment result is segment revenue less segment expenses. Segment expenses consist of cost of sales, selling and distribution costs, general and administrative expenses and other income and expenses that can be directly attributed to the segment on a reasonable basis. Capital expenditure comprises additions to property, plant and equipment. Impairment loss and provisions relate only to those charges made against allocated assets.

The following table presents revenue and profit and certain asset and liability information regarding the Group's business segments:

Year ended 31 December 2008	Production and wholesale of pharmaceutical products	Production and wholesale of medical equipment	Eliminations	Group
Sales to external customers	13,260,214	1,075,653	–	14,335,867
Total revenue	**13,260,214**	**1,075,653**	–	**14,335,867**
Gross profit	8,405,364	353,035	–	8,758,399
Segment result	**4,694,120**	**225,989**	–	**4,920,109**
Financial expense, net				(232,620)
Profit before income tax				4,687,489
Income tax expense				(1,184,381)
Profit for the year				**3,503,108**
Segment assets	17,018,798	1,191,534	–	18,210,332
Total assets	17,018,798	1,191,534	–	18,210,332
Segment liabilities	**1,983,319**	**87,224**	–	**2,070,543**
Unallocated liabilities				3,525,397

Year ended 31 December 2008	Production and wholesale of pharmaceutical products	Production and wholesale of medical equipment	Eliminations	Group
Total liabilities				**5,595,940**
Capital expenditure (Note 8)	672,172	40,248	–	712,420
Intangible assets acquisition (Note 9)	2,228,620	–	–	2,228,620
Depreciation and amortisation	553,693	50,511	–	604,204
Impairment loss	174,022	25,727		199,749

Year ended 31 December 2007	Production and wholesale of pharmaceutical products	Production and wholesale of medical equipment	Eliminations	Group
Sales to external customers	9,762,637	1,608,708	–	11,371,345
Total revenue	**9,762,637**	**1,608,708**	–	**11,371,345**
Gross profit	6,127,524	724,072	–	6,851,596
Segment result	**4,163,254**	**450,333**	–	**4,613,587**
Financial expense, net				(291,638)
Profit before income tax				4,321,949
Income tax expense				(1,058,709)
Profit for the year				**3,263,240**
Segment assets	13,711,609	1,582,516	–	15,294,125
Total assets	13,711,609	1,582,516	–	15,294,125
Segment liabilities	**1,208,628**	**96,362**	–-	**1,304,990**
Unallocated liabilities				4,386,442
Total liabilities				**5,691,432**
Capital expenditure (Note 8)	446,758	37,375	–	484,133
Intangible assets acquisition (Note 9)	165,220	–	–	165,220
Depreciation and amortisation	466,755	60,845	–	527,600
Impairment loss		42,403		42,403

The Group considers that there is only one geographical segment – Russian Federation and does not present information on secondary segments.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

7. Balances and Transactions with Related Parties

In accordance with IAS 24 "Related Party Disclosures", parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions or if parties are under common control (this includes parents, subsidiaries and fellow subsidiaries). In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

Related parties may enter into transactions which unrelated parties might not enter, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The nature of the related party relationships for those related parties with whom the Group entered into transactions or had balances outstanding at 31 December 2008 and 2007 are detailed below.

Balances with related parties:

2008	Short-term financial assets Note 14	Cash and cash equivalents Note 13 (b)	Trade payables, other payables and accruals – (a) Note 17
Other related parties[1]	–	92,930	6,495
Total	–	**92,930**	**6,495**

2007	Short-term financial assets Note 14	Cash and cash equivalents Note 13 (b)	Trade payables, other payables and accruals – (a) Note 17
Other related parties[1]	5,111	168,836	6,990
Total	**5,111**	**168,836**	**6,990**

(a) This balance represented cash at a bank controlled by a related party.
(b) This balance represented obligation for the license fee, described in section "Transactions with related parties" below.

1 Other related parties represent entities under control of the Company's shareholders having significant influence over the Company.

Major conditions of the loans included in short-term financial assets above are as follows:

Caption	Interest rate %		Maturity period	
	2008	2007	2008	2007
Current loans to related parties	–	2%	–	3 months

Cash balances with the related bank carry no interest. Cash equivalents at 31 December 2008 were represented by deposits with the related bank and carry 9% interest p.a.

Transactions with related parties included in the income statement:

Income Statement caption	Relationship	2008	2007
License fee (included in distribution costs) (A)	Other related parties[1]	23,231	24,522
Warehouse rental expenses (included in distribution costs) (B)	Other related parties[1]	32,108	30,532
Office rental expenses (included in general and administrative expenses) (B)	Other related parties[1]	19,188	14,473

(A) License fee

Licence fee is paid for use of several trade marks owned by an entity under common control. The license fee is paid on a quarterly basis as 5% of the licensed products output applying the standard price list of the Group.

(B) Rental expenses

The Group incurred warehouse and office rental expenses that is payable to an other related party.

Acquisition of intangible assets

In 2007, the Group acquired an intangible asset (trade mark) for RR 160,000 from an other related party.

