# OAO Severstal

*(incorporated as an open joint stock company under the laws of the Russian Federation)*

## US$1,250,000,000 9.75 percent Loan Participation Notes due 2013

*issued by, but with limited recourse to,*
*Steel Capital SA for the sole purpose of financing a loan to*

# OAO Severstal

***Issue Price: 100 percent***

Steel Capital SA (the "**Issuer**") is issuing US$1,250,000,000 in aggregate principal amount of 9.75 percent Loan Participation Notes due 2013 (the "**Notes**"). The Notes are limited recourse obligations of the Issuer and are being offered for the sole purpose of funding a five-year loan (the "**Loan**") to OAO Severstal (the "**Company**" or the "**Borrower"**) pursuant to a loan agreement (the "**Loan Agreement**") dated 25 July 2008 between the Issuer and the Company. The Notes will be constituted by, be subject to, and have the benefit of, a trust deed to be dated 29 July 2008 (the "**Trust Deed**") between the Issuer and Citibank, N.A., London Branch, as trustee (the "**Trustee**"), for the holders of the Notes from time to time (the "**Noteholders**"). In the Trust Deed, the Issuer will charge in favour of the Trustee as security for its payment obligations in respect of the Notes (a) its right to principal, interest and other amounts as lender under the Loan Agreement, (b) its right to receive all sums which may be or become payable by the Borrower under any claim, award or judgment relating to the Loan Agreement and (c) all its rights, title and interest in and to amounts received pursuant to the Loan in an account of the Issuer (as described herein), in each case other than the Reserved Rights (as defined in "Terms and Conditions of the Notes") and certain amounts relating to the Reserved Rights. The Issuer will also assign its administrative rights under the Loan Agreement to the Trustee.

In each case where amounts of principal, interest and additional amounts (if any) are stated to be payable in respect of the Notes, the obligation of the Issuer to make any such payment shall constitute an obligation only to account to the Noteholders, on each date upon which such amounts of principal, interest and additional amounts (if any) are due in respect of the Notes, for an amount equivalent to all principal, interest and additional amounts (if any) actually received by, or for the account of, the Issuer pursuant to the Loan Agreement. The Issuer will have no other financial obligations under the Notes. **Noteholders will be deemed to have accepted and agreed that they will be relying solely and exclusively on the Company's covenant to pay under the Loan Agreement and the credit and financial standing of the Company in respect of the financial servicing of the Notes.**

Subject to receipt by the Issuer of amounts pursuant to the Loan Agreement, interest on the Notes will be payable semi-annually in arrear in equal instalments on 29 January and 29 July in each year commencing on 29 January 2009 as described under "Terms and Conditions of the Notes — Interest". The Loan will bear interest of 9.75 percent per annum. Unless previously redeemed or cancelled, the Notes will be redeemed at their principal amount on 29 July 2013.

Except as set forth herein, payments in respect of the Notes will be made without any deduction or withholding for or on account of taxes of the Grand Duchy of Luxembourg. The Loan may be prepaid at its principal amount, together with accrued interest, at the option of the Company upon the Company or the Issuer being required to deduct or withhold any Russian or Luxembourg taxes from payments to be made by them in respect of the Notes or pursuant to the Loan Agreement or, following enforcement of the security created in the Trust Deed, upon the Trustee being required to deduct or withhold any taxes of the Russian Federation or the jurisdiction in which the Trustee is then resident. The Loan may also be prepaid if it becomes unlawful for the Loan or the Notes to remain outstanding, as set forth in the Loan Agreement, and thereupon (subject to the receipt of the relevant funds from the Company) the principal amount of all outstanding Notes will be prepaid by the Issuer, together with accrued interest.

**AN INVESTMENT IN THE NOTES INVOLVES A HIGH DEGREE OF RISK. SEE "RISK FACTORS" ON PAGE 19.**

Application has been made to the Financial Services Authority in its capacity as competent authority under the Financial Services and Markets Act 2000 ("**FSMA**") (the "**UK Listing Authority**") for approval of this document as a prospectus for the purposes of Directive 2003/71/EC (the "**Prospectus Directive**") and for the Notes to be admitted to the official list of the UK Listing Authority (the "**Official List**") and to the London Stock Exchange plc (the "**London Stock Exchange**") for such Notes to be admitted to trading on the regulated market of the London Stock Exchange (the "**Market**"). The Market is regulated for the purposes of Directive (2004/39/EC) of the European Parliament and of the Council on markets in financial instruments. Application has also been made for the Notes represented by the Rule 144A Global Certificate (as defined below) to be designated as eligible for trading through the Private Offering, Resale and Trading through Automated Linkages ("**PORTAL**") System of the National Association of Securities Dealers, Inc. There can be no assurance that a trading market in the Notes will develop.

The Notes and the Loan (together, the "**Securities**") have not been, and will not be, registered under the United States Securities Act of 1933, as amended (the "**Securities Act**") or with any securities regulatory authority of any State or other jurisdiction of the United States. The Notes may not be offered or sold within the United States or to, or for the account or benefit of, US persons, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. The Notes are being offered and sold outside the United States to non-US persons in reliance on Regulation S ("**Regulation S**") under the Securities Act (the "**Regulation S Notes**") and within the United States to qualified institutional buyers ("**QIBs**"), as defined in Rule 144A ("**Rule 144A**") under the Securities Act, that are also qualified purchasers ("**QPs**"), as defined in Section 2(a)(51) of the US Investment Company Act of 1940 (the "**Investment Company Act**"), in reliance on the exemption from registration under the Securities Act provided by Rule 144A (the "**Rule 144A Notes**"). Prospective purchasers are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A. For a description of these and certain further restrictions on Offers, sales and transfers of the Notes and distribution of this Prospectus, see "Subscription and Sale" and "Selling and Transfer Restrictions".

The Notes will be in registered form in the denomination of US$100,000 and integral multiples of US$1,000 in excess thereof. The Regulation S Notes will be evidenced by a global Certificate (the "**Regulation S Global Certificate**"), which will be registered in the name of a nominee for, and deposited with, a common depositary for Euroclear Bank SA/NV ("**Euroclear**") and Clearstream Banking, société anonyme ("**Clearstream, Luxembourg**"). The Rule 144A Notes will be evidenced by a global certificate (the "**Rule 144A Global Certificate**" and, together with the Regulation S Global Certificate, the "**Global Certificates**"), which will be registered in the name of a nominee of, and deposited with a custodian for, The Depository Trust Company ("**DTC**"). Ownership interests in the Global Certificates will be shown on, and transfers thereof will be effected only through, records maintained by DTC, Euroclear and Clearstream, Luxembourg and their respective participants. Definitive registered certificates ("**Definitive Certificates**") evidencing holdings of Notes will only be available in certain limited circumstances. See "Terms and Conditions of the Notes".

*Global Coordinator and Joint Bookrunner*

**CITI**

*Joint Bookrunners*

**ABN AMRO** **BNP PARIBAS**

*Co-Manager*

**THE ROYAL BANK OF SCOTLAND**

The date of this Prospectus is 25 July 2008

This Prospectus comprises a Prospectus for the purposes of the Prospectus Directive and for the purpose of giving information with regard to the Company, the Company and its consolidated subsidiaries taken as a whole (the "**Group**"), the Issuer, the Loan and the Notes, which is necessary to enable investors to make an informed assessment of the assets and liabilities, financial position, profit and losses and prospects of the Issuer, the Company, and the Group and of the rights attaching to the Notes and the Loan. Each of the Company and the Issuer accepts responsibility for the information contained in this Prospectus. To the best of the knowledge and belief of the Company and the Issuer, each of which has taken all reasonable care to ensure that such is the case, the information contained in this Prospectus is in accordance with the facts and does not omit anything likely to affect the import of such information.

The Company confirms that (i) this Prospectus contains all information with respect to the Company, the Group, the Loan and the Notes which is material in the context of the issue and offering of the Notes; (ii) the statements contained in this Prospectus are in every material particular true and accurate and not misleading; (iii) the opinions, expectations and intentions expressed in this Prospectus are honestly held, have been reached after considering all relevant circumstances and are based on reasonable assumptions; (iv) this Prospectus does not at its date contain any untrue statement of a material fact nor does it omit to state any material fact necessary to make the statements herein, in light of the circumstances under which they were made, not misleading; and (v) all reasonable enquiries have been made by the Company to ascertain such facts and to verify the accuracy of all such information and statements.

None of the Managers (as defined in "Subscription and Sale"), their affiliates or the Trustee makes any representation or warranty, express or implied, as to the accuracy or completeness of the information in this Prospectus. Each person receiving this Prospectus acknowledges that such person has not relied on any of the Managers, their affiliates or the Trustee in connection with its investigation of the accuracy of such information or its investment decision. To the fullest extent permitted by law, the Managers accept no responsibility whatsoever for the contents of this Prospectus, or for any other statement, made or purported to be made by a Manager or on its behalf in connection with the Issuer, the Company, the Group, the Loan or the issue and offering of the Notes. Each Manager accordingly disclaims all and any liability whether arising in tort or contract or otherwise which it might otherwise have in respect of this Prospectus or any such statement.

Each person contemplating making an investment in the Notes must make its own investigation and analysis of the creditworthiness of the Company and its own determination of the suitability of any such investment, with particular reference to its own investment objectives and experience, and any other factors that may be relevant to it in connection with such investment. Each purchaser of the Notes should be aware that it may be required to bear the financial risks of this investment for an indefinite period of time.

No person is authorised to provide any information or to make any representation not contained in this Prospectus and any information or representation not so contained must not be relied upon as having been authorised by or on behalf of the Company, the Issuer, the Trustee, or the Managers.

Neither the delivery of this Prospectus nor the offer, sale or delivery of any Note shall in any circumstances create any implication that there has been no adverse change, or any event reasonably likely to involve any adverse change, in the condition (financial or otherwise) of the Company, the Group or the Issuer since the date of this Prospectus. Unless otherwise stated, all information is given as at the date of this Prospectus.

This Prospectus does not constitute an offer to sell, or a solicitation of an offer to buy, the Notes. The distribution of this Prospectus and the offering, sale and delivery of the Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Company, the Issuer, the Managers and the Trustee to inform themselves about and to observe any such restrictions. This Prospectus may not be used for, or in connection with, any offer to, or solicitation by, anyone in any jurisdiction or under any circumstances in which such offer or solicitation is not authorised or is unlawful. For a description of certain further restrictions on offers, sales and deliveries of the Notes and distribution of this Prospectus, see the section of this Prospectus entitled "Subscription and Sale".

None of the Company, the Group, the Issuer, the Managers or the Trustee nor any of their respective affiliates or agents makes any representation about the legality of the purchase of the Notes by an investor under applicable investment or similar laws. Each prospective investor is advised to consult its own counsel and business adviser as to legal, tax, business, financial and related matters concerning the purchase of the Notes. The contents of this Prospectus are not to be construed as legal, business or tax advice.

Each prospective investor in the Notes must comply with all applicable laws and regulations in force in any jurisdiction in which it purchases, offers or sells the Notes and must obtain any consent, approval or permission required of it for the purchase, offer or sale by it of the Notes under the laws and regulations in force in any jurisdiction to which it is subject or in which it makes such purchases, offers or sales, and none of the Company, the Issuer, the Managers or the Trustee or any of their respective affiliates or agents shall have any responsibility therefor.

This Prospectus contains summaries with respect to certain terms of the Trust Deed and the Loan Agreement, but reference should be made to the actual documents for complete information with respect thereto. All summaries are qualified in their entirety by such reference. These documents will be made available free of charge to prospective investors upon request to the Company or at the office of the paying and transfer agent in London and New York City.

The Issuer is a *société anonyme* incorporated for an unlimited duration under the laws of the Grand Duchy of Luxembourg ("**Luxembourg**"). The Issuer is not a subsidiary of the Company. The registered office of the Issuer is located at 2, Boulevard Konrad Adenauer, L-1115 Luxembourg and its telephone number is +35 242 122 449. The Issuer is registered with the Registre de Commerce et des Sociétés à Luxembourg (the Register of Commerce and Companies in Luxembourg) under number B116975. For further information on the Issuer, see "The Issuer".

*The Notes have not been recommended by or approved by the US Securities and Exchange Commission or any other federal or state securities commission or regulatory authority in the United States, nor has such any commission or regulatory authority passed upon the accuracy or adequacy of this Prospectus. Any representation to the contrary is a criminal offence in the United States.*

THE STATEMENTS HEREIN ABOUT U.S. FEDERAL TAX ISSUES ARE MADE TO SUPPORT MARKETING OF THE NOTES. NO TAXPAYER CAN RELY ON THEM TO AVOID TAX PENALTIES. EACH PROSPECTIVE PURCHASER SHOULD SEEK ADVICE FROM AN INDEPENDENT TAX ADVISOR ABOUT THE TAX CONSEQUENCES UNDER ITS OWN PARTICULAR CIRCUMSTANCES OF INVESTING IN NOTES UNDER THE LAWS OF LUXEMBOURG, THE RUSSIAN FEDERATION, THE UNITED STATES AND ITS CONSTITUENT JURISDICTIONS AND ANY OTHER JURISDICTION WHERE THE PURCHASER MAY BE SUBJECT TO TAXATION.

The Securities have not been and will not be registered under the Securities Act. The Notes may not be offered or sold within the United States or to, or for the account or benefit of, US persons except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. The Regulation S Notes are being offered and sold outside the United States to non-US persons in reliance on Regulation S and the Rule 144A Notes are being offered and sold within the United States to QIBs that are also QPs in reliance on the exemption from registration under the Securities Act provided by Rule 144A. Prospective purchasers are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A. For a description of these and certain further restrictions on offers, sales and transfers of the Notes and distribution of this Prospectus, see "Subscription and Sale" and "Selling and Transfer Restrictions".

This Prospectus has been prepared solely for use in connection with the proposed offering of the Notes described in this Prospectus. This Prospectus is personal to each offeree and does not constitute an offer to any other person or to the public generally to subscribe for or otherwise acquire Notes. Distribution of this Prospectus to any person other than the prospective investor and any person retained to advise such prospective investor with respect to its purchase is unauthorised, and any other disclosure of any of its contents, without the prior written consent of the Company, the Issuer and the Managers is prohibited. Each prospective investor, by accepting delivery of this Prospectus, agrees to the foregoing and to make no photocopies of this Prospectus or any documents referred to in this Prospectus.

**IN CONNECTION WITH THIS ISSUE, CITIGROUP GLOBAL MARKETS LIMITED (THE "STABILISING MANAGER") OR ANY PERSON ACTING ON BEHALF OF THE STABILISING MANAGER MAY OVER-ALLOT NOTES OR EFFECT TRANSACTIONS WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE NOTES AT A LEVEL HIGHER THAN THAT WHICH MIGHT OTHERWISE PREVAIL. HOWEVER, THERE IS NO ASSURANCE THAT THE STABILISING MANAGER (OR ANY PERSONS ACTING ON BEHALF OF THE STABILISING MANAGER) WILL UNDERTAKE STABILISATION ACTION. ANY STABILISATION ACTION MAY BEGIN ON OR AFTER THE DATE ON WHICH ADEQUATE PUBLIC DISCLOSURE OF THE TERMS OF THE OFFER OF THE**

**NOTES IS MADE AND, IF BEGUN, MAY BE ENDED AT ANY TIME, BUT IT MUST END NO LATER THAN THE EARLIER OF 30 DAYS AFTER THE ISSUE DATE OF THE NOTES AND 60 DAYS AFTER THE DATE OF THE ALLOTMENT OF THE NOTES. ANY STABILISATION ACTION OR OVER-ALLOTMENT MUST BE CONDUCTED BY THE RELEVANT STABILISING MANAGER (OR PERSON ACTING ON BEHALF OF ANY STABILISING MANAGER) IN ACCORDANCE WITH ALL APPLICABLE LAWS AND REGULATIONS.**

The Company and the Managers reserve the right to reject any offer to purchase the Notes in whole or in part and to sell to any prospective investor less than the full amount of Notes sought by such investor. The Managers and certain related entities may acquire a portion of the Notes for their own accounts.

## NOTICE TO NEW HAMPSHIRE RESIDENTS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENCE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES ("**RSA**") WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

## NOTICE TO RUSSIAN FEDERATION INVESTORS

Under Russian law, the Notes are securities of a foreign issuer. The Notes are not eligible for initial offering and circulation in the Russian Federation. Neither the issue of the Notes nor a securities prospectus in respect of the Notes has been, or is intended to be, registered with the Federal Service for Financial Markets (the "**FSFM**"). The information provided in this Prospectus is not an offer, or an invitation to make offers, to sell, exchange or otherwise transfer the Notes in the Russian Federation or to any Russian residents except as may be permitted by Russian law. The information contained in this Prospectus does not constitute an advertisement of the Notes in Russia and must not be passed on to third parties or otherwise be made publicly available in Russia.

## AVAILABLE INFORMATION

The Company has agreed that, for so long as any Notes are "restricted securities" within the meaning of Rule 144(a)(3) under the Securities Act, it will, during any period in which it is neither subject to Section 13 or 15(d) of the US Securities Exchange Act of 1934, as amended (the "**Exchange Act**") nor exempt from reporting pursuant to Rule 12g3-2(b) thereunder, provide to any holder or beneficial owner of such restricted securities or to any prospective purchaser of such restricted securities designated by such holder or beneficial owner or to the Principal Paying Agent (as defined herein) for delivery to such holder, beneficial owner or prospective purchaser, in each case upon the request of such holder, beneficial owner, prospective purchaser or Principal Paying Agent, the information required to be provided by Rule 144A(d)(4) under the Securities Act.

## FORWARD LOOKING STATEMENTS

This Prospectus contains "forward looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act which relate to, without limitation, any of the Company's plans, financial position, objectives, goals, strategies and future operations and performance and the assumptions underlying these forward looking statements. Words such as "estimates", "expects", "believes", "intends", "plans", "may", "will", "should" and any similar expressions are used to identify forward looking statements. These forward looking statements are contained in "Risk Factors", "Management's Discussion and Analysis of Financial Condition and Results of Operations", "Business" and elsewhere in this Prospectus. The Company has based these forward looking statements on the current view of its management with respect to future events and financial performance. These views reflect the best judgement of its management but involve uncertainties and are subject to certain known and unknown risks and other important factors beyond the Company's control, the occurrence of which could cause actual results to differ materially from those predicted in the Company's forward looking statements and from past results, performance or achievements. Although the Company believes that the estimates and the projections reflected in such forward looking statements are reasonable, if one or more of the risks or uncertainties materialise or occur, including those identified in this Prospectus, or if any of the underlying assumptions prove to be incomplete or incorrect, the Company's actual results of operations may vary from those expected, estimated or projected. Accordingly, prospective purchasers of the Notes should not place undue reliance on these forward looking statements. The important factors that could cause the Company's actual results, performance or achievements to differ materially from those in these forward looking statements include, but are not limited to, those discussed in "Risk Factors" and "Business". These forward looking statements speak only as at the date of this Prospectus. The Company expressly disclaims any obligation or undertaking to disseminate after the date of this Prospectus any updates or revisions to any forward looking statements contained herein to reflect any change in its expectation with regard thereto or any change in events, conditions or circumstances on which any such forward looking statements are based, unless required to do so by applicable law.

## ENFORCEABILITY OF JUDGMENTS

The Company is an open joint stock company established under the laws of the Russian Federation. A substantial number of the Company's directors and executive officers named in this Prospectus reside outside the United Kingdom and/or the United States. Moreover, a substantial portion of the assets of the Company and of such persons are located outside the United Kingdom and the United States. As a result, it may not be possible for the Trustee, acting on behalf of the Noteholders, to effect service of process within the United Kingdom or the United States upon the Company (although, under the Loan Agreement the Company has appointed an agent for service of process in the United Kingdom) and/or to enforce against the Company or any such person court judgments obtained in the United Kingdom and the United States courts.

Judgments rendered by a court in any jurisdiction outside the Russian Federation may not be enforced by courts in the Russian Federation unless there is (i) an international treaty in effect providing for the recognition and enforcement of judgements in civil cases between the Russian Federation and the jurisdiction where such judgment is rendered, and/or (ii) a federal law of the Russian Federation providing for the recognition and enforcement of foreign court judgments.

The Company is not aware of any treaty or convention directly providing for the recognition and enforcement of judgments in civil and commercial matters between the United Kingdom and the Russian Federation or between the United States and the Russian Federation. However, the Company is aware of one instance in which Russian courts have recognised and enforced an English court judgment. The basis for this was a combination of the principle of reciprocity and the existence of a number of bilateral and multilateral treaties to which both the United Kingdom and the Russian Federation are parties. In the absence of established court practice, however, it is difficult to predict whether a Russian court will be inclined in any particular instance to recognise and enforce an English court judgment on these grounds.

In addition, Russian courts have limited experience in the enforcement of foreign court judgments. The limitations described above may significantly delay the enforcement of such judgment, or completely deprive the Noteholders or the Trustee of effective legal recourse for claims under the Notes relating to the Loan.

The Loan Agreement is governed by English law and provides that if any dispute or difference arises from or in connection with the Loan Agreement, such dispute shall be referred to and finally resolved by arbitration in accordance with the LCI Arbitration Rules. Before any arbitration or arbitral tribunal has been appointed to determine a dispute, however, the Issuer may elect, by notice in writing to the Company, to require that all disputes or a specific dispute be heard by a court of law. The seat of any arbitration will be London, England. The United Kingdom, the United States and the Russian Federation are parties to the United Nations (New York) Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "**New York Convention**"). Consequently, Russian courts should generally recognise and enforce in the Russian Federation an arbitral award from an arbitral tribunal in the United Kingdom, on the basis of the rules of the New York Convention (subject to qualifications provided for in the New York Convention and compliance with Russian procedural regulations and other procedures and requirements established by Russian legislation). However, it may be difficult to enforce arbitral awards in the Russian Federation due to:

- the inexperience of the Russian courts in international commercial transactions;
- official and unofficial political resistance to the enforcement of awards against Russian companies in favour of foreign investors; and
- the inability of Russian courts to enforce such awards.

In September 2002, the new *arbitrazh* procedural code of the Russian Federation (the "**Arbitrazh Procedural Code**") entered into force. The Arbitrazh Procedural Code established the procedure for Russian courts to refuse to recognise and enforce a foreign arbitral award. The Arbitrazh Procedural Code and other Russian procedural legislation could change; therefore, among other things, other grounds for Russian courts to refuse the recognition and enforcement of foreign court judgments and foreign arbitral awards could arise in the future. In practice, reliance upon international treaties may meet with resistance or a lack of understanding on the part of a Russian court or other officials, thereby introducing delay and unpredictability into the process of enforcing any foreign court judgment or arbitral award in the Russian Federation.

## PRESENTATION OF FINANCIAL AND OTHER INFORMATION

### Market and Other Statistical Data

Market data used in this Prospectus, as well as certain statistics, including statistics in respect of product sales by volume of third parties and market share, under the captions "Overview", "Risk Factors", "Management's Discussion and Analysis of Financial Condition and Results of Operations", "Industry" and "Business", have been extracted from official and industry sources and other third-party sources that the Company believes to be reliable, such as the following:

- *CDU TEK.* CDU TEK is the central dispatch unit of the Russian Federation Ministry of Industry and Trade.
- *Chermet Corporation.* The Chermet Corporation is a Russian company that provides and publishes information, statistics and analytic surveys relating to producers of ferrous metals.
- *International Iron and Steel Institute.* The International Iron and Steel Institute ("**IISI**") is one of the largest industry associations in the world. IISI's members include more than 190 steel producers (including the world's 20 largest steel companies), national and regional steel industry associations, and steel research institutes.
- *Metal Bulletin.* Metal Bulletin plc is an independent company quoted on the London Stock Exchange plc (the "**London Stock Exchange**"). It provides news, prices, analysis and research to financial, metals, minerals, energy and other commodity markets through online services and print media.
- *RudProm.* RudProm is an agency that collates statistics about iron ore producers in the former Soviet Union.

Where information in this Prospectus has been sourced from third parties including in respect of information concerning the Company's competitors, this information has been accurately reproduced, and as far as the Company and the Issuer are aware and are able to ascertain from the information published by the aforementioned sources, no facts have been omitted which would render the reproduced information, data and statistics inaccurate or misleading. Such information, data and statistics may be approximations or estimates or use rounded numbers. The Company and the Issuer have accurately reproduced such information and, as far as the Company and the Issuer are aware and are able to ascertain from information published by such third party, no facts have been omitted that would render the reproduced information inaccurate or misleading. Nevertheless, prospective investors are advised to consider this data with caution. Market studies are often based on information or assumptions that may not be accurate or appropriate, and their methodology is inherently predictive and speculative. Prospective investors should note that the Company's estimates are based on such third-party information. Neither the Company nor the Managers have independently verified the figures, market data or other information on which third parties have based their studies.

In addition, some of the information contained in this document has been derived from official data of Russian government agencies and the Bank of Russia. The official data published by Russian federal, regional and local government agencies are substantially less complete or researched than those of more developed countries. Official statistics, including those produced by the Bank of Russia, may also be produced on different bases than those used in more developed countries. Any discussion of matters relating to Russia in this document must, therefore, be subject to uncertainty due to concerns about the completeness or reliability of available official and public information.

The contents of the Group's website do not form any part of this Prospectus.

**Financial Information**

The financial statements of the Group included in this Prospectus beginning on page F-3 and ending on page F-76, together with the notes thereto (the "**Financial Statements**"), as well as the Group's consolidated financial statements as at and for years ended 31 December 2006 and 2005 beginning on page F-91 and ending on page F-137, together with the notes thereto were prepared in accordance with IFRS as issued by the International Accounting Standards Board, ("**IASB**"), in effect at the time of preparing these consolidated financial statements.

The IFRS applied by the Group differs from the IFRS that has been adopted for use in the European Union through the endorsement procedure established by the European Commission. IFRS that was adopted for use in the European Union did not include revised IFRS 3 "Business Combinations" and several Interpretations and Amendments to existing effective IFRS as issued by IASB.

The Financial Statements consist of (i) the Group's consolidated condensed interim financial statements as at and for the three months ended 31 March 2008 beginning on page F-3 and ending on page F-14 (the "**Interim Financial Statements**"), and (ii) the Group's consolidated financial statements as at and for the year ended 31 December 2007 beginning on page F-15 and ending on page F-76 (the "**Annual Financial Statements**").

Some of the data from the Financial Statements presented herein, when shown in tabular format, is identified as "restated". For an explanation of the restatement, see Note 3c of the relevant Annual Financial Statements on page F-29 of this Prospectus.

The financial statements of the Issuer included in this Prospectus, beginning on page F-77 and ending on page F-89, together with the notes thereto (the "**Issuer Financial Statements**"), were prepared in accordance with IFRS.

In this Prospectus,

- "**Russian Rouble**", "**Russian Roubles**", "**Rouble**", "**Roubles**" or "**RUR**" refers to the lawful currency of the Russian Federation;
- "**US dollar**", "**US dollars**" or "**US$**" refers to the lawful currency of the United States of America;
- "**British pound sterling**", "**British pounds sterling**", "**GBP**" or "**£**" refers to the lawful currency of the United Kingdom; and
- "**euro**", or "**€**" refers to the single currency of the participating member states in the Third Stage of the European Economic and Monetary Union of the Treaty Establishing the European Community, as amended from time to time.

**Mining Reserves**

All data relating to the Group's reserves and resources relating to iron ore and coal cited in "Business — Severstal Resources — Reserves and Resources" and "Industry — Russian Methodologies for Reserve and Resource Reporting" and "Industry — International Reporting Methodologies" are calculated by reference to estimates provided by IMC Consulting Ltd in its report dated 14 August 2006, which was prepared in accordance with Australasian Joint Ore Reserves Committee Code ("**JORC**") reporting standards, reduced by actual production since 1 January 2006, and also accounting for the disposal of the Kuzbassugol mining complex in April 2008. For additional information on JORC, see "Industry — Mining Industry — International Reporting Methodologies". The report of IMC Consulting Ltd was not prepared for the purposes of this Prospectus.

**Operating Data**

All data relating to the Group's production and operations, such as volumes of production, production capacity and certain sales information presented by sector, geography and product, cited in "Business", and as cited specifically elsewhere in this Prospectus, were derived from management accounts and information, which were not reviewed or audited by KPMG Limited, the independent auditors of the Group.

**Certain Defined Terms**

In this Prospectus:

- the "**CBR**" means the Bank of Russia;
- the "**Company**" or the "**Borrower**" means OAO Severstal;
- the "**Group**" means the Company and its consolidated subsidiaries;
- the "**Issuer**" means Steel Capital SA;
- the "**FAS**" means the Federal Antimonopoly Service of the Russian Federation;
- the "**Russian Government**" means the federal government of the Russian Federation;
- "**tonnes**" means metric tonnes, and one metric tonne is equal to one thousand kilograms; and
- the "**US**" means the United States, the "**UK**" means the United Kingdom, the "**EU**" means the European Union and its member states as at the date of this Prospectus, "**Russia**" means the Russian Federation, the "**CIS**" means the countries that formerly comprised the Union of Soviet Socialist Republics and that are now members or associate members of the Commonwealth of Independent States: Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan.

**Rounding**

Certain figures included in this Prospectus have been subject to rounding adjustments; accordingly, figures shown for the same category presented in different tables may vary slightly, and figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

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## OVERVIEW OF THE GROUP

*This overview may not contain all the information that may be important to prospective purchasers of the Notes and, therefore, should be read in conjunction with this entire Prospectus, including the more detailed information regarding the Group's business and the Financial Statements and related notes included elsewhere in this Prospectus. Certain statements in this overview include forward-looking statements that also involve risks and uncertainties as described under "Forward-Looking Statements".*

### GENERAL

The Group is an international, vertically-integrated metals and mining company that sells steel and mining products to customers across the world. According to Metal Bulletin, the Group was the world's 15th largest producer of crude steel in 2007, by volume of production. The Group is a full production cycle operation which includes iron ore and coal mining enterprises, steel mills and rolled product plants as well as downstream production and distribution businesses. The Group's production facilities are geographically diversified, with locations in Russia, the United States, Italy, France, Ukraine, the United Kingdom and Kazakhstan. With a focus on high value-added products in attractive niche markets and a successful track record of acquiring and integrating high-quality assets in the United States and Europe, the Group's corporate strategy is to improve its position as a leading global steel company in terms of profitability, with a vertically-integrated, low-cost business structure.

Following a reorganisation of the Group's management structure in April 2008, the Group comprises three business divisions: the Russian Steel Division, Severstal International, and Severstal Resources.

***Russian Steel Division.*** The Russian Steel Division produced approximately 16.4 percent of the total production of Russian crude steel in 2007, making it the third largest producer of crude steel products in Russia by volume of production in that year, in each case according to Chermet Corporation. The Russian Steel Division comprises three segments: the Russian Steel segment, Metalware and Izhora Pipe Mill.

- The Russian Steel segment consists primarily of the Group's steel production facilities in Cherepovets (the "**Cherepovets Steel Plant**"), high-grade automotive galvanising facilities at Severgal and Rolling Mill 5000, which the Group believes to be Russia's only rolling mill that produces 4.8 metre-wide high-quality hot-rolled plates, as well as various supporting functions for trading, maintenance and transportation. With total steelmaking capacity of 13.2 million tonnes of crude steel per year as at 31 December 2007, the Russian Steel segment produced 11.9 million tonnes of crude steel and 10.8 million tonnes of finished steel in 2007.
- Metalware comprises Severstal-Metiz's wire drawing and metalware manufacturing businesses in Russia, Ukraine and the United Kingdom. With total metalware production of 1.0 million tonnes, in 2007, Severstal-Metiz's production represented approximately 34.4 percent of domestic Russian metalware production, based on data from the Association of Metalware Producers of Russia, and approximately 33.2 percent of Ukrainian metalware production, based on data from the Association of Metalware Producers of Ukraine.
- The Izhora Pipe Mill comprises a large-diameter pipe mill in Russia. With total pipemaking capacity of 0.6 million tonnes as at 31 December 2007, Izhora Pipe Mill produced 0.3 million tonnes in 2007.

***Severstal International.*** Severstal International comprises two segments: North America and Lucchini.

- According to the Group's estimates, North America was the fourth largest integrated steel producer by volume of production in the United States in 2007. North America comprises Severstal North America, which is located in Dearborn, Michigan close to a large number of US steel customers, including several major automotive customers; SeverCorr, located in Columbus, Mississippi; and Sparrows Point LLC ("**Sparrows Point**") steel plant, located in Baltimore, Maryland. In addition, the Group is in the process of acquiring further assets in the United States. See "— Recent Developments". North America currently has a total crude steelmaking capacity of 8.1 million tonnes per year, including the capacity of the recently acquired Sparrows Point steel plant and SeverCorr, which has been consolidated into the Group's financial results since January 2008. In 2007, prior to the acquisition of the Sparrows Point steel plant and excluding SeverCorr's production which was being ramped up upon commissioning of the plant, North America's total steel production was approximately 2.0 million tonnes of crude steel and 2.5 million tonnes of finished steel.

- Lucchini is one of the largest European producers of special quality long products by volume of production, based on the Group's estimates. Lucchini has several plants and service centres throughout Europe, with steelmaking capacity of approximately 4 million tonnes of crude steel per year, and total production in 2007 of approximately 3.6 million tonnes of crude steel. It operates in niche markets such as automotive, rails and wire rod. Lucchini comprises the Piombino business unit and the Ascometal business unit. Piombino is a well-known European producer of rails, bars and high-quality wire rods, and Ascometal is a well-known producer of high-quality, tailored products, such as ingots, billets, blooms, bars, wire rod and drawn wire. Until its disposal in the second quarter of 2007, Lucchini also consisted of the Sidermeccanica business unit, a well-known European producer of rolling stock materials.

***Severstal Resources.*** Severstal Resources consists primarily of two iron ore complexes, Karelsky Okatysh and Olkon, and one coal mining complex, Vorkutaugol, each in northwest Russia, as well as gold mining assets in east Russia and in Kazakhstan and a ferrous scrap metal recycling business operating in northwest and central Russia. Severstal Resources was the second largest producer of iron ore pellets and coking coal (before accounting for the sale of the Kuzbassugol mining complex) in Russia in 2007, according to RudProm and CDU TEK, respectively. With the capacity to supply all of the current iron ore and hard coking coal needs of the Russian Steel Division, Severstal Resources forms the basis of the Group's balanced and vertically-integrated business model. With a focus on high value-added products, such as export quality iron ore pellets and coking coal concentrate, Severstal Resources had a total output of 14.7 million tonnes of iron ore and 9.4 million tonnes of coal in 2007. Severstal Resources estimates that, as at 31 December 2007, it had iron ore reserves and resources of approximately 710 million tonnes and 962 million tonnes, respectively, and coal reserves and resources of approximately 276 million tonnes and 27 million tonnes, respectively, based a report issued by IMC Consulting Ltd dated 14 August 2006, prepared in accordance with JORC reporting standards, adjusted for actual production since 1 January 2006, and as further adjusted for the disposal of the Kuzbassugol mining complex (consisting of the Berezovskaya and Pervomayskaya mines) in April 2008 as if it had occurred on 31 December 2007.

For more information concerning the structure and history of the Group, see "Business — Overview of the Group" and "Business — History and Development of the Group".

## COMPETITIVE STRENGTHS

The Group has developed a variety of competitive strengths, which it believes provide it with a greater resilience, compared to some of its competitors, to the cyclical nature of the steel industry and a basis on which to build its position as a global metals and mining company.

### Vertically-Integrated Business with Access to Iron Ore and Coal

The Group is a vertically-integrated steel producer operating on a global scale. Its facilities span the full production cycle from iron ore and coal mining operations to steel mills and rolled product plants as well as downstream production and distribution businesses. Its mining operations in Russia, conducted by the Severstal Resources division, provide supplies of iron ore and coal to its production facilities in Russia, but also have the capacity to supply iron ore to its European operations.

Severstal Resources was the second largest producer of iron ore pellets and coking coal (before accounting for the sale of the Kuzbassugol mining complex) in Russia in 2007, according to RudProm and CDU TEK, respectively. Currently, Severstal Resources has the capacity to provide approximately 100 percent of the iron ore and hard coking coal requirements of the Russian Steel Division's steel operations and in 2007, the Russian Steel Division's steel operations procured approximately 74 percent and 75 percent of its iron ore and coal requirements from Severstal Resources, respectively. Severstal Resources' deposits have technical characteristics enabling it to produce a relatively wide range of products for customers in the metallurgical industries, in addition to the Group's steel operations. Its deposits of iron ore and coal are significant, with estimated mine lives extending ten years and beyond.

The Group's North American business units source the majority of their raw materials from domestic suppliers under a variety of arrangements aimed at ensuring a reliable long-term supply of raw materials at competitive prices, with the balance being purchased in the spot markets. The Group's primary plant at the

Lucchini business unit, Piombino, sourced approximately 69 percent of its carbon coke requirements from its own coke ovens in 2007.

The vertically-integrated nature of the Group also allows it to limit its exposure to raw material price fluctuations and increase efficiencies.

**Geographically Diversified Business with a Broad Range of Products**

The Group's production facilities are geographically diversified, with locations in Russia, the United States, Italy, France, Ukraine, the United Kingdom and Kazakhstan. The Group's largest steel production facilities, located in Cherepovets in northwest Russia, provide it with access to the growing Russian, CIS and Eastern European steel markets. Further, the Group believes that, as a result of its presence in Europe and the United States, it also benefits from greater access to the mature European and North American markets for high-quality and niche steel products. In this regard, its recent acquisition of Sparrows Point, WCI Steel, Inc. ("**WCI Steel**"), and, if successfully completed, Esmark Incorporated ("**Esmark**") (see "— Recent Developments") in the United States and the commissioning of the newly constructed SeverCorr mini-mill in Columbus, Mississippi are expected to enhance its presence in the North American steel market and enable it to increase sales and realise production synergies. SeverCorr also provides the Group with greater access to the growing steel markets in the south of the United States, to balance the Group's presence in the mature steel markets in the north. The global diversified nature of the Group has also enabled it to benefit from the sharing of industry know-how and best practices across business divisions. The Group also believes that its broad range of products has allowed it to meet demand for steel products in each of the markets in which the Group operates.

**Low Cost Producer**

Russia is one of the lowest cost regions for steel production worldwide. With its largest production facilities located in northwest Russia, the Group benefits from relatively low-cost supplies of electricity and natural gas, as well as transportation, given the proximity of its production facilities to producers of raw materials in that region, major steel-consuming markets in the central European part of Russia, and the ports of the St. Petersburg region. In addition to these cost advantages, as one of the largest producers of steel in Russia, the Group benefits from economies of scale in production and negotiating power with its suppliers, including third party suppliers of raw materials. In order to maintain its cost competitiveness, the Group has made and continues to make significant capital expenditures in upgrading its facilities to increase productivity and improve the energy efficiency, as well as optimising the size of its labour force. For example, in 2007 the Group's largest steel production facility, located in Cherepovets, was estimated to be approximately 45 percent self-sufficient in terms of its own generation and consumption of electricity, and the Group plans to further increase the plant's level of energy self-sufficiency (see "— Strategy — Pursue Lower-Cost Steel Production").

**Investment in Modernisation and Advanced Technological Processes**

The Group has invested heavily in modernisation programmes at its main steel production facilities and mining facilities in Russia, as well as its steel production facilities in the United States and Europe, expanding production and achieving operational efficiencies. In 2006 and 2007, the Group's capital expenditure at its three business divisions amounted to approximately US$2,877 million and it currently intends to invest an additional US$16.3 billion from 2008 to 2012 as part of its capital expenditure programme.

The Group has sought to adopt new technological processes when operationally convenient to do so, such as the introduction of pulverised coal injection ("**PCI**") technology into blast furnace "C" at Severstal North America's Dearborn facility during the recent major refurbishments of that blast furnace. In addition to modernisation, the Group has built on existing strengths in advanced technological processes, particularly in the automotive and long products markets where, for example, Lucchini's Ascometal business unit is a recognised market leader in special bar quality ("**SBQ"**) products. As a result, the Group believes that it is well-positioned in high value-added and niche product markets, in addition to its other steel and metalware products from its modern production facilities.

**Experienced Management Team**

The Group's senior management team combines extensive steel and resources industry knowledge with international management and financial expertise, including valuable insight gained from the five independent non-executive directors on the board of directors. At an operational level, the Group has developed, and continues to refine, a management structure that is focused on improving accountability, clarifying responsibilities and streamlining information reporting and decision-making. Backed by international experience and advanced business qualifications, the management team's ability to improve the performance of the Group's assets is evidenced by the increased operating efficiency and profitability of the Cherepovets Steel Plant in recent years. Further, the team's ability to evaluate, negotiate and close complex acquisitions has also been shown recently with Severstal International's acquisition of the Sparrows Point production facilities and WCI Steel (see "— Recent Developments"). These transactions involved lengthy negotiations with a range of stakeholders, including complex discussions with labour unions, often in a competitive tender. Further, the management team has a proven track record of turning around underperforming assets, such as Lucchini and Severstal North America's Dearborn facility where significant operating improvements have been achieved, albeit in favourable market conditions.

**Strong Corporate Governance**

As a global metals and mining company, the Group seeks to adhere to international corporate governance standards. In addition to half of its board of directors being independent, according to UK standards of independence, the Group has established committees of its board of directors in accordance with the UK Combined Code on Corporate Governance and has implemented other measures aimed at promoting transparency and good corporate governance. These measures include internal control procedures and internal audit functions, publishing quarterly financial statements prepared in accordance with IFRS, publishing regular production updates, and requiring the approval of two-thirds of the board of directors for acquisitions with a value in excess of US$500 million and any transaction with a value of more than 10 percent of the book value of the Company's assets.

## STRATEGY

The Group's corporate strategy is to build upon and improve its position as a leading global steel company in terms of profitability, with a vertically-integrated, low-cost business structure. To successfully implement this strategy, the Group intends to do the following:

**Focus on High-Demand Products in Russia**

The Group views the Russian market for steel products as providing significant growth potential. Accordingly, the Group plans to continue to invest in its production facilities in Russia in order to increase production capacity, particularly of long products, pipes, sections and other products used in the construction and infrastructure industries, where demand has been strong and is expected by the Group to increase further. In this regard, the Group has started construction of a new pipe mill close to its main Russian steelmaking facilities in Cherepovets, which is currently expected to be completed in 2009. It also plans to commence the production of heavy structural long products at the Cherepovets Steel Plant, as well as to build two mini-mills in central Russia, each with a capacity of approximately 1 million tonnes of finished long products per year, the first of which is expected to be completed in 2010.

Growth in demand from customers in the oil and gas, ship-building and machinery industries is also a focus of the Group in Russia. For customers in these industries, the Group plans to continue to focus on providing a high standard of customer service, including the customisation of products, the supply of premium quality products and just-in-time deliveries, with a view to differentiating itself from other producers in Russia. To this end, the Group plans to leverage the experience of its operations in Europe and North America. The Group also intends to leverage its North American experience to further develop the Group's high-quality automotive steel products in Russia to meet the requirements of foreign car manufacturers operating in Russia. The Group believes that demand for these niche products is set to grow significantly in the medium and long-term.

**Optimisation of the Group's Operations in the United States**

Following the successful acquisition of Sparrows Point and WCI Steel in 2008, and if completed, the acquisition of Esmark (see "— Recent Developments"), the Group plans to focus on optimising and integrating the operations of the facilities acquired with the existing production facilities of Severstal North America and SeverCorr. The Group also plans to consolidate its presence in the growing steel markets in the south of the United States, with the construction of a second phase at SeverCorr, bringing its total production capacity to approximately 3.0 million tonnes of finished products per year. The Group believes that the geographical locations and product lines of these production facilities are complementary. The Group believes that in addition to having a more diverse customer-base and range of products than in the past, its operations in the United States should also benefit from synergies, including knowledge and technology transfers, aggregated purchasing, logistics and other overhead items, and optimised scheduling and production. Increasing the profitability of the entities acquired will also be a focus of the Group's management as well as securing greater reliable long-term supplies of raw materials, in relation to which the Group is considering the acquisition of coal mining assets in the United States (see "— Recent Developments"). In addition, the Group plans to invest in upstream and downstream opportunities that are consistent with reducing costs and marketing value-added products.

**Pursue Lower-Cost Steel Production**

The Group plans to continue to pursue a strategy of lower-cost steel production in relation to its Russian operations (in comparison to global cost levels in steel production), as well as in relation to its European and US operations (in comparison to regional cost levels in steel production). The Group believes that this can be achieved by a combination of capital expenditure on production facilities, energy efficiency improvements and labour productivity gains. The Group's capital expenditure programme includes various projects to improve operational efficiencies and to reduce raw material consumption, such as the planned upgrades to blast furnaces at the Cherepovets Steel Plant to implement PCI technology and reduce the consumption of coal as was recently implemented at blast furnace "C" at Severstal North America's Dearborn facility. The Group plans to improve energy efficiency, including internal electricity generation capacity, is to be improved through measures including the planned construction of a 155 megawatt power generation facility in Cherepovets, currently expected to be completed by the end of 2012, and additional electricity generation at Sparrows Point. The Group plans to continue to focus on optimising the size of its labour force, particularly in Russia, as well as seeking to maintain its relationships with labour unions.

**Organic Growth and Disciplined Acquisitions Strategy**

The Group plans to grow the size of its operations by both organic growth and a disciplined acquisitions strategy focused on acquiring businesses that have the potential to provide synergies and earnings growth, or are of strategic importance for the Group. Currently, the Group's organic growth is expected to come from the construction of the second phase at SeverCorr, which is expected to double that facility's production capacity, together with growth in its Russian steelmaking operations (see "— Focus on High-Demand Products in Russia"). The Group also plans to consider growth opportunities within its mining operations, including by expanding production capacities at its existing mines and by developing new mining deposits.

The Group's acquisition strategy in the steel industry is primarily focused on the CIS and the United States (see also "— Recent Developments"), although as the United States market is relatively mature and consolidated, opportunities in that market are not expected to arise frequently. The Group may also acquire or develop steel operations in regions expected to provide high levels of growth in demand, particularly where low-cost sources of raw materials and other production inputs are readily available. As regards raw materials, the Group plans to seek additional sources of raw materials to enhance its existing vertical integration in Russia and to provide greater certainty of supply for the Group's operations in other markets, including by seeking access to raw materials within the countries in which it operates and elsewhere, particularly in locations with relatively low-cost mining operations and with convenient access to international markets.

In this regard, in May 2008 in connection with an acquisition of a minority stake in Mano River Resources Inc, the Group agreed to acquire a 61.5 percent stake in African Iron Ore Group Ltd, a company involved in the Putu Range iron ore project in eastern Liberia, subject to certain conditions. Through this acquisition, if successfully completed, the Group plans to explore and develop iron ore deposits, with a view to extracting iron ore for export to North America and European markets (see also "— Recent Developments"). Further, the Group is considering the acquisition of coal mining assets in the United States, aimed at securing a long-term supply of coal to its expanded operations in the United States (see also "— Optimisation of the Group's Operations in the United States" and "— Recent Developments"). The Group also plans to expand its mining operations by actively participating in the consolidation of the Russian/CIS iron ore and coking coal industries as well as participating in "greenfield" projects in Russia and neighbouring countries, and forming alliances with mining majors.

**RISK FACTORS**

An investment in the Notes involves a high degree of risk, including but not limited to the following.

- The steel and mining industries are cyclical which may result in unexpected fluctuations in the demand for the Group's products.
- Changes in prices or supply of raw materials, such as coal, iron ore and energy, could adversely affect the Group's profitability.
- The Group will require a significant amount of cash to fund its capital expenditure programme, without which the programme may not be completed on schedule or at all.
- The Group has grown rapidly and intends to make further acquisitions, however it may not be able to successfully integrate or identify suitable acquisition targets.
- Any local or global economic downturn in significant steel-consuming industry sectors, such as the construction industry or the automotive industry, could adversely affect demand for the Group's products.
- The Group's competitive position and future prospects are heavily dependent on its controlling shareholder's and senior management's experience and expertise.
- The Company's subsidiaries have significant borrowings, to which the Notes are structurally subordinated.
- Weaknesses relating to the Russian legal system and Russian legislation create an uncertain environment for investment and for business activity.
- Political risks and governmental instability could adversely affect the value of investments in Russia, including the Notes.
- Arbitrary, selective or unlawful state action, in particular by the tax authorities, could have a material adverse effect on the Group's business.
- The lack of independence of certain members of the judiciary, the difficulty of enforcing court decisions and governmental discretion in instigating, joining and enforcing claims could prevent the Group or the Noteholders from obtaining effective redress in a court proceeding and could materially adversely affect the value of the Notes.

For further information on the risks affecting the Group, see "Risk Factors".

**USE OF PROCEEDS**

The proceeds of the issue of the Notes will be used by the Issuer for the sole purpose of financing the Loan. The proceeds from the Loan (expected to be US$1,250,000,000 before taking account of commissions and expenses), which is being funded in full by the issue of the Notes, will be used by the Company: (i) for working capital; and/or (ii) for general corporate purposes; and/or (iii) to finance acquisitions and/or to refinance indebtedness. Total commissions and expenses relating to the offering of the Notes are expected to be approximately US$12,500,000. The net proceeds of the Loan to the Company are expected to be approximately US$1,237,500,000.

## Recent Developments

### WCI Steel

In July 2008, the Group acquired the outstanding equity of WCI Steel, which operates a steel mill in Warren, Ohio, for a total cash consideration of approximately US$140 million plus the assumption of, according to the Group's estimates, approximately US$285 million of liabilities and the repayment of debt in an additional amount of approximately US$274.9 million, including payments connected with the redemption of certain senior secured notes of WCI Steel referred to below. WCI Steel's product line comprises custom and commodity flat rolled steel products, including hot-rolled, cold-rolled and galvanised steel. WCI Steel has an estimated production capacity of approximately 1.85 million tonnes of crude steel per year and produced approximately 1.0 million tonnes of crude steel in 2007. The Group believes that WCI Steel's product line, which includes high-carbon and alloy products, and its geographical location close to some of the Group's existing customers and operations, should provide a range of advantages to the Group's US operations in addition to the increased capacity the acquisition gives to the Group in the US market for flat products. The Group's preliminary estimate of the capital expenditure that would be required at WCI Steel for the period from 2008 to 2012 is approximately US$175 million.

In connection with the acquisition, WCI Steel has called for the redemption of the US$100 million aggregate principal amount outstanding of its 8 percent senior secured notes due 2016. Notice of the redemption has been mailed to record holders of such notes and the notes are expected to be redeemed in August 2008.

Recently, an unsuccessful bidder for WCI Steel, together with certain existing minority shareholders of WCI Steel, brought proceedings against WCI Steel, the Company and another member of the Group, seeking an injunction to prevent the completion of the acquisition of WCI Steel by the Group. The plaintiffs alleged that the board of directors of WCI Steel breached its fiduciary duties by, among other matters, not accepting the unsuccessful bidder's bid. The proceedings did not assert any claims against the Company or the other member of the Group. A hearing was held on 27 June 2008, at the conclusion of which the court denied the plaintiffs' application for a preliminary injunction, thereby permitting completion of the acquisition.

### Esmark

On 30 May 2008, the Group commenced an all cash US$17 per share offer to acquire all of the outstanding shares of common stock of Esmark, a manufacturer and distributor of flat rolled and other steel products in the United States. Initially, the Group's offer was not supported by Esmark's board of directors. However, on 25 June 2008, the Group entered into an agreement with Esmark in connection with which the Group has increased the purchase price in the tender offer to US$19.25 per share in cash and Esmark's board of directors has recommended that Esmark's shareholders tender their shares to the Group. The expiration date of the tender offer has been extended to 10:00 am, New York City time, 4 August 2008. The offer and related transactions contemplated by the agreement are subject to certain customary closing conditions. The Group has entered into an agreement with Esmark's majority shareholder to tender its shares in the tender offer. The Group has also entered into an agreement that satisfies the successorship clause of the United Steelworkers' collective bargaining agreement. If the acquisition is successfully completed, the Group will acquire all of Esmark's business, including Wheeling-Pittsburgh Steel Corporation, Esmark Steel Services Group, Inc and the remaining 50 percent interest in Mountain State Carbon, LLC, a blast furnace coking coal production joint venture with the Group.

The Group's operating and restructuring plan for Esmark, upon successful completion of the acquisition, includes a five-year capital investment programme and is designed to derive value from Esmark through operational improvements, including the maximisation and optimisation of production at the EAF, upgrades to enhance the quality and capacity of the hot strip mill, improvements of the downstream operations, and leveraging synergies and geographical alignment between the Group's other assets in the United States. The Group believes that its combined operations in the United States, including Esmark, would create one of North America's leading producers of flat rolled steel, further expanding the Group's product offerings to its customers in a market that has displayed consistent demand for high quality steel.

The acquisition of Esmark, if successfully completed, is expected to provide the Group with substantial synergies with its current US operations at the Dearborn facility, SeverCorr, Sparrows Point and

WCI Steel. Full ownership of Mountain State Carbon, LLC is also expected to increase the Group's vertical integration with raw materials in the United States. In addition, Esmark's service centres and corrugated sheet production facilities are expected to enhance the Group's operations in the US by allowing it to reach more customers and add value to its steel products.

Following completion of the tender offer, subject to the terms and conditions set forth in the offer to purchase, the Group intends to consummate a second-step merger where all remaining Esmark stockholders will receive the same cash price paid in the tender offer, subject to any available appraisal rights under Delaware law. If the offer is accepted at the revised offer price of US$19.25 per share, the total purchase price for all of the outstanding shares of common stock of Esmark would be approximately US$775 million. The Group has also purchased Esmark's aggregate US$110 million term loan facilities from Essar Steel Holdings Limited ("**Essar Steel**"). The Group has, on behalf of Esmark, paid Essar Steel certain other termination and change of control fees and prepayment penalties in connection with certain existing arrangements between Esmark and Essar Steel, including a US$25 million termination fee and a US$20.25 million payment in lieu of the exercise by Essar Steel of its conversion rights related to the term loan facilities referred to above.

**Mano River Resources Inc/African Iron Ore Group**

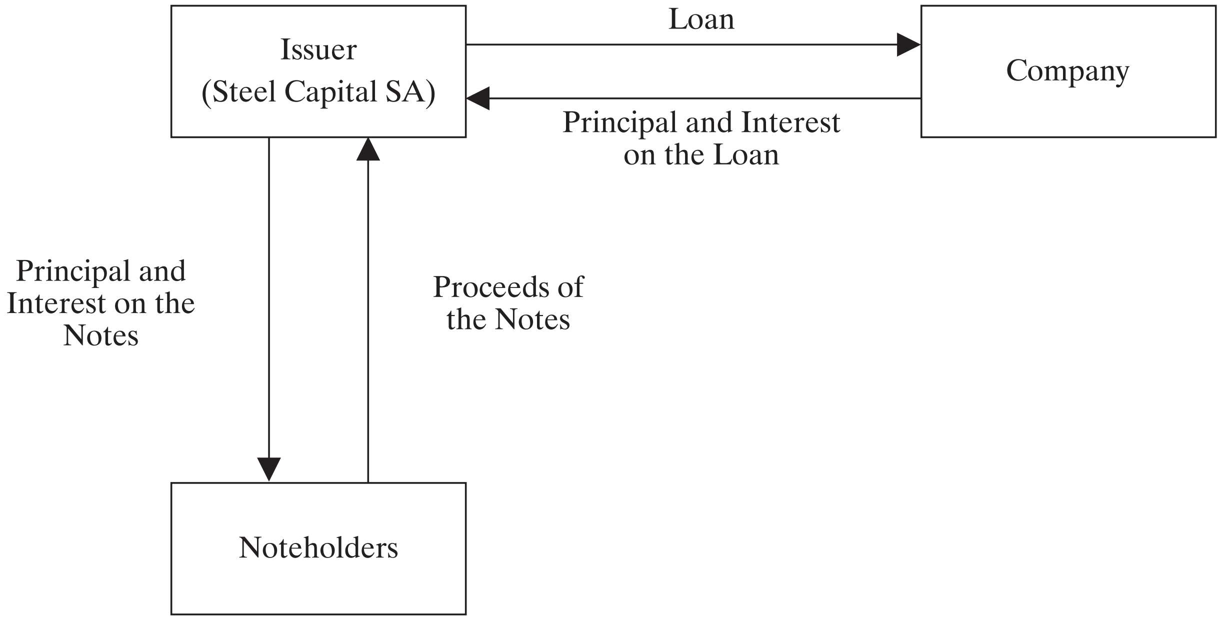
In May 2008, the Group entered into arrangements to acquire a minority stake in Mano River Resources Inc ("**Mano**"), a company focused on the exploration and development of iron ore, diamonds and gold in west Africa, listed on the London Stock Exchange's Alternative Investment Market and on the TSX-Venture Exchange in Canada. The acquisition price was approximately US$4 million. The Group has also agreed to acquire a 61.5 percent stake in African Iron Ore Group Ltd, a company currently majority-owned by Mano and involved in the Putu Range iron ore project in eastern Liberia, for approximately US$37.5 million, subject to certain conditions, including Mano converting its exploration licence into a mineral development agreement with the government of Liberia.

**Potential Coal Mining Acquisitions**

The Group is considering the strategic acquisition of coal mining assets in the United States. After completing the assessment of potential acquisition targets, the Group may decide to submit a bid on one or more coal mining assets in the near term, possibly as early as July 2008. If the Group were to submit any such bids, and if one or more of the relevant acquisition targets were successfully acquired, the aggregate purchase price for such assets could be material to the Group's financial condition and results of operations. However, there can be no assurance that any such bids will be made or, if made, that any such acquisitions of coal mining assets will be successfully completed.

**OVERVIEW OF TRANSACTION STRUCTURE**

*The following summary description should be read in conjunction with, and is qualified in its entirety by, the Terms and Conditions of the Notes and the provisions of the Loan Agreement that are set out elsewhere in this Prospectus.*




The transaction will be structured around the Loan to the Company by the Issuer. The Issuer will issue the Notes, which will be limited recourse loan participation notes issued for the sole purpose of funding the Loan to the Company. The Notes will be constituted by, be subject to, and have the benefit of, the Trust Deed. The obligations of the Issuer to make payments under the Notes shall constitute an obligation only to account to the Noteholders for an amount equal to the sums of principal, interest and/or additional amounts (if any) actually received by or for the account of the Issuer pursuant to the Loan Agreement less any amount in respect of the Reserved Rights (as defined in the Trust Deed).

As provided in the Trust Deed, the Issuer, with full title guarantee and as continuing security for the payment of all sums under the Trust Deed and the Notes, will charge in favour of the Trustee (the "**Charge**"):

(a) all principal, interest and other amounts now or hereafter payable by the Company to the Issuer as lender under the Loan Agreement;

(b) the right to receive all sums which may be or become payable by the Company under any claim, award or judgment relating to the Loan Agreement; and

(c) all the rights, title and interest in and to all sums of money now or in the future deposited in an account with Citibank, N.A., London Branch in the name of the Issuer (the "**Account**") and the debts represented thereby (including interest from time to time earned on the Account, if any),

provided that for the avoidance of doubt, the Issuer shall remain the legal and beneficial owner of the property subject to the Charge following the granting of the Charge and that Reserved Rights and any amounts relating to Reserved Rights are excluded from the Charge.

In addition, the Issuer with full title guarantee will assign absolutely to the Trustee for the benefit of the Trustee and the Noteholders all the rights, title, interest and benefits, both present and future, which have accrued or may accrue to the Issuer as lender under or pursuant to the Loan Agreement (as amended from time to time) (including, without limitation, all monies payable to the Issuer and any claims, awards and judgments in favour of the Issuer in connection with the Loan Agreement (as amended from time to time) and the right to declare the Loan immediately due and payable and to take proceedings to enforce the obligations of the Company thereunder) other than any rights, title, interests and benefits which are subject to the Charge and other than the Reserved Rights and any amounts relating to the Reserved Rights. As a consequence of such assignment, the Trustee will assume the rights of the Issuer under the Loan Agreement as set out in the relevant provisions of the Trust Deed.

The Issuer will covenant not to agree to any amendments to or any modification or waiver of, or suffer any breach of, the terms of the Loan Agreement unless the Trustee has given its prior written consent. The Issuer will further agree to act at all times in accordance with any instructions of the Trustee from time to time with respect to the Loan Agreement (subject to being indemnified and/or secured to its satisfaction by the Company), save as otherwise provided in the Trust Deed or the Loan Agreement. Any amendments, modifications, waivers or authorisations made with the Trustee's consent shall be notified to the Noteholders in accordance with Condition 14 of the Terms and Conditions relating to the Notes, unless the Trustee agrees otherwise, and shall be binding on the Noteholders.

The security under the Trust Deed will become enforceable upon the occurrence of a Relevant Event, that is, the earlier of (a) the failure by the Issuer to make any payment of principal or interest or additional amounts (if any) on the Notes when due; or (b) the Issuer becoming insolvent or bankrupt or unable to pay its debts, stopping, suspending or threatening to stop or suspend payment of all or (in the opinion of the Trustee) a material part of its debts, proposing or making a general assignment or an arrangement or composition with or for the benefit of the relevant creditors in respect of any such debts or a moratorium is agreed or declared in respect of or affecting all or (in the opinion of the Trustee) a material part of the debts of the Issuer or an order is made or an effective resolution is passed for the winding up or dissolution of the Issuer or the Issuer becomes subject to any insolvency, bankruptcy, *concordat préventif de faillite*, moratorium (*sursis de paiement*), controlled management (*gestion contrôlée*), general settlement with creditors, liquidation, reorganisation and any other similar legal proceedings affecting the Issuer or a *commissaire à la gestion contrôlée, a liquidateur, a commissaire, a curateur*, an *administrateur* or any similar officer is appointed as a consequence of the financial difficulties affecting the Issuer.

## OVERVIEW OF THE OFFERING AND PROVISIONS OF THE NOTES AND THE LOAN

*The following overview contains basic information about the Notes and the Loan and should be read in conjunction with, and is qualified in its entirety by, the information set forth under "The Loan Agreement" and "Terms and Conditions of the Notes" appearing elsewhere in this Prospectus.*

| | |
|---|---|
| ***Issuer*** | Steel Capital SA (the "**Issuer**"). |
| ***Company (as Borrower)*** | OAO Severstal (the "**Borrower**" or the "**Company**") with its registered office and business headquarters at Ul. Mira 30, 162600 Cherepovets, Russia. |
| ***Offering*** | US$1,250,000,000 9.75 percent Loan Participation Notes due 2013. |
| ***Trustee*** | Citibank, N.A., London Branch. |
| ***Principal Paying Agent and Transfer Agent*** | Citibank, N.A., London Branch. |
| ***Registrar*** | Citigroup Global Markets Deutschland AG & Co. KGaA. |
| ***New York Paying Agent and Transfer Agent*** | Citibank, N.A., New York branch. |
| ***Issue Price of Notes*** | 100 percent of the principal amount of Notes. |
| ***Closing Date*** | 29 July 2008. |
| ***Maturity Date*** | 29 July 2013. |
| ***Interest*** | On each Interest Payment Date (being 29 January and 29 July in each year commencing on 29 January 2009), the Issuer shall account to the Noteholders for an amount equivalent to amounts of interest actually received by or for the account of the Issuer pursuant to the Loan Agreement, which interest under the Loan is equal to 9.75 percent per annum (as set forth in Clause 4.1 of the Loan Agreement). |
| ***Status*** | The Notes will constitute the obligation of the Issuer to apply the proceeds from the issue of the Notes solely for financing the Loan and to account to the Noteholders for an amount equivalent to sums of principal, interest and additional amounts (if any) actually received by or for the account of the Issuer pursuant to the Loan Agreement, less any amount in respect of Reserved Rights, all as more fully described in "Terms and Conditions of the Notes — 1 Status". |
| ***Security*** | The Notes will be secured by a charge on:<br>• all principal, interest and other amounts now or hereafter payable by the Company to the Issuer as Lender under the Loan Agreement and the right to receive all sums which may be or become payable by the Company under any claim, award or judgment relating to the Loan Agreement; and<br>• all of the Issuer's rights, title and interest in and to all sums of money now or in the future deposited in the Account, together with the debts represented thereby (including interest from time to time earned thereon, if any), pursuant to the Trust Deed, in each case, other than certain Reserved Rights and its right to any amounts in respect of such Reserved Rights. |

| | |
|---|---|
| ***Assignment of Rights*** | The Issuer with full title guarantee will assign absolutely its rights under the Loan Agreement (save for those rights charged or excluded as described above) to the Trustee pursuant to the Trust Deed. |
| ***Form*** | The Notes will be issued in registered form in the denomination of US$100,000, and integral multiples of US$1,000 in excess thereof. The Regulation S Notes and the Rule 144A Notes will be represented by a Regulation S Global Certificate and a Rule 144A Global Certificate, respectively. The Regulation S Global Certificate and the Rule 144A Global Certificate will be exchangeable for Definitive Certificates in the limited circumstances specified in the Regulation S Global Certificate and the Rule 144A Global Certificate. |
| ***Initial Delivery of Notes*** | On or before the Issue Date, the Rule 144A Global Certificate will be deposited with a custodian for DTC, and the Regulation S Global Certificate will be deposited with a common depositary for Euroclear and Clearstream, Luxembourg. The Rule 144A Notes will be registered in the name of a nominee of DTC, and the Regulation S Notes will be registered in the name of a common nominee for Euroclear and Clearstream, Luxembourg. |
| ***Optional Redemption by the Issuer in Limited Circumstances*** | In limited circumstances as more fully described in the Loan Agreement, the Notes may be redeemed at the option of the Issuer in whole, but not in part, at any time, upon giving notice to the Trustee, at the principal amount thereof, together with accrued and unpaid interest and additional amounts, if any, to the date of redemption in the event that it becomes unlawful for the Issuer to fund the Loan or allow the Loan to remain outstanding under the Loan Agreement or allow the Notes to remain outstanding. In such a case, the Issuer would require the Loan to be repaid in full. |
| ***Mandatory Redemption*** | The Issuer is required to redeem the Notes in whole, but not in part, at 100 percent of their aggregate principal amount plus accrued and unpaid interest and all additional amounts, if any, if the Loan should become repayable and be repaid pursuant to the Loan Agreement prior to the Maturity Date, including if the Company prepays the Loan because it is required to pay additional amounts on account of withholding taxes or is required to pay additional amounts on account of certain costs incurred by the Issuer pursuant to the Loan Agreement. |
| ***Relevant Events*** | In the case of certain events in relation to the Issuer (as defined in the Trust Deed), the Trustee may, subject as provided in the Trust Deed, enforce the security created in the Trust Deed in favour of the Noteholders. |
| ***Withholding Tax*** | All payments in respect of the Notes by or on behalf of the Issuer will be made free and clear of, and without deduction or withholding for or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or on behalf of Luxembourg or any political subdivision or any authority thereof or therein having the power to tax, other than as required by law. In such event, the sum payable by the Company |

to the Issuer will be required (subject to certain exceptions) to be increased to the extent necessary to ensure that the Noteholders receive the sum which they would have received had no such deduction or withholding been required. The sole obligation of the Issuer in this respect will be to account to the Noteholders for sums equivalent to the sums received from the Company.

***Certain Restrictions and Covenants***

The Issuer will have the benefit of certain covenants made by the Company, including a negative pledge, a limitation on the incurrence of indebtedness and restrictions on mergers and disposals, all as fully described in the Loan Agreement.

***Events of Default***

In the case of an Event of Default (as defined in the Loan Agreement), the Trustee may, subject as provided in the Trust Deed, declare all amounts payable under the Loan Agreement by the Company to be due and payable.

***Use of Proceeds***

The Issuer will lend an amount equivalent to the gross proceeds of the Notes to the Company. The Company intends to use the net proceeds:

(i) for working capital; and/or

(ii) for general corporate purposes; and/or

(iii) to finance acquisitions and/or to refinance indebtedness.

***Further Issues***

The Issuer may from time to time, without the consent of the Noteholders, create and issue further Notes on the same terms as existing Notes and such further Notes shall be consolidated and form a single series with such existing Notes.

***Ratings***

Moody's Investors Service, Inc. ("**Moody's**") have assigned a Ba2 rating to the Company and a Ba2 rating to this issue of Notes. Standard & Poor's Ratings Service, a division of The McGraw-Hill Companies, Inc. ("**Standard & Poor's**"), have assigned a BB credit rating to the Company and a BB rating to this issue of Notes. Fitch Ratings Ltd ("**Fitch**") have assigned a rating of BB to the Company and a BB rating to this issue of Notes. A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by Moody's and/or Standard & Poor's and/or Fitch. A suspension, reduction or withdrawal of either or both of the ratings assigned to the Notes or the Company may adversely affect the market price of the Notes.

***Listing and Admission to Trading***

Application has been made to the Financial Services Authority in its capacity as competent authority under the Financial Services and Markets Act 2000 ("**FSMA**") (the "**UK Listing Authority**") for the Notes to be admitted to the official list of the UK Listing Authority (the "**Official List**") and to the London Stock Exchange plc (the "**London Stock Exchange**") for such Notes to be admitted to trading on the regulated market of the London Stock Exchange (the "**Market**"). The Market is regulated for the purposes of the Directive (2004/39/EC) of the European Parliament and of the Council on markets in financial instruments.

| | |
|---|---|
| ***Governing Law*** | The Notes, the Trust Deed and the Loan Agreement will be governed by English law. |
| ***Selling Restrictions*** | The Notes are subject to selling restrictions in the United Kingdom, the United States and the Russian Federation. See "Subscription and Sale". |
| ***ERISA Considerations*** | The Notes may be regarded for ERISA purposes as equity interests in a separate entity whose sole asset is the Loan. Accordingly, the Notes should not be acquired by any benefit plan investor or a governmental, church or non-US plan that is subject to any Federal, state, local or non-US law that is substantially similar to the provisions of Section 406 of the US Employee Retirement Income Security Act of 1974, as amended, or Section 4975 of the US Internal Revenue Code of 1986, as amended, or any entity whose assets are treated as assets of any such plan. Each purchaser and/or holder of Notes and each transferee therefore will be deemed to have made certain representations as to its status under ERISA. Potential purchasers should read the sections entitled "ERISA" and "Selling and Transfer Restrictions". |
| ***Security Codes*** | Regulation S ISIN: XS0376189857<br>Regulation S Common Code: 037618985<br>Rule 144A ISIN: US858057AA1<br>Rule 144A CUSIP: 858057AA0<br>PORTAL: P858057AA0 |

## OVERVIEW FINANCIAL INFORMATION OF THE GROUP

The following tables set forth, in summary form, consolidated balance sheet, income statement and other information relating to the Group. Such information has been derived from the Financial Statements of the Group prepared in accordance with IFRS. The reports of KPMG Limited appear elsewhere in this Prospectus. The financial information presented below should be read in conjunction with such Financial Statements, reports and "Management's Discussion and Analysis of Financial Condition and Results of Operations".

### CONSOLIDATED INCOME STATEMENT

| | Year ended 31 December | | | Three months ended 31 March | |
|---|---|---|---|---|---|
| | 2007 | 2006 (restated) | 2005 (restated) | 2008 | 2007 (restated) |
| | *(Amounts expressed in thousands of US dollars, except as otherwise stated)* | | | | |
| **Sales** | | | | | |
| Sales — external | 14,543,043 | 11,723,318 | 9,786,057 | 4,144,363 | 3,526,021 |
| Sales — to related parties | 701,868 | 725,714 | 665,589 | 164,630 | 166,502 |
| | 15,244,911 | 12,449,032 | 10,451,646 | 4,308,993 | 3,692,523 |
| Cost of sales | (10,541,571) | (8,601,227) | (6,831,138) | (3,165,953) | (2,531,468) |
| **Gross profit** | 4,703,340 | 3,847,805 | 3,620,508 | 1,143,040 | 1,161,055 |
| General and administrative expenses | (691,210) | (654,987) | (524,662) | (230,850) | (169,410) |
| Distribution expenses | (909,510) | (697,308) | (657,684) | (275,665) | (233,529) |
| Indirect taxes and contributions | (153,614) | (142,109) | (95,343) | (45,503) | (35,147) |
| Share of associates' (loss)/profit | (89,397) | (1,193) | (4,190) | (542) | 2,413 |
| Net income/(loss) from securities operations | 25,564 | 28,263 | 24,443 | (8,064) | 1,503 |
| Loss on disposal of property, plant and equipment | (35,280) | (39,292) | (36,780) | (14,495) | (9,230) |
| Net other operating (expenses)/ income | (7,520) | (27,109) | (20,344) | 197,185 | (1,037) |
| **Profit from operations** | 2,842,373 | 2,314,070 | 2,305,948 | 765,106 | 716,618 |
| Impairment of property, plant and equipment | (29,109) | (57,736) | (111,384) | (1,855) | (950) |
| Net gain on restructuring of tax liabilities | — | 14,669 | 174,178 | — | — |
| Negative goodwill, net | 12,223 | 4,213 | 7,630 | 2,166 | 633 |
| Net other non-operating expenses | (58,576) | (53,536) | (52,753) | (32,629) | (17,969) |
| **Profit before financing and taxation** | 2,766,911 | 2,221,680 | 2,323,619 | 732,788 | 698,332 |
| Interest income | 172,937 | 102,402 | 65,134 | 28,944 | 36,765 |
| Interest expense | (288,293) | (244,977) | (203,057) | (90,875) | (68,363) |
| Foreign exchange difference | 2,900 | 33,324 | (60,231) | 13,887 | (180) |
| **Profit before income tax** | 2,654,455 | 2,112,429 | 2,125,465 | 684,744 | 666,554 |
| Income tax expense | (681,269) | (635,298) | (500,907) | (232,770) | (190,279) |
| **Profit from continuing operations** | 1,973,186 | 1,477,131 | 1,624,558 | 451,974 | 476,275 |
| Profit from discontinued operations | 433 | 32,849 | 602 | — | 4,935 |
| **Profit for the year/period** | 1,973,619 | 1,509,980 | 1,625,160 | 451,974 | 481,210 |
| Attributable to: | | | | | |
| shareholders of OAO Severstal | 1,936,423 | 1,454,198 | 1,561,182 | 438,706 | 458,091 |
| minority interest | 37,196 | 55,782 | 63,978 | 13,268 | 23,119 |
| Weighted average number of shares outstanding during the period (millions of shares) | 1,007.7 | 928.4 | 912.2 | 1,007.7 | 1,007.7 |
| Basic and diluted earnings per share (US dollars) | 1.92 | 1.57 | 1.71 | 0.44 | 0.45 |

**CONSOLIDATED BALANCE SHEET**

| | As at 31 December | | | As at 31 March |
|---|---|---|---|---|
| | 2007 | 2006 (restated) | 2005 (restated) | 2008 |
| | *(Amounts expressed in thousands of US dollars)* | | | |
| **Assets** | | | | |
| **Current assets:** | | | | |
| Cash and cash equivalents | 1,546,881 | 1,701,022 | 1,327,887 | 2,406,295 |
| Short-term bank deposits | 665,977 | 1,147,270 | 674,512 | 321,472 |
| Short-term financial investments | 267,633 | 321,842 | 267,851 | 206,127 |
| Trade accounts receivable | 1,674,618 | 1,324,585 | 1,174,193 | 2,003,879 |
| Amounts receivable from related parties | 162,719 | 127,703 | 173,808 | 99,692 |
| Inventories | 2,537,470 | 2,222,372 | 1,725,528 | 2,837,856 |
| VAT recoverable | 283,745 | 339,392 | 442,297 | 302,511 |
| Income tax recoverable | 75,993 | 35,904 | 28,671 | 98,629 |
| Assets held for sale | 461,196 | — | — | 451,662 |
| Other current assets | 321,362 | 259,208 | 181,685 | 402,584 |
| **Total current assets** | 7,997,594 | 7,479,298 | 5,996,432 | 9,130,707 |
| **Non-current assets:** | | | | |
| Long-term financial investments | 152,866 | 199,940 | 89,541 | 144,216 |
| Investment in associates and joint ventures | 589,092 | 354,906 | 210,652 | 199,131 |
| Property, plant and equipment | 7,292,811 | 6,470,385 | 5,319,568 | 8,705,285 |
| Intangible assets | 611,261 | 61,666 | 56,523 | 624,712 |
| Assets held for sale | — | 113,516 | 66,117 | — |
| Restricted cash | — | — | — | 14,468 |
| Deferred tax assets | 52,324 | 30,150 | 35,076 | 61,146 |
| Amounts receivable from related parties | — | — | 35,095 | — |
| Other non-current assets | 21,474 | 3,844 | 3,105 | 43,124 |
| **Total non-current assets** | 8,719,828 | 7,234,407 | 5,815,677 | 9,792,082 |
| **Total assets** | 16,717,422 | 14,713,705 | 11,812,109 | 18,922,789 |
| **Liabilities and shareholders' equity** | | | | |
| **Current liabilities:** | | | | |
| Trade accounts payable | 1,090,884 | 1,038,901 | 866,629 | 1,325,472 |
| Bank customer accounts | — | 31,143 | 98,867 | — |
| Amounts payable to related parties | 58,915 | 175,740 | 491,957 | 72,130 |
| Short-term debt finance | 972,079 | 957,564 | 996,125 | 1,257,587 |
| Income taxes payable | 41,381 | 44,348 | 86,001 | 96,978 |
| Other taxes and social security payable | 200,424 | 199,963 | 257,678 | 297,927 |
| Dividends payable | 107,485 | 23,243 | 12,275 | 6,078 |
| Liabilities related to assets held for sale | 91,750 | — | — | 103,993 |
| Other current liabilities | 600,580 | 506,848 | 379,218 | 708,277 |
| **Total current liabilities** | 3,163,498 | 2,977,750 | 3,188,750 | 3,868,442 |
| **Non-current liabilities:** | | | | |
| Long-term debt finance | 2,354,823 | 2,048,035 | 1,931,694 | 2,852,956 |
| Deferred tax liabilities | 374,636 | 403,076 | 356,739 | 436,332 |
| Retirement benefit liability | 387,398 | 442,954 | 338,486 | 437,514 |
| Liabilities related to assets held for sale | — | 1,792 | 172 | — |
| Other non-current liabilities | 226,388 | 286,090 | 281,075 | 394,986 |
| **Total non-current liabilities** | 3,343,245 | 3,181,947 | 2,908,166 | 4,121,788 |

| | As at 31 December | | | As at 31 March |
|---|---|---|---|---|
| | 2007 | 2006 (restated) | 2005 (restated) | 2008 |
| | *(Amounts expressed in thousands of US dollars)* | | | |
| **Equity**: | | | | |
| Share capital | 3,311,288 | 3,311,288 | 3,311,254 | 3,311,288 |
| Additional capital | 1,165,530 | 1,165,530 | 60,367 | 1,165,530 |
| Foreign exchange differences | 1,176,321 | 535,591 | 34,368 | 1,562,220 |
| Retained earnings | 4,082,834 | 2,983,954 | 1,818,475 | 4,404,914 |
| Hedging reserve | — | — | — | (21,698) |
| **Total equity attributable to shareholders of parent** | 9,735,973 | 7,996,363 | 5,224,464 | 10,422,254 |
| **Minority interest** | 474,706 | 557,645 | 490,729 | 510,305 |
| **Total equity** | 10,210,679 | 8,554,008 | 5,715,193 | 10,932,559 |
| **Total equity and liabilities** | 16,717,422 | 14,713,705 | 11,812,109 | 18,922,789 |

## SUMMARY CASH FLOW DATA

| | Year ended 31 December | | | Three months ended 31 March | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2008 | 2007 |
| | *(Amounts expressed in thousands of US dollars)* | | | | |
| **Net cash from operating activities** | 2,315,089 | 1,729,658 | 1,934,791 | 695,341 | 669,507 |
| **Cash from investing activities** | (1,981,967) | (2,169,137) | (1,178,089) | (73,150) | (959,246) |
| **Cash from financing activities** | (569,249) | 726,365 | (448,628) | 72,953 | 42,307 |

## OTHER MEASURES

| | Year ended 31 December | | | Three months ended 31 March | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2008 | 2007 |
| | | | *(US$ millions)* | | |
| EBITDA(1) | 3,680.4 | 2,957.1 | 2,839.3 | 1,035.5 | 904.0 |
| Interest expense(2) | 288.3 | 245.0 | 203.1 | 90.9 | 68.4 |
| Net interest expense(3) | 115.4 | 142.6 | 138.0 | 62.0 | 31.6 |
| Total debt(4) | 3,326.9 | 3,005.6 | 2,927.8 | 4,110.5 | 3,299.7 |
| Cash and cash equivalents | 1,546.9 | 1,701.0 | 1,327.9 | 2,406.3 | 1,500.7 |
| Short-term deposits | 666.0 | 1,147.3 | 674.5 | 321.5 | 1,711.8 |
| Net debt(5) | 1,114.0 | 157.3 | 925.4 | 1,382.7 | 87.2 |
| Certain ratios | | | | | |
| EBITDA/Interest expense | 12.8 | 12.1 | 14.0 | 11.4 | 13.2 |
| EBITDA/Net interest expense | 31.9 | 20.7 | 20.6 | 16.7 | 28.6 |
| Net debt/EBITDA | 0.3 | 0.1 | 0.3 | 0.3(6) | 0.1(6) |
| Total debt/EBITDA | 0.9 | 1.0 | 1.0 | 1.0(7) | 0.9(7) |

Notes:

(1) The Group defines EBITDA as profit from operations plus depreciation and amortisation and loss on disposal of property, plant and equipment.

- EBITDA is presented as a supplemental measure of the Group's operating performance, which the Group believes is frequently used by securities analysts, investors and other interested parties in the evaluation of companies in the steel industry.
- EBITDA has limitations as an analytical tool, and investors should not consider it in isolation, or as a substitute for analysis of the Group's operating results as reported under IFRS. Some of these limitations are as follows:
  - EBITDA does not reflect the impact of financing costs, which can be significant and could further increase if the Group incurs more debt, on the Group's operating performance.
  - EBITDA does not reflect the impact of income taxes on the Group's operating performance.

- EBITDA does not reflect the impact of depreciation and amortisation on the Group's operating performance. The assets of the Group's businesses which are being depreciated, depleted and/or amortised will have to be replaced in the future and such depreciation and amortisation expense may approximate the cost to replace these assets in the future. By excluding this expense from EBITDA, EBITDA does not reflect the Group's future cash requirements for these replacements. EBITDA also does not reflect the impact of loss on disposal of property, plant and equipment.
- Other companies in the steel and mining industries may calculate EBITDA differently or may use it for different purposes than the Group, limiting its usefulness as a comparative measure.
- The Group relies primarily on its IFRS operating results and uses EBITDA only supplementally. See the Financial Statements included elsewhere in this Prospectus. EBITDA is not defined by, or presented in accordance with, IFRS. EBITDA is not a measurement of the Group's operating performance under IFRS and should not be considered as an alternative to profit, operating profit, net cash provided by operating activities or any other measure of performance under IFRS or as an alternative to cash flow from operating activities or as a measure of the Group's liquidity. In particular, EBITDA should not be considered as a measure of discretionary cash available to the Group to invest in the growth of its business.

**Consolidated EBITDA Reconciliation**

| | Year ended 31 December | | | Three months ended 31 March | |
|---|---|---|---|---|---|
| | **2007** | **2006** | **2005** | **2008** | **2007** |
| | | | *(US$ millions)* | | |
| Profit from Operations | 2,842.4 | 2,314.1 | 2,305.9 | 765.1 | 716.6 |
| Add: | | | | | |
| Depreciation and amortisation | 802.7 | 603.7 | 496.6 | 255.9 | 178.2 |
| Loss on disposal of plant, property, plant & equipment | 35.3 | 39.3 | 36.8 | 14.5 | 9.2 |
| Consolidated EBITDA[(1)] | 3,680.4 | 2,957.1 | 2,839.3 | 1,035.5 | 904.0 |

(2) Interest expense consists of the interest expense portion of net financing (expense)/income and does not include the interest expense portion of net income from banking/bank lending operations.

(3) Net interest expense consists of the interest expense and interest income, and does not include the interest expense portion of net income from banking/bank lending operations.

(4) Total debt consists of current and non-current debt finance.

(5) Net debt consists of total debt less cash and cash equivalents and short-term deposits.

(6) Based on EBITDA for the three months ended 31 March, multiplied by four, and net debt as at 31 March.

(7) Based on EBITDA for the three months ended 31 March, multiplied by four, and total debt as at 31 March.