Compensation to key management personnel

Key management personnel comprise 3 persons as at 31 December 2008 and 2007. Total compensation to key management personnel, amounted to RR 35,224 for the year ended 31 December 2008 (2007: RR 82,257). Such compensation represented the following short-term employee benefits: (i) payroll and bonuses included in general and administrative expenses and (ii) for the year ended 31 December 2007 one-off remuneration for achievement of the IPO-related targets (Notes 18 and 23) included in other expenses in the income statement.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

8. Property, Plant and Equipment

Property, plant and equipment consist of the following:

31 December 2008	Land	Buildings	Plant and machinery	Equipment and motor vehicles	Assets under construction	Total
Cost						
Balance at 31 December 2007	32,982	1,810,835	1,939,827	206,696	430,861	4,421,201
Additions	4	147	107,641	89,701	514,927	712,420
Transfers	–	157,210	305,242	3323	(465,775)	–
Disposals	–	(8,855)	(29,800)	(17,352)	(15,424)	(71,431)
Balance at 31 December 2008	**32,986**	**1,959,337**	**2,322,910**	**282,368**	**464,589**	**5,062,190**
Accumulated Depreciation						
Balance at 31 December 2007	–	158,579	515,168	56,188	–	729,935
Depreciation charge	–	56,423	279,846	58,542	–	394,811
Disposals	–	(3,250)	(24,513)	(11,088)	–	(38,851)
Impairment charge (a)	–	1,497	24,201	29	33,459	59,186
Balance at 31 December 2008	**–**	**213,249**	**794,702**	**103,671**	**33,459**	**1,145,081**
Net Book Value						
Balance at 31 December 2007	**32,982**	**1,652,256**	**1,424,659**	**150,508**	**430,861**	**3,691,266**
Balance at 31 December 2008	**32,986**	**1,746,088**	**1,528,208**	**178,697**	**431,130**	**3,917,109**

31 December 2007	Land	Buildings	Plant and machinery	Equipment and motor vehicles	Assets under construction	Total
Cost						
Balance at 31 December 2006	37,654	1,813,350	1,933,214	146,531	228,168	4,158,917
Additions	8,059	–	17,598	67,086	391,390	484,133
Transfers to non-current assets classified as held for sale	(12,731)	–	(81,983)	(1,408)	(79,079)	(175,201)
Transfers	–	–	89,815	10,309	(100,124)	–
Disposals	–	(2,515)	(18,817)	(15,822)	(9,494)	(46,648)
Balance at 31 December 2007	**32,982**	**1,810,835**	**1,939,827**	**206,696**	**430,861**	**4,421,201**
Accumulated Depreciation						
Balance at 31 December 2006	–	111,325	228,123	30,888	–	370,336
Depreciation charge	–	48,890	273,907	34,421	–	357,218
Transfers to non-current assets classified as held for sale	–	–	(13,579)	(378)	–	(13,957)
Disposals	–	(1,636)	(15,686)	(8,743)	–	(26,065)
Impairment charge (b)	–	–	42,403	–	–	42,403
Balance at 31 December 2007	**–**	**158,579**	**515,168**	**56,188**	**–**	**729,935**
Net Book Value						
Balance at 31 December 2006	**37,654**	**1,702,025**	**1,705,091**	**115,643**	**228,168**	**3,788,581**
Balance at 31 December 2007	**32,982**	**1,652,256**	**1,424,659**	**150,508**	**430,861**	**3,691,266**

(a) Impaired assets represented (i) a workshop building which construction was started several years ago but then management decided to continue with the existing premises and (ii) equipment for production of medical devices removed from active use due to decline in customer demand. The impairment charge equals to the carrying value of those building and equipment.

(b) Impaired assets represented property and equipment for production of needles for syringes which was terminated by the Group due to low profitability. The impairment charge equals to the carrying value of that equipment.

The Group did not use borrowings to finance capital expenditures, thus no interest expense was capitalized in 2008 and 2007.

The Group assets include only a minor portion of the land on which the Group's factories and buildings, comprising the Group's principal manufacturing facilities, are located, whilst the major portion of the land is held under operating lease agreements with the state municipal bodies. The lease agreements specify lease terms between 10 and 50 years with an option to prolong the lease term for another 10 years. In addition, the lease agreements include a purchase option after termination of the lease. Purchase price will be determined based on fair value of the land as determined by the municipal authorities. The total amount of rental payments for the use of the land during 2008 was RR 8,397 (2007: RR 8,382). Such payments are reassessed by the state authorities on an annual basis. No such reassessment has been completed for 2009.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

In 2008, several social objects (buildings of a former kindergarden unused for several years) with zero carrying value were sold to municipality for a cash consideration of RR 34,107 and the respective gain was recognised in the income statement.

9. Intangible Assets

	Goodwill	Trademarks	Total
Cost			
Balance at 31 December 2007	1,180,469	3,527,688	4,708,157
Additions (a)	–	2,228,620	2,228,620
Balance at 31 December 2008	**1,180,469**	**5,756,308**	**6,936,777**
Accumulated Amortisation			
Balance at 31 December 2007	–	239,680	239,680
Impairment (b)	–	140,563	140,563
Amortisation expense	–	209,393	209,393
Balance at 31 December 2008	**–**	**589,636**	**589,636**
Net Book Value			
Balance at 31 December 2007	**1,180,469**	**3,288,008**	**4,468,477**
Balance at 31 December 2008	**1,180,469**	**5,166,672**	**6,347,141**

	Goodwill	Trademarks	Total
Cost			
Balance at 31 December 2006	1,180,469	3,362,468	4,542,937
Additions (Note 7)	–	165,220	165,220
Balance at 31 December 2007	**1,180,469**	**3,527,688**	**4,708,157**
Accumulated Amortisation			
Balance at 31 December 2006	–	69,298	69,298
Amortisation expense	–	170,382	170,382
Balance at 31 December 2007	**–**	**239,680**	**239,680**
Net Book Value			
Balance at 31 December 2006	**1,180,469**	**3,293,170**	**4,473,639**
Balance at 31 December 2007	**1,180,469**	**3,288,008**	**4,468,477**

(a) Additions during 2008 represented acquisition of Afobazol trade mark (see note 5.1).

(b) The impairment mainly relates to the effect of higher discount rates used in the value in use calculations of trademarks that were tested for impairment. The increase in discount rates from 13% to 18.1% for the first 10 years and declining thereafter, mainly relates to the effect of the current financial crisis.