# RISK FACTORS

*An investment in the Notes involves a high degree of risk. Prospective investors should consider carefully the risks set forth below in this Prospectus prior to making any investment decision with respect to the Notes. The risks described below could have a material adverse effect on the Group's and the Issuer's business, financial condition, results of operations, future prospects and the value of the Notes.*

*Investors should note that the risks described below are not the only risks the Group and the Issuer face. The Group and the Issuer have described only the risks that they consider to be material. However, there may be additional risks that the Group or the Issuer currently consider not to be material or of which the Group or the Issuer are not currently aware, and any of these risks could have the effects set forth above.*

## RISK FACTORS RELATING TO THE GROUP AND THE STEEL AND MINING INDUSTRIES

***The steel and mining industries are cyclical, which may result in adverse fluctuations in the demand for the Group's products***

The industries in which a large proportion of the Group's customers operate, such as the automotive, construction, and oil and gas industries, are cyclical in nature, which can result in adverse fluctuations in the demand for steel products. Demand for the raw materials necessary for the production of steel products, such as iron ore and coal, is generally correlated with the demand for steel products. Particular economic and market factors may also have a significant effect on certain parts of the Group's operations, such as an economic downturn in the United States leading to a decrease in production by automotive manufacturers, resulting in a decrease in demand for the Group's automotive flat steel products. In addition, increased competition from emerging or established steel producers and mining operations may cause oversupply or undersupply of steel and mining products on the global markets. Adverse fluctuations in the demand for the Group's products or the supply of competing products may result in overproduction or underproduction, increased costs or general uncertainty in the industry, any of which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Any change in prices or supply of raw materials may cause the Group's financial results to vary, and this could have a material adverse affect on its results of operations***

The Group requires substantial amounts of raw materials in the steel production process, in particular coal and iron ore. Although Severstal Resources has a relatively secure supply of iron ore and coal for the Russian Steel Division, the availability of coal, iron ore and/or slabs for Severstal International, particularly North America and Lucchini, and the availability of other necessary raw materials such as scrap may be negatively affected by a number of factors largely beyond the control of the Group, including interruptions in production by suppliers, supplier allocation to other purchasers, price fluctuations and transport costs. In addition, the Group's operations require substantial amounts of other raw materials, including various types of limestone, alloys, refractories, oxygen, fuel and gas, the price and availability of which are also subject to market conditions. The Group may not be able to adjust its prices to recover the costs of increases in the prices of such raw materials. Any change in the prices or supply of raw materials could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group will require a significant amount of cash to fund its capital expenditure programme. If the Group is unable to generate this cash through operations or external sources, this programme may not be completed on schedule or at all***

Steel production and mining are capital-intensive businesses. In particular, the Group currently intends to spend approximately US$16.3 billion in its capital expenditure programme from 2008 to 2012 including on the modernisation and development of its existing steel production and mining facilities see "Business — Investment in Modernisation and Advanced Technological Processess". The Group plans to rely on cash generated from its operations, and to a lesser extent external financing, to provide the capital needed for the capital expenditure programme. However, there can be no assurance that the Group will be able to generate adequate cash from operations or that external financing, if necessary, will be available on reasonable terms. In addition, capital expenditure programmes are subject to a variety of potential problems and uncertainties, including changes in economic conditions, delays in completion or delivery, cost overruns and defects in design or construction, which may require additional cash investment. For example, the recent construction of the production facilities at SeverCorr in the United States experienced significant cost overruns as a result of higher than expected construction costs. Further, the Group's capital expenditure programme includes plans to acquire significant amounts of new equipment, including more advanced technologies. While such new production equipment and technologies are aimed at increasing the operational performance of the Group's facilities, there can be no assurance that the equipment will meet its intended production targets on a timely basis, or at all, the result of which could be reduced production, delays or additional costs. Further, to finance the programme, the Group may incur a substantial amount of additional indebtedness, the interest and principal repayments on which may be a significant drain on the cash flows of the Group. A failure or delay of the Group's capital expenditure programme or the significant increases in the financing costs that may be incurred to fund the programme could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group has grown rapidly and intends to pursue opportunities to grow its operations through further acquisitions, but there can be no assurance that the Group will be able to successfully integrate such acquired companies or identify suitable acquisition targets***

In recent years, the Group has increased its ownership interests in a number of companies and acquired other companies, businesses and production assets, in particular the acquisition of Lucchini by the Group, mining operations by Severstal Resources and several other acquisitions by Severstal International in the United States (see "Business — Severstal International — North America"). The Group intends to consider future acquisitions of assets or companies that may enable it to expand its current operations and increase integration and production synergies. In particular, the Group plans to target synergies in its operations in the United States, particularly if the acquisition of Esmark is successfully completed (see "Business — Recent Developments"), including knowledge and technology transfers, aggregated purchasing, logistics and other overhead items, and optimised scheduling and production. Also, the Group plans to expand its mining operations, including in relation to coal assets in the United States (see "Business — Recent Developments").

The success of past, current and future acquisitions will depend on the Group's ability to manage the assimilation of the acquired assets or companies into its operations despite the inherent difficulties, such as cultural differences, redundancies of personnel, incompatibility of equipment and information technology, production failures or delays, loss of significant customers, problems with minority shareholders in acquired companies and their material subsidiaries, the potential disruption of the Group's own business, the assumption of liabilities relating to the acquired assets or businesses, the possibility that indemnification agreements with the sellers of such assets may be unenforceable or insufficient to cover potential liabilities, the impairment of relationships with employees and counterparties as a result of difficulties arising out of integration, poor records or internal controls and difficulty in establishing immediate control over cash flows. Furthermore, there can be no assurance that the Group will be able to achieve the targets synergies in its operations in the United States or elsewhere in connection with the recent or planned acquisitions.

Furthermore, the value of any business the Group acquires or invests in may be lower than the amount that the Group pays for it if, for example, there is a decline in the position of that business in the market or markets in which it operates or there is a decline in the market generally. Developed markets, such as those in Western Europe and the United States, may offer lower margins, as a general matter, than those in Russia and the CIS. The Group may not be able to identify suitable acquisition targets, and future acquisitions may not be available to the Group on terms as favourable as in the past. The Group faces significant competition for potential acquisitions. When making acquisitions it may not be possible for the Group to conduct a detailed investigation of the nature of the assets being acquired due to, for example, time constraints in making the acquisition decision and other factors. The Group may also become responsible for additional liabilities or obligations not foreseen by the Group at the time of an acquisition, including in particular with respect to any financial liabilities entered into by previous management prior to completion.

Any or all of these difficulties, if they materialise, could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Any local or global economic downturn in significant steel-consuming industry sectors could adversely affect demand for the Group's products***

Certain significant steel-consuming industry sectors, such as the automotive and construction industries, are particularly sensitive to changes in general economic conditions. As a result, the demand for steel products in these industry sectors may decrease disproportionately as economic conditions deteriorate. Significant decreases in the demand for steel products in any industry sector in which the Group generates substantial portions of its revenues, for example any decrease in demand caused by the recent downturn in the US automotive industry, could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group may experience equipment failure or other unanticipated events, which may result in significant interruption in manufacturing processes, production curtailment and shutdowns***

The Group's manufacturing processes depend on critical pieces of steel-making equipment, such as furnaces, continuous casters and rolling equipment, and electrical equipment, such as transformers. This equipment may, on occasion, be out of service as a result of malfunction or defect. In addition, the Group's facilities are subject to the risk of damage due to unanticipated events, such as fires, explosions or adverse weather conditions. In the event of equipment failure or damage to its facilities, the Group may experience loss of revenues or customers due to material plant shutdowns or periods of reduced production and may require large capital expenditures to repair or replace faulty machinery or to repair damaged facilities, and if the equipment failure or damage to facilities extends to injuries to employees or has an environmental impact, other costs or liabilities arising out of those circumstances. For example, on 5 January 2008, an explosion occurred at blast furnace "B" at Severstal North America's Dearborn facility involving significant damage to the furnace and its closure. The blast furnace is to be rebuilt and is currently expected to be operational by the end of 2009, and Severstal North America estimates that the lost production will be approximately 1,300,000 tonnes of crude steel, with a significant consequential effect on the facility's downstream operations. Also in January 2008, a fire at blast furnace 5 at the Cherepovets Steel Plant, caused by the escape of gases from the third Cowper stove due to a corroded cover, resulted in a temporary cessation of operations. There can be no assurance that similar or other incidents involving equipment failure or other interruptions in production will not occur in the future, or that such incidents will have a contained effect on the Group's production. Any resulting loss of revenues or customers or large unexpected capital expenditures would have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group's mining operations are subject to hazards and risks that could lead to unexpected production delays, increased costs, damage to property or injury or death to persons***

The Group's mining operations include open-pit and underground mining, both of which involve significant hazards and risks. Hazards associated with the Group's open-pit mining operations include flooding of the open pit, collapses of the open-pit wall, accidents related to the operation of large open-pit mining and rock transportation equipment, accidents related to the preparation and ignition of large-scale open-pit blasting operations, production disruptions due to weather and hazards related to the disposal of mineralised wastewater, such as groundwater and waterway contamination. Hazards associated with the Group's underground mining operations include underground fires and explosions, including those caused by flammable gas, cave-ins or ground falls, discharges of gases and toxic chemicals, flooding, sinkhole formation and ground subsidence and other accidents and conditions resulting from drilling, blasting and removing and processing material from an underground mine. If any of these hazards or accidents results in significant injury to employees and damage to equipment or other property, the Group may experience unexpected production delays, increased production costs, and increased capital expenditures to repair or replace equipment or property, as well as claims from affected employees and environmental and other authorities for any alleged breaches of applicable laws or regulations. For example, in June 2007, at the Vorkutaugol mining complex, there was an explosion and fire, which resulted in ten casualties and the suspension of mining (see "Business — Health, Safety and Environment — Severstal Resources"). Any such disruptions to mining, delays and costs could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Additional or stricter environmental rules and regulations may significantly increase the Group's cost of compliance***

The Group's steel-making plants and mining operations involve potential environmental problems including the generation of pollutants and the storage and disposal of wastes and other hazardous materials. As a result, the Group must comply with stringent regulatory requirements necessitating the commitment of significant financial resources and expects that the global trend towards stricter environmental laws and regulations will continue. Any significant increase in the cost of complying with such environmental rules and regulations in the future could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Estimates of the Group's mining reserves and resources are subject to uncertainties and estimates of its resources are speculative***

The Group's estimates of its iron ore and coal reserves and resources contained in this Prospectus are calculated by reference to estimates provided by IMC Consulting Ltd in its report dated 14 August 2006, prepared in accordance with JORC reporting standards. See "Presentation of Financial and Other Information — Mining Reserves". Such estimates were based on interpretations of geological data obtained from sampling techniques and projected rates of production. Sampling techniques and projections are inherently uncertain and variances in reserve and resource estimates under different methodologies may be difficult to determine and evaluate. In addition, reserve and resource estimates do not account for the possibility that the initial phase of drilling and exploration may take several years before production is possible or for the effect of market prices of iron ore or coal on the economic feasibility of mining any particular deposit.

If the Group's actual production of iron ore and coal in the future is significantly less than the Group's planned production based on these estimates of its reserves, the Group may not be able to supply iron ore and coal to its steel operations at an economically feasible price or at all, which would have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***An increase in existing trade barriers or the imposition of new trade barriers in the Group's principal export markets could cause a significant decrease in the demand for its products in those markets***

Some of the products of the Group's Russian operations are subject to various trade barriers, such as anti-dumping duties, tariffs and quotas, in its principal export markets, including the European Union and the United States. See "Regulatory Matters — Trade Barriers and Anti-Dumping Regulations". These trade barriers affect the demand for the Group's products by effectively increasing the prices for those products compared to domestically available products. An increase in existing trade barriers, or the imposition of new trade barriers, could cause a significant decrease in the demand for the Group's products in its principal export markets, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The reduction or elimination of trade barriers in the Group's principal domestic markets may increase competition, which could adversely affect the demand for or prices of its products in those markets***

The Russian Government has enacted various trade barriers, such as import customs duties, specific kinds of duties (including anti-dumping duties) and licensing against imports of foreign steel products. For example, Russia has in place import customs duties with respect to certain steel products imported from outside of Russia, excluding countries in the CIS. These customs duties are generally: (i) 5 percent of the customs value of some commodity steel products (for example, rolled steel and steel rod); (ii) 15 percent of the customs value of a variety of value-added products (for example, pipe); and (iii) 20 percent of the customs value of certain high value-added products. These trade barriers provide protection for domestic steel producers in Russia against foreign competition by effectively increasing the prices of imported products compared to domestically available products. However, Russia's entry into the WTO, which could occur in 2008 or shortly after, may involve agreements requiring Russia to reduce or eliminate these trade barriers and there can be no assurance that other similar agreements will not be concluded in the future. The reduction or elimination of trade barriers would increase competition in the Russian steel industry, resulting in lower prices for steel products. Significant decreases in prices for domestic steel products in

Russia would have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Russian Government may impose export tariffs on Russian steel producers, which could adversely affect the demand for its products***

According to media reports, the Russian Government is considering the adoption of export tariffs on certain steel products, potentially including products produced by the Group. However, no decision has been made to this effect and, therefore, the impact of any such export tariffs as may be adopted on the Group's business, results of operations and prospects is uncertain.

***The Group's business entails significant health, safety and environmental liability risks***

The Group operates industrial facilities in Europe and the United States where heavy metals or hazardous substances that are liable to present significant risks to the health or safety of neighbouring populations and to the environment are present. In this respect, the Group has in the past and may in the future incur liability (a) for having caused injury or damages to persons or property, or (b) for the pollution of the environment.

Although the Group has made provisions for such future potential liability, there can be no assurance that the amounts covered by such provisions will prove to be sufficient in the future due to the intrinsic uncertainties involved in projecting expenditures and liabilities relating to health, safety and the environment. It is likely that the assumptions used to determine these provisions will need to be adjusted in the future due to future changes in regulations, changes in the interpretation or application of regulations by the relevant authorities, or, with respect to issues related to restoration of the environment, changes in technical, hydrological or geological restrictions, or the discovery of pollution that is not yet known. It is likely that the Group's current insurance policies will be insufficient to cover the costs of any such future material liability (see "— The Group's existing and future insurance coverage may not be sufficient to cover costs arising from hazards and other operational risks arising from its steel and mining operations"). Any such liability shortfalls could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Achieving environmental compliance at sites that are currently in operation or that have been decommissioned entails a risk that could generate substantial financial costs for the Group***

The competent authorities have made, are making or may in the future make specific requests that the Group carries out environmental improvement works, such as cleaning up and rehabilitating sites, and controling emissions at sites in Europe where it is currently operating, or where it has operated in the past (including at sites it has disposed of), at neighbouring sites or at sites where the Group stored or disposed of waste. The Group may be required to incur significant costs to fulfil these obligations, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group's existing and future insurance coverage may not be sufficient to cover costs arising from hazards and other operational risks arising from its steel and mining operations***

Although the Group believes that, with respect to each of its production facilities, it maintains insurance at levels generally in line with the relevant local market standards, some of its business divisions do not have comprehensive business interruption insurance and most of the Group's business divisions do not maintain environmental liability insurance. In particular, the Russian Steel Division maintains only limited levels of insurance against business interruption, but does not have insurance against third-party liabilities for property or environmental damage. The Group would therefore suffer significant losses in the event of damage to or destruction of any of its principal operating assets in Russia or in the event that any claim is brought against the Group relating to personal injury, death or property damage caused by the Group's operations in Russia. In addition, no assurance can be given that the Group will be able to maintain existing insurance or obtain additional insurance coverage at commercially reasonable rates, which could lead to future shortfalls between the Group's liability and its insurance coverage. Any such liability shortfalls could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group maintains a significant part of the social and physical infrastructure in the Cherepovets area, which requires a substantial commitment of resources and may limit its ability to make rapid or significant reductions in the number of its employees***

The Group has been responsible for maintaining a portion of the social and physical infrastructure in and around the city of Cherepovets and currently owns various social assets. The Group is by far the largest employer in Cherepovets, and it estimates that its payments to the City of Cherepovets accounted for a significant proportion of the City's total budget for the year ended 31 December 2007. The Group expects that the City of Cherepovets will continue to rely on it for a substantial portion of its budget and that it will continue to maintain its current commitments in respect of social, employment and welfare infrastructure in the Cherepovets area.

As a result, the Group's ability to change the number of its employees may be subject to political and social considerations. This substantial commitment of resources and inability to make rapid or significant reductions in the number of its employees reduces the Group's ability to adjust its operations to respond to changes in market conditions. The Group's limited flexibility and significant level of additional fixed resource commitments could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The steel industry is highly competitive, and the Group may not be able to compete successfully***

The markets for steel and steel products are highly competitive. Steel producers are also in competition with producers of substitute materials, particularly in the automotive, construction and packaging industries. The Group's competitors include major international steel producers, some of which are larger or have greater capital resources than the Group or, in some cases, have lower raw materials costs than the Group. Competitors may have competitive advantages in terms of location and access to key suppliers and transport routes. The Group's competitive position may also be affected by the recent trend towards consolidation in the steel industry. The highly competitive nature of the industry combined with excess production capacity for some steel products has exerted, and may in the future continue to exert, downward pressure on prices of certain of the Group's products. There can be no assurance that the Group will be able to compete effectively in the future.

In addition, as a major Russian steel producer, the Company appears on the register of the Russian Federal Antimonopoly Service ("**FAS**") maintained for companies with a 35 percent share in a particular goods market. The measures applicable to the Company as a result of this inclusion could restrict its ability to set prices for such goods.

Failure by the Group to compete effectively for any of these reasons could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Inflation in Russia could increase the Group's costs***

The Russian economy has been characterised by high rates of inflation in recent years. The annual inflation rate was approximately 11.9 percent in 2007, 9.0 percent in 2006 and 10.9 percent in 2005 according to Russian Federal State Statistics Service. Certain of the Group's costs of its Russian operations, such as wage costs, maintenance costs, construction costs and utilities costs, are sensitive to rises in the general price level in Russia. However, due to competitive pressures, the Group may not be able to raise prices sufficiently to preserve operating margins. Accordingly, high rates of inflation could increase the Group's costs and there can be no assurance that the Group will be able to maintain or increase its operating margins to cover such costs and failure to do so could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Wage increases in Russia may reduce the Group's profit margins***

Wage costs in Russia have historically been significantly lower than wage costs in the more economically developed countries of North America and Europe for similarly skilled employees. However, if wage costs were to increase in Russia, the Group's profit margins could be reduced. The Group might need to increase the levels of its employee compensation more rapidly than in the past to remain competitive.

Unless the Group is able to continue to increase the efficiency and productivity of its employees, wage increases could have a material adverse effect on its business, results of operations, financial condition and prospects.

***The Group's Russian operations obtain significant amounts of their electricity and natural gas supply from companies that are currently the subject of a liberalisation programme, which could result in increased prices or supply interruptions***

In 2007, the Group's Russian operations purchased significant volumes of natural gas from subsidiaries of OAO Gazprom ("**Gazprom**"), a government-controlled entity, and significant amounts of electricity from OAO Vologodskaya Sbytovaya Kompaniya, a recently privatised part of the formerly government-controlled Russian electricity industry. A restructuring plan is currently being implemented for the Russian power sector aimed at introducing competition, liberalising the wholesale electricity market and moving from regulated pricing to a market-based system in stages from 2008 to 2011. Liberalisation may result in higher prices for electricity or natural gas and potential interruptions in their supply. For example, according to projections from the Ministry of Economic Development and Trade of the Russian Federation, the wholesale price of natural gas could rise by approximately 40 percent compared to current levels.

Any interruption in the supply of energy or substantial increase in costs could adversely affect the Group's future profitability to the extent it is unable to pass on higher costs to its customers. This could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Company is beneficially controlled by a single person, whose interests could conflict with those of the Noteholders***

The Company is beneficially controlled by Mr. Alexey Mordashov (the "**Controlling Shareholder**"), who as at 3 July 2008, controlled indirectly approximately 82.373 percent of the Company's shares (see "Principal Shareholders"). As a result, the Controlling Shareholder has the ability to exert significant influence over certain actions requiring shareholder approval, including, but not limited to, increasing or decreasing the authorised share capital of the Company (and disapplying pre-emptive rights), the election of directors, declaration of dividends, the appointment of management and other policy decisions. While transactions with the Controlling Shareholder and his affiliates can benefit the Company, the interests of the Controlling Shareholder could at times conflict with the interests of Noteholders. Although the Group has in the past sought and continues to seek to conclude related party transactions on an arm's-length basis, conflicts of interest may arise between the Group, its affiliates and the Controlling Shareholder or his affiliates, resulting in the conclusion of transactions on terms not determined by market forces. See "Management" and "Related Party Transactions". Any such conflict of interest could adversely affect the Group's business, financial condition and results of operations, future prospects and the value of the Notes.

***The Group's competitive position and future prospects are heavily dependent on its controlling shareholder's and senior management's experience and expertise***

The Group's controlling shareholder, who is also the Group's chief executive officer, and senior management team have been and, the Group believes, will continue to be important in the implementation of the Group's strategy and the operation of the Group's day-to-day activities. The experience, personal connections and relationships of members of senior management are important to the conduct of its business. There can be no assurance that these individuals will continue to make their services available to the Group in the future. The Group does not maintain key man insurance covering any of its senior managers. Moreover, competition in Russia for management and technical personnel, such as steel and mining engineers, with relevant expertise is intense due to the small number of qualified individuals, and this situation could seriously affect the Group's ability to retain its existing senior management and technical personnel and attract additional suitably qualified senior management and technical personnel. The loss or diminution in the services of members of the Group's senior management team or technical personnel or an inability to attract and retain additional senior management and technical personnel could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Severe weather conditions could significantly affect the Group's business and financial results***

The climate of the region of Russia where the Group's main operational site is located limits operations during certain times of the year. In addition, a substantial part of the Group's sales by volume from its Russian steel operations to be sold internationally are routed through the port of St. Petersburg, which experiences occasional shutdowns due to bad weather and can only be fully utilised during the summer navigation period, while the river is not frozen over. Unusually severe weather conditions could negatively affect distribution and therefore revenues from international sales. Any of these climatic limits could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Disruption in rail transport and increased rail costs could significantly hinder the Group's operations and product distribution in Russia***

The Group's Russian operations depend on the Russian railway system and rely predominantly on the rail freight network operated by JSC Russian Railways ("**Russian Railways**") for transport of raw materials and deliveries of its steel products to its facilities, consignment agents and customers. Russian Railways is the predominant company in the Russian railway sector with the country's largest fleet of rolling stock. It also plays a monopolistic role as the sole railway infrastructure operator, and it enjoys a near monopoly in the provision of locomotive services.

The physical infrastructure and other assets owned and operated by Russian Railways, particularly its rail network, largely date back to Soviet times and have in many cases, not been adequately maintained.

The Russian railway system is subject to risks of disruption as a result of the declining physical condition of the facilities, a shortage of rail cars, the limited capacity of border stations and load shedding, including those due to poorly maintained rail cars and train collisions. In particular, the rolling stock of Russian Railways is generally in a poor state of repair. While the Group owns and leases railcars, and rents additional railcars, such assets are sufficient for only a portion of the Group's total transportation requirements. The failure of Russian Railways to upgrade its rolling stock within the next few years could result in a shortage of available working rolling stock, a disruption in transportation of the Group's raw materials and products and increased costs of rail transport. There can be no assurance that the age and insufficient funding and maintenance of a substantial part of the Russian railway network and other infrastructure operated by Russian Railways will not in the future lead to material disruptions of the Group's business or increase the Group's costs of doing business.

In addition, the Russian Government sets rail tariffs and may further increase these tariffs, as it has done in the past. Such increases in railway tariffs have resulted in significant increases in the Group's transportation costs. Both the privatisation of Russian Railways and its cost of upgrading its rolling stock and other facilities could further contribute to increased tariffs.

Any disruption in transportation or increase in tariffs could significantly increase the Group's costs, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group may be subject to administrative sanctions, required divestitures or limitations on operations if it fails, or is found to have failed, to comply with the prior approval or subsequent notification requirements of the Russian Federal Antimonopoly Service with respect to its acquisitions of companies that are incorporated and operating in Russia or assets located in Russia***

The Group has expanded its operations through the acquisition of companies that are incorporated and operating in Russia or assets that are located in Russia, such as the mining companies that currently comprise Severstal Resources. Some of these acquisitions are, or were, subject to the prior approval or subsequent notification requirements of the FAS, or its predecessor agencies. Certain portions of these requirements are vaguely worded and there can be no assurance that the Group will be able to comply fully or that the FAS will not challenge the Group's past compliance, which could result in administrative sanctions, required divestitures or limitations on operations. Any such sanctions, divestitures or limitations would materially adversely affect the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group's business could be adversely affected if it fails to obtain or renew necessary licences or fails to comply with the terms of its licences***

The Group's business depends on the continuing validity of its licences, the issuance to it of new licences and its compliance with the terms of its licences, including subsoil licences for the Group's mining operations in Russia. Regulatory authorities exercise considerable discretion in the timing of licence issuance and renewal and in monitoring of licensees' compliance with licence terms. Requirements imposed by these authorities may be costly and time-consuming and may result in delays in the commencement or continuation of exploration or production operations. Moreover, legislation on subsoil rights remains internally inconsistent and vague, and the acts and instructions of licensing authorities and procedures by which licences are issued are often arguably inconsistent with legislation.

In certain circumstances, state authorities in Russia may seek to interfere with the issuance of licences, for example by initiating legal proceedings alleging that the issuance of a licence violates the civil rights or legal interests of a person or legal entity. The licensing process may also be influenced by outside commentary, political pressure and other extra-legal factors. In the case of subsoil licences, unsuccessful applicants may bring direct claims against the issuing authorities that the licence was issued in violation of applicable law or regulation. If successful, such proceedings and claims may result in the revocation or invalidation of the licence. Accordingly, licences that the Group requires may be invalidated or may not be issued or renewed. Licences that are issued or renewed may not be issued or renewed in a timely fashion or may involve conditions that restrict the Group's ability to conduct its operations or to do so profitably. As part of their obligations under licensing regulations and the terms of their licences, the Group's Russian subsidiaries are also required to comply with numerous industrial standards, maintain production levels, recruit qualified personnel, maintain necessary equipment and a system of quality control, monitor the Group's operations, maintain appropriate filings and, upon request, submit appropriate information to licensing authorities, which are entitled to control and inspect their activities. In most cases, a licence may be suspended or terminated if the licensee does not comply with the "significant" or "material" terms of the licence. However, the Ministry of Natural Resources and Ecology of the Russian Federation has not issued any new interpretive guidance on the meaning of "significant" or "material" terms of licences. Court decisions on the meaning of these terms have been inconsistent and, under Russia's civil law system, do not have significant value as precedents for future judicial proceedings. These deficiencies result in the regulatory authorities, prosecutors and courts having significant discretion over enforcement and interpretation of the law, which may be used arbitrarily to challenge the rights of subsoil licensees. As a result, while the Group seeks to comply with the terms of its subsoil licences and believes that it is currently in material compliance with the terms of such licences, there can be no assurance that its licences will not be suspended or terminated. In the event that the licensing authorities in Russia discover a material violation by a member of the Group, that member of the Group may be required to suspend its operations or to incur substantial costs in eliminating or remedying the violation, which could have an adverse effect on the Group's business or results of operations.

In addition, the Group's business outside of Russia also depend on the continuing validity of licences, the issuance to them of new licences and compliance with the terms of such licences, which may involve uncertainties and costs to the Group. For example, under Italian law, companies carrying out certain activities were required to file an application by the end of 2007 in order to obtain the environmental authorisation known as "AIA", or the Integrated Pollution Prevention and Control Certificate. Lucchini's Trieste plant obtained the AIA in February 2008, but its issuance has been challenged by the Municipality of Trieste, which Lucchini is now defending. An application for the AIA for Lucchini's Piombino plant has also been made. However, the relevant authorities have made specific additional requests, which are currently being processed by Lucchini, and accordingly, the licence has not yet been issued. Even once issued, AIAs typically contain additional compliance requirements and detailed terms to be met, which are likely to involve significant costs to the Group. The Group does not consider its current difficulties with obtaining AIAs in Italy to be materially affecting its business. There can be no assurance that similar difficulties with other licences, should they occur in the future, will not have such an effect.

Any or all of these factors may affect the Group's ability to obtain, maintain or renew necessary licences. If the Group is unable to obtain, maintain or renew necessary licences or is only able to obtain or renew them with newly introduced material restrictions, it may be unable to benefit fully from its reserves, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group has engaged and may continue to engage in related party transactions***

The Group has engaged in transactions with certain of its shareholders, including the Controlling Shareholder, directors and executive officers and companies controlled by them or in which they or the Group own an interest (see "Related Party Transactions"). The Group believes that these related party transactions have been and will continue to be concluded at arm's length. However, there can be no assurance that the terms on which these related party transactions are conducted have not and will not differ significantly from the terms on which third party transactions have been and are conducted. The practice of related party transactions may result in transactions conducted on terms less favourable to the Group than would otherwise have been negotiated with third parties and could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Employees and former employees of the Group and service providers or customers of the Group (as well as neighbouring populations) may have been exposed, and, to a certain extent, may still be exposed, to toxic or hazardous substances***

The Group's steel and mining operations use and have in the past used large quantities of heavy metals, chemical, toxic or hazardous substances. In spite of safety and monitoring procedures implemented by the Group and each production site, employees and in some cases the employees of other companies and service providers have been or may have been exposed to such substances and some employees may have developed specific pathologies from such exposure, which could induce them to file claims against the Group in future years.

Certain employees of the Group or of other companies and service providers that work with the Group have been exposed to materials or equipment containing asbestos. The Group is involved in legal actions and occupational illness claims due to past exposure to asbestos. Owing to the latency periods for various asbestos-related pathologies, the possibility that an increasing number of legal actions or occupational illness claims will be filed in the years ahead cannot be excluded. In addition, employees of the Group or its service providers or customers or persons living near the Group's manufacturing facilities are exposed or have in the past been exposed to certain substances that are currently considered not to be hazardous. However, chronic toxicity, even in very low concentrations or exposure doses, could be discovered in the future. This could also lead to claims against the Group.

If any of the events described above lead to a material liability for the Group in the future, this could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Group's effective tax rate and financial condition could be affected by the Russian tax status of the non-Russian subsidiaries of the Group***

The Group operates in various jurisdictions and includes companies incorporated outside of Russia. Tax liabilities of the Group are determined on the basis that these companies are not subject to Russian taxation other than through withholding of tax in cases where that is required. Russian tax laws do not provide detailed rules on taxation of foreign companies. It is possible that with the evolution of these rules or changes in the approach of the Russian tax authorities, the non-taxable status of some or all foreign companies of the Group in Russia may be challenged.

The Group believes that its interpretation of the relevant tax legislation is and will be sustainable. Moreover, the Group believes that it has accrued all applicable taxes; however, the interpretations of the relevant authorities could differ and if the authorities were successful in enforcing their interpretation, the effect could be significant to the financial position of the Group.

***The Group bears the risk of interest rate fluctuations***

Interest rates on the Group's debt finance are either fixed or variable, at a fixed spread over LIBOR or Euribor for the duration of each contract. Accordingly, the Group is exposed to the effect of fluctuations in interest rates with an immediate effect on the interest costs of the Group, in the case of borrowings at a variable rate interest, and an effect on the rate at which borrowings at fixed rates of interest are refinanced or renewed from time to time. Interest rates, in particular in Russia, have been subject to significant fluctuations in the past. There can be no assurance that the costs associated with an increase in the rates of interest at which the Group borrows funds will be able to be passed on in the form of higher prices to its customers. Accordingly, increases in interest rates may have a material adverse effect on the Group's business, results of operations, financial condition and prospects.

***The Group may incur losses as the result of fluctuations in the foreign currency exchange rates of the Rouble, the US dollar or the euro***

The Group is exposed to translational and transactional foreign currency exchange rate risks. Translational foreign currency exchange rate risks are the result of translating assets and liabilities denominated in the Rouble or euro into US dollar amounts for financial reporting purposes. Transactional foreign currency exchange rate risks arise as a result of payments the Group makes or receives that involve foreign currency exchange. Currently, most of the Group's borrowings are denominated in US dollars or euros, whereas the Group's expenses and revenue are primarily in Roubles, US dollars and euros. The Group does not hedge this foreign exchange risk. The Group is therefore exposed to the effects of currency fluctuations between the US dollar, the euro and the Rouble. The strengthening of the Rouble in real terms relative to the US dollar in recent years has been favourable to the Group by reducing the Rouble cost of its US dollar denominated borrowings. However, there is no guarantee that such trends will continue, and the Rouble may depreciate in value against the US dollar or the euro in the future. As the Group reports its financial results in US dollars and must frequently exchange or translate foreign currency into Roubles or Roubles into foreign currency, fluctuations in foreign currency exchange rates could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Russia's property law is subject to uncertainty and contradiction***

The legal framework relating to the ownership and use of land and other real property in Russia is not yet sufficiently developed to support private ownership of land and other real estate to the same extent as is common in some of the more developed market economies of North America and Europe. It is often difficult to determine with certainty the validity and enforceability of title to land in Russia and the extent to which it is encumbered. Moreover, in order to use and develop real property in Russia, approvals, consents and registrations of various federal, regional and local governmental authorities are required. Further, it is not always clear which governmental body or official has the right to lease or otherwise regulate the use of real property. In addition, building and environmental regulations often contain requirements that are impossible to fully comply with in practice. Failure to obtain or comply with the required approvals, consents, registrations or other regulations may lead to severe consequences for the landowners and other real estate owners and lessees, including in respect of any current construction activities. If the real property owned or leased by the Group is found not to be in compliance with all applicable approvals, consents, registrations or other regulations, the Group may lose the use of such real property, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Shareholder liability under Russian legislation could cause the Company to become liable for the obligations of its Russian subsidiaries and its Russian joint venture entities***

Under Russian law, the Company may be jointly and severally liable for the obligations of its Russian subsidiaries or joint venture entities together with such entities if (i) the Company has the ability to make decisions for such Russian subsidiaries or joint venture entities as a result of its ownership interest, the terms of a binding contract or in any other way, (ii) the Company has the ability to issue mandatory instructions to such Russian subsidiaries or joint venture entities and that ability is provided for by the charter of the relevant Russian subsidiary or joint venture entity or in a binding contract and (iii) the relevant Russian subsidiary or joint venture entity concluded the transaction giving rise to the obligations pursuant to the Company's mandatory instructions. In addition, the Company may have secondary liability for the obligations of its Russian subsidiaries or joint venture entities if (i) it has the ability to make decisions for the relevant Russian subsidiary or joint venture entity as a result of its ownership interest, the terms of a binding contract, or in any other way and (ii) the relevant Russian subsidiary or joint venture entity becomes insolvent or bankrupt due to the Company's fault (i.e., the Company has used its ability referred to in (i) above knowing that this would result in insolvency or bankruptcy of the relevant Russian subsidiary or joint venture entity). This type of liability could result in significant losses, and could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Incomplete, unreliable or inaccurate official data and statistics could create uncertainty***

The Group relies on and refers to information and statistics from various third party sources and its own internal estimates. For example, substantially all the information contained in this Prospectus concerning the Group's competitors has been derived from publicly available information. The Group believes that these sources and estimates are reliable, but has not independently verified them. There can be no assurance that statistics derived from third party sources are true and accurate in all material respects.

## Risk Factors Relating to Russia

The Group is a Russian group. A substantial portion of the Group's fixed assets are located in Russia and a significant portion of the Group's revenues are derived from Russia. There are certain risks associated with investments in Russia.

***Emerging markets such as Russia are subject to greater risks than more developed markets, including significant economic, political and social, and legal and legislative risks; in addition, financial turmoil in any emerging market could disrupt the Group's business, as well as cause the price of the Notes to suffer***

Generally, investment in emerging markets is suitable only for sophisticated investors who are familiar with and who fully appreciate the significance of the risks involved in investing in emerging markets and prospective investors are urged to consult with their own legal and financial advisors before making an investment in the Notes.

Investors should note that emerging markets such as Russia are subject to rapid change and that the information set out in this Prospectus may become outdated relatively quickly. Moreover, financial turmoil in any emerging market country tends to adversely affect prices in equity markets of all emerging market countries as investors move their money to more stable developed markets. As has happened in the past, financial problems or an increase in the perceived risks associated with investing in emerging economies could dampen foreign investment in Russia and adversely affect the Russian economy. In addition, during such times, companies that operate in emerging markets can face severe liquidity constraints as foreign funding sources are withdrawn. Thus, even if the Russian economy remains relatively stable, financial turmoil in any emerging market country could adversely affect the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

### Political Risks

***Conflict between federal and regional authorities and other domestic political conflicts could create an uncertain operating environment and hinder the Group's ability to plan long-term and adversely affect the value of the Group's investments in Russia***

The Russian Federation is a federation of sub-federal political units, some of which exercise considerable autonomy over their internal affairs pursuant to agreements with the federal authorities. In practice, the division of authority between federal and regional authorities remains uncertain and contested. This uncertainty could hinder the Group's long-term planning efforts, create uncertainties in the Group's operating environment in Russia and prevent the Group from effectively and efficiently carrying out its business strategy.

In the past, ethnic, religious, historical and other divisions have given rise to tensions and, in certain cases, military conflict such as in Chechnya where normal economic activity ceased for a period of time. Violence and attacks in connection with this conflict also spread to other parts of Russia and resulted in terrorist attacks in Moscow. In the future, such tensions, military conflict or terrorist activities could result in significant political consequences, including the imposition of a state of emergency in some or all of Russia or heightened security measures, which may disrupt normal economic activity and have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Political and governmental instability could adversely affect the value of investments in Russia, including the Notes***

Since 1991, Russia has moved from a one-party state with a centrally planned economy to a federal republic with democratic institutions and a market-oriented economy. However, the Russian political system remains vulnerable to popular dissatisfaction, including dissatisfaction with the results of privatisations in the 1990s, as well as to demands for autonomy from particular regional and ethnic groups. The course of political, economic and other reforms has in some respects been uneven, and the composition of the Russian Government — the prime minister and the other heads of federal ministries — has at times been unstable. However, over the period from 2000 to 2008, President Vladimir Putin achieved and generally maintained political and governmental stability in the country which accelerated the reform process and made the political and economic situation in Russia more conducive to investment. In May 2008, Mr. Dmitry Medvedev was inaugurated as the president following his election in March 2008. Upon his inauguration, President Medvedev appointed Mr. Vladimir Putin as the Prime Minister. Whilst such appointment demonstrated a likely continuity of Mr. Putin's policy, future changes in the Russian Government, as well as major policy shifts or lack of consensus among the President, the government, Russia's parliament and powerful economic groups, could lead to political instability, which could have a material adverse effect on the value of investments in Russia generally. Further governmental instability or discontinuation of reform policies could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Arbitrary, selective or unlawful state action, in particular by the tax authorities, could have a material adverse effect on the Group's business***

State authorities have a high degree of discretion in Russia and at times exercise their discretion arbitrarily, without hearing or prior notice, and sometimes in a manner that is contrary to law. Possible state actions include withdrawal of licences, interference with or nullification of contracts and transactions entered into in connection with privatisations, invalidation of share issuances and registrations, sudden and unexpected tax audits, criminal prosecutions and civil actions.

In particular, the Ministry for Taxes and Levies (now succeeded by the Federal Tax Service) has begun to attack certain Russian companies' use of tax-optimisation schemes, and press reports have speculated that these enforcement actions have been selective. In 2003, Russian authorities arrested Mikhail Khodorkovsky and Platon Lebedev, key shareholders and managers of OAO NK Yukos, then Russia's largest oil company by production, on tax evasion and related charges, and on 31 May 2005 each was sentenced to nine years' imprisonment on these charges. Significant back tax claims have since been brought against Yukos, resulting in the auction of its major production subsidiary, OAO Yuganskneftegaz, and the global bankruptcy of Yukos. Yuganskneftegaz was acquired, indirectly, by OJSC OC Rosneft, a state-owned oil company, resulting in the first effective re-nationalisation of a significant company that had been privatised in the 1990s. In addition, the press has reported significant claims for back taxes and related penalties against other oil companies, including TNK-BP and Sibneft as well as against Vimpelcom.

There can be no assurance that business activities of the Group will not be affected by the tax audits undertaken by the Federal Tax Service. In addition, as the Group is the largest taxpayer in the region where it is located, any substantial decrease in its tax liabilities may be investigated by the tax authorities in more aggressive fashion than would usually be the case.

Arbitrary, selective or unlawful state action, if directed at the Group, could lead to the loss of key licences, termination of contracts, invalidation of share issuances, civil litigation, criminal proceedings and imprisonment of key personnel, any of which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

**Economic Risks**

***Economic instability in Russia could adversely affect the Group's business***

Since the dissolution of the Soviet Union, the Russian economy has experienced at various times:

- significant declines in gross domestic product;
- hyperinflation;
- increases in, or high, interest rates;
- an unstable currency;
- high state debt relative to gross domestic product;
- a weak banking system providing limited liquidity to Russian enterprises;
- a large number of loss-making enterprises that continued to operate due to the lack of effective bankruptcy proceedings;
- the use of fraudulent bankruptcy actions in order to take unlawful possession of property;
- significant use of barter transactions and illiquid promissory Notes to settle commercial transactions;
- widespread tax evasion;
- the growth of "black" and "grey" market economies;
- high levels of capital flight;
- high levels of corruption and the penetration of organised crime into the economy;
- significant increases in unemployment and underemployment; and
- the impoverishment of a large portion of the Russian population.

In particular, the Russian economy has been subject to abrupt downturns. For example, on 17 August 1998, in the face of a rapidly deteriorating economic situation, the Russian Government defaulted on its Rouble-denominated securities, the CBR stopped its support of the Rouble and a temporary moratorium was imposed on certain hard currency payments. These actions resulted in an immediate and severe devaluation of the Rouble and a sharp increase in the rate of inflation; a dramatic decline in the prices of Russian debt and equity securities; and an inability of Russian issuers to raise funds in the international capital markets. These problems were aggravated by the near collapse of the Russian banking sector after the events of 17 August 1998, which further impaired the ability of the banking sector to act as a reliable and consistent source of liquidity to Russian companies and resulted in the loss of bank deposits in some cases. In 2004, several Russian banks experienced a sharp reduction in liquidity, and the licences of certain of them were withdrawn.

There can be no assurance that the positive trends in the Russian economy dominating over the last eight years, such as the increase in the gross domestic product, a relatively stable Rouble and a reduced rate of inflation, will continue or will not be abruptly reversed. As Russia produces and exports large quantities of oil, natural gas and other mineral resources, the Russian economy is particularly vulnerable to market downturns or economic slowdowns elsewhere in the world, which may cause fluctuations in the prices of oil, natural gas and minerals on the world market, which reached record high levels in 2008. A significant or sustained decline in the price of oil, natural gas or minerals could significantly slow or disrupt the Russian economy. The occurrence of any of these events could adversely affect Russia's economy and the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Introduction of currency restrictions may limit the Group's ability to execute its strategy or operate its business or could otherwise adversely affect the Russian capital markets***

During the 1990s, Russia's currency regulation and control regime severely limited, and at times prohibited, certain hard currency payments and operations. Despite recent liberalisation, there can be no assurance that Russia's currency regulation and control regime will not impose new restrictions or prohibitions. Restrictions or prohibitions on hard currency payments and operations could limit the

Group's ability to invest in its capital improvement programmes, pursue attractive acquisition opportunities or purchase raw materials or sell its products internationally. In addition, such restrictions or prohibitions may limit an investor's ability to repatriate earnings from securities of Russian issuers, including the Group, or otherwise have a negative impact on the Russian capital markets. The consequences of any new restrictions or prohibitions could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Russian banking system remains underdeveloped, with a limited number of creditworthy Russian banks, and another banking crisis could place severe liquidity constraints on the Group's business***

Russia's banking and other financial systems are not well developed or regulated, and Russian legislation relating to banks and bank accounts is subject to varying interpretations and inconsistent application. The 1998 financial crisis resulted in the bankruptcy and liquidation of many Russian banks and almost entirely eliminated the developing market for commercial bank loans at that time. From April through July 2004, the Russian banking sector experienced its first serious turmoil since the financial crisis of August 1998. As a result of various market rumours and, in some cases, certain regulatory and liquidity problems, several privately-owned Russian banks experienced liquidity problems and were unable to attract funds on the interbank market or from their client base. Simultaneously, they faced large withdrawals of deposits by both retail and corporate customers. Several of these privately-owned Russian banks collapsed or ceased or severely limited their operations. Russian banks owned or controlled by the Government or the CBR and foreign-owned banks generally were not adversely affected by the turmoil.