Carrying amount and remaining amortization period of major trade marks as of 31 December are as follows:

Name	Carrying amount		Remaining amortization period (years)	
	2008	2007	2008	2007
Afobazol	2,060,199	-	20	-
Arbidol	1,818,691	1,922,123	17	18
Flucostat	707,496	747,733	17	18

Impairment testing of goodwill

Goodwill acquired through business combinations before 2008 has been allocated for impairment testing purposes to the following groups of cash-generating units, which are also reportable segments of the Group:

- production and wholesale of pharmaceutical products group of units ("Pharmaceuticals"); and
- production and wholesale of medical equipment group of units ("Equipment").

Carrying amount of goodwill allocated to each group of cash generating units:

	Pharmaceuticals		Equipment		Total	
	2008	2007	2008	2007	2008	2007
Carrying amount of goodwill	961,615	961,615	218,854	218,854	1,180,469	1,180,469

The recoverable amount of the cash-generating units has been determined based on a value in use calculation using cash flow projections based on financial budgets approved by management covering a five-year period and cash flows beyond the five-year period are extrapolated using a 24% and 5% growth rate that is the same as the mid-term average growth rate for Pharmaceuticals and Equipment groups of cash-generating units, respectively. The discount rate applied to cash flow projections is 18.1%.

Key assumption used in value in use calculations

The calculation of value in use for both Pharmaceuticals and Equipment groups of cash-generating units are most sensitive to the following assumptions:

- Discount rates;
- Raw material price inflation;
- Currency rates changes;

Growth rate used to extrapolate cash flows beyond the budget period.

Discount rates – Discount rates reflect management's estimate of the risks specific to each group of units. This is the benchmark used by management to assess operating performance and to evaluate future investment proposals. In determining appropriate discount rates for each group of units, regard has been given to the Capital Assets Pricing Model calculation at the beginning of the budgeted year.

Raw material price inflation – past actual raw materials price movements, including the effect of the devaluation of the Russian Ruble for US dollar denominated raw materials, have been used as an indicator of future price movements.

Currency exchange rates changes – estimated values based on current market values.

Growth rate estimates – rates are based on published industry research.

Sensitivity to changes in assumptions

Management believes that no reasonably possible change in any of the above key assumptions would cause the carrying value of the group of units to materially exceed its recoverable amount.

10. Non-Current Assets Classified as Held for Sale

Sale of non-current Assets Classified as Held for Sale

"TMK" LLC (Note 1) was sold during the first quarter of 2008 for a cash consideration of RR 122,169. This arrangement resulted in a loss amounting to RR 13,953 that was recognised in the income statement (Note 23).

The remainder of the non-current Assets Classified as Held for Sale in the balance sheet as at 31 December 2007 amounted to RR 18,855 and represented some non-current assets located in St.Petersburg. These assets were sold in the first quarter of 2008 for a cash consideration of RR 18,917 (Note 23).

Part of the cash consideration for "TMK" LLC and other non-current Assets Classified as Held for Sale, totalling RR 17,831, was collected in advance in 2006 and 2007.

11. Inventories

Inventories consist of the following:

	2008	2007
Raw materials – at cost	1,113,174	841,703
Work in progress – at cost	179,319	134,554
Finished goods:		
– at cost	1,216,896	851,052
– at net realisable value	1,192,417	783,938
	2,484,910	**1,760,195**

Movements in allowance for impairment of inventories consist of the following:

	2008	2007
Balance at 1 January	67,114	35,607
Additional allowance	–	43,224
Unused amounts reversed	(6,675)	–
Utilised during the year	(35,961)	(11,717)
Balance at 31 December	24,479	67,114

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

12. Trade Receivables

	2008	2007
Trade receivables (net of allowance for impairment of receivables of RR 568,676 (2007: RR 167,933))	4,761,359	4,176,200
	4,761,359	**4,176,200**

At 31 December 2008 RR 172,870 of trade receivables were denominated in currencies other than Russian Roubles, primarily in US$ (2007: RR 129,304).

Movements in allowance for impairment of trade receivables consist of the following:

	2008	2007
Balance at 1 January	167,933	79,308
Additional allowance	484,194	95,483
Unused amounts reversed	(53,977)	–
Utilised during the year	(29,474)	(6,858)
Balance at 31 December	**568,676**	**167,933**

The additional allowance for impairment in 2008 includes RR 476,131 in relation to the bankruptcy of one of the Group's distributors CJSC "Genesis" (Note 21).

13. Cash and Cash Equivalents and Bank Overdraft

Cash and cash equivalents consist of the following:

	2008	2007
Cash in bank – Russian Roubles	183,688	119,126
Cash in bank – US$ and Euro	2,378	13,463
Short-term bank deposits with original maturity less than 90 days – Russian Roubles	–	60,000
	186,066	**192,589**

On 3 December 2007 the Company entered into an overdraft facility agreement with Citibank ZAO for RR 40,000 with an interest of 14% per annum. The overdraft and related interest accrued is payable monthly. Citibank

retains the right to immediately demand full repayment of the outstanding overdraft amount and interest accrued. On 8 February 2008 the amount of overdraft was increased to RR 200,000 and on 25 December 2008 the interest was increased from 14% to 18% per annum.

14. Financial Assets

Short-term financial assets at fair value through profit or loss

	2008	2007
Promissory notes	104,300	81,300
Loans to related parties (Note 7)	–	5,111
Trading securities and other	9,695	25,488
	113,995	**111,899**

Long-term financial assets at fair value through profit or loss

	2008	2007
Non-listed shares	–	245,398
	–	**245,398**

In December 2007, the Group acquired 19.88% of "Dipaka Trading Limited", a company registered under the laws of Cyprus, for a cash consideration of US$10 million (RR 245,398). The investment in Dipaka Trading Limited was sold in the fourth quarter of 2008 for RR 268,944. A gain on disposal amounting to RR 23,546 was recognised in the income statement.

15. Borrowings and Loans

	2008	2007
Long-term borrowings and loans		
(a) Syndicated borrowing organised by Citibank ("Citibank loan")	2,328,985	3,256,151
(b) Other loans	14,249	8,799
Less: Current portion of long-term borrowings and loans	(1,582,722)	(1,310,374)
	760,512	**1,954,576**

Long-term debt is repayable as follows:

	2008
1 to 2 years	380,182
2 to 3 years	380,330
	760,512

As at 31 December 2008 and 2007 all the borrowings are US$ denominated. The foreign exchange risk in this respect is not covered by any derivative instruments.

(a) The Citibank loan was provided in December 2006 in two credit facilities:

- Facility A in the total amount of US$ 91 million with maturity period of 3 years; and
- Facility B in the total amount of US$ 55 million with maturity period of 5 years.

Interest rate for facility A was initially established as 3 month LIBOR plus margin of 1.50% p.a.

Interest rate for facility B was initially established as 3 month LIBOR plus margin of 1.90% p.a.

On 18 December 2008 several banks, representing 52.27% of the syndicate in the Citibank loan, declared that a market disruption event occurred in relation to their loan balances. In accordance with the Citibank loan agreement the interest rate quoted by those banks for the next interest period was determined based on the actual cost of funding for each individual bank (which was higher than LIBOR and was ranging from 2.46% p.a. to 5% p.a.) plus the standard margin of 1.50% p.a. for facility A and 1.90% p.a. for facility B. This change was effective only for the interest period ending 18 March 2009 and since that date interest rate for the both facilities is determined based on the initial conditions, i.e. 3 month LIBOR plus the standard margin per facility.

In September 2007, when LIBOR rate interest was approximately 5.7%, the Group entered into an Interest Rate Swap agreement in respect to all interest payments due in respect to the Citibank loan basically swapping the LIBOR rate interest obligations into a fixed rate of 4.932% per annum. In this manner the Group protects itself against fluctuations of LIBOR rates. For more details see Note 27.

The Citibank loan is secured by guarantees issued by all the Group's subsidiaries.

The Citibank loan agreement establishes certain financial ratios, restrictions on disposal of assets and distribution of dividends.

In 2008, the Group repaid US$ 53,384 thousand (RR 1,337,232) of the Citibank loan (2007: US$ 13,346 thousand (RR 329,726)).

(b) Other loans mature in September 2009 and bear fixed interest rate 5-7% per annum.

16. Other Taxes Payable

Taxes payable, other than income tax, are comprised of the following:

	2008	2007
Value-added tax	292,064	157,585
Property and other taxes	47,243	55,221
	339,307	**212,806**

17. Trade and Other Payables and Accruals

	2008	2007
Trade payables	1,193,029	766,007
Payable for Afobazol trade mark acquisition (Notes 5.1 and 28)	235,000	–
Payable for minority interests acquisitions (Note 5.2)	24,606	–
Other payables – related party (Note 7)	6,495	6,990
Other payables and accruals	248,414	273,523
	1,707,544	**1,046,520**

At 31 December 2008 RR 527,018 of trade payables were denominated in currencies other than Russian Rouble, primarily in US$ (2007: RR 274,167).

18. Share Capital

In accordance with its charter documents the share capital of the Company is RR 37,793. The authorised number of ordinary shares is 37,792,603 with par value of 1 (one) Russian Ruble. All authorised shares are issued and fully paid. There were no transactions with own shares during 2008.

As at 31 December 2008 and 2007 more than half of voting shares of OJSC "Pharmstandard" were held by "Augment Investments Limited" ("Augment"), a company registered under the laws of Cyprus. On 26 March 2008, Victor Kharitonin, a Russian citizen, obtained control over more than a half of voting shares of the Company. He became the Group's ultimate controlling party since that date.

In May 2007 16,349,408 ordinary shares representing 43.3 percent of share capital of the Company were sold by Augment to public investors as a result of the Initial Public Offering conducted simultaneously at Russian stock exchanges (RTS and MICEX) where 18.3% of the shares were offered and at the London stock exchange (LSE) where the remaining 25% were offered.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

In addition, in May 2008, 944,815 ordinary shares representing 2.5 % of share capital of the Company were sold by Augment and were offered at LSE. After this transaction, 45.6% of share capital was publicly listed of which 27.5% on LSE.

In accordance with Russian legislation, dividends may only be declared from accumulated undistributed and unreserved earnings as shown in Russian statutory financial statements. The Company had approximately RR 6,152,441 of undistributed and unreserved earnings as at 31 December 2008 (2007: RR 3,779,003). In addition, the Company's share in the undistributed and unreserved earnings of the subsidiaries was approximately RR 9,826,453 as at 31 December 2008 (2007: RR 7,698,340).

In accordance with the Citibank loan agreement (Note 15) the Group shall not pay, make or declare any dividend or other distribution without the prior written consent of the lenders.

Earnings per share are calculated by dividing the net income attributable to ordinary shareholders by the weighted average number of ordinary shares in issue during the period. The Group has no dilutive potential ordinary shares; therefore, the diluted earnings per share equal basic earnings per share.

Earnings per Share

Earnings per share are as follows:

	2008	2007
Weighted average number of ordinary shares outstanding	37,792,603	37,792,603
Profit for the year attributable to the shareholders	3,504,046	3,227,895
Basic and diluted earnings per share, Russian Roubles	92.72	85.41

19. Revenue

The Group's products are divided into pharmaceuticals, including products sold in the OTC ("Over-the-counter") market or with a prescription, and medical equipment and disposables.

Sales breakdown by product groups comprised the following:

Product group	2008	2007
PHARMACEUTICAL PRODUCTS		
OTC		
Branded	9,087,126	7,427,511
Non-branded	1,466,262	1,092,351
	10,553,388	**8,519,862**
Prescription		
Branded	2,349,202	937,999
Non-branded	288,355	250,201
	2,637,557	**1,188,200**
Other	69,269	54,575
Total pharmaceutical products (a)	**13,260,214**	**9,762,637**
Medical equipment and disposables	**1,075,653**	**1,608,708**
	14,335,867	**11,371,345**

(a) In Russia, classification of pharmaceuticals as prescription products (Rx) or non-prescription over-the-counter products (OTC) is regulated by the government and is periodically re-visited. The recent re-visiting of OTC and Rx products classification introduced in 2008 had a significant influence of the Group's product portfolio structure. For the purpose of comparative analysis, the prior year figures were restated accordingly. The above changes in the Group portfolio structure do not affect the sales results.