Recently, there has been a rapid increase in lending by Russian banks, which many believe has been accompanied by deterioration in the credit quality of the borrowers. In addition, a robust domestic corporate debt market is leading to Russian banks increasingly holding large amounts of Russian corporate Rouble-denominated bonds in their portfolios, which is further deteriorating the risk profile of Russian bank assets. The serious deficiencies in the Russian banking sector, combined with the deterioration in the credit portfolios of Russian banks, may result in the banking sector being more susceptible to market downturns or economic slowdowns, including due to Russian corporate defaults that may occur during any such market downturn or economic slowdown. There are currently also only a limited number of creditworthy Russian banks, most of which are located in Moscow. The bankruptcy or insolvency of any banks with which the Group does business could adversely affect the Group's business. Another banking crisis, or the bankruptcy or insolvency of the banks which hold the Group's funds, could result in the loss of its income for several days or affect its ability to complete banking transactions in Russia, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes. Furthermore, any shortages of funds or other disruptions to banking experienced by the Group's banks from time to time could also have a material adverse effect on the Group's ability to complete its planned developments or obtain finance required for its planned growth and thus could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Russia's physical infrastructure is in poor condition***

The physical infrastructure in Russia, including rail and road networks, power generation and transmission, communication systems, and building stock, largely dates back to Soviet times and has not been adequately funded and maintained. Electricity and heating shortages in some regions of Russia have seriously disrupted the local economies. In May 2005, an electricity blackout affected much of Moscow and some other regions in the central part of Russia for one day, disrupting normal business activity, and in January 2006, electricity supplies to certain industrial customers in Moscow were reduced as a result of extreme cold in Moscow. Other parts of the country face similar problems.

Road conditions throughout Russia are also poor, with many roads not meeting modern quality requirements. Some areas within Russia, particularly those surrounding ageing nuclear power plants, are potentially hazardous. The federal government is actively pursuing the reorganisation of the nation's rail, electricity and telephone systems. Any such reorganisation may result in increased charges and tariffs while failing to generate the anticipated capital investment needed to repair, maintain and improve these systems.

The poor condition or further deterioration of Russia's physical infrastructure may harm the national economy, disrupt access to communications, increase the cost of doing business in Russia or disrupt business operations, any or all of which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

**Social Risks**

***Social instability could lead to labour and social unrest, increased support for renewed centralised authority, nationalism or violence.***

The past failures of the Russian Government and many private enterprises to pay full salaries on a regular basis and the failure of salaries and benefits generally to keep pace with the rapidly increasing cost of living have led in the past, and could lead in the future, to labour and social unrest. For example, in January 2005, a new law took effect that replaced years-old benefits (including free use of public transportation, free medicine and heavily subsidised utilities) for pensioners, the disabled, war veterans and certain other categories of Russian citizens with cash payments. Groups of pensioners and political organisations held massive demonstrations across Russia protesting against the new law and temporarily blocked various transportation routes. In view of these demonstrations, certain Russian cities and regions restored in part free public transportation and increased cash benefits. Currently the protests have ceased. However, there can be no assurance that such protests will not occur again, whether as a result of any new law or regulation having a similar effect being adopted or otherwise. Labour and social unrest could have political, social and economic consequences, such as increased support for a renewal of centralised authority; increased nationalism, with support for re-nationalisation of property, or expropriation of or restrictions on foreign involvement in the economy of Russia; and increased violence. Any of these could have an adverse effect on confidence in Russia's social environment and the value of investments in Russia, could restrict the Group's operations and lead to a loss of revenue, and could otherwise have a material adverse effect on the Group's business, financial condition, results of operations and future prospects and the value of the Notes.

***Crime and corruption could disrupt the Group's ability to conduct its business and could materially adversely affect the Group's financial condition and results of operations***

Organised criminal activity has reportedly increased significantly since the dissolution of the Soviet Union in 1991, particularly in large metropolitan centres. In addition, the Russian and international press have reported high levels of official corruption in Russia and other CIS countries, including the bribery of officials for the purpose of initiating investigations by state agencies, obtaining licences or other permissions or in order to obtain the right to supply goods or services to state agencies. Press reports have also described instances in which state officials have engaged in selective investigations and prosecutions to further interests of the state and individual officials. Additionally, published reports indicate that a significant number of Russian media regularly publish slanted articles in return for payment.

Recent reports in the media have suggested that such practices continue to exist in the country, including tactics in connection with the acquisition of companies or their assets by so-called "raiders". Any allegations of the Group's involvement in such practices would pose a risk of prosecution and of possible criminal or administrative liability or reputational damage. The proliferation of organised or other crime, corruption and other illegal activities that disrupt the Group's ability to conduct its business effectively, or any claims that it has been involved in corruption, or illegal activities (even if false) that generate negative publicity, could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

**RISKS RELATING TO THE RUSSIAN LEGAL SYSTEM AND RUSSIAN LEGISLATION**

***Weaknesses relating to the Russian legal system and Russian legislation create an uncertain environment for investment and for business activity***

Russia continues to develop its legal framework in accordance with international standards and the requirements of a market economy. Since 1991, new Russian domestic legislation has been put into place. Currently, this system includes the Constitution of the Russian Federation of 1993, the Civil Code of the Russian Federation and other federal laws, decrees, orders and regulations issued by the President, government and federal ministries, which can be complemented by regional and local rules and regulations, adopted in certain spheres of regulation. These legal norms on the one hand can overlap or contradict one another and on the other hand can leave gaps in the regulatory infrastructure. Several fundamental Russian laws have only recently become effective. Consequently, certain areas of judicial practice are not yet formed, and are often difficult to predict.

Among the risks of the current Russian legal system are:

- inconsistencies among (1) federal laws, (2) decrees, orders and regulations issued by the president, the Russian Government, federal ministries and regulatory authorities and (3) regional and local laws, rules and regulations;
- limited judicial and administrative guidance on interpreting Russian legislation;
- the relative inexperience of judges and courts in interpreting new principles of Russian legislation, particularly business and corporate law;
- substantial gaps in the regulatory structure due to delay or absence of implementing legislation;
- a high degree of unchecked discretion on the part of governmental authorities; and
- bankruptcy procedures that are not well developed and are subject to abuse.

All of these weaknesses could affect the Group's ability to enforce its rights under contracts, or to defend itself against claims by others, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The lack of independence of certain members of the judiciary, the difficulty of enforcing court decisions and governmental discretion in instigating, joining and enforcing claims could prevent the Group or the Noteholders from obtaining effective redress in a court proceeding and could materially adversely affect the value of the Notes***

The independence of the judicial system and its immunity from economic, political and nationalistic influences in Russia are also less than complete. The Russian court system in the past has been and may still be understaffed and underfunded. Russia, along with many western European states, such as Germany and France, is a civil law jurisdiction and, as such, judicial precedents generally have no binding effect on subsequent decisions. Enforcement of court judgments by law enforcement agencies can sometimes be time consuming because of the large number of outstanding court judgments. Additionally, court claims are often used in furtherance of political aims. The Group may be or may become subject to such claims and may not be able to receive a fair trial.

There are also legal uncertainties relating to property rights. During Russia's transformation from a centrally planned economy to a market economy, legislation has been enacted to protect private property against expropriation and nationalisation. However, it is possible that, due to the lack of experience in enforcing these provisions and due to political changes, these protections would not be enforced in the event of an attempted expropriation or nationalisation, or in the event that the Group's business is reorganised. Expropriation or nationalisation of any of the Group's entities, their assets or portions thereof, or their break-up into separate companies, potentially without adequate compensation, could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***In the event that the title to any Russian company acquired by the Group through privatisation, bankruptcy sale or by other means is successfully challenged, the Group may lose its ownership interest in that company or its assets***

Almost all of the Group's steel making and mining assets in Russia consist of companies that have been privatised or that the Group acquired through bankruptcy proceedings or directly or indirectly from others who acquired them through privatisation or bankruptcy proceedings, and the Group may seek to acquire additional companies that have been privatised or that have undergone bankruptcy proceedings. Privatisation legislation in Russia is vague, internally inconsistent and in conflict with other elements of Russian legislation. Although the statute of limitations for challenging transactions entered into in the course of privatisations is currently three years, privatisations may still be vulnerable to challenge, including through selective action by governmental authorities motivated by political or other extra-legal considerations.

If any of the Group's acquisitions is challenged as having been improperly conducted and the Group is unable to defend itself successfully, the Group may lose its ownership interests, which could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Changes and inconsistencies in the Russian tax system could adversely affect the Group's business***

Generally, taxes payable by Russian companies can be substantial. These taxes include, among others, income taxes, value-added tax or VAT, excise taxes, social and pension contributions and property tax.

The discussion below provides general information regarding Russian taxes and is not intended to be inclusive of all issues. Investors should seek advice from their own tax advisors as to these tax matters before investing in the Notes.

Laws related to these taxes, such as the Tax Code of the Russian Federation (the "**Tax Code**"), have been in force for a short period relative to tax laws in more developed market economies, and the Russian Government's implementation of these tax laws is often unclear or inconsistent. Historically, the system of tax collection has been relatively ineffective, resulting in continual change in the interpretation of the existing laws in an attempt to increase revenues. Although the quality of tax legislation has generally improved with the introduction of the first and second parts of the Tax Code. the possibility exists that Russia may impose arbitrary or onerous taxes and penalties in the future, which could adversely affect the business of the Group and the Russian subsidiaries of the Group.

The tax environment in Russia has historically been complicated by the fact that various authorities have interpreted tax legislation inconsistently. There have recently been significant changes to the Russian taxation system; including amendments to the chapters on VAT and on income tax, effective from 1 January 2008, as well as changes to Part One of the Tax Code (tax administration provisions) effective from 1 January 2007.

In practice, the Russian tax authorities have their own interpretation of the tax laws that rarely favours taxpayers. In some instances, the tax authorities have applied new interpretations of tax laws retroactively. There is no established precedent or consistent court practice in respect of these issues. Taxpayers often have to resort to court proceedings to defend their position against the tax authorities. Recent events in Russia suggest that the tax authorities may be taking a more assertive position in their interpretation of the legislation and assessments. Also, differing interpretations of tax regulations exist both among and within government ministries and organisations at the federal, regional and local levels, creating uncertainties and inconsistent enforcement.

The Russian tax system still fails to address many of the existing problems, and local tax officials have recently made several material tax claims against major Russian companies.

In addition, on 12 October 2006, the Plenum of the High Arbitration Court of the Russian Federation issued Ruling No. 53 (the "**Ruling**") that introduced a concept of "unjustified tax benefit" which is defined mainly by reference to specific examples of such tax benefits (for example, absence of business purpose) which may lead to their disallowance. Based on the available court practice relating to the Ruling, it is apparent that the tax authorities actively seek to apply this concept when challenging tax positions taken by taxpayers. Although the intention of the Ruling was to combat abuse of tax law, the tax authorities have started applying the "unjustified tax benefit" concept in a broader sense than may have been intended by the High Arbitration Court. To date, in the majority of cases where this concept has been applied, the courts have ruled in favour of taxpayers, but the interpretations of the "unjustified tax benefit" concept have been too few to anticipate how it may be interpreted in the future. Furthermore, Ruling No. 64. of the Plenum of the Supreme Court of the Russian Federation titled "Concerning the Practical Application by Courts of Criminal Legislation Concerning Liability for Tax Crimes" dated 28 December 2006 is indicative of the trend to broaden the application of criminal liability for tax violations.

Tax declarations, together with related documentation, such as customs declarations, are subject to review and investigation by a number of authorities, each of which may impose penalties and interest charges. Generally, taxpayer activities are subject to inspection for the three-year period immediately preceding the year in which the tax audit is carried out. As previous audits do not exclude subsequent claims relating to the audited period, the statute of limitations is not entirely effective. In addition, on 14 July 2005 the

Russian Constitutional Court issued a decision that effectively allowed the statute of limitations for tax liabilities to be extended beyond the three-year term set forth in the Tax Code if a court determines that the taxpayer has obstructed or hindered the course of a tax audit. Moreover, amendments to Part One of the Tax Code effective as 1 January 2007 provide for the possibility of extension of the three-year term in cases where actions of the audited tax payer created insurmountable obstructions to the tax authorities' audit. Since the terms "obstructed", "hindered" or "insurmountable obstacles" are not specifically defined in Russian law, the tax authorities may attempt to interpret these terms broadly, effectively linking any difficulty experienced in the course of their tax audit with obstruction by the tax payer and using that as a basis to seek tax adjustments and penalties beyond the three-year term. In some instances, changes in tax regulations have been given retroactive effect.

In its decision of 26 July 2001, the Constitutional Court also introduced the concept of "a taxpayer acting in bad faith" without clearly stipulating the criteria for it. Similarly, this concept is not defined in Russian tax law. Nonetheless, this concept has been used by the tax authorities to deny, for instance, the taxpayer's right to rely on the letter of the tax law. The tax authorities often exercise significant discretion in interpreting this concept in a manner that is unfavourable to taxpayers.

There is no concept of a tax group in Russia, nor can a consolidated filing be made by Russian companies for tax purposes. Therefore, Russian companies and each of their Russian subsidiaries pay their own Russian taxes and may not surrender profit or losses to other group companies for tax purposes.

Dividends received by Russian companies are subject to income tax at a rate of 9 percent. Subject to certain conditions, this tax may be reduced to zero. However, there remains a risk of additional tax liabilities and inefficiencies in multi-level Russian groups such as the Group.

Even if further reforms to tax laws are enacted, they may not result in a reduction of the tax burden on Russian companies and/or the establishment of a more efficient tax system. Conversely, they may introduce additional tax collection measures. There can be no assurance that the Tax Code will not be changed in the future in a manner adverse to the stability and predictability of the tax system.

The conditions mentioned above create tax risks in Russia that are more significant than those typically found in countries with more developed tax systems, imposing additional burdens and costs on the Group's operations and management resources. In addition to creating a substantial tax burden, these risks and uncertainties complicate the Group's tax planning and related business decisions, potentially exposing it and its Russian subsidiaries to significant fines and penalties and enforcement measures, and could adversely affect the Group's business, financial condition and results of operations. Increases in the taxes payable by the Group and the imposition of fines, penalties or interest charges, could have a material adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***Vaguely drafted Russian transfer pricing rules and lack of reliable pricing information may affect the Group's results of operations***

Russian transfer pricing rules came into force in 1999, giving the tax authorities the right to make transfer pricing adjustments and impose additional tax liabilities in respect of "controlled" transactions, provided that the transaction price differs from the market price by more than 20 percent. "Controlled" transactions currently include transactions with related parties, barter (in-kind exchange) transactions, foreign trade transactions and any transactions with significant price fluctuations (i.e., if the price of such transactions differs from the prices for similar transactions by more than 20 percent within a short period of time). Transfer pricing adjustments are also applicable to transactions with securities and derivatives.

The transfer pricing rules are vaguely drafted, generally leaving wide scope for interpretation by the tax authorities and courts. Moreover, in the event that a transfer pricing adjustment is assessed by the tax authorities, the transfer pricing rules do not provide for an offsetting adjustment to the related counterparty in the transaction.

At present a draft law is under discussion in the Russian Government that will potentially tighten transfer pricing rules further. At this point it cannot be predicted when this law will be enacted, if at all, and what the provisions or effect on taxpayers, including the Group, may be.

While the Company and certain of its subsidiaries engage in numerous transactions that may be deemed to be related-party transactions, they seek to conduct such transactions at prices that would be considered market prices in transactions between unrelated parties. However, it is not always possible to determine a market price for a specific transaction, and the Russian tax authorities may take a view as to what constitutes an appropriate market price that differs from the Group's view. As a result, the Russian tax authorities may challenge prices in such transactions and propose tax adjustments. If any such tax adjustments are implemented, the Group could incur significant additional liabilities on account of taxes, interest and penalties. Such additional liabilities could have an adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

## Risk Factors Related to the Notes

***The Notes may not be a suitable investment for all investors***

Each potential investor in the Notes must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- have sufficient knowledge and experience to make a meaningful evaluation of the Notes, the merits and risks of investing in the Notes and the information contained in this Prospectus;
- have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Notes and the impact such investment will have on its overall investment portfolio;
- have sufficient financial resources and liquidity to bear all of the risks of an investment in the Notes;
- understand thoroughly the terms of the Notes and be familiar with the behaviour of the relevant financial markets; and
- be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

***Payments under the Loan Agreement are structurally subordinated to existing indebtedness of the Group's subsidiaries, and these subsidiaries may incur further such indebtedness in the future***

The obligations of the Company under the Loan Agreement are structurally subordinated to the existing obligations of the Company's subsidiaries. In addition, subject to certain limitations set forth in the Loan Agreement, the Company and its subsidiaries may be able to incur substantial additional debt in the future, including debt that may be secured or structurally senior to the debt under the Loan. Any such additional debt incurred by the Company's subsidiaries would be structurally senior to the obligations of the Company under the Loan Agreement. As at 31 March 2008, the Group (excluding the Company) had approximately US$2.8 billion of total debt financing. Secured indebtedness of the Company or any of its subsidiaries may also rank effectively senior to the obligations of the Company under the Loan Agreement. The incurrence of such additional indebtedness by the Company or its subsidiaries could have an adverse effect on the Group's business, financial condition, results of operations, future prospects and the value of the Notes.

***The Company may be unable to repay its obligations under the Loan Agreement***

At maturity, the Company may not have the funds to fulfil its obligations under the Loan Agreement and may not be able to arrange for additional financing. If the maturity date of the Loan occurs at a time when other arrangements prohibit the Company from repaying the Loan, the Company would try to obtain waivers of such prohibitions from the lenders under those arrangements, or the Company could attempt to refinance the borrowings that contain the restrictions. If the Company could not obtain the waivers or refinance these borrowings, the Company would be unable to repay the Loan.

***Noteholders' recourse against the Issuer is limited***

The Issuer is only obliged to make payments under the Notes to the Noteholders in an amount equivalent to sums of principal, interest and/or additional amounts (if any) actually received by or for the account of the Issuer under the Loan Agreement, less any amount in respect of Reserved Rights. Consequently, if the Company fails to fully satisfy its obligations under the Loan Agreement, the Noteholders will receive less than the scheduled amount of principal, interest and/or additional amounts (if any) on the relevant due date.

***Noteholders have no direct recourse against the Company***

Except as otherwise disclosed in "Terms and Conditions of the Notes" and in the Trust Deed, no proprietary or other direct interest in the Issuer's rights under or in respect of the Loan Agreement or the Loan exists for the benefit of the Noteholders. Subject to the terms of the Trust Deed, no Noteholder will have any entitlement to enforce any of the provisions of the Loan Agreement or have direct recourse against the Group, except through action by the Trustee under the Security Interests (as defined in "Terms and Conditions of the Notes"). Neither the Issuer nor the Trustee under the Assigned Rights (as defined in "Terms and Conditions of the Notes") shall be required to monitor the financial performance or status of the Group or to enter into proceedings to enforce payment under the Loan Agreement unless it has been indemnified and/or secured by the Noteholders to its satisfaction against all liabilities, proceedings, claims and demands to which it may thereby become liable and all costs, charges and expenses which may be incurred by it in connection therewith.

Payments of principal and/or interest by the Company under the Loan Agreement to, or to the order of, the Trustee or the Principal Paying Agent will satisfy the Issuer's obligations in respect of the Notes. Consequently, Noteholders will have no further recourse against the Issuer or the Group after such payment is made.

***The debt agreements that the Group has entered into include covenants that may restrict the Group from making certain business decisions and/or carrying out its business strategy***

The agreements that govern the Group's debt instruments, including the Loan Agreement, contain certain restrictions limiting its flexibility in operating its business. Such restrictions limit its ability to:

- create liens;
- borrow money;
- sell or otherwise dispose of assets; and
- engage in mergers or consolidation.

These restrictions could hinder the Group's ability to carry out its business strategy and the Group's ability to make payments on the Loan.

In addition, a breach of the Loan Agreement or the terms of other debt instruments could cause a default under the terms of the Group's other financing arrangements, causing all debt under those financing arrangements to become due. No assurance can be given that if the indebtedness under the Loan Agreement were to be accelerated, the assets of the Group would be sufficient to generate the funds necessary to repay the Loan, and thus the Notes, in full in satisfaction of its obligations under the Loan Agreement.

***The Group may prepay the loan under the Loan Agreement***

Under the terms of the Loan Agreement, the Group may, subject to certain conditions, prepay the Loan if it is required to increase its payments for tax reasons regardless of whether the increased payment obligation results from any change in the applicable tax laws or treaties or from the change in application of existing tax laws or treaties or from enforcement of the security provided for in connection with the Notes. The Group may also prepay the Loan if it is required to indemnify the Issuer in respect of certain increased costs to the Issuer (as set forth in the Loan Agreement). In the event that it becomes unlawful for the Issuer to allow the Loan to remain outstanding under the Loan Agreement, to allow the Notes to remain outstanding, to maintain or give effect to any of its obligations under the Loan Agreement and/or to charge or receive or be paid interest at the rate then applicable to the Loan, the Group may be required by the Issuer to prepay the Loan in full. In case of any such prepayment, all outstanding Notes would be redeemable at par together with accrued interest.

***There is no active trading market for the Notes***

Prior to their issue, there was no public market for the Notes. Although application has been made to list the Notes on the London Stock Exchange, an active trading market in the Notes may not develop or be maintained after listing. If an active trading market does not develop or cannot be maintained, this could have a material adverse effect on the liquidity and the trading price of the Notes. In addition, Securities markets, in recent periods, have experienced significant price fluctuations. These fluctuations were often unrelated to the operating performance of the companies whose securities are traded on such stock markets. Market fluctuations as well as adverse economic conditions have negatively affected the market price of many securities and may affect the market price of the Notes.

***The Company's payments under the Loan and the Issuer's payments under the Notes may be subject to withholding tax***

In general, interest payments on borrowed funds made by a Russian entity to a non-resident are subject to Russian withholding tax at a rate of 20 percent if a lender is not an individual, unless such payments are reduced or eliminated pursuant to the terms of an applicable double tax treaty. Based on professional advice it has received, the Group believes that interest payments on the Loan made to the Issuer will not be subject to withholding tax under the terms of the Convention between the Russian Federation and Luxembourg for the Avoidance of Double Taxation and the prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, signed on 28 June 1993. However, there can be no assurance that such double tax treaty relief will be available.

In circumstances where payments under the Loan Agreement become payable to the Trustee pursuant to the security arrangements described herein, benefits of the Russia-Luxembourg double tax treaty will cease and payments of interest under the Loan Agreement to the Trustee should be made subject to Russian income tax withholding at a rate of 20 percent or such other rate as may be in force at the time of payment. It is not expected that the Trustee will, or will be able to, claim a withholding tax exemption under any double tax treaty under such circumstances. In addition, while some Noteholders might be eligible for an exemption from or a reduction in Russian withholding tax under applicable double tax treaties, there is no assurance that such exemption or reduction will be available in practice under such circumstances.

If payments under the Loan are subject to any withholding of Russian or Luxembourg tax, the Company will be obliged to increase the amounts payable as may be necessary to ensure that the recipient receives a net amount that will not be less than the amount it would have received in the absence of such withholding taxes. It is currently unclear whether the provisions obliging the Company to gross up interest payments will be enforceable under Russian law. There is a risk that a gross-up for withholding tax will not take place and that interest payments made by the Company under the Loan Agreement will be reduced by Russian income tax withheld by the Company at the rate of 20 percent, or such other rate as may be in force at the time of payment. See "Taxation."

Payments in respect of the Notes will be made, except in certain limited circumstances, without deduction or withholding for or on account of Luxembourg taxes. However, pursuant to a European Directive regarding the taxation of savings income in the form of interest payments within the European Community ("**EU Savings Directive**"), interest on the Notes paid to individuals who are beneficial owners of interest and residents in European Union Member States as well as certain residual entities may be subject to withholding tax in Luxembourg. For further information on this legislation and the applicability of withholding tax in Luxembourg, see "Taxation — Grand Duchy of Luxembourg." If any payments to non-resident Noteholders in respect of the Notes become subject to deduction or withholding for or on account of Luxembourg taxes (other than pursuant to the EU Savings Directive), the Company will, subject to certain limitations, be obliged under the terms of the Loan Agreement to increase interest payments (pay additional amounts) as may be necessary so that the net payments received by the Noteholders will not be less than the amount they would have received in the absence of such withholding. For further information regarding the circumstances in which the payment of such additional amount will be required and the limitations thereon, see "Terms and Conditions of the Notes — 8 Taxation."

Because of the limited recourse nature of the Notes, if the Company fails to pay any such gross-up amounts, the amounts payable by the Issuer under the Loan Agreement will be correspondingly reduced. Any failure by the Group to pay such amounts would constitute an Event of Default under the Loan

Agreement. In certain circumstances (including following enforcement of the security upon the occurrence of a Relevant Event as defined in the Loan Agreement), in the event that the Group is obliged to increase the amounts payable, it may prepay the principal of the Loan together with accrued interest, and all outstanding Notes would be redeemed by the Issuer (to the extent that the Issuer has actually received the relevant funds from the Company) at par together with accrued and unpaid interest and additional amount, if any, to the date of the redemption. See "Terms and Conditions of the Notes — 6 Redemption". As indicated above, it is currently unclear whether the provisions obliging the Group to gross-up payments would be enforceable in Russia.

***Tax might be withheld on disposals of the Notes in Russia, reducing their value***

If a non-resident Noteholder that is a legal person or organisation sells Notes and receives proceeds from a source within Russia, there is a risk that the part of the payment, if any, representing accrued interest may be subject to 20 percent Russian withholding tax, although such tax may be reduced or eliminated under an applicable tax treaty subject to compliance with the treaty clearance formalities. Where proceeds from a disposition of the Notes are received from a source within Russia by an individual non-resident Noteholder, individual income tax would be charged at a rate of 30 percent on gross proceeds from such disposal of the Notes less any available documented cost deduction. Although such tax may be reduced or eliminated under an applicable tax treaty subject to compliance with the treaty clearance formalities, in practice, individuals would not be able to obtain advance treaty relief on receipt of proceeds from a source within Russia. The only means to claim treaty protection is by filing a tax return and claiming a refund of tax from the budget, which can be extremely difficult, if not impossible. Furthermore, even though the Tax Code requires only a Russian professional asset manager or broker, or another person (including a foreign company with a permanent establishment or any registered presence in Russia or an individual entrepreneur located in Russia) acting in a similar capacity to withhold the tax from payment to an individual associated with a disposal of securities, there is no guarantee that other Russian companies or foreign companies with a registered presence in Russia or an individual entrepreneur located in Russia would not seek to withhold the tax. The imposition or possibility of imposition of this withholding tax could adversely affect the value of the Notes. See "Taxation".

***Interest rate risks***

As the Notes bear a fixed rate of interest, an investment in the Notes involves the risk that subsequent changes in market interest rates may adversely affect the value of the Notes.

***Exchange rate risks and exchange controls***

The Issuer will pay principal and interest on the Notes in US dollars. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "**Investor's Currency**") other than the US dollar. These include the risk that exchange rates may significantly change (including changes due to devaluation of the US dollar or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to the US dollar would decrease (i) the Investor Currency's equivalent yield on the Notes; (ii) the Investor's Currency equivalent value of the principal payable on the Notes; and (iii) the Investor's Currency equivalent market value of the Notes.

***Changes to the credit ratings of the Company or the Notes may adversely affect the value of the Notes***

The Notes have been rated BB by Fitch, Ba2 by Moody's and BB by Standard & Poor's. The foregoing credit ratings do not mean that the Notes are a suitable investment. A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation. The ratings do not address the likelihood that the principal on the Notes will be prepaid, paid on an expected final payment date or paid on any particular date before the legal final maturity date of the Notes. The ratings do not address the marketability of the Notes or any market price. The significance of each rating should be analysed independently from any other rating. Any changes in the credit ratings of the Company or the Notes could adversely affect the value of the Notes and the price that a subsequent purchaser will be willing to pay for the Notes.

***Legal investment considerations may restrict certain investments***

The investment activities of certain investors are subject to investment laws and regulations, or to the review by, or regulation of, certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (i) the Notes are legal investments to it; (ii) the Notes can be used as collateral for various types of borrowing; and (iii) other restrictions apply to its purchase or pledge of any Notes. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of the Notes under any applicable risk based capital or similar rules.

***The Notes may only be transferred in accordance with the procedures of the depositaries in which the Notes are deposited***

Except in limited circumstances, the Notes will be issued only in global form with interests therein held through the facilities of Euroclear, Clearstream, Luxembourg and/or DTC. Ownership of beneficial interests in the Notes is shown on, and the transfer of that ownership is effected only through, records maintained by Euroclear, Clearstream, Luxembourg and/or DTC or their nominees and the records of their participants. The laws of some jurisdictions may require that certain purchasers of securities take physical delivery of such securities in definitive form. These laws may impair the ability to transfer beneficial interests in the Notes. Because Euroclear, Clearstream, Luxembourg and/or DTC can only act on behalf of their participants, which, in turn, act on behalf of owners of beneficial interests held through such participants and certain banks, the ability of a person having a beneficial interest in a note to pledge or transfer such interest to persons or entities that do not participate in the Euroclear, Clearstream, Luxembourg and/or DTC systems may be impaired.

***The United States federal income tax characterisation of the Notes is uncertain***

No authority directly addresses the US federal income tax characterisation of securities like the Notes and the Issuer has not and will not seek a ruling from the US Internal Revenue Service ("**IRS**") as to their characterisation for such purposes. To the extent relevant for US federal income tax purposes, the Issuer intends to treat the Notes as indebtedness for such purposes. No assurance can be given that the IRS will not assert, or a court would not sustain, a position regarding the characterisation of the Notes that is contrary to this treatment. Alternative characterisations include treatment of the Notes as beneficial ownership of the Loan or as equity in the Issuer, which is a passive foreign investment company. Prospective investors should seek advice from their own tax advisors as to the consequences to them of investing in the Notes, including their treatment for US federal income tax purposes.

**RISK FACTORS RELATING TO LUXEMBOURG LAW**

***Insolvency laws in Luxembourg could negatively affect the ability of Noteholders to enforce their rights***

Any insolvency proceedings with regard to the Issuer would most likely be based on and governed by the insolvency laws of Luxembourg, the jurisdiction under which the Issuer is organised. As a result, in the event of the Issuer's insolvency, a Noteholder's claim against the Issuer will most likely be subject insolvency laws of Luxembourg. The insolvency laws of Luxembourg may not be as favourable to the interest of Noteholders as the laws in other jurisdictions. In the event that the Issuer experiences financial difficulty, it is not possible to predict with certainty in which jurisdiction or jurisdictions insolvency or similar proceedings would be commenced or how these proceedings would be resolved. In addition, there can be no assurance as to how the insolvency laws of Luxembourg will be applied in insolvency proceedings relating to several jurisdictions.

## USE OF PROCEEDS

The proceeds of the issue of the Notes will be used by the Issuer for the sole purpose of financing the Loan. The proceeds from the Loan (expected to be US$1,250,000,000 before taking account of commissions and expenses), which is being funded in full by the issue of the Notes, will be used by the Company: (i) for working capital; and/or (ii) for general corporate purposes; and/or (iii) to finance acquisitions and/or to refinance indebtedness. Total commissions and expenses relating to the offering of the Notes are expected to be approximately US$12,500,000. The net proceeds of the Loan to the Company are expected to be approximately US$1,237,500,000.

## EXCHANGE RATE INFORMATION

The official currency of Russia, where a substantial amount of the Group's assets are located, is the Rouble. However, the Financial Statements are reported in US dollars. As a result, fluctuations in the value of the Rouble against the US dollar may affect these results when translated into US dollars. See "Risk Factors — The Group may incur losses as the result of fluctuations in the foreign currency exchange rates of the Rouble, the US dollar or the euro" and "Management's Discussion and Analysis of Financial Condition and Results of Operations — Quantitative and Qualitative Disclosure on Market Risk — Foreign currency exchange risk".

The table below sets forth, for the periods and dates indicated, certain information regarding the exchange rate between the Rouble and the US dollar, based on the official exchange rate quoted by CBR. Fluctuations in the exchange rates between the rouble and the US dollar in the past are not necessarily indicative of fluctuations that may occur in the future. These rates may also differ from the actual rates used in the preparation of the Financial Statements and other information presented in this Prospectus.

| | Roubles per US dollar | | | |
|---|---|---|---|---|
| | **High** | **Low** | **Average(1)** | **Period End** |
| **Year Ended 31 December** | | | | |
| 2005 | 29.00 | 27.46 | 28.32 | 28.78 |
| 2006 | 28.48 | 26.18 | 27.09 | 26.33 |
| 2007 | 26.58 | 24.26 | 25.49 | 24.55 |

| | Roubles per US dollar | | | |
|---|---|---|---|---|
| | **High** | **Low** | **Average(1)** | **Period End** |
| **2008** | | | | |
| January | 24.89 | 24.29 | 24.50 | 24.48 |
| February | 24.78 | 24.12 | 24.53 | 24.12 |
| March | 24.05 | 23.51 | 23.76 | 23.52 |
| April | 23.67 | 23.34 | 23.51 | 23.65 |
| May | 23.88 | 23.55 | 23.72 | 23.74 |
| June | 23.81 | 23.45 | 23.64 | 23.45 |
| July (through 25 July) | 23.55 | 23.12 | 23.34 | 23.38 |

Source: CBR

Note:

(1) The average in respect of a year is calculated as the average of the exchange rates on the last business day of each month for the relevant annual period. The period average in respect of a month is calculated as the average of the exchange rates for each business day in the relevant month.

No representation is made that the Rouble amounts referred to in this Prospectus could have been or could be converted into US dollars at the above exchange rates or at any other rate.

## CAPITALISATION

The following table sets forth the Group's cash and cash equivalents, short-term debt finance and capitalisation as at 31 March 2008 on a consolidated basis and as adjusted for the the issue of the Notes and the receipt of the proceeds of the Loan, assuming that such issue and the receipt of such proceeds occurred on 31 March 2008, but not adjusted for any other changes subsequent to that date.

Prospective investors should read this table in conjunction with "Selected Consolidated Financial Information", "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the Financial Statements, which are included in this Prospectus beginning on page F-3.

| | As at 31 March 2008 | |
|---|---|---|
| | **Actual** | **As adjusted for the offering[1]** |
| | *(US$ thousands)* | |
| **Cash and cash equivalents** | **2,406,295** | **3,656,295** |
| **Short-term debt finance** | **1,257,587** | **1,257,587** |
| **Long-term debt finance** | **2,852,956** | **4,102,956** |
| **Equity** | | |
| Share capital | 3,311,288 | 3,311,288 |
| Additional capital | 1,165,530 | 1,165,530 |
| Foreign exchange differences | 1,562,220 | 1,562,220 |
| Hedging reserve | (21,698) | (21,698) |
| Retained earnings | 4,404,914 | 4,404,914 |
| **Equity attributable to shareholders of the parent** | **10,422,254** | **10,422,254** |
| **Minority interest** | **510,305** | **510,305** |
| **Total equity** | **10,932,559** | **10,932,559** |
| **Total capitalisation[2]** | **13,785,515** | **15,035,515** |

Notes:

(1) Adjusted to give effect to the issuance of the Notes and the receipt of the proceeds of such issuance, but not adjusted for any other changes subsequent to 31 March 2008. The proceeds to the Company of US$1,250,000,000 from the issuance of the Notes, before taking into account commissions and expenses, have been added to cash, pending their use as described under "Use of Proceeds".

(2) Total capitalisation is the sum of long-term debt finance and total equity.

In April and May 2008, the Group was advanced the remaining undrawn €400 million under the EBRD syndicated facility. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Net Indebtedness — Major Indebtedness". In June 2008, the Group entered into a revolving credit facility for an aggregate principal amount of US$490 million, for a term of five years, in connection with Sparrows Point.

In June 2008, the Company declared a dividend on its ordinary shares of RUR 4.0 per share in respect of the fourth quarter of 2007 and of RUR 5.2 per share in respect of the first quarter of 2008. In July 2008, the Group completed the acquisition of WCI Steel (see "Business — Recent Developments — WCI Steel").

Other than as described above, there has been no material change in the Group's total capitalisation since 31 March 2008.

## SELECTED CONSOLIDATED FINANCIAL INFORMATION

The following tables set forth, in summary form, consolidated balance sheet, income statement and other information relating to the Group. Such information has been derived from the Financial Statements of the Group prepared in accordance with IFRS. The reports of KPMG Limited appear elsewhere in this Prospectus. The financial information presented below should be read in conjunction with such Financial Statements, reports and "Management's Discussion and Analysis of Financial Condition and Results of Operations".

### CONSOLIDATED INCOME STATEMENT

| | Year ended 31 December | | | Three months ended 31 March | |
|---|---|---|---|---|---|
| | 2007 | 2006 (restated) | 2005 (restated) | 2008 | 2007 (restated) |
| | *(Amounts expressed in thousands of US dollars, except as otherwise stated)* | | | | |
| **Sales** | | | | | |
| Sales — external | 14,543,043 | 11,723,318 | 9,786,057 | 4,144,363 | 3,526,021 |
| Sales — to related parties | 701,868 | 725,714 | 665,589 | 164,630 | 166,502 |
| | 15,244,911 | 12,449,032 | 10,451,646 | 4,308,993 | 3,692,523 |
| Cost of sales | (10,541,571) | (8,601,227) | (6,831,138) | (3,165,953) | (2,531,468) |
| **Gross profit** | 4,703,340 | 3,847,805 | 3,620,508 | 1,143,040 | 1,161,055 |
| General and administrative expenses | (691,210) | (654,987) | (524,662) | (230,850) | (169,410) |
| Distribution expenses | (909,510) | (697,308) | (657,684) | (275,665) | (233,529) |
| Indirect taxes and contributions | (153,614) | (142,109) | (95,343) | (45,503) | (35,147) |
| Share of associates' (loss)/profit | (89,397) | (1,193) | (4,190) | (542) | 2,413 |
| Net income/(loss) from securities operations | 25,564 | 28,263 | 24,443 | (8,064) | 1,503 |
| Loss on disposal of property, plant and equipment | (35,280) | (39,292) | (36,780) | (14,495) | (9,230) |
| Net other operating (expenses)/ income | (7,520) | (27,109) | (20,344) | 197,185 | (1,037) |
| **Profit from operations** | 2,842,373 | 2,314,070 | 2,305,948 | 765,106 | 716,618 |
| Impairment of property, plant and equipment | (29,109) | (57,736) | (111,384) | (1,855) | (950) |
| Net gain on restructuring of tax liabilities | — | 14,669 | 174,178 | — | — |
| Negative goodwill, net | 12,223 | 4,213 | 7,630 | 2,166 | 633 |
| Net other non-operating expenses | (58,576) | (53,536) | (52,753) | (32,629) | (17,969) |
| **Profit before financing and taxation** | 2,766,911 | 2,221,680 | 2,323,619 | 732,788 | 698,332 |
| Interest income | 172,937 | 102,402 | 65,134 | 28,944 | 36,765 |
| Interest expense | (288,293) | (244,977) | (203,057) | (90,875) | (68,363) |
| Foreign exchange difference | 2,900 | 33,324 | (60,231) | 13,887 | (180) |
| **Profit before income tax** | 2,654,455 | 2,112,429 | 2,125,465 | 684,744 | 666,554 |
| Income tax expense | (681,269) | (635,298) | (500,907) | (232,770) | (190,279) |
| **Profit from continuing operations** | 1,973,186 | 1,477,131 | 1,624,558 | 451,974 | 476,275 |
| Profit from discontinued operations | 433 | 32,849 | 602 | — | 4,935 |
| **Profit for the year/period** | 1,973,619 | 1,509,980 | 1,625,160 | 451,974 | 481,210 |
| Attributable to: | | | | | |
| shareholders of OAO Severstal | 1,936,423 | 1,454,198 | 1,561,182 | 438,706 | 458,091 |
| minority interest | 37,196 | 55,782 | 63,978 | 13,268 | 23,119 |
| Weighted average number of shares outstanding during the period (millions of shares) | 1,007.7 | 928.4 | 912.2 | 1,007.7 | 1,007.7 |
| Basic and diluted earnings per share (US dollars) | 1.92 | 1.57 | 1.71 | 0.44 | 0.45 |

## CONSOLIDATED BALANCE SHEET

| | As at 31 December | | | As at 31 March |
|---|---|---|---|---|
| | 2007 | 2006 (restated) | 2005 (restated) | 2008 |
| | *(Amounts expressed in thousands of US dollars)* | | | |
| **Assets** | | | | |
| **Current assets:** | | | | |
| Cash and cash equivalents | 1,546,881 | 1,701,022 | 1,327,887 | 2,406,295 |
| Short-term bank deposits | 665,977 | 1,147,270 | 674,512 | 321,472 |
| Short-term financial investments | 267,633 | 321,842 | 267,851 | 206,127 |
| Trade accounts receivable | 1,674,618 | 1,324,585 | 1,174,193 | 2,003,879 |
| Amounts receivable from related parties | 162,719 | 127,703 | 173,808 | 99,692 |
| Inventories | 2,537,470 | 2,222,372 | 1,725,528 | 2,837,856 |
| VAT recoverable | 283,745 | 339,392 | 442,297 | 302,511 |
| Income tax recoverable | 75,993 | 35,904 | 28,671 | 98,629 |
| Assets held for sale | 461,196 | — | — | 451,662 |
| Other current assets | 321,362 | 259,208 | 181,685 | 402,584 |
| **Total current assets** | 7,997,594 | 7,479,298 | 5,996,432 | 9,130,707 |
| **Non-current assets:** | | | | |
| Long-term financial investments | 152,866 | 199,940 | 89,541 | 144,216 |
| Investment in associates and joint ventures | 589,092 | 354,906 | 210,652 | 199,131 |
| Property, plant and equipment | 7,292,811 | 6,470,385 | 5,319,568 | 8,705,285 |
| Intangible assets | 611,261 | 61,666 | 56,523 | 624,712 |
| Assets held for sale | — | 113,516 | 66,117 | — |
| Restricted cash | — | — | — | 14,468 |
| Deferred tax assets | 52,324 | 30,150 | 35,076 | 61,146 |
| Amounts receivable from related parties | — | — | 35,095 | — |
| Other non-current assets | 21,474 | 3,844 | 3,105 | 43,124 |
| **Total non-current assets** | 8,719,828 | 7,234,407 | 5,815,677 | 9,792,082 |
| **Total assets** | 16,717,422 | 14,713,705 | 11,812,109 | 18,922,789 |
| **Liabilities and shareholders' equity** | | | | |
| **Current liabilities:** | | | | |
| Trade accounts payable | 1,090,884 | 1,038,901 | 866,629 | 1,325,472 |
| Bank customer accounts | — | 31,143 | 98,867 | — |
| Amounts payable to related parties | 58,915 | 175,740 | 491,957 | 72,130 |
| Short-term debt finance | 972,079 | 957,564 | 996,125 | 1,257,587 |
| Income taxes payable | 41,381 | 44,348 | 86,001 | 96,978 |
| Other taxes and social security payable | 200,424 | 199,963 | 257,678 | 297,927 |
| Dividends payable | 107,485 | 23,243 | 12,275 | 6,078 |
| Liabilities related to assets held for sale | 91,750 | — | — | 103,993 |
| Other current liabilities | 600,580 | 506,848 | 379,218 | 708,277 |
| **Total current liabilities** | 3,163,498 | 2,977,750 | 3,188,750 | 3,868,442 |
| **Non-current liabilities:** | | | | |
| Long-term debt finance | 2,354,823 | 2,048,035 | 1,931,694 | 2,852,956 |
| Deferred tax liabilities | 374,636 | 403,076 | 356,739 | 436,332 |
| Retirement benefit liability | 387,398 | 442,954 | 338,486 | 437,514 |
| Liabilities related to assets held for sale | — | 1,792 | 172 | — |
| Other non-current liabilities | 226,388 | 286,090 | 281,075 | 394,986 |
| **Total non-current liabilities** | 3,343,245 | 3,181,947 | 2,908,166 | 4,121,788 |

| | As at 31 December | | | As at 31 March |
|---|---|---|---|---|
| | 2007 | 2006 (restated) | 2005 (restated) | 2008 |
| | *(Amounts expressed in thousands of US dollars)* | | | |
| **Equity**: | | | | |
| Share capital | 3,311,288 | 3,311,288 | 3,311,254 | 3,311,288 |
| Additional capital | 1,165,530 | 1,165,530 | 60,367 | 1,165,530 |
| Foreign exchange differences | 1,176,321 | 535,591 | 34,368 | 1,562,220 |
| Retained earnings | 4,082,834 | 2,983,954 | 1,818,475 | 4,404,914 |
| Hedging reserve | — | — | — | (21,698) |
| **Total equity attributable to shareholders of parent** | 9,735,973 | 7,996,363 | 5,224,464 | 10,422,254 |
| **Minority interest** | 474,706 | 557,645 | 490,729 | 510,305 |
| **Total equity** | 10,210,679 | 8,554,008 | 5,715,193 | 10,932,559 |
| **Total equity and liabilities** | 16,717,422 | 14,713,705 | 11,812,109 | 18,922,789 |

**SUMMARY CASH FLOW DATA**

| | Year ended 31 December | | | Three months ended 31 March | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2008 | 2007 |
| | *(Amounts expressed in thousands of US dollars)* | | | | |
| **Net cash from operating activities** | 2,315,089 | 1,729,658 | 1,934,791 | 695,341 | 669,507 |
| **Cash from investing activities** | (1,981,967) | (2,169,137) | (1,178,089) | (73,150) | (959,246) |
| **Cash from financing activities** | (569,249) | 726,365 | (448,628) | 72,953 | 42,307 |

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following is a discussion of the Group's financial condition and results of operations as at and for the years ended 31 December 2005 (restated), 2006 (restated) and 2007 and as at and for the three months ended 31 March 2007 (restated) and 2008, and of the material factors that the Group believes are likely to affect its financial condition and results of operations. You should read this section in conjunction with the Financial Statements included in this Prospectus beginning on page F-3. The Financial Statements have been prepared in accordance with IFRS.