20. Cost of Sales

The components of cost of sales were as follows:

	2008	2007
Materials and components	4,102,248	2,997,475
Production overheads	734,949	815,557
Depreciation and amortisation	535,583	481,309
Direct labour costs	204,688	225,408
	5,577,468	**4,519,749**

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

21. Selling and Distribution Costs

Selling and distribution costs were as follows:

	2008	2007
Advertising	1,061,815	753,580
Labour costs	476,985	397,082
Freight, communication and insurance of goods in transit	122,246	126,817
Trainings and other services	47,009	26,492
Certification expenses	29,996	29,092
Rent	35,873	35,211
Commission and license fee	36,886	105,681
Materials, maintenance and utilities	42,834	43,969
Travel and entertainment	56,148	43,986
Depreciation	45,201	27,920
Allowances for impairment of receivables (see Note 12)	476,131	–
Other expenses	35,717	36,211
	2,466,841	**1,626,041**

The Group entered into a number of operating lease agreements for warehouses. Rental agreements are revised on an annual basis. Future minimum operating lease payments classified as selling and distribution costs will not substantially change in 2009 compared to 2008.

22. General and Administrative Expenses

General and administrative expenses were as follows:

	2008	2007
Labour costs	403,121	356,500
Utilities and services	63,002	48,050
Travel and entertainment	15,494	10,783
Taxes other than income tax	15,213	17,589
Property insurance	14,756	13,481
Freight and communication	26,171	20,142
Depreciation	23,420	18,371
Rent	26,520	34,286
Materials and maintenance	24,777	19,745
Other	43,774	31,572
	656,248	**570,519**

The Group entered into a number of operating lease agreements for office premises. Rental agreements are revised on an annual basis. Future minimum operating lease payments classified as are general and administrative expense will not substantially change in 2009 compared to 2008.

23. Other Income and Other Expenses

Other income comprised the following:

	2008	2007
Income from non-core operations (a)	107,220	–
Gain from disposal of property, plant and equipment and investments property	18,996	3,556
Gain from disposal of long-term financial assets	23,546	–
Gain from sale of non-current assets classified as held for sale (Note 10)	–	11,478
Foreign exchange gain, net	–	259,098
	149,762	**274,142**

(a) Income from non-core operations includes agency fee and reimbursement of marketing and promotional expenses incurred in respect of certain products.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

Other expenses comprised the following:

	2008	2007
Foreign exchange loss, net	524,842	–
Impairment of equipment (Note 8)	59,186	42,403
Impairment of intangible assets (Note 9)	140,563	–
Legal, audit, one-off management remuneration (Note 7) and other non-recurring expenses incurred in connection with the IPO (Note 18)	–	110,016
Charity	1,959	4,114
Other taxes	93,784	56,381
Impairment of other short-term financial assets	3,715	13,657
Loss recognised on non-current assets classified as held for sale (Note 10)	13,891	24,101
Other	27,023	64,919
	864,963	**315,591**

24. Financial Income and Expense

Financial income and expense comprised the following:

	2008	2007
Interest income:		
Income from changes of fair value of financial assets recognised in the income statement	–	10,578
Income from Interest Rate Swap (Notes 15 and 27)	–	6,790
Interest income from loans and deposits	22,569	11,361
	22,569	**28,729**
Interest expense:		
Loss from changes of fair value of financial assets recognised in the income statement	8,457	–
Loss from Interest Rate Swap (Notes 15 and 27)	43,608	–
Expense from changes in fair value of the Interest Rate Swap (Notes 15 and 27)	44,490	44,598
Interest expense on borrowings and loans	158,634	275,769
	255,189	**320,367**

25. Income Tax

	2008	2007
Income tax expense – current	1,458,057	1,106,218
Correction of prior periods after reconciliation with tax authorities (a)	–	(14,480)
Deferred tax credit – effect from change in profit tax rate (b)	(116,374)	–
Deferred tax credit – origination and reversal of temporary differences	(157,302)	(33,029)
Income tax expense	**1,184,381**	**1,058,709**

(a) The Group identified overpayment of income tax in prior periods as a result of routine reconciliation with tax authorities. As a result, the respective receivable from the budget was recognised as at 31 December 2007.

(b) On 20 November 2008, the Russian Government enacted a law which reduced the statutory income tax rate from 24% to 20% effective from 1 January 2009. This reduction in the statutory income tax rate is reflected in the deferred tax balances as at 31 December 2008.

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

Income before taxation for financial reporting purposes is reconciled to tax expense as follows:

	2008	2007
Profit before income tax	4,687,489	4,321,949
Theoretical tax charge at statutory rate of 24%	1,124,997	1,037,268
Correction of prior periods after reconciliation with tax authorities	–	(14,480)
Effect from change in profit tax rate	(116,374)	–
Tax effect of items which are not deductible or assessable for taxation purposes:		
Non-deductible expenses	87,199	113,788
IFRS adjustments and other items	88,559	(77,867)
Income tax expense	**1,184,381**	**1,058,709**

Movements in deferred tax balances were as follows:

	31 December 2006	Differences recognition and reversal	31 December 2007	Effect from change in profit tax rate recognised in equity	Effect from change in profit tax rate recognised in income statement	Differences recognition and reversal	31 December 2008
Tax effects of deductible temporary differences – asset (liability):							
Property, plant and equipment (Note 8)	(340,988)	(19,371)	(360,359)	34,937	23,286	11,020	(291,116)
Intangible assets (Note 9)	(721,766)	24,740	(697,026)	–	110,792	31,801	(554,433)
Trade and other receivables	(44,957)	49,356	4,399	–	(24,248)	141,090	121,241
Inventories	205	(18,483)	(18,278)	–	(4,222)	43,613	21,113
Trade and other payables and other taxes	21,524	(1,868)	19,656	–	11,025	(85,805)	(55,124)
Financial instruments	–	–	–	–	–	17,817	17,817
Other	5,154	(1,345)	3,809	–	(259)	(2,234)	1,316
Total net deferred tax liability	**(1,080,828)**	**33,029**	**(1,047,799)**	**34,937**	**116,374**	**157,302**	**(739,186)**

The recognition and reversals of temporary differences primarily relates to the following:

- depreciation of property, plant and equipment in excess of the depreciation for tax purposes;
- fair value adjustments on acquisition;
- fair value of financial instruments in excess of the cost of these instruments for tax purpose;
- impairment of trade receivables;
- allowances to write inventory down to net realizable value;
- amortisation of trade marks in excess of the amortisation for tax purposes; and deemed cost adjustments upon conversion to IFRS.

The aggregate amount of temporary differences associated with investments in subsidiaries for which deferred tax liabilities have not been recognised was approximately RR 10,204,820 as at 31 December 2008 (2007: RR 7,698,340).

26. Contingencies, Commitments and Operating Risks

Operating environment of the group

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. The ongoing global financial crisis has resulted in capital markets instability, significant deterioration of liquidity in the banking sector, and tighter credit conditions within Russia. While the Russian Government has introduced a range of stabilization measures aimed at providing liquidity and supporting debt refinancing for Russian banks and companies, there continues to be uncertainty regarding the access to capital and cost of capital for the Group and its counterparties, which could affect the Group's financial position, results of operations and business prospects.

Taxation

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant additional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As at 31 December 2008 management believes that its interpretation of the relevant legislation is appropriate and that the Group's tax, currency and customs positions will be sustained.

Because of the uncertainties associated with the Russian tax and legal systems, the ultimate amount of taxes, penalties and interest assessed, if any, may be in excess of the amount expensed to date and accrued as of 31 December 2008. It is not practical to determine the amount of unasserted claims that may manifest, if any, or the likelihood of any unfavourable outcome. Should the Russian tax authorities decide to issue a claim and prove successful in the court, they would be entitled to recover the amount claimed, together with fines amounting to 20% of such amount and interest at the rate of 1/300 of the Central Bank of Russian Federation rate for

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

each day of delay for late payment of such amount. Management believes that it is not probable that the ultimate outcome of such matters would result in a liability. Therefore, no provision for these contingencies was recorded in these consolidated financial statements.

Insurance policies

The Group holds insurance policies in relation to its property, plant and equipment, which cover majority of property, plant and equipment items. The Group holds no insurance policies in relation to its operations, or in respect of public liability.

27. Financial Instruments and Financial Risk Management Objectives and Policies

Fair values

Set out below is a comparison by category of carrying amounts and fair values of all of the Group's financial instruments except trade receivables and trade and other payables. Management believes that fair value of trade receivables and trade and other payables equal their carrying value.

	2008		2007	
	Fair value	Net carrying value	Fair value	Net carrying value
Financial assets				
Cash and cash equivalents (Note 13)	186,066	186,066	192,589	192,589
Short-term loans to related parties (Note 7)	–	–	5,111	5,111
Promissory notes (Note 14)	104,300	104,300	81,300	81,300
Other short-term investments (Note 14)	9,695	9,695	25,488	25,488
Long-term investment in non-listed shares (Note 14)	–	–	245,398	245,398
Financial liabilities				
Overdraft	199,242	199,242	–	–
Borrowings and loans (Note 15)	2,343,234	2,343,234	3,264,950	3,264,950
Derivative financial instruments	89,087	89,087	44,598	44,598
Other non-current liabilities	34,048	34,048	36,826	36,826

Fair values of long-term borrowings and loans are approximately equal to their carrying value as they are based on variable interest rates (LIBOR). Fair value of other non-current liabilities and derivative financial instruments (see below) has been calculated by discounting the expected future cash flows at prevailing interest rates. Fair value of long-term investment in non-listed shares has been determined by reference to its recent purchase price (see Note 14). Fair values of other items above approximate their carrying amounts due to their short maturity.

Financial risk management objectives and policies

The Group's principal financial instruments comprise bank loans and cash and cash equivalents. The main purposes of these financial instruments are to raise finance for the Group's operations and investment activities. The Group has various other financial assets and liabilities such as promissory notes, trade receivables and trade payables, which relate directly to its operations. During the year the Group did not undertake active trading in financial instruments. To reduce the risk of interest fluctuations related to long term LIBOR borrowings, the Group entered into an interest rate swap agreement (more details see below).

The main risks arising from the Group's financial instruments are interest rate risk, liquidity risk, foreign currency risk and credit risk. Management reviews and agrees policies for managing each of these risks which are summarised below.

Interest rate risk

The Group is exposed to interest rate risk through interest cash flow and market value fluctuations as the majority of interest rates on long-term borrowings are floating and based on LIBOR as disclosed in Note 15.

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 for one year assuming the parallel shifts in the yield curves (through the impact on floating rate borrowings and changes in fair value in respect of the Interest Rate Swap):

	Increase/decrease in basis points	Effect on the income statement (interest expense)	Effect on the income statement (due to fair value change)
As at 31 December 2008			
	200	(46,567)	36,842
	(100)	23,298	(20,918)
As at 31 December 2007			
	200	(65,131)	51,383
	(200)	65,131	(80,720)

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

Foreign exchange risk

The Group has US dollar denominated long-term borrowings (see Note 15) and also certain US dollar denominated trade payables (Note 17) and trade receivables (Note 12). Therefore, the Group is exposed to foreign exchange risk.