In addition, the following discussion contains certain forward-looking statements that reflect the Group's plans, estimates and beliefs. The Group's actual results may differ materially from those discussed in these forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to those discussed below and elsewhere in this Prospectus, including "Risk Factors".

### Overview of the Group

The Group is an international, vertically-integrated metals and mining company that sells steel and mining products to customers across the world. According to Metal Bulletin, the Group was the world's 15th largest producer of crude steel in 2007, by volume of production. The Group is a full production cycle operation which includes iron ore and coal mining enterprises, steel mills and rolled product plants as well as downstream production and distribution businesses. The Group's production facilities are geographically diversified, with locations in Russia, the United States, Italy, France, Ukraine, the United Kingdom and Kazakhstan. With a focus on high value-added products in attractive niche markets and a successful track record of acquiring and integrating high-quality assets in the United States and Europe, the Group's corporate strategy is to improve its position as a leading global steel company in terms of profitability, with a vertically-integrated, low-cost business structure.

### The Group's Financial Statements and Scope of Consolidation

The Financial Statements have been prepared in accordance with IFRS as issued by the IASB, in effect at the time of the preparation of the Financial Statements. Such IFRS differ from the IFRS that has been adopted for use in the European Union through the endorsement procedure established by the European Commission. IFRS that was adopted for use in the European Union did not include revised IFRS 3 "Business Combinations" and several Interpretations and Amendments to existing effective IFRS as issued by IASB.

In addition, IFRS differ in various material respects from generally accepted accounting principles in the United States.

The Financial Statements include the accounts of the Group's subsidiaries from the date that control effectively commenced until the date that control effectively ceased. Acquisitions of controlling interests in companies that were previously under the control of the Controlling Shareholder of the Group are accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date on which control was obtained by the Controlling Shareholder. Acquisitions by the Controlling Shareholder of additional interests in the acquired companies, after control over those companies has been obtained by the Controlling Shareholder, are treated as if those additional interests were acquired by the Group. Intra-Group balances, transactions, unrealised gains and losses arising from such transactions have been eliminated in these Financial Statements.

The list of the Group's subsidiaries, associates and joint ventures with effective ownership interests as at 31 December 2005, 2006 and 2007 is included in the Annual Financial Statements.

Following a reorganisation of the Group's management structure in April 2008, the Group currently consists of three business divisions: the Russian Steel Division (see "Business — Russian Steel Division"), Severstal International (see "Business — Severstal International") and Severstal Resources (see "Business — Severstal Resources"), which are divided into six reporting segments for the purposes of the Financial Statements. The following discussion follows the reporting segment structure consistent with the Financial Statements. A brief description of the reporting segments comprising each division is set forth below.

**Russian Steel Division**

The Russian Steel Division produced approximately 16.4 percent of the total production of Russian crude steel in 2007, making it the third largest producer of crude steel products in Russia by volume of production in that year, in each case according to Chermet Corporation. The Russian Steel Division consists of the Russian Steel segment, the Metalware segment and the Izhora Pipe Mill segment ("**IPM**").

***Russian Steel segment***

The Russian Steel segment consists primarily of the Cherepovets Steel Plant, high-grade automotive galvanising facilities at Severgal and Rolling Mill 5000, which the Group believes to be Russia's only rolling mill that produces 4.8 metre-wide high-quality hot-rolled plates, as well as various supporting functions for trading, maintenance and transportation. With total steelmaking capacity of 13.2 million tonnes of crude steel per year as at 31 December 2007, the Russian Steel Segment produced 11.9 million tonnes of crude steel and 10.8 million tonnes of finished steel in 2007.

***Metalware segment***

The Metalware segment comprises Severstal-Metiz's wire drawing and metalware manufacturing businesses in Russia, Ukraine and the United Kingdom. With total metalware production of 1.0 million tonnes in 2007, Severstal-Metiz's production represented approximately 34.4 percent of domestic Russian metalware production, based on data from the Association of Metalware Producers of Russia, and approximately 33.2 percent of Ukrainian metalware production, based on data from the Association of Metalware Producers of Ukraine.

***IPM***

IPM consists of a large-diameter pipe mill in Russia. With a total pipemaking capacity of 0.6 million tonnes as at 31 December 2007, IPM produced 0.3 million tonnes in 2007.

**Severstal International**

Severstal International includes the Lucchini segment and the North America segment ("**North America**").

***Lucchini segment***

The Lucchini segment produces special and high-quality steel and quality and specialty long products. Production sites are located in Italy and France. This segment also includes a network of distribution companies, which are located primarily in Western Europe. The Group acquired a controlling interest in Lucchini in October 2006. The results of operations of the Lucchini segment have been included in the Group's Financial Statements since April 2005, when control of the Lucchini segment was acquired by entities under common control with the Group.

***North America***

North America includes Severstal North America LLC ("**Severstal North America**"), SeverCorr LLC ("**SeverCorr**") and Sparrows Point. In the following discussion, Severstal North America is the only segment of North America that was consolidated into the Annual Financial Statements. Although SeverCorr was acquired by the Group in January 2008, its acquisition was from entities under common control with the Group and in accordance with the Group's accounting policies, the corresponding figures in the Interim Financial Statements have been restated to show SeverCorr as a consolidated subsidiary. Sparrows Point was acquired in May 2008 and accordingly is not reflected in the Financial Statements.

North America has three plants in the United States and produces hot-rolled, cold-rolled and galvanised steel and a full range of flat-rolled products. North America operates a full cycle integrated iron and steel mill in the United States and has joint control and non-controlling equity interests in US-based steel-galvanising, steel-slitting and coking-coal production entities. See "— Recent Developments".

**Severstal Resources**

Severstal Resources is represented by the Mining segment.

***Mining segment***

The Mining segment includes gold mining in one location in Kazakhstan and the following operations in Russia: coking coal production in two locations (although one coal mine was disposed of in April 2008), one location where iron ore concentrate is produced, one location where pellets are produced, gold mining in two locations and also coal refining facilities and other auxiliary businesses. The Group acquired a controlling interest in the entities that comprise the Mining segment in June 2006.

**Financing segment**

This segment operated a commercial bank and ceased its existence in November 2007 when the bank was sold. This transaction was accounted for as a discontinued operation in the Financial Statements.

## KEY FACTORS AFFECTING THE GROUP'S FINANCIAL RESULTS

The Group's results are affected by a variety of factors, including, but not limited to, the following:

**Macroeconomic trends**

The majority of the Group's operations are based in Russia, Western Europe (primarily in Italy and France) and the United States. As a result, macroeconomic trends in these regions and region-specific factors significantly influence the Group's performance. In particular, the Group believes that GDP growth in Russia has generally increased demand for it products, positively affecting the Group's pricing, sales and profit from operations.

The following table sets forth certain information for Russia, Italy, France and the United States as at and for the dates indicated:

| | For the year ended 31 December | | |
|---|---|---|---|
| | **2005** | **2006** | **2007** |
| **Russia** | | | |
| GDP growth(1) | 6.4% | 7.4% | 8.1% |
| Percent change in consumer price index(1) | 10.9% | 9.0% | 11.9% |
| **Italy** | | | |
| GDP growth(2) | 0.6% | 1.8% | 1.5% |
| Percent change in consumer price index(2) | 2.2% | 2.2% | 2.0% |
| **France** | | | |
| GDP growth(2) | 1.9% | 2.2% | 2.2% |
| Percent change in consumer price index(2) | 1.9% | 1.9% | 1.6% |
| **United States** | | | |
| GDP growth(3) | 3.1% | 2.9% | 2.2% |
| Percent change in consumer price index(4) | 3.4% | 3.2% | 2.8% |
| **Average nominal exchange rates** | | | |
| Roubles per US dollar(5) | 28.32 | 27.18 | 25.57 |
| Roubles per euro(5) | 35.16 | 34.11 | 35.01 |

Source:

(1) Russian Federal State Statistics.

(2) Eurostat.

(3) Bureau of Economic Analysis, US Department of Commerce.

(4) Bureau of Labor Statistics, US Department of Labor.

(5) Bank of Russia.

**Exchange rate movements**

The majority of the Group's operations are based in Russia, Western Europe (primarily in Italy and France) and the United States. The functional currency is determined separately for each of the Group's entities. For all of the Group's Russian entities, the majority of costs and revenues are denominated in

Roubles, and accordingly, their functional currency is the Rouble. The functional currency of the Group's entities located in North America is the US dollar. The functional currency of the majority of the Group's entities located in Western Europe is the euro.

Since the Group's consolidated financial statements prior to 1 January 2004 were presented in US dollars, management has elected to continue the use of US dollars as the Group's presentation currency in order to facilitate the comparability of its financial results.

Transactions in foreign currencies are translated to the functional currency of each entity at the foreign exchange rate ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the functional currency of each entity at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies, are translated to the functional currency of the entity at the foreign exchange rate ruling at the date of the transaction. Foreign exchange gains and losses arising on translation are recognised as a part of net financing expense in the income statement.

Within Russia, official exchange rates are determined daily by the CBR. Market rates may differ from the official rates although these differences are generally within narrow parameters. However, any conversion of Rouble amounts into US dollars should not be construed as a representation that Rouble amounts have been, could be, or will be in the future, convertible into US dollars at the exchange rates used, or at any other exchange rate. See also "Exchange Rate Information" and "— Quantitative and Qualitative Disclosure on Market risk — Foreign currency exchange risk".

**Commodity price risk**

The Group's revenue is exposed to the market risk of price fluctuations related to the sale of steel products. Prices for the steel products that the Group sells both inside and outside of Russia are generally determined by market forces. These prices may be influenced by factors such as supply and demand, production costs (including the costs of raw material inputs) and global and Russian economic growth. Over the periods covered by this discussion and analysis, fluctuations in market demand for, and market prices of, steel products significantly affect the revenues received by the Group from the sale of steel products. These fluctuations are likely to continue to affect the revenue that the Group receives from the sale of its products.

**Costs**

The Group requires substantial amounts of raw materials in the steel production process, in particular iron ore, coal and scrap. The prices for these raw materials, other than scrap, have generally tended to increase through the period covered in this discussion and analysis up to the date of this Prospectus. In furtherance of the Group's vertical integration strategy, it has consolidated the Mining segment primarily to secure a supply of iron ore and coking coal concentrate at competitive market rates and, to a significant extent, largely to insulate it, on a consolidated basis, from the impact of increases in prices of iron ore and coal. However, the Group continues to rely on external suppliers for a number of its key raw materials.

The Group also consumes large volumes of electricity and natural gas, which are largely supplied to the Russian Steel segment, the Metalware segment and the Mining segment by monopoly providers in Russia, and to North America and the Lucchini segment by market participants, including certain local utilities. Through 2005 up to the date of this Prospectus, natural gas and electricity tariffs have been steadily increasing, and the Group does not expect this trend to change. The rates of increase may be higher than the rates at which the Group is able to increase its steel prices. In addition, competition in the railway transport in Russia, and the Group is, in part, dependent on the monopoly railway service provider for delivery of both raw materials and products. The Russian monopoly providers regularly increase prices for their services at a rate that may be higher than the rate at which the Group is able to increase the price of its steel products.

In addition to increases in electricity, raw materials, transportation and natural gas prices, increasing wage costs in Russia have added to the costs of the Group's Russian operations over the period covered in this discussion and analysis.

**Restructured tax liabilities**

OAO Vorkutaugol and OAO Mine Vorgashorskaya had significant amounts of taxes in arrears when the Controlling Shareholder acquired them in June 2003. In November 2005, these subsidiaries signed restructuring agreements with the tax authorities. Pursuant to these agreements, the principal amounts of taxes, fines and 15 percent of tax interest are payable in instalments over four years. If those payments are made on schedule, the remaining 85 percent of tax interest liability at the date of restructuring will be forgiven. The Group is confident that all payments will be in accordance with the agreed schedules, and has recognised the gains arising in the income statements for the years ended 31 December 2005 and 2006. Restructured tax liabilities are subject to interest at the rate of 5 percent per annum.

**RECENT DEVELOPMENTS**

**WCI Steel**

In July 2008, the Group acquired the outstanding equity of WCI Steel, which operates a steel mill in Warren, Ohio, for a total cash consideration of approximately US$140 million plus the assumption of, according to the Group's estimates, approximately US$285 million of liabilities and the repayment of debt in an additional amount of approximately US$274.9 million, including payments connected with the redemption of certain senior secured notes of WCI Steel referred to below. WCI Steel's product line comprises custom and commodity flat rolled steel products, including hot-rolled, cold-rolled and galvanised steel. WCI Steel has an estimated production capacity of approximately 1.85 million tonnes of crude steel per year and produced approximately 1.0 million tonnes of crude steel in 2007. The Group believes that WCI Steel's product line, which includes high-carbon and alloy products, and its geographical location close to some of the Group's existing customers and operations, should provide a range of advantages to the Group's US operations in addition to the increased capacity the acquisition gives to the Group in the US market for flat products. The Group's preliminary estimate of the capital expenditure that would be required at WCI Steel for the period from 2008 to 2012 is approximately US$175 million.

In connection with the acquisition, WCI Steel has called for the redemption of the US$100 million aggregate principal amount outstanding of its 8 percent senior secured notes due 2016. Notice of the redemption has been mailed to record holders of such notes and the notes are expected to be redeemed in August 2008.

Recently, an unsuccessful bidder for WCI Steel, together with certain existing minority shareholders of WCI Steel, brought proceedings against WCI Steel, the Company and another member of the Group, seeking an injunction to prevent the completion of the acquisition of WCI Steel by the Group. The plaintiffs alleged that the board of directors of WCI Steel breached its fiduciary duties by, among other matters, not accepting the unsuccessful bidder's bid. The proceedings did not assert any claims against the Company or the other member of the Group. A hearing was held on 27 June 2008, at the conclusion of which the court denied the plaintiffs' application for a preliminary injunction, thereby permitting completion of the acquisition.

**Esmark**

On 30 May 2008, the Group commenced an all cash US$17 per share offer to acquire all of the outstanding shares of common stock of Esmark, a manufacturer and distributor of flat rolled and other steel products in the United States. Initially, the Group's offer was not supported by Esmark's board of directors. However, on 25 June 2008, the Group entered into an agreement with Esmark in connection with which the Group has increased the purchase price in the tender offer to US$19.25 per share in cash and Esmark's board of directors has recommended that Esmark's shareholders tender their shares to the Group. The expiration date of the tender offer has been extended to 10:00 am, New York City time, 4 August 2008. The offer and related transactions contemplated by the agreement are subject to certain customary closing conditions. The Group has entered into an agreement with Esmark's majority shareholder to tender its shares in the tender offer. The Group has also entered into an agreement that satisfies the successorship clause of the United Steelworkers' collective bargaining agreement. If the acquisition is successfully completed, the Group will acquire all of Esmark's business, including Wheeling-Pittsburgh Steel Corporation, Esmark Steel Services Group, Inc and the remaining 50 percent interest in Mountain State Carbon, LLC, a blast furnace coking coal production joint venture with the Group.

The Group's operating and restructuring plan for Esmark, upon successful completion of the acquisition, includes a five-year capital investment programme and is designed to derive value from Esmark through operational improvements, including the maximisation and optimisation of production at the EAF, upgrades to enhance the quality and capacity of the hot strip mill, improvements of the downstream operations, and leveraging synergies and geographical alignment between the Group's other assets in the United States. The Group believes that its combined operations in the United States, including Esmark, would create one of North America's leading producers of flat rolled steel, further expanding the Group's product offerings to its customers in a market that has displayed consistent demand for high quality steel.

The acquisition of Esmark, if successfully completed, is expected to provide the Group with substantial synergies with its current US operations at the Dearborn facility, SeverCorr, Sparrows Point and WCI Steel. Full ownership of Mountain State Carbon, LLC is also expected to increase the Group's vertical integration with raw materials in the United States. In addition, Esmark's service centres and corrugated sheet production facilities are expected to enhance the Group's operations in the US by allowing it to reach more customers and add value to its steel products.

Following completion of the tender offer, subject to the terms and conditions set forth in the offer to purchase, the Group intends to consummate a second-step merger where all remaining Esmark stockholders will receive the same cash price paid in the tender offer, subject to any available appraisal rights under Delaware law. If the offer is accepted at the revised offer price of US$19.25 per share, the total purchase price for all of the outstanding shares of common stock of Esmark would be approximately US$775 million. The Group has also purchased Esmark's aggregate US$110 million term loan facilities from Essar Steel Holdings Limited ("**Essar Steel**"). The Group has, on behalf of Esmark, paid Essar Steel certain other termination and change of control fees and prepayment penalties in connection with certain existing arrangements between Esmark and Essar Steel, including a US$25 million termination fee and a US$20.25 million payment in lieu of the exercise by Essar Steel of its conversion rights related to the term loan facilities referred to above.

**Mano River Resources Inc/African Iron Ore Group**

In May 2008, the Group entered into arrangements to acquire a minority stake in Mano River Resources Inc ("**Mano**"), a company focused on the exploration and development of iron ore, diamonds and gold in west Africa, listed on the London Stock Exchange's Alternative Investment Market and on the TSX-Venture Exchange in Canada. The acquisition price was approximately US$4 million. The Group has also agreed to acquire a 61.5 percent stake in African Iron Ore Group Ltd, a company currently majority-owned by Mano and involved in the Putu Range iron ore project in eastern Liberia, for approximately US$37.5 million, subject to certain conditions, including Mano converting its exploration licence into a mineral development agreement with the government of Liberia.

**Potential Coal Mining Acquisitions**

The Group is considering the strategic acquisition of coal mining assets in the United States. After completing the assessment of potential acquisition targets, the Group may decide to submit a bid on one or more coal mining assets in the near term, possibly as early as July 2008. If the Group were to submit any such bids, and if one or more of the relevant acquisition targets were successfully acquired, the aggregate purchase price for such assets could be material to the Group's financial condition and results of operations. However, there can be no assurance that any such bids will be made or, if made, that any such acquisitions of coal mining assets will be successfully completed.

**Credit Rating Upgrade**

On 20 June 2008, Fitch Ratings upgraded the Group's long-term issuer default and senior unsecured ratings to "BB/Stable" from "BB−/Stable" (BB minus).

**Operational outlook**

Since 31 March 2008, the Group has continued to perform generally in line with management's expectations. Compared with the previous period, the Group has continued to experience growth in sales from the commencement of operations at SeverCorr, the positive effects of on-going capital expenditures, recent acquisitions and favourable market conditions. The negative effect on margins from the acquisition of less profitable companies is expected to generally be offset by the effect of continuing development of the Group's core assets. The Group's capital expenditures continue to be generally in accordance with the Group's investment programme.

## Description of the Group's Income Statement Line Items

The following discussion provides a description of the composition of the principal line items on the Group's income statement for the periods presented.

### Sales

The Group generates sales primarily through the manufacture and sale of a wide range of iron and steel products: cold-rolled sheet, color coated sheet, metalware products, large diameters pipes, long products, hot-rolled strip and plate, pellets and iron ore, large group of coke products and by-products.

### Cost of sales

Cost of sales includes raw materials, consumables, energy costs, repair and maintenance expenses, labour costs, geological services and the majority of depreciation and amortisation charges.

### Gross profit

Gross profit represents the Group's total sales less cost of sales. Gross margin is gross profit divided by sales.

### General and administrative expenses

General and administrative expenses consist of a wide range of administrative costs and the cost of general management and related depreciation and amortisation. General and administrative expenses primarily include labour costs, repair services, insurance expenses, material and fuel expenses related to administrative and managerial activities of the Group.

### Distribution expenses

Distribution expenses consist primarily of expenses related to selling activities of the Group. Distribution expenses include labour cost and taxes on labour cost, depreciation and amortisation relates with selling activities, advertising expenses, transportation expenses.

### Indirect taxes and contributions

Indirect taxes and contributions consist of taxes other than income tax. Primarily indirect taxes and contributions include extraction taxes on the extracted coal and iron ore concentrate and property tax payable on property, plant and equipment used in operations.

### Share of associate's losses/profits

Associates are those enterprises in which the Group has significant influence, but does not have control over the financial and operating policies. The Financial Statements include the Group's share of the total recognised gains and losses of associates accounted for on an equity accounting basis, from the date that significant influence effectively commences until the date that significant influence effectively ceases. When the Group's share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate. Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

### Net income/loss from security operations

Net income/loss from security operations consists primarily of profit on held for trading securities, profit on held to maturity securities and originated loans and profit on available-for-sale securities.

**Loss/gain on disposals of property, plant and equipment**

Loss/gain on disposals of property, plant and equipment arises when the derecognition of an item of property, plant and equipment occurs and the loss/gain is calculated as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

**Net other operating expenses/income**

Net other operating expenses/income consists primarily of profit/loss from the sale of inventory, fines and penalties for contracting breaching, change in provision for contingencies.

**Profit from operations**

Profit from operations is calculated by subtracting net operating expenses from gross profit.

**Impairment of property, plant and equipment**

The carrying amounts of the Group's property, plant and equipment assets are reviewed annually date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount.

**Negative goodwill**

Where an investment in subsidiary, associate or jointly control entity is made, any excess of the Group's share in the fair value acquired of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition is recognised on the income statement immediately as negative goodwill.

**Profit before financing and taxation**

Profit before financing and taxation is calculated by subtracting net non-operating expenses from profit from operations.

**Interest income**

Interest income consists primarily of interest earned on bank deposits and originated loans.

***Interest expense***

Interest expense consists primarily of interest accrued on the Group's borrowings (including bank borrowings, finance leases and loans from related parties), interest expense on pension liability and expense on tax restructuring, expense on dismantlement provision.

***Profit before income tax***

Profit before income tax is profit before financing and taxation adjusted by interest income, interest expense and foreign exchange difference.

***Income tax expense***

Taxes on income include current income taxes, deferred income taxes and corrections to prior years' current tax charges. Current income taxes include all domestic and foreign income taxes, which are calculated in accordance with the rules established by the taxation authorities in the jurisdictions in which the Group operates. Deferred income taxes reflect the temporary differences between the carrying values of assets and liabilities and their respective tax bases, as well as unused tax loss and tax credit carry-forwards, on which deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which those assets can be utilised. The Group's overall income tax rate varies due to different tax rates in jurisdictions where the Group conducts business, the proportion of income earned in each such jurisdiction and varying tax treatment of costs and expenses.

***Profit from continuing operations***

Profit from continuing operations is profit before income tax less income tax expense.

***Profit from discontinued operations***

Profit from discontinued operations results from the disposal of a separate business for which the related assets, liabilities and operating results can be distinguished operationally and for financial reporting purposes. The results of discontinued operations, net of taxes and the gain or loss on their disposal are presented separate from continuing operations in the income statements.

***Profit for the period***

Profit for the period is calculated by adding profit from discontinued operations to profit from continuing operations.

## RESULTS OF OPERATIONS

### For the three months ended 31 March 2007 (restated) and 2008

The following discussion is based on, and should be read in conjunction with the Interim Financial Statements beginning on page F-3 of this Prospectus.

The following table sets forth the Group's consolidated condensed interim income statement for the three months ended 31 March 2007 (restated) and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 (restated) | 2008 | | |
| | *(US$ millions)* | | | |
| **Sales** | | | | |
| Sales — external | 3,526.0 | 4,144.4 | 618.4 | 17.5% |
| Sales — to related parties | 166.6 | 164.6 | (2.0) | (1.2)% |
| | 3,692.6 | 4,309.0 | 616.4 | 16.7% |
| Cost of sales | (2,531.5) | (3,166.0) | (634.5) | 25.1% |
| **Gross profit** | **1,161.1** | **1,143.0** | **(18.1)** | **(1.6)%** |
| General and administrative expenses | (169.4) | (230.9) | (61.5) | 36.3% |
| Distribution expenses | (233.5) | (275.7) | (42.2) | 18.1% |
| Indirect taxes and contributions | (35.1) | (45.5) | (10.4) | 29.6% |
| Share of associates' profit/(loss) | 2.4 | (0.5) | (2.9) | (120.8)% |
| Net income/(loss) from securities operations | 1.5 | (8.1) | (9.6) | (640.0)% |
| Loss on disposal of property, plant and equipment | (9.2) | (14.5) | (5.3) | 57.6% |
| Net other operating (expenses)/income | (1.2) | 197.3 | 198.5 | — |
| **Profit from operations** | **716.6** | **765.1** | **48.5** | **6.8%** |
| Impairment of property, plant and equipment | (1.0) | (1.9) | (0.9) | 90.0% |
| Negative goodwill, net | 0.6 | 2.2 | 1.6 | 266.7% |
| Net other non-operating expenses | (17.9) | (32.6) | (14.7) | 82.1% |
| **Profit before financing and taxation** | **698.3** | **732.8** | **34.5** | **4.9%** |
| Interest income | 36.8 | 28.9 | (7.9) | (21.5)% |
| Interest expense | (68.4) | (90.9) | (22.5) | 32.9% |
| Foreign exchange difference | (0.1) | 13.9 | 14.0 | — |
| **Profit before income tax** | **666.6** | **684.7** | **18.1** | **2.7%** |
| Income tax expense | (190.3) | (232.7) | (42.4) | 22.3% |
| **Profit from continuing operations** | **476.3** | **452.0** | **(24.3)** | **(5.1)%** |
| Profit from discontinued operations | 4.9 | — | (4.9) | — |
| **Profit for the period** | **481.2** | **452.0** | **(29.2)** | **(6.1)%** |

***Sales***

The Group's consolidated sales increased by US$616.4 million, or 16.7 percent, from US$3,692.6 million for the three months ended 31 March 2007 to US$4,309.0 million for the three months ended 31 March 2008. The increase was primarily due to a US$206.0 million increase in sales of the Mining segment, a US$194.5 million increase in sales of the Russian Steel segment, and a US$135.8 million increase in sales of North America. The increase in sales was partially offset by a US$144.2 million increase in intersegment sales. Other segments also demonstrated an increase in sales compared to the prior period. Changes in the prices of the Group's various products are generally consistent with the prevailing market trends for each such product.

Compared to the three months ended 31 March 2007, the Group's sales to related parties decreased by US$2.0 million, or 1.2 percent, from US$166.6 million in the three months ended 31 March 2007 to US$164.6 million in the three months ended 31 March 2008. See "Related Party Transactions". The decrease in sales to related parties did not have a significant offsetting effect on the overall increase of the Group's sales.

*Sales by product*

The following table sets forth the Group's sales by product for the three months ended 31 March 2007 and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 | 2008 | | |
| | *(US$ millions)* | | | |
| Hot-rolled strip and plate | 950.2 | 968.1 | 17.9 | 1.9% |
| Long products | 774.0 | 924.5 | 150.5 | 19.4% |
| Cold-rolled sheet | 311.3 | 385.5 | 74.2 | 23.8% |
| Galvanised and other metallic coated sheet[1] | 333.7 | 375.6 | 41.9 | 12.6% |
| Semi-finished products | 281.3 | 298.5 | 17.2 | 6.1% |
| Metalware products | 218.6 | 281.1 | 62.5 | 28.6% |
| Shipping and handling costs billed to customers | 156.2 | 192.1 | 35.9 | 23.0% |
| Large-diameter pipes | 63.1 | 160.0 | 96.9 | 153.6% |
| Pellets and iron ore | 68.1 | 125.6 | 57.5 | 84.4% |
| Others tubes and pipes, formed shapes | 88.5 | 102.3 | 13.8 | 15.6% |
| Rails, wheels and axles | 100.7 | 71.1 | (29.6) | (29.4)% |
| Colour coated sheet | 67.1 | 68.1 | 1.0 | 1.5% |
| Scrap | 32.1 | 59.2 | 27.1 | 84.4% |
| Coal and coking coal concentrate | 79.7 | 50.4 | (29.3) | (36.8)% |
| Gold | — | 44.6 | 44.6 | — |
| Others | 168.0 | 202.3 | 34.3 | 20.4% |
| **Sales** | **3,692.6** | **4,309.0** | **616.4** | **16.7%** |

(1) Hereinafter referred to as "**Galvanised sheet**".

*Sales by delivery destination*

The following table sets forth the Group's sales by delivery destination for the three months ended 31 March 2007 and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 | 2008 | | |
| | | (US$ millions) | | |
| Russia | 1,427.0 | 1,820.8 | 393.8 | 27.6% |
| Europe | 1,388.1 | 1,482.7 | 94.6 | 6.8% |
| North America | 535.7 | 620.5 | 84.8 | 15.8% |
| The Middle East | 117.8 | 136.2 | 18.4 | 15.6% |
| South-East Asia | 56.1 | 132.6 | 76.5 | 136.4% |
| Central & South America | 57.8 | 24.6 | (33.2) | (57.4)% |
| China and Central Asia | 87.5 | 82.6 | (4.9) | (5.6)% |
| Africa | 22.6 | 9.0 | (13.6) | (60.2)% |
| **Sales** | **3,692.6** | **4,309.0** | **616.4** | **16.7%** |

*Sales by segment*

The following table sets forth the Group's sales by segment for the three months ended 31 March 2007 and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 | 2008 | | |
| | | (US$ millions) | | |
| Mining segment | 491.8 | 697.8 | 206.0 | 41.9% |
| Russian Steel segment | 1,891.9 | 2,086.4 | 194.5 | 10.3% |
| Lucchini segment | 977.6 | 1,056.8 | 79.2 | 8.1% |
| North America | 455.5 | 591.3 | 135.8 | 29.8% |
| IPM | 63.1 | 160.0 | 96.9 | 153.6% |
| Metalware segment | 224.1 | 272.3 | 48.2 | 21.5% |
| Intersegment transactions | (411.4) | (555.6) | (144.2) | 35.1% |
| **Sales** | **3,692.6** | **4,309.0** | **616.4** | **16.7%** |

*Mining segment*

The Mining segment's sales increased by US$206.0 million, or 41.9 percent, from US$491.8 million in the three months ended 31 March 2007 to US$697.8 million in the three months ended 31 March 2008. Included in these amounts are intersegment sales, primarily to the Russian Steel segment, of US$267.6 million in the three months ended 31 March 2007 and US$363.3 million in the three months ended 31 March 2008. Excluding intersegment sales, sales of the Mining segment increased by US$110.3 million, or 49.0 percent, from US$224.2 million in the three months ended 31 March 2007 to US$334.5 million in the three months ended 31 March 2008. The increase was primarily due to an increase in the average price per tonne, changes in sales by volume as described below and the beginning of gold sales at the end of 2007.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Mining segment by product:

*Pellets and iron ore.* The Mining segment's sales of pellets and iron ore increased by US$57.5 million, or 84.4 percent, from US$68.1 million in the three months ended 31 March 2007 to US$125.6 million in the three months ended 31 March 2008. The increase was primarily due to an increase in the average price per tonne of US$12.2 and an increase in sales by volume of 523.3 thousand tonnes due to a partial redirection of intersegment sales to third parties, an increase of production efficiency, an improvement of transportation logistics and the start of production at a new deposit.

*Coal and coking coal concentrate.* The Mining segment's sales of coal and coking coal concentrate decreased by US$29.3 million, or 36.8 percent, from US$79.7 million in the three months ended 31 March 2007 to US$50.4 million in the three months ended 31 March 2008. This decrease was primarily due to a decrease in sales by volume of 813.4 thousand tonnes due to a decrease in production as a result of more difficult geological conditions, which was partially offset by a US$11.2 increase in the average price per tonne.

*Russian Steel segment*

The Russian Steel segment's sales increased by US$194.5 million, or 10.3 percent, from US$1,891.9 million in the three months ended 31 March 2007 to US$2,086.4 million in the three months ended 31 March 2008. Included in the above amount are intersegment sales of US$190.5 million in the three months ended 31 March 2008 and US$123.4 million in the three months ended 31 March 2007. This increase was primarily due to the market driven increase in the average price per tonne, which was partially offset by a decrease in sales by volume. The decrease in sales by volume was due to partial redirection of domestic Russian sales to export markets which entails a longer shipping process resulting in a delay in the sale of the product.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Russian Steel segment by product:

*Hot-rolled strip and plate.* Sales of hot-rolled strip and plate decreased by US$13.6 million, or 1.9 percent, from US$733.0 million in the three months ended 31 March 2007 to US$719.4 million in the three months ended 31 March 2008. The decrease was primarily due to a decrease in sales by volume of 182.5 thousand tonnes due to an increased volume of hot-rolled sheet being used as feedstock for the increased production of cold-rolled, galvanised, colour-coated sheet and increased supplies to IPM, which was partially offset by an increase in the average price per tonne of US$83.3.

*Cold-rolled sheet.* Sales of cold-rolled sheet increased by US$37.3 million, or 15.9 percent, from US$234.5 million in the three months ended 31 March 2007 to US$271.8 million in the three months ended 31 March 2008. This increase was primarily due to an increase in sales by volume of 24.1 thousand tonnes and an increase in the average price per tonne of US$56.0.

*Galvanised sheet.* Sales of galvanised sheet decreased by US$15.2 million, or 8.4 percent, from US$181.8 million in the three months ended 31 March 2007 to US$166.6 million in the three months ended 31 March 2008. The decrease was primarily due to a decrease in the average price per tonne of US$6.2, which was partially offset by an increase in sales by volume of 15.5 thousand tonnes.

*Semi-finished products.* Sales of semi-finished products increased by US$4.8 million, or 5.0 percent, from US$95.8 million in the three months ended 31 March 2007 to US$100.6 million in the three months ended 31 March 2008. This increase was primarily due to an increase in the average price per tonne of US$93.5, which was partially offset by a decrease in sales by volume of 39.6 thousand tonnes primarily due to increased volumes of semi-finished products being used as feedstock for higher-value added products.

*Colour-coated sheet.* Sales of colour-coated sheet increased by US$1.0 million, or 1.5 percent, from US$67.1 million in the three months ended 31 March 2007 to US$68.1 million in the three months ended 31 March 2008. The increase was primarily due to an increase in sales by volume of 1.0 thousand tonnes, which was partially offset by a decrease in the average price per tonne of US$3.9.

*Lucchini segment*

The Lucchini segment's sales increased by US$79.2 million, or 8.1 percent, from US$977.6 million in the three months ended 31 March 2007 to US$1,056.8 million in the three months ended 31 March 2008, which was mainly driven by higher prices and increased sales by volume caused by increased demand and an increase in production as a result of greater efficiency.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Lucchini segment by product:

*Semi-finished products.* Sales of semi-finished products increased by US$12.5 million, or 6.7 percent, from US$185.5 million in the three months ended 31 March 2007 to US$198.0 million in the three months ended 31 March 2008. The increase was primarily due to an increase in sales by volume of 73.6 thousand tonnes due to the factors discussed above, partially offset by a decrease in the average price per tonne of US$ 119.4.

*Rails, wheels and axles.* Sales of rails, wheels and axles decreased by US$29.6 million, or 29.4 percent, from US$100.7 million in the three months ended 31 March 2007 to US$71.1 million in the three months ended 31 March 2008. This decrease was primarily due to a decrease in the average price per tonne of US$218.5 and a decrease in sales by volume of 11.0 thousand tonnes. The decrease in sales by volume was primarily caused by the disposal of Sidermeccanica in June 2007.

*Long products.* Sales of long products increased by US$88.9 million, or 15.1 percent, from US$588.6 million in the three months ended 31 March 2007 to US$677.5 million in the three months ended 31 March 2008. This increase was primarily due to an increase in the average price per tonne of US$122.9 and an increase in sales by volume of 16.6 thousand tonnes due to the factors discussed above.

*North America*

North America's sales increased by US$135.8 million, or 29.8 percent, from US$455.5 million in the three months ended 31 March 2007 to US$591.3 million in the three months ended 31 March 2008. The increase was primarily due to the commencement of the operations at SeverCorr, which did not operate in the three months ended 31 March 2007, which was partially offset by the decrease in production levels at Severstal North America, which resulted from the blast furnace accident in January 2008.

Set forth below is a discussion of the sales, excluding intersegment sales, of North America by product:

*Hot-rolled strip and plate.* North America's sales of hot-rolled strip and plate increased by US$31.6 million, or 14.6 percent, from US$217.1 million in the three months ended 31 March 2007 to US$248.7 million in the three months ended 31 March 2008. The increase was primarily due to an increase in the average price per tonne of US$35.7 and an increase in sales by volume of 29.4 thousand tonnes due to the commencement of operations at SeverCorr.

*Cold-rolled sheet.* North America's sales of cold-rolled sheet increased by US$36.9 million, or 48.0 percent, from US$76.8 million in the three months ended 31 March 2007 to US$113.7 million in the three months ended 31 March 2008. The increase was primarily due to an increase in sales by volume of 55.8 thousand tonnes due to the commencement of operations at SeverCorr, which was partially by a decrease in the average price per tonne of US$22.5.

*Galvanised sheet.* North America's sales of galvanised sheet increased by US$57.0 million, or 37.5 percent, from US$151.9 million in the three months ended 31 March 2007 to US$208.9 million in the three months ended 31 March 2008. The increase was primarily due to an increase in sales by volume of 68.2 thousand tonnes due to the commencement of operations at SeverCorr, which was partially offset by decrease in the average price per tonne of US$10.4.

*IPM*

IPM's sales increased by US$96.9 million, or 153.6 percent, from US$63.1 million in the three months ended 31 March 2007 to US$160.0 million in the three months ended 31 March 2008. The increase was primarily due to an increase in the average price per tonne of US$458.5 and to an increase in sales by volume of 38.4 thousand tonnes. The increase in sales by volume was due to IPM operating at a higher capacity in the three months ended 31 March 2008 than for the three months ended 31 March 2007.

*Metalware segment*

The Metalware segment's sales increased by US$48.2 million, or 21.5 percent, from US$224.1 million in the three months ended 31 March 2007 to US$272.3 million in the three months ended 31 March 2008.

Included in the above amounts are intersegment sales in the amount of US$1.4 million and US$1.7 million during the three months ended 31 March 2007 and 2008, respectively. The increase was primarily due to an increase in the average price per tonne of US$231.6, which was partially offset by the decrease in sales by volume of 7.1 thousand tonnes due to a shift in production from high volumes of low-margin products to lower volumes of high-margin products.

***Cost of sales***

The Group's cost of sales increased by US$634.5 million, or 25.1 percent, from US$2,531.5 million in the three months ended 31 March 2007 to US$3,166.0 million in the three months ended 31 March 2008. This increase was primarily due to a US$298.5 million increase in cost of sales of the Russian Steel segment, a US$222.1 million increase in Severstal North America's cost of sales and a US$134.4 million increase in the Mining segment's cost of sales offset by US$167.9 million in intersegment transactions.

*Cost of sales by segment*

The following table sets forth the Group's cost of sales by segment for the three months ended 31 March 2007 and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 | 2008 | | |
| | *(US$ millions)* | | | |
| Mining segment | (301.3) | (435.7) | (134.4) | 44.6% |
| Russian Steel segment | (1,143.8) | (1,442.3) | (298.5) | 26.1% |
| Lucchini segment | (798.6) | (864.4) | (65.8) | 8.2% |
| North America | (422.0) | (644.1) | (222.1) | 52.6% |
| IPM | (55.0) | (110.7) | (55.7) | 101.3% |
| Metalware segment | (197.7) | (223.6) | (25.9) | 13.1% |
| Intersegment transactions | 386.9 | 554.8 | 167.9 | 43.4% |
| **Cost of sales** | **(2,531.5)** | **(3,166.0)** | **(634.5)** | **25.1%** |

*Mining segment*

The Mining segment's cost of sales increased by US$134.4 million, or 44.6 percent, from US$301.3 million in the three months ended 31 March 2007 to US$435.7 million in the three months ended 31 March 2008. This increase was primarily due to a US$65.7 million increase in raw materials expense, contributed to by a US$23.6 million increase in fuel and energy expenses and a US$29.5 million increase in labour costs generally consistent with wage inflation in Russia during the period.

*Raw materials expense.* The increase in raw materials expense was mainly due to the Group's acquisition in July 2007 of scrap metal businesses. The acquisitions of these businesses increased in use of raw materials, which resulted in an increase in raw materials expense.

*Fuel and energy expense.* The increase in fuel and energy expenses was primarily due to an increase in the volume of production of iron ore and its related increase in energy consumption and market-driven increases in energy tariffs and fuel prices.

*Labour and related tax expense.* The increase in labour and related tax expense was primarily due to the increase in the average salaries of employees, while the average number of employees did not change significantly compared with the three months ended 31 March 2007.