The Group monitors the foreign exchange risk by following changes in exchange rates in the currencies in which its cash, payables and borrowings are denominated. However, the Group does not have formal arrangements to mitigate this foreign exchange risk.

The table below shows the sensitivity to a reasonably possible change in the US dollar exchange rate, with all other variables held constant, of the Group's profit before tax:

	Increase/decrease in US$ rate	Effect on profit before tax
As at 31 December 2008		
US$/Roubles exchange rate	+25%	(688,074)
US$/Roubles exchange rate	+10%	(275,230)
As at 31 December 2007		
US$/Roubles exchange rate	+7%	(233,902)
US$/Roubles exchange rate	-7%	233,902

Liquidity risk

The Group's policy is to maintain sufficient cash and cash equivalents or have available funding through an adequate amount of committed credit facilities to meet its operating and financial commitments. The Group performs continuous monitoring of cash deficit risks and continuous monitoring of repayment of its financial liabilities on time. The Group performs daily planning and control cash flow procedures.

The table below summarises the maturity profile of the Group's non-derivative financial liabilities based on contractual undiscounted payments including interest except for trade payables which normally have maturity periods shorter than 4 months.

As at 31 December 2008	Total	Less than 3 months	3 to 6 months	6 to 12 months	1 to 5 years
Borrowings (a)	2,489,338	418,926	418,926	852,102	799,384
Payable for trade mark (Note 28)	235,000	235,000	–	–	–
Other non-current liabilities	80,810	–	–	16,875	63,935
Total	**2,805,148**	**653,926**	**418,926**	**868,977**	**863,319**

As at 31 December 2007	Total	Less than 3 months	3 to 6 months	6 to 12 months	1 to 5 years
Borrowings (a)	3,709,520	379,335	379,335	758,669	2,192,181
Other non-current liabilities	79,825	–	–	12,347	67,418
Total	**3,789,345**	**379,335**	**379,335**	**771,016**	**2,259,599**

(a) The Citibank loan received in 2006 (see Note 15 for details) is including contractual principal amount of a debt and interest rate calculated in according with corresponding terms of the loan agreement at 31 December 2008 and 2007 (Notes 15 and 28).

Credit Risk

Financial assets, which potentially are subject to credit risk, consist principally of trade receivables. The Group has policies in place to ensure that sales of products and services are made to customers with an appropriate credit history. Sales to customers are made in accordance with annually approved Marketing and Credit policy. The Group daily monitors sales and receivables conditions using effective internal control procedures.

The carrying amount of accounts receivable, net of allowance for impairment of receivables, represents the maximum amount exposed to credit risk. Although collection of receivables could be affected by economic factors, management believes that there is no significant risk of loss to the Group beyond the allowance already recorded.

Cash is placed in financial institutions, which are considered at time of deposit to have minimal risk of default.

The table below summarises the Group's trade receivables aging. The allowances for doubtful accounts is allocated on aggregate basis with the Group's allowances for doubtful accounts policy (see Note 4).

						Not impaired but past due	
	Total	Neither impaired nor past due	less 1 month	1-2 months	2-3 months	3 to 6 months	> 6 months
31 December 2008	4,761,359	3,890,073	793,465	54,283	6,013	14,734	2,791
31 December 2007	4,176,200	3,240,772	792,664	66,548	49,989	22,335	3,892

(All amounts are in thousands of Russian Roubles, if not otherwise indicated)

Sales concentration to a small group of customers

The Group works with five distributors that together represent about 50% of the Group's revenue for 2008 and 2007. Given the Russian market structure limited number of large distributors is not unusual. The Group has no other significant concentrations of credit risk but is exposed to general risk of the global credit crisis and its effects on the Group's distributors.

Capital Risk Management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt (while taking into consideration terms and conditions set by the Citibank Loan Agreement, Note 15).

The Group monitors capital using a gearing ratio, which is net debt divided by total capital plus net debt. The Group's policy is to keep the gearing ratio not more than 60%. The Group includes within net debt borrowings and loans, trade and other payables less cash and cash equivalents. Capital includes equity attributable to the equity holders of the parent.

	2008	2007
Borrowings and loans	2,343,234	3,264,950
Trade and other payables	1,707,544	1,046,520
Bank overdraft	199,242	–
Less: cash and cash equivalents	(186,066)	(192,589)
Net debt	4,063,954	4,118,881
Equity	12,451,189	9,041,814
Capital and net debt	16,515,143	13,160,695
Gearing ratio	**25%**	**31%**

28. Post Balance Sheet Events

Addendum to purchase contract for Donelle Company Limited

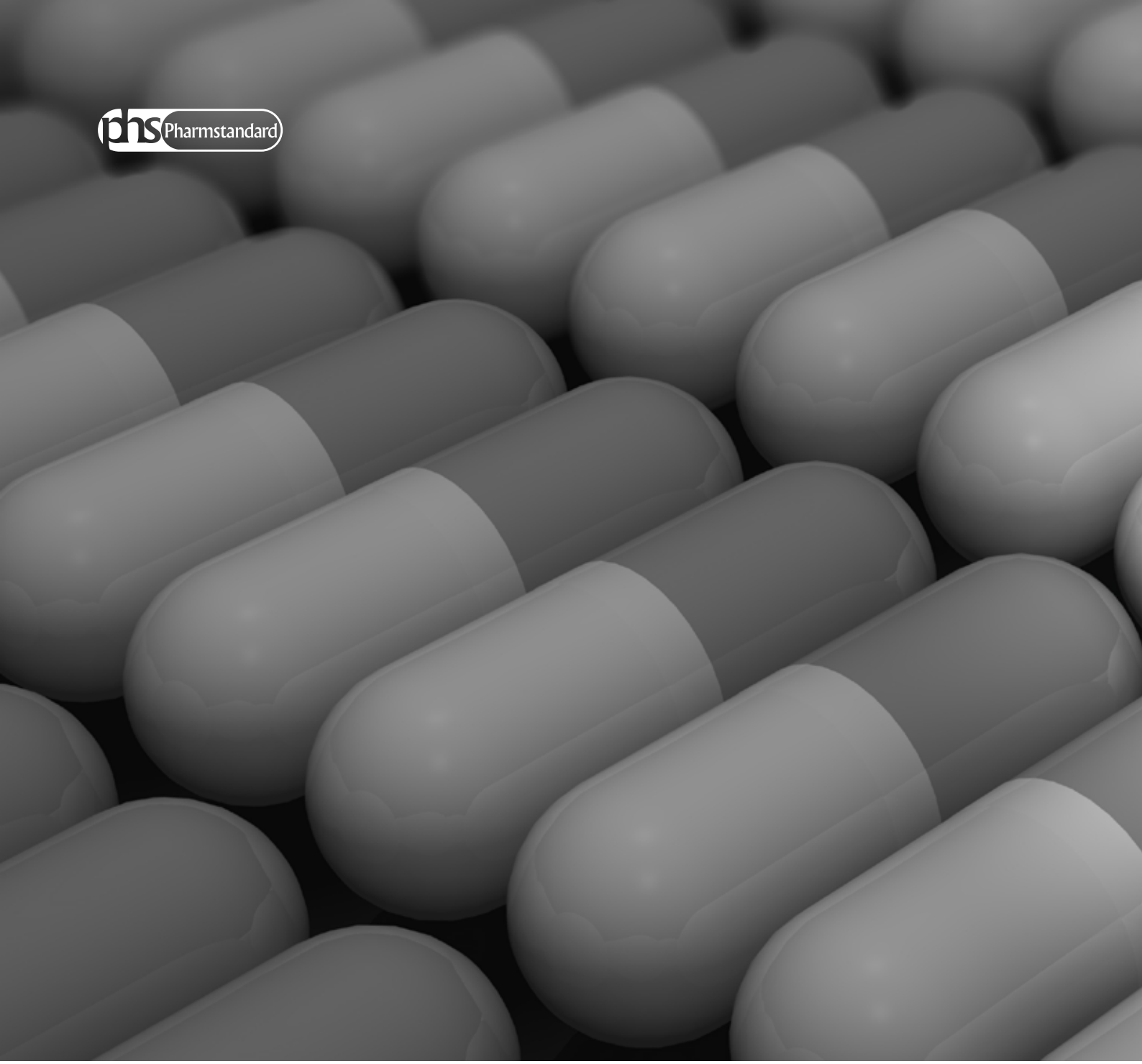
On 12 March 2009 the Company signed an addendum to the contract with the sellers of Donelle Company Limited in relation to the Afobazol® trade mark. Parties agreed that the Company will return back 10.93% of the shares in Donelle Company Limited to the sellers in lieu of paying the remaining balance of RR 235,000 (see Notes 5.1 and 17). This transaction will be recorded in 2009 as an increase in minority interest with the corresponding decrease in other accounts payable.

Withdrawal of some series of defective Mildronat in ampoules from the market

Since February 2008, the Group has an agreement with Grindeks (Latvia) on exclusive rights to promotion and distribution on the Russian market of products under Mildronat trade mark held by Grindeks. Under this agreement Mildronat products are partially imported by Pharmstandard and partially purchased from the local manufacturer licensed by Grindeks and unrelated to the Group. On 24 March 2009, Russian Medical Supervisory Authority issued an order for withdrawal from the market of certain series of Mildronat in ampoules produced in 2008 by the local manufacturer due to a production error identified in February 2009. Total sales of the defective Mildronat series were RR 218,383 in 2008 and about RR 25,000 in 2009.

As a result, management expects distributors will return unsold defective series of Mildronat in ampoules which, together with the Group's defective series of Mildronat in stock, will be returned to Grindeks in accordance with the agreement.

These Mildronat returns were booked consistently with the accounting policy for other defective stock returns, i.e. as reversal of the respective sales and cost of sales in the consolidated income statement. The total amount recoverable from Grindeks of RR 379,460 was deducted from the outstanding payable to this vendor as of 31 December 2008.



Company Management and Investor Relations Department are open to dialogue and always ready to help you with understanding of the Company's processes, plans, developments and financials.

05 Contacts

INVESTOR RELATIONS

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Our company regards openness and business transparency as important competitive advantages. With these principles in mind, Pharmstandard has developed investment management philosophy aimed at facilitating stable growth in share capital and good returns on investment.

In dealing with investors, Pharmstandard is guided by following principles:

- Ensuring organizational structure transparency;
- Providing complete, accurate information to shareholders and potential investors
- Working towards reduction of short-term and long-term investment risks;
- Providing investors with tools to monitor reliability and efficiency of their investments.

Company Management and Investor Relations Department are open to dialogue and always ready to help you with understanding of the Company's processes, plans, developments and financials.

Investor Relations department is always glad to answer you questions. Any feedback is highly appreciated.

IR department contacts

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COVERING ANALYSTS

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A number of investment banks and companies provide analytical coverage of Pharmstandard's activities. In the following table you will find information about analysts who issue regular reports on Pharmstandard's operations and status. Please contact them for additional information about the Company.

	Company	Analyst
1	UBS	Svetlana Sukhanova
2	JP Morgan	Elena Jouronova
3	Renaissance Capital	Natasha Zagvozdina
4	Citigroup	Marat Ibragimov
5	Goldman Sachs	Anton Farlenkov
6	Merill Lynch	Odile-Lange Broussy
7	Nomura	Mikhail Terentiev
8	Unicredit Aton	Anna Kochkina
9	Capital	Marina Samokhvalova
10	BKS	Tatiana Bobrovskaya
11	Rye, Man and Gor Securities	Ekaterina Andriyanova
12	Bank of Moscow	Sabina Mukhamedzhanova

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