*Russian Steel segment*

The Russian Steel segment's cost of sales increased by US$298.5 million, or 26.1 percent, from US$1,143.8 million in the three months ended 31 March 2007 to US$1,442.3 million in the three months ended 31 March 2008. The increase was primarily due to a US$205.4 million increase in raw materials expense, a US$42.8 million increase in fuel and energy costs and a US$20.9 million increase in labour costs.

*Raw materials expense.* The increase in raw materials expense was mainly due to an increase in prices for pellets, coking coal and scrap metal, all of which are feedstock used by the Russian Steel segment.

*Fuel and energy expense.* The increase in fuel and energy expenses was mainly due to an increase in energy tariffs and fuel prices.

*Labour and related tax expense.* The increase in labour costs was primarily due to the increase in the average salaries of employees. The average number of employees did not change significantly.

*Lucchini segment*

The Lucchini segment's cost of sales increased by US$65.8 million, or 8.2 percent, from US$798.6 million in the three months ended 31 March 2007 to US$864.4 million in the three months ended 31 March 2008.

The increase in cost of sales was generally consistent with the increase in sales by volume. The structure of costs did not change significantly in the three months ended 31 March 2008, from the three months ended 31 March 2007.

*Raw materials expense.* The increase in the prices of raw materials and fuel and energy was consistent with overall inflation in the region of operations and thus contributed to the increase of cost of sales.

*North America*

North America's cost of sales increased by US$222.1 million, or 52.6 percent, from US$422.0 million in the three months ended 31 March 2007 to US$644.1 million in the three months ended 31 March 2008.

The increase in cost of sales was primarily attributable to the commencement of operations at SeverCorr, which did not operate in the three months ended 31 March 2007 and a corresponding increase in the sales by volume. Additional increases in cost of sales were primarily due to an increase in prices for raw materials, fuel and energy and to a higher than normal consumption of coal and coking coal concentrate during the first months of operation of blast furnace "C" after the reconstruction.

*IPM*

IPM's cost of sales increased by US$55.7 million, or 101.3 percent, from US$55.0 million in the three months ended 31 March 2007 to US$110.7 million in the three months ended 31 March 2008. The increase was driven by the increase in sales by volume, as discussed above, which resulted in increases in raw materials expenses and labour costs.

*Raw materials expense.* The increase in raw materials expense was mainly due to an increase in the volume of production of pipes and a corresponding increase in the sales by volume. The volume of production in the three months ended 31 March 2008 was double the volume in the three months ended 31 March 2007, when IPM was operating at a lower capacity.

*Labour and related taxes expense.* The increase in labour and related taxes expense was due to the increase both in the average salary and the average number of employees required to support the increased levels of production.

*Metalware segment*

The Metalware segment's cost of sales increased by US$25.9 million, or 13.1 percent, from US$197.7 million in the three months ended 31 March 2007 to US$223.6 million in the three months ended 31 March 2008. This increase was primarily due to a significant increase in prices for long products in the three months ended 31 March 2008, which are the primary type of raw material used in production of metalware.

***Profit from operations***

Compared to the prior period, the Group's profit from operations increased by US$48.5 million, or 6.8 percent, from US$716.6 million in the three months ended 31 March 2007 to US$765.1 million in the three months ended 31 March 2008. The increase was due to a US$66.6 million decrease in net operating expenses partially offset by a US$18.1 million decrease in gross profit.

The decrease in gross profit was primarily due to the factors discussed above. The decrease in net operating expenses was primarily due to a US$198.5 million decrease in net other operating expenses, representing mainly the one-off effect of the US$177.0 million contract termination payment received by the Group from one of its electricity suppliers, which was recognised by the Group as a net operating gain. Excluding the one-off effect of this net operating gain, the Group's operating expenses increased in the three months ended 31 March 2008 compared to the three months ended 2007.

The following table sets forth the Group's net operating expenses for the three months ended 31 March 2007 and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 | 2008 | | |
| | (US $millions) | | | |
| General and administrative expenses | (169.4) | (230.9) | (61.5) | 36.3% |
| Distribution expenses | (233.5) | (275.7) | (42.2) | 18.1% |
| Indirect taxes and contributions | (35.1) | (45.5) | (10.4) | 29.6% |
| Share of associates' profits/(losses) | 2.4 | (0.5) | (2.9) | (120.8)% |
| Net income/(loss) from securities operations | 1.5 | (8.1) | (9.6) | (640.0)% |
| Loss on disposal of property, plant and equipment | (9.2) | (14.5) | (5.3) | 57.6% |
| Net other operating (expenses)/income | (1.2) | 197.3 | 198.5 | — |
| **Net operating expenses** | **(444.5)** | **(377.9)** | **66.6** | **(15.0)%** |

*Mining segment*

The Mining segment's profit from operations increased by US$54.1 million, or 57.9 percent, from US$93.5 million in the three months ended 31 March 2007 to US$147.6 million, in the three months ended 31 March 2008. The increase in profit from operations was due to a US$71.6 million increase in gross profit, primarily as a result of the factors described above and was offset by a US$17.5 million increase in net operating expenses.

The increase in the Mining segment's net operating expenses was primarily due to a US$5.8 million increase in general and administrative expenses and US$14.0 million increase in distribution expenses, which was partially offset by US$5.3 million decrease in loss on disposal of property, plant and equipment.

The increase in general and administrative expenses was primarily due to an increase in the average salaries of employees and costs of labour safety improvement programmes. The increase in distribution costs was primarily due to the increase in railway tariffs and transportation expenses in the three months ended 31 March 2008 compared to the three months ended 31 March 2007. The decrease in loss on disposal of property, plant and equipment was primarily due to the disposal of assets in the ordinary course of business.

*Russian Steel segment*

The Russian Steel segment's profit from operations decreased by US$171.2 million, or 32.0 percent, from US$514.5 million in the three months ended 31 March 2007 to US$343.3 million in the three months ended 31 March 2008. The decrease in profit from operations was due to a US$104.0 million decrease in gross profit, primarily as a result of factors described above and a US$67.2 million increase in net operating expenses.

The increase in the Russian Steel segment's net operating expenses was primarily due to a US$42.2 million increase in general and administrative expenses, a US$13.5 million increase in distribution expenses primarily driven by the increase in railway tariffs and a US$7.2 million increase in indirect taxes and contributions primarily due to an increase in property taxes.

The increase in general and administrative expenses was primarily due to an increase in expenses for payments to third-party consultants and the increase in performance bonuses paid to staff. Performance bonuses included bonuses paid to management and administrative employees of the Group's Corporate Center, who are the employees of the Company.

*Lucchini segment*

The Lucchini segment's profit from operations increased by US$1.7 million, or 1.7 percent, from US$97.7 million in the three months ended 31 March 2007 to US$99.4 million in the three months ended 31 March 2008. This increase was due to a US$13.4 million increase in gross profit, as discussed above, which was partially offset by a US$11.7 million increase in net operating expenses.

The Lucchini segment's net operating expenses increased by US$11.7 million, or 14.4 percent, from US$81.3 million in the three months ended 31 March 2007 to US$93.0 million in the three months ended 31 March 2008. This increase was primarily due to a US$3.6 million increase in distribution expenses and a US$6.3 million increase in general and administrative expenses.

*North America*

Compared to the prior period, North America's profit from operations increased by US$87.8 million, or 373.6 percent, in the three months ended 31 March 2008. The increase was due to a US$174.1 million decrease in net operating expenses, partially offset by a US$86.3 million decrease in gross profit. The decrease in gross profit was a result of the factors described above.

The decrease in net operating expenses was primarily due to a US$197.7 million decrease in net other operating expenses, which primarily consisted of the gain from the termination of a long-term-electricity-supply contract and related compensation received by North America. This was partially offset by a US$10.6 million increase in general and administrative expenses primarily attributable to the commencement of operations at SeverCorr, a US$3.9 million decrease in share of associates' profits and a US$7.2 million increase in loss on disposal of property, plant and equipment due to the blast furnace "B" accident.

*IPM*

IPM's profit from operations increased by US$30.6 million, or 746.3 percent, from US$4.1 million in the three months ended 31 March 2007 to US$34.7 million in the three months ended 31 March 2008. The increase was due to a US$41.2 million increase in gross profit, as discussed above, which was partially offset by a US$10.6 million increase in net operating expenses.

IPM's net operating expenses increased by US$10.6 million, or 265.0 percent, from US$4.0 million in the three months ended 31 March 2007 to US$14.6 million in the three months ended 31 March 2008. This increase was primarily due to a US$9.3 million increase in distribution expenses and a US$1.6 million increase in general and administrative expenses, which was consistent with the significant increase in the volume of production and related increase in the sales by volume in the three months ended 31 March 2008 in comparison with the three months ended 31 March 2007.

*Metalware segment*

The Metalware segment's profit from operations increased by US$20.8 million, or 315.2 percent, from US$6.6 million in the three months ended 31 March 2007 to US$27.4 million in the three months ended 31 March 2008. This increase was due to a US$22.3 million increase in gross profit, as discussed above, which was partially offset by a US$1.5 million increase in operating expenses.

The Metalware segment's operating expenses increased by US$1.5 million, or 6.5 percent, from US$19.8 million in the three months ended 31 March 2007 to US$21.3 million in the three months ended 31 March 2008. The increase was primarily due to a US$2.6 million increase in general and administrative expenses, which resulted from an increase in labour costs due to the increase in the average salaries of employees.

***Profit before financing and taxation***

Compared to the prior period, the Group's profit before financing and taxation increased by US$34.5 million, or 4.9 percent, from US$698.3 million in the three months ended 31 March 2007 to US$732.8 million in the three months ended 31 March 2008. This increase was due to a US$48.5 million increase in profit from operations, as described above, partially offset by a US$14.0 million increase in net non-operating expenses.

The increase in net non-operating expenses of US$14.0 million was primarily due to a US$14.7 million increase in net other non-operating expenses and a US$0.9 million increase in net impairment of property, plant and equipment, which was partially offset by an increase of US$1.6 million in negative goodwill.

The following table sets forth the Group's net non-operating expenses for the three months ended 31 March 2007 and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 | 2008 | | |
| | *(US$ millions)* | | | |
| Impairment of property, plant and equipment | (1.0) | (1.9) | (0.9) | 90.0% |
| Negative goodwill, net | 0.6 | 2.2 | 1.6 | 266.7% |
| Net other non-operating expenses | (17.9) | (32.6) | (14.7) | 82.1% |
| **Net non-operating expenses** | **(18.3)** | **(32.3)** | **(14.0)** | **76.5%** |

*Negative goodwill*

Negative goodwill for the three months ended 31 March 2008 represents the excess of share in net assets of subsidiaries acquired over the purchase consideration in relation to an acquisition by the Mining segment.

*Net other non-operating expenses*

The increase in net other non-operating expenses was primarily due to a US$7.8 million increase in charitable donations, a US$2.6 million increase in social expenditures and a US$3.6 million increase in net loss on a disposal of subsidiaries.

***Profit for the period***

The increase in profit before financing and taxation was primarily due to the factors described above. Compared to the prior period, however, the Group's profit for the period decreased by US$29.2 million, or 6.1 percent, from US$481.2 million in the three months ended 31 March 2007 to US$452.0 million in the three months ended 31 March 2008. The decrease was primarily due to a US$16.4 million increase in net financing expense and a US$42.4 million increase in income tax expense.

*Net financing expense*

Net financing expense comprises interest income, interest expense, including amortisation of transaction costs, and foreign exchange gains or losses. Net financing expense increased by US$16.4 million, from US$31.7 million in the three months ended 31 March 2007 to US$48.1 million in the three months ended 31 March 2008. The increase was primarily due to a US$22.5 million increase in interest expense, from US$68.4 million in the three months ended 31 March 2007 to US$90.9 million in the three months ended 31 March 2008, a US$7.9 million decrease in interest income, which was offset by a US$14.0 million increase in net foreign exchange difference.

The decrease in interest income was primarily due to lower average cash and short-term deposits during the three months ended 31 March 2008 compared to the three months ended 31 March 2007 due to the use of cash resources for investment purposes.

The increase in interest expense was primarily due to new borrowings, including the EBRD syndicated facility for €600 million of which €200 million had been drawn as at 31 March 2008.

*Income tax expense*

Income tax expense increased by US$42.4 million, or 22.3 percent, from US$190.3 million in the three months ended 31 March 2007 to US$232.7 million in the three months ended 31 March 2008. The increase was due to the US$18.1 million increase in profit before income tax and the increase in effective interest tax rate from 28.5 percent to 34.0 percent. A substantial portion of the Group's profit before income tax was generated within Russia and was subject to a flat 24 percent statutory income tax rate. Segments operating in Western Europe and the United States are subject to the local federal and state income taxes, which generally resulted in an effective income tax rate above 30 percent of profit before income tax.

The increase in the effective tax rate was mainly due to losses at SeverCorr and some other entities of the Group amounting to US$71.0 million because the related deferred tax asset was not recognised. The increase was also due to increased profits before taxes of non-Russian entities of the Group, which were taxed at a higher rate and the one-time effect of the termination payment received by the Group with respect to a of a long-term electricity supply contract, resulting in a taxable gain of US$177.0 million, which was taxed at a rate of 35 percent. However, if these non-recurring items were ignored, the effective tax rate did not change significantly.

**For the years ended 31 December 2006 (restated) and 2007**

The following discussion is based on, and should be read in conjunction with, the Group's Annual Financial Statements, included in this Prospectus beginning on page F-15.

The following table sets forth the Group's consolidated income statement for the years ended 2006 (restated) and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 (restated) | 2007 | | |
| | | *(US$ millions)* | | |
| **Sales** | | | | |
| Sales — external | 11,723.3 | 14,543.0 | 2,819.7 | 24.1% |
| Sales — to related parties | 725.7 | 701.9 | (23.8) | (3.3)% |
| | 12,449.0 | 15,244.9 | 2,795.9 | 22.5% |
| Cost of sales | (8,601.2) | (10,541.6) | (1,940.4) | 22.6% |
| **Gross profit** | **3,847.8** | **4,703.3** | **855.5** | **22.2%** |
| General and administrative expenses | (655.0) | (691.2) | (36.2) | 5.5% |
| Distribution expenses | (697.3) | (909.5) | (212.2) | 30.4% |
| Indirect taxes and contributions | (142.1) | (153.6) | (11.5) | 8.1% |
| Share of associates' loss | (1.2) | (89.4) | (88.2) | — |
| Net income from securities operations | 28.3 | 25.6 | (2.7) | (9.5)% |
| Loss on disposal of property, plant and equipment | (39.3) | (35.3) | 4.0 | (10.2)% |
| Net other operating expenses | (27.1) | (7.5) | 19.6 | (72.3)% |
| **Profit from operations** | **2,314.1** | **2,842.4** | **528.3** | **22.8%** |
| Impairment of property, plant and equipment | (57.7) | (29.1) | 28.6 | (49.6)% |
| Net gain on restructuring of tax liabilities | 14.7 | — | (14.7) | — |
| Negative goodwill, net | 4.2 | 12.2 | 8.0 | 190.5% |
| Net other non-operating expenses | (53.6) | (58.6) | (5.0) | 9.3% |
| **Profit before financing and taxation** | **2,221.7** | **2,766.9** | **545.2** | **24.5%** |
| Interest income | 102.4 | 172.9 | 70.5 | 68.8% |
| Interest expense | (245.0) | (288.2) | (43.2) | 17.6% |
| Foreign exchange difference | 33.3 | 2.9 | (30.4) | (91.3)% |
| **Profit before income tax** | **2,112.4** | **2,654.5** | **542.1** | **25.7%** |
| Income tax expense | (635.3) | (681.3) | (46.0) | 7.2% |
| **Profit from continuing operations** | 1,477.1 | 1,973.2 | 496.1 | 33.6% |
| Profit from discontinued operations | 32.9 | 0.4 | (32.5) | (98.8)% |
| **Profit for the year** | **1,510.0** | **1,973.6** | 463.6 | 30.7% |

***Sales***

Compared to the prior year, the Group's consolidated sales increased by US$2,795.9 million, or 22.5 percent, from US$12,449.0 million in 2006 to US$15,244.9 million in 2007. This increase was primarily due to a US$1,651.5 million increase in sales of the Russian Steel segment, a US$705.9 million increase in sales of the Mining segment and a US$399.0 million increase in sales of the Lucchini segment. Changes in the prices of the Group's various products are generally consistent with the prevailing market trends for each such product.

The Group's sales to related parties decreased by US$23.8 million, from US$725.7 million in 2006 to US$701.9 million in 2007. The Group's sales to related parties comprised 5.8 percent and 4.6 percent of the Group's total sales in 2006 and 2007, respectively.

*Sales by product*

The following table sets forth the Group's sales by product for the years ended 31 December 2006 and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 | 2007 | | |
| | | *(US$ millions)* | | |
| Hot-rolled strip and plate | 3,435.5 | 3,681.6 | 246.1 | 7.2% |
| Long products | 2,301.6 | 3,097.9 | 796.3 | 34.6% |
| Galvanised and other metallic coated sheet | 1,105.5 | 1,307.3 | 201.8 | 18.3% |
| Cold-rolled sheet | 1,328.1 | 1,258.6 | (69.5) | (5.2)% |
| Semi-finished products | 939.4 | 1,101.9 | 162.5 | 17.3% |
| Metalware products | 833.9 | 1,002.2 | 168.3 | 20.2% |
| Shipping and handling costs billed to customers | 537.4 | 644.0 | 106.6 | 19.8% |
| Large-diameter pipes | — | 530.7 | 530.7 | — |
| Others tubes and pipes, formed shapes | 320.4 | 391.7 | 71.3 | 22.3% |
| Rails, wheels and axles | 375.3 | 321.8 | (53.5) | (14.3)% |
| Pellets and iron ore | 242.7 | 304.8 | 62.1 | 25.6% |
| Scrap | 26.5 | 301.5 | 275.0 | 1,037.7% |
| Colour coated sheet | 148.5 | 281.1 | 132.6 | 89.3% |
| Coal and coking coal concentrate | 249.3 | 264.8 | 15.5 | 6.2% |
| Others | 604.9 | 755.0 | 150.1 | 24.8% |
| **Sales** | **12,449.0** | **15,244.9** | **2,795.9** | **22.5%** |

*Sales by delivery destination*

The following table sets forth the Group's consolidated sales by delivery destination for the years ended 31 December 2006 and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 | 2007 | | |
| | | *(US $millions)* | | |
| Russia | 4,912.6 | 6,744.1 | 1,831.5 | 37.3% |
| Europe | 4,390.8 | 5,308.7 | 917.9 | 20.9% |
| North America | 2,406.1 | 1,889.3 | (516.8) | (21.5)% |
| The Middle East | 215.1 | 450.4 | 235.3 | 109.4% |
| China and Central Asia | 138.0 | 353.6 | 215.6 | 156.2% |
| South-East Asia | 143.6 | 291.1 | 147.5 | 102.7% |
| Central & South America | 156.7 | 151.3 | (5.4) | (3.4)% |
| Africa | 86.1 | 56.4 | (29.7) | (34.5)% |
| **Sales** | **12,449.0** | **15,244.9** | **2,795.9** | **22.5%** |

*Sales by segment*

The following table sets forth the Group's sales by segment for the years ended 31 December 2006 and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 | 2007 | | |
| | | (US $millions) | | |
| Mining segment | 1,491.0 | 2,196.9 | 705.9 | 47.3% |
| Russian Steel segment | 6,317.5 | 7,969.0 | 1,651.5 | 26.1% |
| Lucchini segment | 3,357.5 | 3,756.5 | 399.0 | 11.9% |
| Severstal North America | 1,868.4 | 1,691.9 | (176.5) | (9.4)% |
| IPM | — | 550.7 | 550.7 | — |
| Metalware segment | 838.9 | 1,011.7 | 172.8 | 20.6% |
| Intersegment transactions | (1,424.3) | (1,931.8) | (507.5) | 35.6% |
| **Sales** | **12,449.0** | **15,244.9** | **2,795.9** | **22.5%** |

*Mining segment*

The Mining segment's sales increased by US$705.9 million, or 47.3 percent, from US$1,491.0 million in 2006 to US$2,196.9 million in 2007. Included in these amounts are intersegment sales, primarily to the Russian Steel segment, of US$853.0 million in 2006 and US$1,142.7 million in 2007. Excluding intersegment sales, sales of the Mining segment increased by US$416.2 million, or 65.2 percent, from US$638.0 million in 2006 to US$1,054.2 million in 2007. The increase was primarily due to increases in the average price per tonne and by an increase in sales by volume as described below.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Mining segment by product:

*Pellets and iron ore.* The Mining segment's sales of pellets and iron ore increased by US$62.1 million, or 25.6 percent, from US$242.7 million in 2006 to US$304.8 million in 2007. The increase was primarily due to an increase in the average price per tonne of US$8.2 and an increase in sales by volume of 431.5 thousand tonnes primarily due to the start of production at a new deposit.

*Coal and coking coal concentrate.* The Mining segment's sales of coal and coking coal concentrate increased by US$15.5 million, or 6.2 percent, from US$249.3 million in 2006 to US$264.8 million in 2007. The increase was primarily due to an increase in sales by volume of 60.8 thousand tonnes primarily due to commencement of mining production in the Kuzbass area and to a US$2.4 increase in the average price per tonne.

*Russian Steel segment*

The Russian Steel segment's sales increased by US$1,651.5 million, or 26.1 percent, from US$6,317.5 million in 2006 to US$7,969.0 million in 2007. The increase was primarily due to increases in average prices and to an increase in sales by volume due to the increased efficiency of the steel converter operations. Included in the above amounts are intersegment sales of US$647.9 million in 2007 and US$392.7 million in 2006.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Russian Steel segment by product:

*Hot-rolled strip and plate.* Sales of hot-rolled strip and plate increased by US$446.8 million, or 17.6 percent, from US$2,539.5 million in 2006 to US$2,968.3 million in 2007. The increase was primarily due to an increase in the average price per tonne of US$70.1 and by an increase in sales by volume of 174.0 thousand tonnes due to more favourable pricing conditions for hot-rolled strip and plate.

*Cold-rolled sheet.* Sales of cold-rolled sheet increased by US$26.9 million, or 2.9 percent, from US$917.8 million in 2006 to US$944.7 million in 2007. The increase was primarily due to an increase in the average price per tonne of US$81.6, partially offset by a decrease in sales by volume of 152 thousand tonnes due to increased volumes of cold-rolled sheet being used as feedstock for galvanised sheet production and due to decreased availability of hot-rolled and semi-finished feedstock.

*Galvanised sheet.* Sales of galvanised sheet increased by US$112.9 million, or 19.5 percent, from US$577.8 million in 2006 to US$690.7 million in 2007. The increase was primarily due to increase in the average price per tonne of US$87.8 and by an increase in sales by volume of 56.4 thousand tonnes primarily due to increased production at Severgal.

*Semi-finished products.* Sales of semi-finished products increased by US$184.7 million, or 95.2 percent, from US$194.1 million in 2006 to US$378.8 million in 2007. The increase was primarily due to an increase in the average price per tonne of US$93.6 and by an increase in sales by volume of 303.8 thousand tonnes due to more favourable pricing conditions for semi-finished products.

*Lucchini segment*

The Lucchini segment's sales increased by US$399.0 million, or 11.9 percent, from US$3,357.5 million in 2006 to US$3,756.5 million in 2007.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Lucchini segment by product:

*Semi-finished products.* Sales of semi-finished products decreased by US$22.1 million, or 3.0 percent, from US$745.2 million in 2006 to US$723.1 million in 2007. The decrease was primarily due to a decrease in the average price per tonne of US$354.4, which was partially offset by an increase in sales by volume of 378.1 thousand tonnes primarily due to decreased intersegment sales and increased sales of slabs to third party customers.

*Rails, wheels and axles.* Sales of rails, wheel and axles decreased by US$53.6 million, or 14.3 percent, from US$375.3 million in 2006 to US$321.7 million in 2007. The decrease was primarily due to a decrease in volume by 55 thousand tonnes due to the disposal of Sidermeccanica, partially offset by an increase in the average price per tonne of US$8.3.

*Long products.* Sales of long products increased by US$460.0 million, or 26.5 percent, from US$1,735.6 million in 2006 to US$2,195.6 million in 2007. The increase was primarily due to an increase in the average price per tonne of US$250.5, partially offset by a decrease in sales by volume of 87.7 thousand tonnes due to the increase sales of semi-finished products which are normally used as feedstock for long products.

*Severstal North America*

Severstal North America's sales decreased by US$176.5 million, or 9.4 percent, from US$1,868.4 million in 2006 to US$1,691.9 million in 2007. The decrease in the volume of production and related decrease in the sales by volume was primarily due to modernisation, repairs and maintenance works performed at a blast furnace during 2007, which caused a temporary outage of the furnace. The temporary outage resulted in decreased production which led to a decrease of US$182.8 million in sales of hot-rolled strip and plate, and a decrease of US$96.4 million in sales of cold-rolled sheet but was partially offset by a US$88.9 million increase in sales of galvanised sheet.

Set forth below is a discussion of the sales, excluding intersegment sales, of Severstal North America by product:

*Hot-rolled strip and plate.* Severstal North America's sales of hot-rolled strip and plate decreased by US$182.8 million, or 20.4 percent, from US$896.1 million in 2006 to US$713.3 million in 2007. This decrease was primarily due to a decrease in sales by volume of 245.9 tonnes due to the factors discussed above, and a decrease in the average price per tonne of US$23.8.

*Cold-rolled sheet.* Severstal North America's sales of cold-rolled sheet decreased by US$96.4 million, or 23.5 percent, from US$410.3 million in 2006 to US$313.9 million in 2007. This decrease was primarily due to a decrease in sales by volume of 146.1 tonnes due to the factors discussed above, which was partially offset by an increase in the average price per tonne of US$15.4.

*Galvanised sheet.* Severstal North America's sales of galvanised sheet increased by US$88.9 million, or 16.8 percent, from US$527.7 million in 2006 to US$616.6 million in 2007. This increase was primarily due to an increase in sales by volume of 69.1 tonnes, or 10.7 percent, and by an increase in the average price per tonne of US$45.2.

*IPM*

IPM's sales in 2007 were US$550.7 million. IPM did not produce or sell any large-diameter pipes in 2006.

*Metalware segment*

The Metalware segment's sales increased by US$172.8 million, or 20.6 percent, from US$838.9 million in 2006 to US$1,011.7 million in 2007. Included in the above amounts are intersegment sales of US$9.1 million in 2006 and US$9.7 million in 2007. The increase was primarily due to the increase in the average price per tonne of US$197.7, which was partially offset by a decrease in sales by volume of 45.3 thousand tonnes due to a shift in production to lower volumes of higher-value added products.

***Cost of sales***

The Group's cost of sales increased by US$1,940.4 million, or 22.6 percent, from US$8,601.2 million in 2006 to US$10,541.6 million in 2007.

*Cost of sales by segment*

The following table sets forth the Group's cost of sales by segment for the years ended 31 December 2006 and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 | 2007 | | |
| | | *(US$ millions)* | | |
| Mining segment | (965.8) | (1,497.5) | (531.7) | 55.1% |
| Russian Steel segment | (3,804.8) | (4,837.3) | (1,032.5) | 27.1% |
| Lucchini segment | (2,807.2) | (3,194.4) | (387.2) | 13.8% |
| Severstal North America | (1,711.9) | (1,664.1) | 47.8 | (2.8)% |
| IPM | — | (379.8) | (379.8) | — |
| Metalware segment | (736.6) | (871.8) | (135.2) | 18.4% |
| Intersegment transactions | 1,425.1 | 1,903.3 | 478.2 | 33.6% |
| **Cost of Sales** | **(8,601.2)** | **(10,541.6)** | **(1,940.4)** | **22.6%** |

*Mining segment*

The Mining segment's cost of sales increased by US$531.7 million, or 55.1 percent, from US$965.8 million in 2006 to US$1,497.5 million in 2007. The increase was primarily due to an increase in raw materials expenses, an increase in cost of services rendered by contractors and an increase in labour costs.

*Raw materials expense.* The increase in raw materials expense was mainly due to the Group's acquisition of scrap metal businesses in January 2007. The acquisitions of these businesses increased the use of raw materials, which resulted in an increase in raw materials expense.

*Cost of services.* The increase in cost of services was primarily due to the cost of remedial action following accident at the Komsomolskaya mine (see "Business — Severstal Resources") and an overall increase of the fees charge by contractors.

*Labour and related tax expense.* The increase in labour and related tax expense was primarily due to the increase in the average salaries of employees, partially offset by the decrease in the average number of employees.

*Russian Steel segment*

The Russian Steel segment cost of sales increased by US$1,032.5 million, or 27.1 percent, from US$3,804.8 million in 2006 to US$4,837.3 million in 2007. The increase was primarily due to an increase in raw materials expense, an increase in labour costs, an increase in energy costs and the appreciation of the Rouble, the functional currency of major entities in the Russian Steel segment, against the US dollar, the Group's reporting currency.

*Raw materials.* The increases in prices and the increase in consumption of coal and coking coal concentrate and pellets and iron ore led to an increase in raw materials expense.

*Labour and related taxes expense.* The increase in labour and related taxes expense was primarily due to the increase in the average salaries and a slight increase in the number of employees.

*Lucchini segment*

The Lucchini segment's cost of sales increased by US$387.2 million, or 13.8 percent, from US$2,807.2 million in 2006 to US$3,194.4 million in 2007.

The increase in the cost of sales was mainly due to the increase in prices of raw materials and the appreciation of the euro, the functional currency of the Lucchini segment entities, against the US dollar, the Group's reporting currency. The increase was partially offset by a slight decrease in sales by volume.

*Severstal North America*

Severstal North America's cost of sales decreased by US$47.8 million, from US$1,711.9 million in 2006 to US$1,664.1 million in 2007. This decrease was primarily due to a decrease in sales by volume, which was partially offset by an increase in cost of services due to the repair and maintenance works performed at a blast furnace and a higher than normal consumption of coal and coking coal concentrate during the first months of operation of blast furnace "C".

*IPM*

IPM became a separate segment effective 1 January 2007 from the Russian Steel segment and it commenced commercial operations in early 2007. IPM's cost of sales for 2007 was US$379.8 million, which was primarily due to the start of operations.

Cost of sales for 2007 primarily comprised raw materials expense, which amounted to US$296.1 million. Labour costs and related taxes amounted to US$17.9 million and depreciation and amortisation expenses amounted to US$22.8 million.

*Metalware segment*

The Metalware segment's cost of sales increased by US$135.2 million or by 18.4 percent, from US$736.6 million during 2006 to US$871.8 million during 2007. The increase was primarily due to an increase in raw materials expense by US$95.1 million, an increase in fuel and energy expense by US$13.5 million and an increase in labour costs by US$17.6 million.

*Raw materials expense.* The increase in raw materials expense was primarily due to the increase in prices for long products, which is the primary feedstock for the production of metalware products.

*Fuel and energy expense.* The increase in fuel and energy expense was primarily due to the increase in energy tariffs and an increase in fuel prices.

*Labour and tax related expense.* The increase in labour costs was due to the increase in the average salaries of employees, which was partially offset by the reduction in the number of employees due to the implementation of optimisation and modernisation programmes at the Metalware segment's facilities.

***Profit from operations***

The Group's profit from operations increased by US$528.3 million, or 22.8 percent, from US$2,314.1 million in 2006 to US$2,842.4 million in 2007. The increase was due to a US$855.5 million increase in gross profit, primarily due to the factors discussed above, which was partially offset by a US$327.2 million increase in net operating expenses, primarily driven by a US$212.2 million increase in distribution expenses.

The following table sets forth the Group's net operating expenses for the years ended 31 December 2006 and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 | 2007 | | |
| | *(US$ millions)* | | | |
| General and administrative expenses | (655.0) | (691.2) | (36.2) | 5.5% |
| Distribution expenses | (697.3) | (909.5) | (212.2) | 30.4% |
| Indirect taxes and contributions | (142.1) | (153.6) | (11.5) | 8.1% |
| Share of associates' loss | (1.2) | (89.4) | (88.2) | — |
| Net income from securities operations | 28.3 | 25.6 | (2.7) | (9.5)% |
| Loss on disposal of property, plant and equipment | (39.3) | (35.3) | 4.0 | (10.2)% |
| Net other operating expenses | (27.1) | (7.5) | 19.6 | (72.3)% |
| **Net operating expenses** | **(1,533.7)** | **(1,860.9)** | **(327.2)** | **21.3%** |

*Mining segment*

Compared to the prior period, the Mining segment's profit from operations increased by US$44.1 million, or 18.6 percent, from US$237.7 million in 2006 to US$281.8 million in 2007. The increase in profit from operations was due to a US$174.2 million increase in gross profit, primarily as a result of the factors described above, partially offset by a US$130.1 million increase in net operating expenses.

The increase in the Mining segment's operating expenses was primarily due to a US$84.6 million increase in distribution expenses, a US$16.6 million increase in indirect taxes and contributions and a US$12.5 million increase in general and administrative expenses.

The increase in distribution expenses was primarily due to the increase in railway transportation costs. The increase in indirect taxes and contributions was mainly due to the increase in extraction tax payable on the extracted coal and iron ore and the increase in property tax payable on property, plant and equipment put into operation. General and administrative expenses increased primarily due to the implementation of labour safety improvement programmes and the increase in the number of employees and the average salaries of employees.

*Russian Steel segment*

Compared to the prior period, the Russian Steel segment's profit from operations increased by US$445.0 million, or 25.9 percent, from US$1,720.1 million in 2006 to US$2,165.1 million in 2007. The increase in profit from operations was due to a US$619.0 million increase in gross profit, primarily as a result of the factors described above, partially offset by a US$174.0 million increase in net operating expenses.

The increase in the Russian Steel segment's operating expenses was primarily due to a US$93.0 million increase in the share of associates' losses, a US$86.6 million increase in distribution costs and a US$11.8 million increase in general and administrative expenses, partially offset by a US$$21.3 million decrease in other net operating expenses.

The increase in the share of associates' losses was due to the losses reported by SeverCorr in 2007, when it was accounted for as an associate. The increase in distribution costs was primarily due to an increase in railway tariffs and an increase in sales by volume to Russia. The increase in general and administrative expenses was primarily due to an increase in the average salaries of employees.

*Lucchini segment*

The Lucchini segment's profit from operations increased by US$8.5 million, or 4.1 percent, from US$207.9 million in 2006 to US$216.4 million in 2007. The decrease was primarily due to a US$11.8 million increase in gross profit, as discussed above, which was partially offset by a US$3.3 million increase in net operating expenses.

The Lucchini segment's net operating expenses increased by US$3.3 million, or 1.0 percent, from US$342.4 million in 2006 to US$345.7 million in 2007. The increase was primarily due to a US$16.8 million increase in distribution expenses and a US$4.2 million increase in net other operating expenses, partially offset by a US$7.1 million increase in net income from securities operations, a US$2.9 million decrease in loss on disposal of property, plant and equipment and a US$5.0 million decrease in indirect taxes and contributions.

*Severstal North America*

Severstal North America's profit from operations decreased by US$132.6 million, from US$134.2 million in 2006 to US$1.6 million in 2007. The decrease was primarily due to a US$128.7 million decrease in gross profit primarily due to the factors described above and a US$3.9 million increase in net operating expenses.

The increase in net operating expenses was primarily due to a US$3.0 million increase in general and administrative expenses and a US$4.0 million increase in loss on disposal of property, plant and equipment, which was partially offset by a US$2.4 million increase in the share of associates' profit.

*IPM*

IPM's profit from operations increased by US$128.9 million, from a US$1.8 million loss in 2006 to US$127.1 million profit in 2007. The increase was due to the fact that IPM only started commercial operations in early 2007 but was under construction in 2006.

IPM's net operating expenses in 2007 were US$43.8 million. These expenses included US$29.1 million of distribution expenses such as railway transportation expenses and US$9.5 million of general and administrative expenses. The general and administrative expenses included labour costs and US$4.4 million of indirect taxes and contributions.

*The Metalware segment*

The Metalware segment's profit from operations increased by US$52.7 million, or 227.2 percent, from US$23.2 million in 2006 to US$75.9 million in 2007. The increase was due to a US$37.6 million increase in gross profit, as discussed above, and a US$15.1 million decrease in net operating expenses.

The Metalware segment's net operating expenses decreased by US$15.1 million, or 19.4 percent, from US$79.1 million in 2006 to US$64.0 million in 2007. The decrease was primarily due to a US$12.4 million gain on disposal of property, plant and equipment and a US$8.9 million increase in net other operating income, partially offset by a US$5.9 million increase in general and administrative expenses, which resulted from an increase in labour costs due to the increase in the average salaries of employees.

***Profit before financing and taxation***

Compared to the prior year, the Group's profit before financing and taxation increased by US$545.2 million, or 24.5 percent in 2007. The increase was due to a US$528.3 million increase in profit from operations and a US$16.9 million decrease in net non-operating expenses.

The increase in profit from operations was due to the factors discussed above. The decrease in net non-operating expenses was primarily due to a US$28.6 million decrease in impairment of property, plant and equipment and a US$8.0 million increase in negative goodwill, partially offset by a US$6.0 million increase in other net non-operating expenses and a US$14.7 million decrease in net gain on restructuring of tax liabilities. See "— For the years ended 31 December 2005 and 2006 — Profit before financing and taxation."

The following table sets forth the Group's net non-operating expenses for the years ended 31 December 2006 and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 | 2007 | | |
| | *(US$ millions)* | | | |
| Impairment of property, plant and equipment | (57.7) | (29.1) | 28.6 | (49.6)% |
| Net gain on restructuring tax liabilities | 14.7 | — | (14.7) | (100.0)% |
| Negative goodwill, net | 4.2 | 12.2 | 8.0 | 190.5% |
| Net other non-operating expenses | (53.6) | (58.6) | (5.0) | 9.3% |
| **Net non-operating expenses** | **(92.4)** | **(75.5)** | **16.9** | **(18.3)%** |

*Impairment of property, plant and equipment*

Due to the change in the accounting policy for property, plant and equipment from the revaluation model to the cost model the decrease in impairment of property, plant and equipment was primarily attributable to the decrease of impairment in the Mining segment of US$13.3 million and in the Metalware segment of US$18.7 million, partially offset by the increase of impairment in the Lucchini segment by US$6.1 million.

*Net gain on restructuring tax liabilities*

See "— For the years ended 31 December 2005 and 2006 — Profit before financing and taxation".

*Negative goodwill*

The negative goodwill in 2007 was primarily attributable to the acquisition of scrap metal businesses by the Mining segment.

***Profit for the year***

The Group's profit for the year increased by US$463.6 million, or 30.7 percent, from US$1,510.0 million in 2006 to US$1,973.2 million in 2007. The increase was due to a US$545.2 million increase in profit before financing and taxation, which was partially offset by a US$3.1 million increase in net financing expenses, a US$46.0 million increase in income tax expense and a US$32.5 million decrease in profit from discontinued operations. The increase in profit before financing and taxation is primarily due to the factors described above.

*Net financing expense*

Net financing expense comprises interest income, interest expense, including amortisation of transaction costs, and foreign exchange gains or losses. Net financing expense increased by US$3.1 million, from US$109.3 million in 2006 to US$112.4 million in 2007. This increase was due to a US$43.2 million increase in interest expense, from US$245.0 million in 2006 to US$288.2 million in 2007, a US$30.4 million decrease in foreign exchange gain, which was offset by a US$70.5 million increase in interest income.

The increase in interest income was primarily due to the higher average cash and financial investment balances during 2007 compared to 2006 and the increase in bank interest rates.

*Income tax expense*

Income tax expense increased by US$46.0 million in 2007, primarily due to an increase in profit before tax of US$542.1 million, which was partially offset by the decrease in effective tax rates from 30.0 percent to 25.7 percent. The majority of the Group's profits were generated within Russia and were subject to non-deductibility for tax purposes of certain items, which increase the effective income tax rate by approximately one to two percent above the statutory rate. Severstal North America was subject to US income tax, which generally reflects the effective US tax rate of approximately 30 percent of profit before tax. Other international subsidiaries of the Group are subject to their respective national tax legislation and statutory tax rates.

*Profit from discontinued operations*

Profit from discontinued operations decreased by US$32.5 million in 2007, primarily due to the disposal of Metallurgical Commercial Bank.

**For the years ended 31 December 2005 (restated) and 2006 (restated)**

The following discussion is based on, and should be read in conjunction with, the Annual Financial Statements included in this Prospectus beginning on page F-15.

The following table sets forth the Group's consolidated income statement for the years ended 2005 (restated) and 2006 (restated):

| | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2005 (restated) | 2006 (restated) | Year on year change | Year on year percent change |
| | | (US$ millions) | | |
| **Sales** | | | | |
| Sales — external | 9,786.1 | 11,723.3 | 1,937.2 | 19.8% |
| Sales — to related parties | 665.5 | 725.7 | 60.2 | 9.0% |
| | 10,451.6 | 12,449.0 | 1,997.4 | 19.1% |
| Cost of sales | (6,831.1) | (8,601.2) | (1,770.1) | 25.9% |
| **Gross profit** | **3,620.5** | **3,847.8** | **227.3** | **6.2%** |
| General and administrative expenses | (524.7) | (655.0) | (130.3) | 24.8% |
| Distribution expenses | (657.7) | (697.3) | (39.6) | 6.0% |
| Indirect taxes and contributions | (95.3) | (142.1) | (46.8) | 49.1% |
| Share of associates' loss | (4.2) | (1.2) | 3.0 | (71.4)% |
| Net income from securities operations | 24.4 | 28.3 | 3.9 | 16.0% |
| Loss on disposal of property, plant and equipment | (36.8) | (39.3) | (2.5) | 6.8% |
| Net other operating expenses | (20.3) | (27.1) | (6.8) | 33.5% |
| **Profit from operations** | **2,305.9** | **2,314.1** | **8.2** | **0.4%** |
| Impairment of property, plant and equipment | (111.4) | (57.7) | 53.7 | (48.2)% |
| Gain on restructuring tax of liabilities | 174.2 | 14.7 | (159.5) | (91.6)% |
| Negative goodwill, net | 7.6 | 4.2 | (3.4) | (44.7)% |
| Net other non-operating expenses | (52.7) | (53.6) | (0.9) | 1.7% |
| **Profit before financing and taxation** | **2,323.6** | **2,221.7** | **(101.9)** | **(4.4)%** |
| Interest income | 65.1 | 102.4 | 37.3 | 57.3% |
| Interest expense | (203.1) | (245.0) | (41.9) | 20.6% |
| Foreign exchange difference | (60.1) | 33.3 | 93.4 | (155.4)% |
| **Profit before income tax** | **2,125.5** | **2,112.4** | **(13.1)** | **(0.6)%** |
| Income tax expense | (500.9) | (635.3) | (134.4) | 26.8% |
| **Profit from continuing operations** | **1,624.6** | **1,477.1** | **(147.5)** | **(9.1)%** |
| Profit from discontinued operations | 0.6 | 32.9 | 32.3 | 5,383.3% |
| **Profit for the year** | **1,625.2** | **1,510.0** | **(115.2)** | **(7.1)%** |

***Sales***

Compared to the prior year, the Group's consolidated sales increased by US$1,997.4 million, or 19.1 percent, from US$10,451.6 million in 2005 to US$12,449.0 million in 2006. This increase was primarily due to a US$353.2 million increase in sales of the Russian Steel segment, a US$99.5 million increase in sales of the Mining segment and a US$1,510.0 million increase in sales of the Lucchini segment. Changes in the prices of the Group's various products are generally consistent with the prevailing market trends for each such product.

The Group's sales to related parties increased by US$60.2 million, from US$665.5 million in 2005 to US$725.7 million in 2007. The Group's sales to related parties comprised 6.4 percent and 5.8 percent of the Group's total sales in 2005 and 2006, respectively.

*Sales by product*

The following table sets forth the Group's sales by product for the years ended 31 December 2005 and 2006:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2005 | 2006 | | |
| | | *(US$ millions)* | | |
| Hot-rolled strip and plate | 3,443.6 | 3,435.5 | (8.1) | (0.2)% |
| Long products | 1,436.8 | 2,301.6 | 864.8 | 60.2% |
| Galvanised and other metallic coated sheet | 1,051.4 | 1,105.5 | 54.1 | 5.2% |
| Cold-rolled sheet | 1,541.0 | 1,328.1 | (212.9) | (13.8)% |
| Semi-finished products | 879.6 | 939.4 | 59.8 | 6.8% |
| Metalware products | 574.5 | 833.9 | 259.4 | 45.2% |
| Shipping and handling costs billed to customers | 174.2 | 537.4 | 363.2 | 208.5% |
| Others tubes and pipes, formed shapes | 210.6 | 320.4 | 109.8 | 52.1% |
| Rails, wheels and axles | 149.1 | 375.3 | 226.2 | 151.7% |
| Pellets and iron ore | 337.5 | 242.7 | (94.8) | (28.1)% |
| Scrap | 19.5 | 26.5 | 7.0 | 35.9% |
| Colour-coated sheet | — | 148.5 | 148.5 | — |
| Coal and coking coal concentrate | 143.1 | 249.3 | 106.2 | 74.2% |
| Others | 490.7 | 604.9 | 114.2 | 23.3% |
| **Sales** | **10,451.6** | **12,449.0** | **1,997.4** | **19.1%** |

*Sales by delivery destination*

The following table sets forth the Group's consolidated sales by delivery destination for the years ended 31 December 2005 and 2006:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2005 | 2006 | | |
| | | *(US$ millions)* | | |
| Russia | 3,785.1 | 4,912.6 | 1,127.5 | 29.8% |
| Europe | 2,751.2 | 4,390.8 | 1,639.6 | 59.6% |
| North America | 2,198.2 | 2,406.1 | 207.9 | 9.5% |
| The Middle East | 353.3 | 215.1 | (138.2) | (25.8)% |
| China and Central Asia | 569.9 | 138.0 | (431.9) | (75.8)% |
| South-East Asia | 408.2 | 143.6 | (264.6) | (64.8)% |
| Central & South America | 237.1 | 156.7 | (80.4) | (33.9)% |
| Africa | 148.6 | 86.1 | (62.5) | (42.1)% |
| **Sales** | **10,451.6** | **12,449.0** | **1,997.4** | **19.1%** |

*Sales by segment*

The following table sets forth the Group's sales by segment for the years ended 31 December 2005 and 2006:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2005 | 2006 | | |
| | *(US$ millions)* | | | |
| Mining segment | 1,391.5 | 1,491.0 | 99.5 | 7.2% |
| Russian Steel segment | 5,964.3 | 6,317.5 | 353.2 | 5.9% |
| Lucchini segment | 1,847.5 | 3,357.5 | 1,510.0 | 81.7% |
| Severstal North America | 1,822.6 | 1,868.4 | 45.8 | 2.5% |
| IPM | — | — | — | — |
| Metalware segment | 618.8 | 838.9 | 220.1 | 35.6% |
| Intersegment transactions | (1,193.1) | (1,424.3) | (231.2) | 19.4% |
| **Sales** | **10,451.6** | **12,449.0** | **1,997.4** | **19.1%** |

*Mining segment*

The Mining segment's sales increased by US$99.5 million, or 7.2 percent, from US$1,391.5 million in 2005 to US$1,491.0 million in 2006. Included in these amounts are intersegment sales, primarily to the Russian Steel segment, of US$805.5 million in 2005 and US$853.0 million in 2006. Excluding intersegment sales, sales of the Mining segment increased by US$52.0 million, or 8.9 percent, from US$586.0 million in 2005 to US$638.0 million in 2006. The increase was primarily due to an increase in the average price per tonne, and an increase in sales by volume as described below.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Mining segment by product:

*Pellets and iron ore.* The Mining segment's sales of pellets and iron ore decreased by US$94.8 million, or 28.1 percent, from US$337.5 million in 2005 to US$242.7 million in 2006. The decrease was primarily due to a decrease in the average price per tonne of US$7.0 and a decrease in sales by volume of 957.6 thousand tonnes driven by an increase of intersegment sales to the Russian Steel segment.

*Coal and coking coal concentrate.* The Mining segment's sales of coal and coking coal concentrate increased by US$106.2 million, or 74.2 percent, from US$143.1 million in 2005 to US$249.3 million in 2006. The increase was primarily due to a US$3.9 increase in the average price per tonne and an increase in sales by volume of 1,940.5 thousand tonnes driven by commencement of mining operations at the Severnaya mine and at the Moschny coal seam in Vorgashora.

*Russian Steel segment*

The Russian Steel segment's sales increased by US$353.2 million, or 5.9 percent, from US$5,964.3 million in 2005 to US$6,317.5 million in 2006. Included in the above amounts are intersegment sales of US$338.4 million in 2005 and US$392.7 million in 2006. The increase was primarily due to an increase in the average price per tonne, which was partially offset by a decrease in sales by volume due to the reduction of production caused by periodic maintenance that resulted in a 130-day closure of blast furnace 5.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Russian Steel segment by product:

*Hot-rolled strip and plate.* Sales of hot-rolled strip and plate decreased by US$107.6 million, or 4.1 percent, from US$2,647.1 million in 2005 to US$2,539.5 million in 2006. The decrease was primarily due to a decrease in the average price per tonne of US$9.9 and by a decrease in sales by volume of 110.1 thousand tonnes due to the factors discussed above.

*Cold-rolled sheet.* Sales of cold-rolled sheet decreased by US$195.1 million, or 17.5 percent, from US$1,112.9 million in 2005 to US$917.8 million in 2006. This decrease was primarily due to a decrease in the average price per tonne of US$59.2, and by a decrease in sales by volume of 158.7 thousand tonnes due to the factors discussed above.

*Galvanised sheet.* Sales of galvanised sheet increased by US$109.9 million, or 23.5 percent, from US$467.9 million in 2005 to US$577.8 million in 2006. The increase was primarily due to an increase in the average price per tonne of US$36.0, and by an increase in sales by volume of 106.7 thousand tonnes due to commencement of operations at Severgal. (See "Business — Russian Steel Division — Facilities — Severgal".

*Semi-finished products.* Sales of semi-finished products decreased by US$188.8 million, or 49.3 percent, from US$382.9 million in 2005 to US$194.1 million in 2006. The decrease was primarily due to a decrease in the average price per tonne of US$10.7, and by a decrease in sales by volume of 526.1 thousand tonnes due to the factors discussed above.

*Lucchini segment*

The Lucchini segment's sales increased by US$1,510.0 million, or 81.7 percent, from US$1,847.5 million in 2005 to US$3,357.5 million in 2006. The increase in sales was mainly attributable to the fact that the Lucchini segment's results of operation for 2005 were only consolidated effective 1 May 2005, and therefore were not reflected in the Financial Statements for the entire year ended 31 December 2005.

Set forth below is a discussion of the sales, excluding intersegment sales, of the Lucchini segment by product:

*Semi-finished products.* Sales of semi-finished products increased by US$248.5 million, or 50.0 percent, from US$496.7 million in 2005 to US$745.2 million in 2006. The increase was primarily due to an increase in the average price per tonne of US$330.3 and by an increase in sales by volume of 2.4 thousand tonnes due to the factors discussed above.

*Rails, wheels and axles.* Sales of rails, wheel and axles increased by US$226.2 million, or 151.7 percent, from US$149.1 million in 2005 to US$375.3 million in 2006. The increase was primarily due to an increase in sales by volume of 227.9 thousand tonnes due to the factors discussed above, which was partially offset by a decrease in the average price per tonne of US$43.5.

*Long products.* Sales of long products increased by US$737.4 million, or 73.9 percent, from US$998.2 million in 2005 to US$1,735.6 million in 2006. The increase was primarily due to an increase in sales by volume of 964.3 thousand tonnes due to the factors discussed above, partially offset by a decrease in the average price per tonne of US$18.7.

*Severstal North America*

Severstal North America's sales increased by US$45.8 million, or 2.5 percent, from US$1,822.6 million in 2005 to US$1,868.4 million in 2006. This increase was primarily due to an increase of US$99.6 million in sales of hot-rolled strip and plate and a US$19.9 million increase in sales of others products, partially offset by a decrease of US$17.8 million in sales of cold-rolled sheet and US$55.8 million decrease in sales of galvanised sheet.

Set forth below is a discussion of the sales, excluding intersegment sales, of Severstal North America by product:

*Hot-rolled strip and plate.* Severstal North America's sales of hot-rolled strip and plate increased by US$99.6 million, or 12.5 percent, from US$796.5 million in 2005 to US$896.1 million in 2006. The increase was primarily due to an increase in the average price per tonne of US$32.0 and an increase in sales by volume of 90.3 thousand tonnes primarily due to more favourable pricing conditions for hot-rolled strip and plate.

*Cold-rolled sheet.* Severstal North America's sales of cold-rolled sheet decreased by US$17.8 million, or 4.2 percent, from US$428.1 million in 2005 to US$410.3 million in 2006. The decrease was primarily due to a decrease in sales by volume of 33.5 thousand tonnes partially offset by an increase in the average price per tonne of US$9.4.

*Galvanised sheet.* Severstal North America's sales of galvanised sheet increased by US$55.8 million, or 9.6 percent, from US$583.5 million in 2005 to US$527.7 million in 2006. The increase was primarily due to an increase in the average price per tonne of US$9.2, but was partially offset by a decrease in sales by volume of 76.1 thousand tonnes primarily due to lower demand from the automotive industry.

*Metalware segment*

The Metalware segment's sales increased by US$220.1 million, or 35.6 percent, from US$618.8 million in 2005 to US$838.9 million in 2006. Included in the above amounts are intersegment sales of US$13.2 million in 2005 and US$9.1 million in 2006. The increase was primarily due to an increase in sales by volume of 305.3 thousand tonnes due to the acquisitions of Dneprometiz and Carrington Wire Ltd and to an increase in the average price per tonne of US$8.2.

***Cost of sales***

The Group's cost of sales increased by US$1,770.1 million, or 25.9 percent, from US$6,831.1 million in 2005 to US$8,601.2 million in 2006.

*Cost of sales by segment*

The following table sets forth the Group's cost of sales by segment for the years ended 31 December 2005 and 2006:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2005 | 2006 | | |
| | | *(US$ millions)* | | |
| Mining segment | (745.4) | (965.8) | (220.4) | 29.6% |
| Russian Steel segment | (3,405.4) | (3,804.8) | (399.4) | 11.7% |
| Lucchini segment | (1,569.2) | (2,807.2) | (1,238.0) | 78.9% |
| Severstal North America | (1,716.3) | (1,711.9) | 4.4 | (0.3)% |
| IPM | (2.3) | — | — | — |
| Metalware segment | (557.0) | (736.6) | (179.6) | 32.2% |
| Intersegment transactions | 1,164.5 | 1,425.1 | 260.6 | 22.4% |
| **Cost of sales** | **(6,831.1)** | **(8,601.2)** | **(1,770.1)** | **25.9%** |

*Mining segment*

The Mining segment's cost of sales increased by US$220.4 million, or 29.6 percent, from US$745.4 million in 2005 to US$965.8 million in 2006. The increase was primarily due to an increase in raw materials, spare parts and fuel and energy expense, an increase in labour costs and related taxes, and an increase in depreciation and amortisation expense.

*Raw materials, spare parts and fuel and energy expenses.* The increase in raw materials, spare parts, fuel and energy expenses was partially due to the increase in the sales by volume, partially due to the increase in prices for the main types of raw materials.

*Labour and related taxes expense.* The increase in labour and related taxes expense was primarily due to an increase in the number of employees and an increase in the average salaries of employees generally in line with inflation in Russia.

*Depreciation expense.* The increase in depreciation expense was primarily due to additions to fixed assets.

*Russian Steel segment*

The Russian Steel segment's cost of sales increased by US$399.4 million, or 11.7 percent, from US$3,405.4 million in 2005 to US$3,804.8 million in 2006. The increase was due to an increase in prices for raw materials and fuel and energy expenses, an increase in depreciation and amortisation expense, an increase in labour costs and related taxes, and an increase due to the appreciation of the Rouble, the functional currency of major entities of the Russian Steel segment, against the US dollar, the Group's reporting currency. The increase was partially offset by a positive effect of efficiency improvements, which decreased the consumption of raw materials per unit of production.

*Raw materials and fuel and energy expenses.* The increase in prices for raw materials and fuel and energy expenses resulted in a US$114.0 million increase in 2006, which was mainly attributable to the increase in prices for scrap metal, ferro-alloys and fuel and energy. The increase in prices for the above-mentioned materials and resources was partially offset by a decrease in the cost of iron ore and pellets and coal and coking coal concentrates.

*Depreciation expense.* The increase in depreciation expense was primarily due to the re-evaluation of the useful lives of fixed assets in 2005 and due to an increase in additions of fixed assets.

*Labour costs and related taxes expense.* The increase in labour and related taxes expense was primarily due to the increase in the average salaries of employees generally in line with wage inflation in Russia.

*Lucchini segment*

The Lucchini segment's cost of sales increased by US$1,238.0 million, or 78.9 percent, from US$1,569.2 million in 2005 to US$2,807.2 million in 2006.

The increase in cost of sales was mainly attributable to the fact that the Lucchini segment's results of operation for 2005 were only consolidated effective 1 May 2005, and therefore were not accounted for the entire 12 months of 2005. Other factors contributing to the increase in cost of sales were increases in prices of raw materials and the appreciation of the euro, the functional currency of the Lucchini segment entities, against the US dollar, the Group's reporting currency.

The increase in the prices of raw materials and fuel and energy was generally consistent with the overall inflation in the region of operations.

*Severstal North America*

Severstal North America's cost of sales decreased by US$4.4 million, from US$1,716.3 million in 2005 to US$1,711.9 million in 2006. The decrease was the result of a US$72.8 million decrease in prices for raw materials, mostly due to more efficient procurement and stock management, partially offset by a decrease in raw material efficiency per tonne of production, a US$8.6 million increase in energy prices, as well as increases in the price of zinc used in the galvanising operations and increases in sales by volume.

*Metalware segment*

The Metalware segment's cost of sales increased by US$179.6 million, or 32.2 percent, from US$557.0 million in 2005 to US$736.6 million in 2006. The increase was generally in line with the increase in the sales by volume of 31.6 percent and was primarily due to a US$130.0 million increase in raw materials, spare parts and fuel and energy expenses, a US$17.8 million increase in labour costs and related taxes and a US$5.7 million increase in depreciation and amortisation expenses.

*Raw materials, spare parts and fuel and energy expense.* Raw materials, spare parts and fuel and energy expense increased primarily due to the increase in sales by volume and the overall increases in prices.

*Labour and related taxes expense.* The increase in labour and related taxes expense was primarily due to an increase in the average number of employees and an increase in the average salary generally in line with inflation in Russia.

*Depreciation expense.* The increase in depreciation expense was primarily due to additions to fixed assets during 2006.

***Profit from operations***

The Group's profit from operations increased by US$8.2 million, or 0.4 percent, from US$2,305.9 million in 2005 to US$2,314.1 million in 2006. The increase was due to a US$227.3 million increase in gross profit, primarily due to the factors discussed above, and was partially offset by a US$219.1 million increase in operating expenses.

The increase in net operating expenses was primarily due to a US$130.3 million increase in general and administrative expenses, a US$46.8 million increase in indirect taxes and contributions and a US$39.6 million in distribution expenses.

The following table sets forth the Group's operating expenses for the years ended 31 December 2005 and 2006:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2005 | 2006 | | |
| | | *(US$ millions)* | | |
| General and administrative expenses | (524.7) | (655.0) | (130.3) | 24.8% |
| Distribution expenses | (657.7) | (697.3) | (39.6) | 6.0% |
| Indirect taxes and contributions | (95.3) | (142.1) | (46.8) | 49.1% |
| Share of associates' loss | (4.2) | (1.2) | 3.0 | (71.4)% |
| Net income from securities operations | 24.4 | 28.3 | 3.9 | 16.0% |
| Loss on disposal of property, plant and equipment | (36.8) | (39.3) | (2.5) | 6.8% |
| Net other operating expenses | (20.3) | (27.1) | (6.8) | 33.5% |
| **Net operating expenses** | **(1,314.6)** | **(1,533.7)** | **(219.1)** | **16.7%** |

*Mining segment*

Compared to the prior period, the Mining segment's profit from operations decreased by US$200.2 million, from US$437.9 million in 2005 to US$237.7 million in 2006. The decrease was primarily due to a US$120.9 million decrease in gross profit, due to the factors discussed above, and a US$79.3 million increase in net operating expenses.

The increase in the Mining segment's operating expenses was primarily due to a US$32.1 million increase in general and administrative expenses, a US$40.2 million increase in distribution expenses and a US$6.4 million increase in indirect taxes and contributions.

The increase in distribution expenses was primarily due to the increase in railway transportation costs. The increase in indirect taxes and contributions was primarily due to the increase in extraction tax payable on the extracted coal and iron ore. The increase in general and administrative expenses was primarily due to the increase in labour costs and related taxes due to the increase in the number of employees and the increase in the average salaries of employees.

*Russian Steel segment*

The Russian Steel segment's profit from operations decreased by US$59.7 million, or 3.4 percent, from US$1,779.8 million in 2005 to US$1,720.1 million in 2006. The decrease was primarily due to a US$46.2 million decrease in gross profit, due to the factors discussed above, and a US$13.5 million increase in net operating expenses.

The increase in the Russian Steel segment's net operating expenses was primarily due to a US$39.7 million increase in general and administrative expenses and a US$26.4 million increase in indirect taxes and contributions, which was partially offset by a US$53.6 million decrease in distribution expenses.

The increase in general and administrative expenses was primarily due to an increase in labour costs and related taxes as the average salary and average number of employees increased and to an overall increase in prices for services and goods. The increase in indirect taxes and contributions was primarily attributable to an increase in property tax and tax penalties. The decrease in distribution expenses was primarily attributable to the decrease in the sales by volume to the Russian market.

*Lucchini segment*

The Lucchini segment's profit from operations increased by US$154.7 million, from US$53.2 million in 2005 to US$207.9 million in 2006. The increase was primarily due to a US$272.0 million increase in gross profit, due to the factors discussed above, which was partially offset by a US$117.3 million increase in net operating expenses.

The increase in net operating expenses was primarily due to a US$65.8 million increase in general and administrative expenses, and to increases in distribution expenses and in indirect taxes and contributions. These increases were generally consistent with the overall increase in sales by volume.

*Severstal North America*

Severstal North America's profit from operations increased by US$52.4 million, from US$81.8 million in 2005 to US$134.2 million in 2006. The increase was primarily due to a US$50.2 million increase in gross profit, due to the factors discussed above, and a US$2.2 million decrease in net operating expenses.

The decrease in net operating expenses was mainly attributable to a decrease in distribution expenses.

*Metalware segment*

The Metalware segment's profit from operations increased by US$33.2 million, from a loss of US$10.0 million in 2005 to a profit of US$23.2 million in 2006. The increase was primarily due to a US$40.5 million increase in gross profit, due to the factors discussed above, but was partially offset by a US$7.3 million increase in net operating expenses.

The increase in net operating expenses was primarily due to a US$15.7 million increase in distribution expenses, partially offset by a US$5.8 million decrease in general and administrative expenses.

The increase in distribution expenses was primarily attributable to an increase in sales by volume causing increases in transportation costs. The decrease in general and administrative expenses was primarily attributable to more effective cost management and a decrease in the number of administrative employees.

***Profit before financing and taxation***

Compared to the year ended 31 December 2005, the Group's profit before financing and taxation decreased by US$101.9 million in 2006.

The decrease was due to a US$8.2 million increase in profit from operations, due to the factors discussed above, offset by a US$110.1 million increase in net non-operating expenses.

The increase in net non-operating expenses was primarily attributable to a US$159.5 million decrease in net gain on restructuring of tax liabilities, which was partially offset by a US$53.7 million decrease in impairment of property, plant and equipment.

The following table sets forth the Group's net non-operating income/(expenses) for the years ended 31 December 2005 and 2006:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2005 | 2006 | | |
| | | (US$ millions) | | |
| Impairment of property, plant and equipment | (111.4) | (57.7) | 53.7 | (48.2)% |
| Gain on restructuring of tax liabilities | 174.2 | 14.7 | (159.5) | (91.6)% |
| Negative goodwill, net | 7.6 | 4.2 | (3.4) | (44.7)% |
| Net other non-operating expenses | (52.7) | (53.6) | (0.9) | 1.7% |
| **Net non-operating income/(expenses)** | **17.7** | **(92.4)** | **(110.1)** | **(622.0)%** |

*Impairment of property, plant and equipment*

The appraisal procedures performed in 2005 resulted in an impairment charge of US$111.4 million due to projected declines in prices for steel products.

*Gain on restructuring of tax liabilities*

The gain on restructuring of tax liabilities in both years related to the restructuring of OAO Vorkutaugol and OAO Mine Vorgashorskaya taxes. OAO Vorkutaugol and OAO Mine Vorgashorskaya had significant amounts of taxes in arrears when they were acquired by the Controlling Shareholder in June 2003.

In November 2005, these subsidiaries signed restructuring agreements with the Russian tax authorities. In accordance with these agreements, the principal amounts of taxes, fines and 15 percent of tax interest are payable by instalments over four years. If those payments are made on schedule, the remaining 85 percent of tax interest liability at the date of restructuring will be forgiven. The Group is confident that all payments will be in accordance with the agreed schedule and has recognised a US$200.9 million gain on tax restructuring in the income statement for the year ended 31 December 2005. This gain is comprised of US$186.8 million of tax interest, which is to be forgiven in accordance with the restructuring agreements, and has been derecognised from liabilities, and US$14.1 million of the remaining liabilities discounted at the interest rate of 9.86 percent over the period of 2006-2009. During 2005, tax authorities accrued an additional US$26.7 million of tax interest on tax liabilities being restructured. These amounts were recognised as an expense in the income statement for the year ended 31 December 2005. During 2006, the Group was able to include part of this tax interest into restructuring, recognising a gain of US$14.7 million in the income statement for the year ended 31 December 2006. Restructured tax liabilities are subject to interest at the rate of 5 percent per annum, which is recognised as interest expense since November 2005.

Accordingly, net gain on restructuring of tax liabilities is shown in the income statement as follows:

| | Year ended 31 December | |
|---|---|---|
| | **2005** | **2006** |
| Tax interest accrued prior to restructuring | (26.7) | — |
| Gain on restructuring of tax liabilities | 200.9 | 14.7 |
| **Net gain on restructuring of tax liabilities** | **174.2** | **14.7** |

***Profit for the year***

The Group's profit for the year decreased by US$115.2 million, from US$1,625.2 million in 2005 to US$1,510.0 million in 2006. The decrease was due to a US$101.9 million decrease in profit before financing and taxation, for the reasons described above, and a US$41.9 million increase in interest expense, partially offset by a US$37.3 million increase in interest income, a US$93.4 million increase in foreign exchange gain, and a US$32.3 million increase in profit from discontinued operations and an increase in income tax expense of US$134.4 million.

*Net financing expense*

Net financing expense decreased by US$88.8 million, from US$198.1 million in 2005 to US$109.3 million in 2006. The decrease was due to the increase in interest income of US$37.3 million and an increase in foreign exchange gain of US$93.4 million, partially offset by the increase in interest expense by US$41.9 million.

Foreign exchange gains increased by US$93.4 million in 2006 compared to 2005, mainly resulting from the appreciation of the Rouble against the US dollar.

Interest income increased by US$37.3 million primarily due to higher average cash, short-term bank deposits and financial investment balances in 2006 compared to 2005.

Interest expense increased by US$41.9 million primarily due to the increase in debt financing in 2006 compared to 2005.

*Income tax expense*

Income tax expense increased by US$134.4 million or 26.8 percent, from US$500.9 million in 2005 to US$635.3 million in 2006. The increase was primarily due to an increase in effective tax rate from 23.6 percent to 30.1 percent, partially offset by the decrease in profit before income tax by US$13.1 million. Increase in the effective tax rate was mainly attributable to the increase in non-deductible expenses and a change in the reassessment of deferred tax liabilities of US$31.1 million.

## LIQUIDITY AND CAPITAL RESOURCES

As at 31 March 2008, the Group had total cash and cash equivalents of US$2,406.3 million and short-term bank deposits of US$321.5 million.

The Group has financed and expects to continue to finance its operations and capital expenditures primarily through the Group's operating cash flows and, to the extent required, through borrowings or capital raising activities, including this offering of the Notes. Historically, a significant portion of the Group's capital expenditures has been related to the modernisation of the Group's producing assets. In addition, the Group has made a number of acquisitions and paid dividends to shareholders in the period under review. For a discussion of the Group's historical and expected capital expenditures, see "Business".

### Cash flows

***For the three months ended 31 March 2007 (restated) and 2008***

The following table sets forth the Group's consolidated cash flow for the three months ended 31 March 2007 and 2008:

| | Three months ended 31 March | | Period on period change | Period on period percent change |
|---|---|---|---|---|
| | 2007 | 2008 | | |
| | | *(US$ millions)* | | |
| **Net cash from operating activities** | | | | |
| Profit before financing and taxation | 698.3 | 732.8 | 34.5 | 4.9% |
| Adjustments to reconcile profit to cash generated from operations | 177.3 | 289.1 | 111.8 | 63.1% |
| Changes in operating assets and liabilities | 37.0 | (76.0) | (113.0) | (305.4)% |
| Interest paid (excluding banking operations) | (63.4) | (58.0) | 5.4 | (8.5)% |
| Income tax paid | (179.7) | (192.6) | (12.9) | 7.2% |
| **Total** | **669.5** | **695.3** | **25.8** | **3.9%** |
| **Cash from investing activities** | | | | |
| Capital expenditures[1] | (343.1) | (421.3) | (78.2) | 22.8% |
| Net cash outflow on acquisitions of subsidiaries | (45.3) | — | 45.3 | (100.0)% |
| Acquisition of minority interests and entities under common control | — | (44.0) | (44.0) | — |
| Purchases of financial investments and associates, net of proceeds on disposal | (55.7) | 2.9 | 58.6 | (105.2)% |
| Net (increase)/decrease in short-term bank deposits | (549.5) | 358.2 | 907.7 | (165.2)% |
| Other | 34.4 | 31.0 | (3.4) | (9.9)% |
| **Total** | **(959.2)** | **(73.2)** | **886.0** | **(92.4)%** |
| **Cash from financing activities** | | | | |
| Proceeds from debt finance | 329.0 | 840.6 | 511.6 | 155.5% |
| Repayment of debt finance | (269.4) | (662.4) | (393.0) | 145.9% |
| Dividends paid | (17.3) | (103.7) | (86.4) | 499.4% |
| Other | — | (1.5) | (1.5) | — |
| **Total** | **42.3** | **73.0** | **30.7** | **72.6%** |
| Effect of exchange rates on cash and cash equivalents | 14.6 | 91.3 | 76.7 | 525.3% |
| **Net (decrease)/increase in cash and cash equivalents** | **(232.8)** | **786.4** | **1,019.2** | **(437.8)%** |

(1) Consisting of cash outlays for purchases of property, plant and equipment and intangible assets.

Net cash from operating activities increased by US$25.8 million, or 3.9 percent, from US$669.5 million for the three months ended 31 March 2007 to US$695.3 million for the three months ended 31 March 2008. The increase was primarily due to the increase in profit before financing and taxation of US$34.5 million due to the factors discussed under "— Results of Operations — For the three months ended 31 March 2007 and 2008", and was affected by a number of factors, including an increase in changes in other taxes and social security payables from an increase of US$7.0 million in the three months ended 31 March 2007 to an increase of US$72.7 million in the three months ended 31 March 2008 and the movement in the changes in inventories from a decrease of US$105.2 million in the three months ended 31 March 2007 to an increase of US$88.4 million in the three months ended 31 March 2008. The increase in net cash from operating activities was partially offset by a US$12.9 million increase in income tax paid resulting from an increase of taxable profit compared with the corresponding period in the previous year.

Net cash used in investing activities decreased by US$886.0 million or 92.4 percent, from US$959.2 million for the three months ended 31 March 2007 to US$73.2 million for the three months ended 31 March 2008. The decrease was primarily attributable to decreases in short-term bank deposits mainly due to the financing of the Phase II construction at SeverCorr, partially offset by the US$78.2 million increase in capital expenditures. Net cash outflow on the acquisition of minority interests and entities under common control for the first quarter 2008 of US$44.0 million was mainly attributable to the cash paid on the acquisition of the remaining minority stake in Celtic Resources Holdings Plc.

Net cash received from financing activities increased by US$30.7 million or 72.6 percent, from US$42.3 million for the three months ended 31 March 2007 to US$73.0 million for the three months ended 31 March 2008. The increase was primarily attributable to proceeds from debt financing, net of repayment, which amounted US$178.2 million in the three months ended 31 March 2008 and US$59.6 million during the three months ended 31 March 2007, which was partially offset by the increase in dividends paid in the amount of US$103.7 million during the three months ended 31 March 2008 in comparison with US$17.3 million during the three months ended 31 March 2007.

***For the years ended 31 December 2006 (restated) and 2007 (restated)***

The following table sets forth the Group's consolidated cash flow for the years ended 31 December 2006 and 2007:

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2006 | 2007 | | |
| | | *(US$ millions)* | | |
| **Net cash from operating activities** | | | | |
| Profit before financing and taxation | 2,221.7 | 2,766.9 | 545.2 | 24.5% |
| Adjustments to reconcile profit to cash generated from operations | 642.3 | 939.7 | 297.4 | 46.3% |
| Changes in operating assets and liabilities | (242.7) | (357.9) | (115.2) | 47.5% |
| Interest paid (excluding banking operations) | (215.1) | (230.8) | (15.7) | 7.3% |
| Income tax paid | (676.6) | (802.9) | (126.3) | 18.7% |
| **Total** | **1,729.7** | **2,315.1** | **585.4** | **33.8%** |
| **Cash from investing activities** | | | | |
| Capital expenditures(1) | (1,252.6) | (1,589.1) | (336.5) | 26.9% |
| Net cash outflow on acquisitions of subsidiaries | (57.6) | (644.1) | (586.5) | — |
| Net cash inflow on disposals of subsidiaries | 1.6 | 236.0 | 234.4 | — |
| Acquisition of minority interests and entities under common control | (294.2) | (232.4) | 61.8 | (21.0)% |
| Purchases of financial investments and associates, net of proceeds on disposal | (254.3) | (516.5) | (262.2) | 103.1% |
| Net (increase)/decrease in short-term bank deposits | (431.1) | 580.7 | 1,011.8 | (234.7)% |
| Other | 119.1 | 183.4 | 64.3 | 54.0% |
| **Total** | **(2,169.1)** | **(1,982.0)** | **187.1** | **(8.6)%** |
| **Cash from financing activities** | | | | |
| Proceeds from debt finance | 1,379.2 | 2,794.3 | 1,415.1 | 102.6% |
| Proceeds from share issue | 1,105.2 | — | (1,105.2) | (100.0)% |
| Repayment of debt finance | (1,495.4) | (2,623.5) | (1,128.1) | 75.4% |
| Dividends paid | (269.3) | (736.2) | (466.9) | 173.4% |
| Other | 6.7 | (3.8) | (10.5) | (156.7)% |
| **Total** | **726.4** | **(569.2)** | **(1,295.6)** | **(178.4)%** |
| Effect of exchange rates on cash and cash equivalents | 86.1 | 82.0 | (4.1) | (4.8)% |
| **Net increase/(decrease) in cash and cash equivalents** | **373.1** | **(154.1)** | **(527.2)** | **(141.3)%** |

(1) Consists of cash outlays for purchases of property, plant and equipment and intangible assets.

Net cash from operating activities increased by US$585.4 million, or 33.8 percent, from US$1,729.7 million for 2006 to US$2,315.1 million for 2007. The increase was primarily due to the increase in profit before financing and taxation by US$545.2 million due to the factors discussed in "— Results of Operations" above) and the increase in depreciation charge which was added back to profit for cash flow purposes, and was offset by significant growth in increases in trade accounts receivable and in decreases in other non-current liabilities.

Net cash used in investing activities decreased by US$187.1 million or 8.6 percent, from US$2,169.1 million for 2006 to US$1,982.0 million for 2007. The decrease was primarily attributable to decrease in short-term bank deposits, the increase in net cash inflow on disposal of subsidiaries by US$234.4 million, mainly attributable to the proceeds received from the disposal of Sidermeccanica, Nutrivid SAS, Ascoforge Safe SAS, OAO Metallurgical Commercial Bank and OOO Uralmash-Metallurgicheskoe Oborudovanie during 2007 and the decrease in cash paid on acquisitions of minority interests and entities under common control by US$61.8 million. Short-term bank deposits are used by the Group to earn investment income, while preserving a strong liquidity position.

The decrease was partially offset by the increase in capital expenditure by US$336.5 million, the increase in net cash outflows on purchases of financial investments and associates by US$262.2 million and the increase in cash outflows on acquisition of subsidiaries by US$586.5 million.

The increase in capital expenditure relates to the implementation of the Group's capital investment and renovation programme. The key areas of capital investment in 2006 were construction works at IPM, Severgal, as well as significant capital improvements at Cherepovets Steel Plant. See "Business — Russian Steel Division". The key areas of capital investments in 2007 were reconstruction of continuous casting machines and hot-rolling mills in the Russian Steel segment. The increase in net cash outflows on purchases of financial investments and associates by US$262.2 million primarily related to the additional equity contribution in Severstal US Holdings LLC. During 2007, the Group spent US$644.1 million on the acquisition of subsidiaries, mainly attributable to the acquisition of controlling stakes in ZAO Vtorchermet, ZAO Neva-Metall, ZAO Neva-Metall Trans, OOO Nerengri-Metallik, ZAO Mine Aprelkovo, Siderco SpA and Celtic Resources Holdings Plc.

Net cash from financing activities decreased by US$1,295.6 million or 178.4 percent, from a net cash inflow of US$726.4 million during 2006 to a net cash outflow of US$569.2 million during 2007 driven by increases in dividend payments and by the absence of proceeds from share issues in 2007 in contrast with 2006 as the Group did not engage in equity capital raising in 2007.

In 2006, the Group received a total of US$1,105.2 million of proceeds from issues of shares in June 2006 and December 2006. The share issue in June 2006 was designed primarily for the acquisition of the controlling stakes in mining companies from the Controlling Shareholder; however, certain shareholders exercised their pre-emptive rights and purchased approximately 13.5 thousand shares. The share issue in December 2006 was designed as part of the initial public offering in November 2006 by the Controlling Shareholder of the Group's global depository receipts representing the Company's shares on the London Stock Exchange.

The cash flow effect of the factors described above was partially offset by the increase in net cash inflow from debt financing during 2007. Net cash inflow from debt financing, net of repayment, amounted to US$170.8 million during 2007 in comparison with the net cash outflow of US$116.2 million during 2006.

***For the years ended 31 December 2005 (restated) and 2006 (restated)***

The following table sets forth the Group's consolidated cash flow for the years ended 31 December 2005 and 2006.

| | Year ended 31 December | | Year on year change | Year on year percent change |
|---|---|---|---|---|
| | 2005 | 2006 | | |
| | (US$ millions) | | | |
| **Net cash from operating activities** | | | | |
| Profit before financing and taxation | 2,323.6 | 2,221.7 | (101.9) | (4.4)% |
| Adjustments to reconcile profit to cash generated from operations | 493.3 | 642.3 | 149.0 | 30.2% |
| Changes in operating assets and liabilities | (125.6) | (242.6) | (117.0) | 93.2% |
| Interest paid (excluding banking operations) | (199.2) | (215.1) | (15.9) | 8.0% |
| Income tax paid | (557.3) | (676.6) | (119.3) | 21.4% |
| **Total** | **1,934.8** | **1,729.7** | **(205.1)** | **(10.6)%** |
| **Cash from investing activities** | | | | |
| Capital expenditures[1] | (1,236.7) | (1,252.6) | (15.9) | 1.3% |
| Net cash outflow on acquisitions of subsidiaries | (4.2) | (57.6) | (53.4) | 1,271.4% |
| Net cash inflow on disposals of subsidiaries | 13.7 | 1.6 | (12.1) | (88.3)% |
| Acquisition of minority interests and entities under common control | 108.5 | (294.2) | (402.7) | (371.2)% |
| Purchases of financial investments and associates, net of proceeds on disposal | (0.9) | (254.3) | (253.4) | 28,155.6% |
| Net decrease/(increase) in short-term bank deposits | (133.5) | (431.1) | (297.6) | 222.9% |
| Other | 75.0 | 119.1 | 44.1 | 58.8% |
| **Total** | **(1,178.1)** | **(2,169.1)** | **(991.0)** | **84.1%** |
| **Cash used in financing activities** | | | | |
| Proceeds from debt finance | 1,157.0 | 1,379.2 | 222.2 | 19.2% |
| Proceeds from share issue | — | 1,105.2 | 1,105.2 | — |
| Repayment of debt finance | (1,358.0) | (1,495.4) | (137.4) | 10.1% |
| Dividends paid | (277.6) | (269.3) | 8.3 | (3.0)% |
| Other | 30.0 | 6.7 | (23.3) | (77.7)% |
| **Total** | **(448.6)** | **726.4** | **1,175.0** | **(261.9)%** |
| Effect of exchange rates on cash and cash equivalents | (70.6) | 86.1 | 156.7 | (222.0)% |
| **Net increase in cash and cash equivalents** | **237.5** | **373.1** | **135.6** | **57.1%** |

(1) Consists of cash outlays for purchases of property, plant and equipment and intangible assets.

Net cash from operating activities decreased by US$205.1 million, or 10.6 percent, from US$1,934.8 million for 2005 to US$1,729.7 million for 2006. The decrease was primarily due to the decrease in profit before financing and taxation of US$101.9 million and to increases in working capital.

Net cash used in investing activities increased by US$991.0 million or 84.1 percent, from US$1,178.1 million for 2005 to US$2,169.1 million for 2006. The increase was primarily attributable to net increases in short-term bank deposits of US$297.6 million, the increase in net cash outflow on acquisitions of minority interests and entities under common control of US$402.7 million, the increase in cash outflow on purchases of financial investments and associates, net of proceeds from disposals of US$253.4 million.

Net cash from financing activities increased by US$1,175.0 million or 261.9 percent, from a net cash outflow of US$448.6 million during 2005 to a net cash inflow of US$726.4 million during 2006. The increase in the cash inflow from financing activities was primarily attributable to the cash proceeds from the issue of shares during 2006 as described above in "— For the years ended 31 December 2006 and 2007".

The decrease in net cash outflow on debt financing also contributed to the increase in the net cash inflow from financing activities. During 2006, net cash outflow on debt repayments, net of proceeds from debt finance, amounted to US$116.2 million in comparison with the net cash outflow of US$201.0 million during 2005.

**Net Indebtedness**

The following table sets out the Group's indebtedness as at 31 March 2008 and 31 December 2007:

| | 31 March 2008 | 31 December 2007 |
|---|---|---|
| | *(US$ millions)* | |
| Citibank CLN — Eurobonds 2009(1) | 325.0 | 325.0 |
| Citibank CLN — Eurobonds 2014(1) | 375.0 | 375.0 |
| EBRD syndicated facility(1) | 315.3 | — |
| Other bank financing(1) | 2,785.2 | 2,799.4 |
| Factoring of receivables(1) | 227.7 | 201.9 |
| Other financing(1) | 85.8 | 96.2 |
| Accrued interest | 53.7 | 41.5 |
| Unamortised balance of transaction costs | (57.1) | (53.3) |
| **Total debt financing** | **4,110.6** | **3,785.7**(2) |

(1) Excludes accrued interest.

(2) As reflected in the balance sheet of the Interim Financial Statements.

***Major Indebtedness***

A syndicated facility with EBRD was entered into in December 2007 and subsequently amended in March 2008, for a maximum amount of €600 million of which €200 million had been drawn as at 31 March 2008. As at the date of this Prospectus, the facility is fully drawn. The facility expires in 2017 with the outstanding amount being amortised from 2009 until the expiration date.

On 24 February 2004, Citigroup Global Markets Deutschland AG & Co. ("**Citigroup Germany**") issued US dollar denominated loan participation notes in an aggregate principal amount of US$325 million for the sole purpose of financing a loan facility between the Company and Citigroup Germany. The loan is due on 24 February 2009 and bears interest at an annual interest rate of 8.625 percent payable on 24 February and 24 August of each year. With effect from 30 June 2008, the Issuer was substituted in place of Citigroup Germany as the issuer of these notes.

On 19 April 2004, Citigroup Germany issued US dollar denominated loan participation notes in an aggregate principal amount of US$375 million for the sole purpose of financing a loan facility between the Company and Citigroup Germany. The loan is due on 19 April 2014 and bears interest at an annual interest rate of 9.25 percent payable on 19 April and 19 October of each year. With effect from 30 June 2008, the Issuer was substituted in place of Citigroup Germany as the issuer of these notes.

On 11 June 2008, Sparrows Point entered into a revolving credit facility with Citicorp USA, Inc. and J.P. Morgan Securities Inc. for US$490 million at a variable rate of interest. The facility is scheduled to terminate in June 2013. The facility is secured by, among other things, receivables and inventories and is not guaranteed by the Company.

Total debt was contractually repayable as at the balance sheet date as follows:

| | 31 March 2008 | 31 December 2007 |
|---|---|---|
| | (US$ millions) | |
| Less than one year | 1,257.6 | 972.7 |
| Between one and five years | 1,398.1 | 1,924.4 |
| After more than five years | 1,454.9 | 888.6 |
| **Total debt financing** | **4,110.6** | **3,785.7**(1) |

(1) As reflected in the balance sheet of the Interim Financial Statements.

### *Commitments and contingencies*

As at 31 March 2008, the Group had capital commitments of US$965.5 million. In the normal course of business, the Group enters into long-term contracts for supply of raw materials and sales of its products. These contracts allow for periodic adjustments in prices depending on prevailing market conditions.

### *Guarantees*

As at 31 March 2008, the Group had US$130.1 million of guarantees issued compared to US$143.2 million as at 31 December 2007.

## QUANTITATIVE AND QUALITATIVE DISCLOSURE ON MARKET RISK

Exposure to credit, liquidity, interest rate and currency risk arises in the normal course of the Group's business. The Russian Steel, Metalware and Mining segments do not currently use derivative financial instruments to reduce exposure to fluctuations in foreign currency exchange rates and interest rates.

The Group believes that the fair value of its financial assets and liabilities approximates the respective carrying amounts, except for the following long-term fixed rate borrowings:

| | As at 31 March 2008 | | |
|---|---|---|---|
| | Market value | Book value | Difference |
| Citibank CLN — Eurobonds 2009(1) | 334,120 | 325,000 | 9,120 |
| Citibank CLN — Eurobonds 2014(1) | 400,651 | 375,000 | 25,651 |
| | 734,771 | 700,000 | 34,771 |

(1) Excludes accrued interest.

### *Credit risk*

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet and guarantees. The Group has developed policies and procedures for the management of credit exposures, including establishing credit committees that actively monitors credit risk.

### *Liquidity risk*

The Group maintains liquidity management with the objective of ensuring that funds will be available at all times to honour cash flow obligations as they become due by preparing annual budgets, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

### *Foreign currency exchange risk*

The Group incurs foreign currency exchange risk when Group entities enter into transactions and balances not denominated in their functional currency. The Group has assets and liabilities denominated in several foreign currencies. Foreign currency exchange risk arises when the actual or forecasted assets in a foreign currency are either greater or less than the liabilities in that currency. The Group's management performs foreign currency exchange rate sensitivity analysis on a yearly basis. For an analysis of such results for

31 December 2005 (restated), 2006 (restated) and 2007 see note 33 to the Annual Financial Statements beginning on page F-69 of this Prospectus.

***Interest rate risk***

Interest rates on the Group's debt financing are either fixed or variable, at a fixed spread over LIBOR or Euribor for the duration of each contract. Changes in interest rates impact primary loans and borrowings by changing either their fair value, as with fixed rate debt, or their future cash flows, as with variable rate debt. The Group's management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising additional debt financing, the Group uses its judgment to decide whether a fixed or variable rate would be more favourable over the expected term.

The following table sets forth the amount of fixed and variable rate instruments as at 31 March 2008:

| | *(US$ millions)* |
|---|---|
| **Fixed rate instruments** | |
| Financial assets | 4,946.5 |
| Financial liabilities | (3,759.6) |
| | 1,186.9 |
| **Variable rate instruments** | |
| Financial assets | 486.0 |
| Financial liabilities | (2,563.8) |
| | (2,077.8) |

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and annualised profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant.

| | **Net profit or loss** | |
|---|---|---|
| | **100 bp increase** | **100 bp decrease** |
| | *(US$ millions)* | |
| **31 March 2008** | | |
| Variable rate instruments | | |
| Financial assets | 3.3 | (3.3) |
| Financial liabilities | (15.1) | 15.1 |
| Cash flow sensitivity (net) | (12) | 12 |

## Significant Accounting Policies, Critical Accounting Judgments and Estimates

The Group believes that its most significant accounting policies and it critical accounting judgments and estimates are those described below.

### Significant accounting policies

The Group believes that its most significant accounting policies to be those described below.

***Basis of consolidation***

*Subsidiaries*

Subsidiaries are those enterprises controlled, directly or indirectly, by the Company. The financial statements of subsidiaries are included in the Financial Statements from the date that control effectively commences until the date that control effectively ceases. The minority interest represents the minorities' proportion of the net identifiable assets of the subsidiaries, including the minorities' share of fair value adjustments on acquisitions.

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, are eliminated in preparing the Financial Statements.

*Investments in associates*

Associates are those enterprises in which the Group has significant influence, but does not have control over the financial and operating policies. The Financial Statements include the Group's share of the total recognised gains and losses of associates accounted for on an equity accounting basis, from the date that significant influence effectively commences until the date that significant influence effectively ceases. When the Group's share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

*Interests in joint ventures*

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity that is subject to joint control, which is when the strategic financial and operating policy decisions relating to the activities of the joint venture require the unanimous consent of the parties sharing control.

Where a Group entity undertakes its activities under joint venture arrangements directly, the Group's share of jointly controlled assets and any liabilities incurred jointly with other venturers are recognised in the financial statements of the relevant entity and classified according to their nature. Liabilities and expenses incurred directly in respect of interests in jointly controlled assets are accounted for on an accrual basis. Income from the sale or use of the Group's share of the output of jointly controlled assets, and its share of joint venture expenses, are recognised when it is probable that the economic benefits associated with the transactions will flow to/from the Group and their amount can be measured reliably.

Joint venture arrangements that involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly controlled entities. The Group reports its interests in jointly controlled entities using the equity method.

Where the Group transacts with its jointly controlled entities, profits and losses are eliminated to the extent of the Group's interest in the joint venture.

*Accounting for business combinations of entities under common control*

IFRS provides no guidance on accounting for business combinations of entities under common control. Management adopted the accounting policy for such transactions based on the relevant guidance of accounting principles generally accepted in the United States ("**US GAAP**"). Management believes that this approach and the accounting policy disclosed below are in compliance with IFRS.

Acquisitions of controlling interests in companies that were previously under the control of the same controlling shareholder as the Group have been accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date on which control was obtained by the common controlling shareholder. The assets and liabilities acquired have been recognised at their book values. The components of equity of the acquired companies have been added to the same components within Group equity except that any share capital of the acquired companies has been recorded as part of additional paid in capital. Cash consideration for such acquisitions has been recognised as a liability to or a reduction of receivables from related parties, with a corresponding reduction in equity, from the date the acquired company is included in the Financial Statements until the cash consideration is paid. The Company's shares issued in consideration for the acquired companies are recognised from the moment the acquired companies are included in these Financial Statements.

Acquisitions by the Controlling Shareholder of additional interests in the acquired companies, after control over those companies has been obtained by the Controlling Shareholder, are treated as if those additional interests were acquired by the Group. No goodwill is recognised on these transactions. The difference between the share of net assets acquired and the cost of investment is recognised directly in equity.

*Goodwill*

Goodwill arising on the acquisition of a subsidiary, associate or a jointly controlled entity represents the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary, associate or jointly controlled entity recognised at the date of acquisition. Goodwill is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill in respect of subsidiaries is disclosed as an intangible asset and goodwill relating to associates and jointly controlled entities is included within the carrying value of the investments in these entities.

Where an investment in subsidiary, associate or jointly control entity is made, any excess of the Group's share in the fair value acquiree's of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition is recognised in the income statement immediately.

***Foreign currency***

Transactions in foreign currencies are translated to the functional currency of each entity at the foreign exchange rate ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the functional currency of each entity at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies are translated to the functional currency of the entity at the foreign exchange rate ruling at the date of the transaction. Foreign exchange gains and losses arising on translation are recognised in the income statement.

***Property, plant and equipment***

Property, plant and equipment are carried at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. In the case of assets constructed by the Group, related works and direct project overheads are included in cost. Repair and maintenance expenses are charged to the income statement as incurred. Gains or losses on disposals of property, plant and equipment are recognised in the income statement.

Depreciation is provided so as to write off property, plant and equipment over its expected useful life. Depreciation is calculated using the straight line basis, except for depreciation on vehicles and certain metal-rolling equipment, which is calculated on the basis of mileage and units of production, respectively. The estimated useful lives of assets are reviewed regularly and revised when necessary.

The principal periods over which assets are depreciated are as follows:

| | |
|---|---|
| Buildings and constructions | 20-50 years |
| Plant and machinery | 10-20 years |
| Other productive assets | 5-20 years |
| Community and infrastructure assets | 5-50 years |

***Leases***

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

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

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the income statement as part of interest expense.

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

***Financial assets***

Financial assets include cash and cash equivalents, investments, and loans and receivables.

Cash and cash equivalents comprise cash balances, cash deposits and highly liquid investments with original maturities of three months or less, that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

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

***Financial liabilities***

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

*Financial liabilities at FVTPL*

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

A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking.

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

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial instruments, which are managed and performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability.

*Other financial liabilities*

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Borrowing costs on loans specifically for the purchase or construction of a qualifying asset are capitalised as part of the cost of the asset they are financing.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised in the income statement.

***Revenue recognition***

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

**Critical accounting judgments and estimates**

Preparation of the consolidated financial statements in accordance with IFRS requires the Group's management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of financial statements, and the reported amounts of revenues and expenses during the reporting period. The determination of estimates requires judgments which are based on historical experience, current and expected economic conditions, and other available information. Actual results could differ from those estimates.

The most significant areas requiring the use of management estimates and assumptions relate to:

- useful economic lives of property, plant and equipment;
- impairment of assets;
- allowances for doubtful debts, obsolete and slow-moving raw materials and spare parts;
- decommissioning liabilities;
- retirement benefit liabilities;
- deferred income tax assets; and
- contingencies.

*Useful economic lives of property, plant and equipment*

The Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end and, 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 on depreciation expense for the period.

*Impairment of assets*

The Group reviews the carrying amount of its tangible and intangible assets to determine whether there is any indication that those assets are impaired. In making the assessments for impairment, assets that do not generate independent cash flows are allocated to an appropriate cash-generating unit. Management necessarily applies its judgment in allocating assets that do not generate independent cash flows to appropriate cash-generating units, and also in estimating the timing and value of underlying cash flows within the value in use calculation. Subsequent changes to the cash generating unit allocation or to the timing of cash flows could impact the carrying value of the respective assets.

*Allowances for doubtful accounts*

The Group makes allowances for doubtful receivables 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 current overall economic conditions, the ageing of accounts receivable balances, historical write-off experience, customer creditworthiness and changes in payment terms. Changes in the economy, industry or specific customer conditions may require adjustments to the allowance for doubtful accounts recorded in the Financial Statements.

*Provision for obsolete inventory*

The Group makes a provision for obsolete and slow-moving raw materials and spare parts. In addition, certain finished goods of the Group are carried at net realisable value. Estimates of net realisable value of finished goods are based on the most reliable evidence available at the time the estimates are made. These estimates take into consideration fluctuations of price or cost directly relating to events occurring subsequent to the balance sheet date to the extent that such events confirm conditions existing at the end of the period.

*Decommissioning Liability*

The Group reviews its decommissioning liability, representing site restoration provisions, at each balance sheet date and adjusts it to reflect the current best estimate in accordance with IFRIC 1 "Changes in Existing Decommissioning, Restoration and Similar Liabilities". The amount recognised as a provision is the best estimate of the expenditures required to settle the present obligation at the balance sheet date based on the requirements of the current legislation of the country where the respective operating assets are located. The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Considerable judgment is required in forecasting future site restoration costs. Future events that may affect the amount required to settle an obligation are reflected in the amount of a provision when there is sufficient objective evidence that they will occur.

*Retirement Benefit Liability*

The Group uses an actuarial valuation method for measurement of the present value of post-employment benefit obligations and related current service cost. This involves the use of demographic assumptions about the future characteristics of the current and former employees who are eligible for benefits (mortality, both during and after employment, rates of employee turnover, disability and early retirement, etc.) as well as financial assumptions (discount rate, future salary and benefit levels, expected rate of return on plan assets, etc.).

*Deferred Income Tax Assets*

Deferred tax assets are reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. The estimation of that probability includes judgments based on the expected performance. Various factors are considered to assess the probability of the future utilisation of deferred tax assets, including past operating results, operational plans, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from these estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected. In the event that the assessment of future utilisation of deferred tax assets must be reduced, this reduction will be recognised in the income statement.

*Contingencies*

By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. The assessment of such contingencies inherently involves the exercise of significant judgment and estimates of the outcome of future events.

**Provisions**

***Retirement benefits***

The Group pays retirement and post-employment medical benefits to former employees. The Group's net obligation in respect to defined retirement benefit plans is calculated separately for each defined benefit plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to its present value and the fair value of any plan assets is deducted. The discount rate used is the yield at the balance sheet date on government bonds that have maturity dates approximating the terms of the Group's obligations. The calculation is performed annually by management using the projected unit credit method. Any actuarial gain or loss arising from the calculation of the retirement benefit obligation is fully recognised in the current year's income statement.

***Decommissioning liability***

The Group has environmental liabilities related to restoration of soil and other related works, which are due upon the closures of certain of its production sites. The Group generally estimates provisions related to environmental issues on a case-by-case basis, taking into account applicable legal requirements. A best estimate, based on available information, is calculated, provided that the available information indicates that the loss is probable. Decommissioning liabilities are estimated using existing technology, at current prices, and discounted using a real discount rate.

# INDUSTRY

*The following information includes extracts from publicly available information, data and statistics and has been extracted from official sources and other sources the Company believes to be reliable. The Company accepts responsibility for accurately reproducing such information, data, and statistics and as far as the Company is aware, no facts have been omitted that would render such information misleading. The Company accepts no further responsibility in respect of such information, data and statistics. Such information, data and statistics may be approximations or use rounded numbers.*

## Steel Industry

### Global Overview

The global steel industry is affected by a combination of factors, including periods of economic growth or recession, worldwide production capacity and the existence of, and fluctuations in, steel imports and protective trade measures. Steel prices respond to supply and demand and fluctuate in response to general and industry-specific economic conditions.

The steel industry is cyclical and highly competitive and historically has been characterised by excess world supply. From 1997 to 2001, the business environment in the steel industry was challenging, resulting in financial difficulties for a number of steel companies. At the same time, difficult market conditions encouraged several companies to implement operational efficiency programmes in order to improve their respective financial profiles. By 2004, worldwide supply and demand were more in balance and supply was constrained by the availability of raw materials largely due to growing demand in China. This led to substantial price increases that continued into early 2005. In the second half of 2005, there was downward pressure on prices due in part to increased steel production in China. Prices have strengthened again recently as worldwide supply and demand have returned to a more balanced position. At the same time, the steel sector has had to face increasing raw materials and energy costs, particularly for iron ore and coal towards the end of 2007 and into 2008. In 2008, the price of steel has also begun to reflect rising raw material costs, with steel prices in several markets increasing significantly.

The steel industry operates predominantly on a regional basis as a result of the high cost of transporting steel. However, despite the limitations associated with transportation costs, as well as the restrictive effects of protective tariffs, duties and quotas, levels of global imports and exports have generally increased in the last decade as production has shifted towards low-cost production regions such as China and the CIS, which includes Russia, Ukraine and other former Soviet states.

While steel production has historically been concentrated in the EU, North America, Japan and the former Soviet Union, steel production in China and elsewhere in Asia has grown in importance over the past decade. In 2007, China was the largest single producer of steel in the world, producing approximately 489 million tonnes of crude steel, as well as the largest consumer of steel, consuming more than 434 million tonnes of crude steel. According to the International Iron and Steel Institute, ("**IISI**") China's steel production in 2007 increased 15.7 percent from 2006, accounting for 36.4 percent of global steel production. This represents a reduction in the rate of growth from the 18.8 percent achieved in 2006, 26.8 percent in 2005 and 26.1 percent in 2004. The value of the global steel market was estimated to be US$958 billion at the end of 2005. According to the IISI, world crude steel output was 1,343.5 million tonnes in 2007, the highest historical level of output to date and representing an increase of 7.5 percent compared to output in 2006. It was also the fifth consecutive year that world crude steel production grew by more than 7 percent.

The following table sets forth estimated crude steel production data by country or region for 2003 through 2006:

| World Crude Steel Production | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|
| | | *(million tonnes)* | | |
| European Union (consisting of 25 countries) | 184.5 | 194.2 | 187.2 | 198.5 |
| Other Europe | 29.3 | 32.1 | 33.2 | 36.4 |
| CIS | 106.2 | 113.1 | 112.9 | 119.8 |
| US | 93.7 | 99.7 | 94.9 | 98.6 |
| North America (excluding the US) | 32.5 | 35.2 | 32.7 | 33.1 |
| South America | 43.0 | 45.9 | 45.3 | 45.3 |
| Middle East/Africa | 29.7 | 31 | 33.3 | 34.2 |
| China | 222.3 | 280.5 | 355.8 | 422.7 |
| Japan | 110.5 | 112.7 | 112.5 | 116.2 |
| Asia (excluding China and Japan) | 109.6 | 116.8 | 129.7 | 136.7 |
| Oceania | 8.4 | 8.3 | 8.6 | 8.7 |
| **World total** | **969.7** | **1,068.7** | **1,146.2** | **1,250.0** |
| *Annual change (percent)* | *7.3* | *10.2* | *7.3* | *9.1* |

Source: IISI

While production in Europe, Japan and the United States remains significant, steel producers in those regions have increasingly focused on rolling and finishing of semi-finished products. The industry is currently seeing a shift in demand from "commodity steel" to "high value-added steel" or "specialised steel" in developed markets.

The term "commodity steel" refers to low-grade steel used primarily for construction and in other basic structural components. Asian steel producers have emerged as the largest producers of commodity steel, as the majority of consumption of commodity steel is in Asian and other emerging markets. The terms "high value-added steel" or "specialised steel" refer to high-grade steel, typically produced with varying alloys to improve strength and/or durability. High value-added steel is used primarily by the automotive, aerospace and railway industries. Prices and margins for high value-added steel tend to be higher than for commodity steel due to the unique structural/chemical characteristics of high-value added steel which end users of high value-added steel typically require.

The following table sets forth estimated crude steel consumption data by country or region for 2003 through 2006.

| World Crude Steel Consumption | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|
| European Union (consisting of 25 countries) | 180.5 | 189.1 | 181.3 | 205.8 |
| Other Europe | 27.9 | 31.3 | 33.5 | 40.1 |
| CIS | 41.5 | 44.9 | 51.5 | 60.5 |
| US | 105.8 | 123.8 | 113.3 | 128.5 |
| North America (excluding the US) | 40.3 | 44.3 | 43.2 | 47.5 |
| South America | 28.8 | 34.1 | 33.7 | 38.1 |
| Middle East/Africa | 53.7 | 55.8 | 62.7 | 68.6 |
| China | 258.6 | 296.6 | 353.0 | 384.3 |
| Japan | 76.4 | 80.5 | 82.9 | 83.3 |
| Asia (excluding China and Japan) | 151.2 | 163.3 | 167.5 | 173.8 |
| Oceania | 8.2 | 8.8 | 8.7 | 8.6 |
| **World total** | **973.0** | **1,072.5** | **1,131.2** | **1,239.1** |
| *Annual change (percent)* | *7.2* | *10.2* | *5.5* | *9.5* |

Source: IISI

Despite producing significant quantities of steel, the United States is a net importer of steel, showing negative steel production growth in the first three quarters of 2007 but showing a turnaround in the fourth quarter with three consecutive months of growth, according to IISI. By contrast, China, Japan and Russia are net exporters of steel. In 2007, the top three steel producing countries were China (producing 489.0 million tonnes), Japan (producing 120.2 million tonnes), and the United States (producing 97.2 million tonnes). Major traded steel products worldwide include semi-finished products, hot and cold-rolled sheets and coils, steel tubes and fittings, galvanised sheet, wire rod and angles and sections.

The strategy and product mix of steel producers generally varies between producers in industrial countries and producers in emerging markets. Historically, commodity steel producers in industrialised countries had limited export markets due to the high cost of transporting steel relative to the low value of commodity steel grades. In the second half of the twentieth century, producers in emerging markets began to compete with steel producers in industrialised countries by taking advantage of the lower manufacturing costs in their countries to offset high transportation costs. In response, producers in Western Europe and Japan invested heavily in new technology and capacity to produce high value-added steel grades in order to differentiate their product portfolio and protect their margins by reducing their exposure to commodity steel prices. However, these similar and simultaneous investments resulted in production overcapacity and put pricing pressures on value-added segments. Recently, the growth and consolidation of both steel consumers and raw material suppliers has weakened the bargaining power of steel producers and put further pressure on their margins. Steel producers have responded with a phase of industry consolidation. In 2002, Usinor, Arbed and Aceralia in Europe merged to form Arcelor, and Kawasaki Steel and NKK in Japan merged to form JFE. In 2002, Nucor acquired the assets of Birmingham Steel and International Steel Group, or ISG, acquired the assets of Acme, LTV and Bethlehem Steel in the United States. In 2004, Ispat International NV and LNM Holdings NV, which comprised the LNM Group, merged to form Mittal Steel, and in early 2005 Mittal Steel merged with ISG.

Consolidation has enabled steel companies to lower their production costs, has allowed for more stringent supply-side discipline, including through selective capacity closures, and has enabled some steel companies to maintain pricing power. Despite the recent consolidation, the global steel market remains highly fragmented. In 2006, the five largest producers — Arcelor Mittal (117.2 million tonnes); Nippon Steel (34.7 million tonnes); JFE Steel (32.0 million tonnes); POSCO (30.1 million tonnes); and Baosteel (22.5 million tonnes) — accounted for approximately 18.9 percent of total worldwide steel production, with Arcelor Mittal, the largest, accounting for 9.4 percent. The 20 largest steel producers accounted for approximately 38.7 percent of total global steel production in 2006.

The recent Arcelor-Mittal merger reflects the desire of many steel companies to integrate and consolidate in order to maintain pricing power and margin stability through the cycle. The steel industry remains one of the most fragmented industrial sectors and is widely affected by economic cycles. Further merger and acquisition activity is expected in the future as industry players look to acquire greater influence over market pricing, thereby reducing their vulnerability to future declines in demand. Industries including automotive and aerospace are similarly affected by economic cycles and have sought to consolidate in order to minimise fluctuations in prices and margins throughout the cycle.

**Russian Steel Industry**

The Soviet Union produced approximately 160 million tonnes of crude steel a year at the end of the 1980s. Following the collapse of the Soviet Union, the steel industry suffered a substantial decline in production, to about 75 million tonnes of crude steel for all the newly independent states combined in 1997. At that point, Russia was producing approximately 38 million tonnes of rolled products annually.

However, steel production started to recover following the devaluation of the Rouble in 1998 due in part to the significant cost benefits that steel exporters experienced in 1999 and 2000. While the major mills were export-oriented and their sales receipts were mostly US dollar-based, their operating costs fell substantially in US dollar terms following the devaluation. In addition, the strength of steel prices in 2000 led to increased capacity utilisation rates, even at technologically inferior mills. Though steel prices decreased in the second half of 2001 and the first half of 2002, beginning in the third quarter of 2002 the steel market demonstrated robust recovery in terms of both prices and volumes. According to IISI, in 2003, 2004, 2005, 2006, and 2007, production of steel grew approximately 7.3 percent, 10.2 percent, 7.3 percent, 9.1 percent, and 7.5 percent, respectively, compared to the previous year.

***Privatisation of the Russian steel industry.*** Privatisation of the Russian steel industry began in 1993 and was primarily "insider" focused, meaning that factories were sold to their employees and management. The privatisation programme provided for Roskommetallurgiya (successor to the USSR Ministry of Metals) to supervise the privatisation process, but no special regime was implemented for the privatisation of the steel industry and accordingly the number of state-owned steel companies declined rapidly so that, by mid-1994, the state's shareholding in iron and steel production companies amounted only to 15 to 25 percent. By the end of 1995, control over most of the largest Russian steel producers such as the Group, MMK, Mechel and NLMK was transferred to private management and ownership. However, because no plan for the privatisation of the steel industry was ever put in place, the state failed to attract the required investment, technology and know-how into this sector. Therefore, starting in 1995, the Russian Government changed the method of privatisation to attract strategic investors into the sector. Pursuant to an edict of President Yeltsin, a holding company, OAO Rossiyskaya Metallurgiya, was established, to which 10 percent stakes in steel-producing companies remaining in state ownership and 100 percent stakes in five leading steel-production scientific-research institutes were transferred. The Russian Government intended to sell 49 percent of shares in OAO Rossiyskaya Metallurgiya, thus retaining control over the companies and attracting investments at the same time. However, investors did not show any interest in the project and OAO Rossiyskaya Metallurgiya was liquidated in 1997. Stakes in several companies were sold in cash auctions. Stakes in the remaining companies were retransferred into the ownership of the Ministry of Property Relations.

The Russian steel industry is now consolidated among six large producers including the Group, Evraz Group SA ("**Evraz**"), OJSC Novolipetsk Steel ("**NLMK**"), OJSC Magnitogorsk Iron & Steel Works ("**MMK**"), Metalloinvest and OAO Mechel ("**Mechel**"). These producers largely control the domestic Russian market.

***Russian steel production.*** In 2007, Russia ranked as the world's fourth-largest producer of steel, producing 72.2 million tonnes of steel, or approximately 5.4 percent of global production. The metals and mining sector is one of the most important sectors of the Russian economy. Russian enterprises produce a wide range of metal products for the domestic economy, in particular for the oil and gas, defence and construction industries.

***Russian market.*** Russian steel production decreased from 1991 through 1998 as a result of the general economic decline in Russia during this period and the consequent reduced demand from the primary steel product consumers: the construction, infrastructure and engineering industries and the military sector. Consumption of rolled steel products in Russia has followed a U-shaped trend since 1990. Consumption was 65 million tonnes in 1990 and then declined steadily, due to reduced consumption by heavy industry, to only 18 million tonnes in 1998. However, the devaluation of the Rouble in 1998 resulted in economic growth and a sharp increase in domestic demand for steel products, and by 2006, Russia's total steel consumption had increased to 42.8 million tonnes, according to IISI.

***Export market.*** Asia, the Middle East and the EU are the primary export destinations for Russian steel producers. In 2006, Russian producers exported 31.5 million tonnes of semi-finished and finished steel products, according to IISI.

**Steel Production Process**

The key stages of the steel production are coke making, iron making, steelmaking and steel rolling. Steel companies actively seek captive iron ore and coking coal resources to ensure a secure supply of raw materials for their steel production.

Following is a brief summary of these processes.

***Coke making.*** Coke is a solid product of coal coking. Coke usually contains 84 to 91 percent carbon and is used as the main fuel in blast furnaces. Coke is produced by heating of the prepared coal charge in the absence of oxygen at temperatures of 900 to 1,200 degrees Celsius (pyrolysis) for 14 to 18 hours in the coke ovens. After discharge from the ovens, coke is delivered to the blast furnaces for further use in iron making.

Other products of the traditional by-product coking process include coke-oven gas and various by-products separated from the coke-oven gas. Coke-oven gas may be used as gaseous fuel in coking and other shops of the steel plant, as well as in adjacent power generation. The other by-products are further processed by the designated on-site shops and eventually sold onto the third-party customers.

***Iron making.*** Prepared iron ore raw materials (sinter and pellets) and coke are used for hot metal production. Coke and natural gas serve as fuel for the blast furnaces. Coke-oven gas, together with top gas from the blast furnaces, is used as fuel for the heating of the stoves. Sinter, pellets and coke are layered and fed into a blast furnace from the top. Fuel combustion, reduction of iron from oxides, carbonisation of iron with partial reduction of silicon and manganese, melting of all components of burden and slag-making all occur inside a blast furnace.

Once formed, hot metal sinks to the bottom of the blast furnace where it is tapped off into the torpedo cars and delivered to the steel making shop to be converted into steel. Hot metal can also be delivered to a pig iron casting machine that produces pig iron for sale as a semi-finished product. Slag from the blast furnaces is recycled and further used in a variety of industries.

At many steel plants, top gas generated in the blast furnaces during the iron making process is also used as a fuel for stoves, coke ovens, boilers, rolling mills and other purposes.

***Steel making.*** Steel is produced from hot metal and/or steel scrap and scrap substitutes using one of the following three technologies.

*Basic oxygen furnace (BOF).* The oxygen converter process is based on the interaction of process oxygen (practically pure oxygen) with the molten charge bath. By blowing oxygen through the bath, the carbon content is reduced and the charge is transformed into low-carbon steel.

Scrap and hot metal are charged into the vessel and oxygen is then blown via a lance into the vessel, oxidising carbon and other impurities (silicon, manganese, etc.), thus lowering the carbon content of the molten charge and partially removing undesired chemical elements. Fluxes, such as metallurgical lime and other, are fed into the vessel to form slag, which absorbs undesired impurities during the steel making process. The steel is then poured into a steel ladle where alloying materials can be added.

The oxygen converter process is generally considered to be the most efficient steelmaking route for producing large volumes of high-quality steel.

*Electric arc furnace process (EAF).* In electric arc furnaces the scrap and other charge elements are being melt by the heat generated by electricity arcing between graphite electrodes and the metallic charge. The key equipment components of the EAF are: a furnace shell, a retractable roof, a graphite electrode arm, a tilting device and a furnace transformer.

The EAF production process consist of charging, melting, oxidation and tapping.

The EAF charge consists of scrap and scrap substitutes, such as DRI/HBI or pig iron, and sometimes hot metal, as well as fluxes. In some furnace designs, charge materials can be added in batches or continuously fed during the melting process.

Once melting stage is completed, the steel is tapped out into a preheated ladle. Often some liquid steel is left in the furnace to facilitate the melting of the next charge.

*Open hearth process.* In the open hearth process the steel is produced by melting scrap, hot metal and other charge components by the radiation heat of the burners positioned above the charge materials surface.

Scrap and other components are charged into the furnace prior to heating. Fuel (such as natural gas, fuel oil etc) is burned to heat the scrap, hot metal is charged and slag is formed and flushed. During melting, the oxidation of carbon and other impurities (such as silicon and manganese) takes place. Fluxes, such as metallurgical lime and other, are used to form slag, which absorbs impurities during the steel making process.

Generally speaking, open hearth furnaces are disadvantaged by relatively high operating costs due to high levels of energy consumption, relatively low productivity, as well as prevailing combination with the ingot cast route. At the same time, open hearth allows higher flexibility in the raw materials use and under certain circumstances may be economically compatible with both EAF and BOF. The tendency of the world steel making industry has been gradual substitution of the open hearth production with either BOF or EAF routes.

***Steel rolling.*** Cast steel is a relatively weak mass of coarse uneven metal crystals or "grains". Rolling the steel makes this coarse grain structure re-crystallise into a much finer grain structure, giving greater toughness, shock resistance and tensile (stress) strength. Rolling is also the main method used to shape steel into different products.

Flat rolling process consists of passing the steel between two rolls revolving at the same speed but in opposite directions. The gap between the rolls is less than the thickness of the steel being rolled, resulting in the steel being reduced in thickness, at the same time, lengthened. In addition to hot rolling, where steel is reheated prior to rolling, it may also be further reduced without preheating in the process called cold rolling, resulting in a different set of properties.

## MINING INDUSTRY

### Iron Ore

The global iron ore industry is characterised by a high degree of consolidation, with BHP Billiton, Vale, and Rio Tinto accounting for approximately 80 percent of the global seaborne iron ore trade. The major iron ore producing countries are Australia, Brazil and China.

Iron ore production costs have declined in recent years, largely due to productivity enhancements. Freight rates remain a major cost constraint, constituting approximately half of total costs, according to Metal Bulletin, and helping to maintain the regional segregation of the industry. Iron ore prices increased during 2007 and have continued to rise in 2008, in response to strong global demand.

The following table sets forth iron ore production by country or region for the years 2000 through 2006:

| Iron ore production | 2002 | 2003 | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|
| China | 231.4 | 261.1 | 310.1 | 426.2 | 588.2 |
| Brazil | 225.1 | 245.6 | 270.5 | 292.4 | 318.6 |
| Australia | 187.2 | 212.0 | 234.7 | 257.5 | 275.1 |
| CIS | 158.7 | 171.2 | 181.3 | 181.8 | 195.4 |
| India | 86.4 | 99.1 | 120.6 | 145.5 | 165 |
| US | 51.3 | 48.5 | 54.7 | 54.3 | 53.0 |
| South Africa | 36.5 | 38.1 | 38.3 | 39.5 | 41.2 |
| European Union (consisting of 25 countries) | 23.0 | 24.4 | 24.9 | 26.0 | 26.1 |
| Other Europe | 5.4 | 4.7 | 5.2 | 8.0 | 8.4 |
| South America (excluding Brazil) | 32.9 | 32.6 | 34.9 | 36.7 | 38.5 |
| North America (excluding US) | 40.8 | 44.6 | 40.1 | 41.8 | 44.8 |
| **World Total** | **986.0** | **1,074.1** | **1,184.4** | **1,320.4** | **1,482.4** |
| *Annual Change (percent)* | *6.8* | *8.9* | *10.3* | *11.5* | *12.2* |

Source: IISI "Steel Statistical Yearbook 2007"

Historically, Europe, Japan and China have been the major iron ore consumption centres. Following an economic slowdown in 2001 and corresponding reduction in iron ore demand, markets rebounded in 2002, with China and certain countries in the CIS showing significant increases in demand in connection with increases in steel production in these countries. Since that time, global consumption of steel, and thus of iron ore, has significantly increased. China has experienced the highest growth in steel consumption, with an increase in demand of more than 111 percent from 205.7 million tonnes in 2002 to 434.4 million tonnes in 2007.

The major exporting countries of iron ore globally include Australia, Brazil and India, and the major importers are major steel producing countries: China, Japan, South Korea, and Germany.

***Russian market.*** According to IISI, total iron ore production in Russia in 2006 was approximately 103.8 million tonnes. Total iron ore exports were approximately 23.7 million tonnes, and total imports were approximately 10.1 million tonnes. Imports to Russia are generally limited by high transportation costs and the lack of port facilities in the Far East and on the Black Sea that are capable of handling large sizes of ore carrying vessels. Russian iron ore production is highly concentrated, and the four largest producers accounted for approximately approximately 84 percent of total iron ore production in Russia in 2006-2007.

Russian steel producers have increasingly sought to acquire control of iron ore production assets, and attained control over nearly all of the major Russian producers of iron ore by the end of 2004. For example, during 2004, Evraz acquired control over KGOK, NLMK acquired control over Stoilensky GOK, and Ural Steel acquired control over Mikhailovsky GOK. This trend continued in 2005-2007, as Evraz acquired a 50 percent stake in Yuzhkuzbassugol (owner and operator of coal mines in Novokuznetsk, Russia), Mechel acquired a 100 percent stake in Yakutugol (owner and operator of coal deposits in Sakha Republic of Russia) and the Group consolidated Severstal Resources, which included the significant coal mining operations of Vorkutaugol and, at that time, Kuzbassugol. Production of iron ore in Russia is concentrated in the Kursk region, representing the majority of Russian production, as well as in the northwest, Urals and Siberian districts. Iron ore produced in Russia is mainly magnetite, not hematite, which is common in Australia and Brazil.

***Production process.*** Approximately 90 percent of iron ore mined in Russia is extracted by open-pit methods, with the balance extracted from underground mines. After extraction, the ore is processed further in order to increase its iron concentration. The iron ore is then crushed to a powder-like consistency, and iron-rich particles are separated from the waste rock by magnetic separation to produce iron ore concentrate. This concentrate is then formed into pellets or sinter that are suitable for use as blast furnace feed.

To produce sinter, iron ore, iron ore concentrates and iron-bearing materials (blast furnace dust, screenings of sinter and pellets, scale, waste and slime), flux (limestone) and coke breeze are weighed and mixed to form sinter burden. This sinter burden is then granulated and laid in two layers in sinter machines. The sinter burden becomes sinter at temperatures of 1,070-1,200 degrees Celsius through the combustion of carbon from the coke breeze, while air is simultaneously drawn through the sinter burden by means of exhausters. After crushing, screening and cooling the sinter is ready for delivery to blast furnaces.

In producing iron ore pellets, iron ore concentrate is mixed with water and other additives, such as hentonite and limestone. The resulting slurry is baked at approximately 1,300 degrees Celsius. After the pellets have been screened and undersized material removed, they are prepared for use in blast furnaces.

***Coal***

Coal may be divided into steam (thermal) coal and coking (metallurgical) coal. Steam coal is used in electricity generation and industrial applications, while coking coal is used to manufacture coke for use in blast furnaces and other metallurgical applications. Coking coal swells when heated in coke ovens to produce hard coke, which characteristic is essential in steel making operations. Approximately 400-500 kilograms of coke is used per tonne of hot metal. Coke is supplemented by the direct injection of PCI at rates of 100-200 kilograms per tonne of hot metal. PCI uses less expensive semi-soft coking coal to reduce costs.

In recent years, the global coal industry has consolidated, partly as a result of oil companies and other non-mining companies exiting the sector. As a result of consolidation, coal suppliers have gained more pricing power.

Historically, Australia, China, Indonesia and South Africa have been the largest coal-producing countries, with Russia increasing its share of world supply in recent years.

***Russian market.*** Russia has the world's second largest coal reserves, after the United States. Its proven coal reserves total approximately 157 billion tonnes, accounting for 16 percent of the world's proven coal reserves. In 2007, Russia exported 93.2 million tonnes of coal, of which approximately 89 percent was steam coal and the balance was coking coal. Approximately 70 percent of Russia's coking coal production capacity was owned by or affiliated with Russian steel producers in 2007.

Coal production in Russia is concentrated in the Kuznetsk Basin and the Kansko-Achinskii Basin, which are east of the Ural Mountains and together account for the majority of Russia's total coal production.

Exports of coal from Russia have increased over the past several years. In 2007 Russian companies exported approximately 93.2 million tonnes of coal, a small increase from 92.1 million tonnes in 2006.

*Producers.* The following table presents the largest Russian coal producers in 2007:

| Company | Production *(million tonnes)* | Coal type |
|---|---|---|
| SUEK | 90.2 | Mostly steaming |
| Kuzbassrazrezugol | 43.1 | Mostly coking |
| Yuzhkuzbassugol | 12.0 | Mostly coking |
| South Kuzbass | 18.5 | Coking/steaming |
| Sibuglemet | 8.7 | Coking/steaming |
| SDS-Holding | 13.0 | Coking/steaming |
| Yakutugol | 10.3 | Mostly coking |
| Vorkutaugol | 6.5 | Coking/steaming |
| Raspadskaya | 13.6 | Coking |

Source: CDU TEK

***Production process.*** Approximately two-thirds of the coal mined in Russia is extracted by open pit methods, with the balance extracted from underground mining. At surface mines, a combination of shovels and draglines is used for moving coal and overburden after drilling and blasting. Production at underground mines in Russia is predominantly from long-wall mining. After mining, depending upon the amount of impurities in the coal, the coal is processed in a wash plant, where it is crushed and beneficiated. Coking coal is then transported to steel plants for conversion to coke for use in steel making. Steam coal is shipped to utilities that use it in boilers to generate steam used in producing electricity.

**Russian Methodologies for Reserve and Resource Reporting**

Severstal Resources has traditionally used Russia's long-established system of reserve and resource reporting, set forth by the Russian Federation Ministry of Natural Resources. In 2005, Severstal Resources began voluntarily using the internationally recognised JORC code of reserves and resource reporting (see "— International Reporting Methodologies"). All data relating to Severstal Resources' iron ore and coal reserves and resources summarised in this Prospectus is calculated by reference to estimates contained in a report issued by IMC Consulting Limited dated 14 August 2006 (adjusted for actual production since January 2006, and as further adjusted for the disposal of the Kuzbassugol mining complex in April 2008), which was prepared in accordance with JORC reporting standards, except Severstal Resources' expected reserves extension based on adjacent reserves acquisition.

The primary difference between Russian and international methodologies is that Russian methodologies rely on "geometrical" methods to determine reserves, as compared to international methodologies, which utilise sampling and extrapolation techniques.

According to the Russian system, deposits are classified into one of four classes, based on the complexity of their geological structure. This classification may take into account quantitative results measuring the inconsistencies in the basic features of mineralisation. This initial classification is intended to identify those resources warranting further study. Depending on the extent of further exploration, mineral resources are subsequently divided into "explored" and "evaluated" deposits. Explored deposits have been sufficiently explored to proceed with a feasibility study relating to commercial development, and evaluated deposits have been explored to the extent necessary to determine whether continued exploration is warranted. Resources that do not meet the standards for explored or evaluated deposits are classified as projected resources. Explored and evaluated deposits are further classified based on the type, quantity and quality of the measurements taken to evaluate the reserves.

Category A reserves include only explored deposits, and must meet the following criteria:

1. the sizes, forms and bedding conditions of the mineral body have been determined; the nature and regularities in their morphology and internal fabric have been studied; the barren and off-grade segments within the mineral bodies have been detected and mapped; and the locations and fault amplitudes of dislocations with a break have been identified;
2. the natural varieties of the minerals within the body have been determined; its categories and grades have been identified and mapped; its compositions and properties have been verified; and the quality

of all categories and grades of the identified minerals have been characterised in terms of all parameters stipulated by industrial regulations;

3. the distribution and forms of those valuable and noxious components found in the mineral body and products of its processing have been investigated; and
4. the mineral reserves have been mapped based on test wells, mine workings and detailed trial runs.

Category B reserves include only explored deposits. Category B reserves have been subject to a high level of investigation, though their boundaries have been determined with less accuracy than Category A reserves. Category B reserves meet the criteria established for Category A reserves, except that Category B reserves may contain a limited extrapolation zone that is substantiated on the basis of geological criteria and geophysical and geochemical research.

Category C1 reserves are characterised by a lower level of accuracy than the determination of Category B reserves. Most explored deposits are Category C1 reserves. Category C1 reserves meet the criteria established for Category B, except that additional extrapolation is permitted in mapping the mineral deposit.

Category C2 reserves consist of evaluated deposits. Category C2 reserves must meet the criteria established for Category C1, except that:

1. the sizes, forms, internal fabric and bedding conditions of the mineral body are confirmed by means of only a limited number of test wells and core samples; and
2. the boundaries of the deposit (including core samples and outcroppings) are mapped based on data gathered from only a limited number of test wells, and a geologically substantiated extrapolation of deposit parameters is permitted.

Resources that do not meet the standards for classification as A, B, C1 or C2 reserves may be classified as probable resources, in Categories P1, P2 or P3. Such deposits have undergone some exploration, but require further geological work in order to be upgraded to A, B, C1 or C2 reserves.

While a direct comparison between international and Russian reporting methodologies is difficult because each is founded on different principles, it is often the case that category A and B Russian reserves correlate to proved reserves, and C1 Russian reserves to probable reserves. However, these relationships may vary among deposits, and at different times for the same deposits.

**International Reporting Methodologies**

Several codes exist for reporting reserves in the international mining industry. The technical differences between these codes are minor, and results are generally comparable regardless of which methodology is employed in assessing a particular deposit. The principal reporting codes in current use are:

- United States Geologic Survey Circular 831 (United States);
- Ontario Securities Commission Instrument 43-101 (Canada);
- Australasian Joint Ore Reserves Committee ("**JORC**") Code (Australia);
- Institute of Materials, Minerals and Mining Reporting Code (United Kingdom and Ireland); and
- South African Institute of Mining and Metallurgy Reporting Code (South Africa).

Each of these codes recognises the difference between mineral resources and reserves. Conversion from a mineral resource to an ore reserve requires the application of "modifying factors", including mining, metallurgical, economic, marketing, legal, environmental, social and governmental factors. A "resource" is geologically defined; it becomes a "reserve" when the modifying factors, especially technical and economic factors, are taken into account. Each of these codes also includes strict guidelines for data quality and reporting in mining commodities.

The Council of Mining and Metallurgical Institutions ("**CMMI**"), which includes representatives of the major international standard-setting organisations, is currently working to establish a common international reporting code standard. CMMI has promulgated common definitions that have been adopted by each of its member organisations in their respective reporting codes, including the principal reporting codes noted above, and these definitions are also incorporated into reporting standards that have been adopted by the United Nations Economic Commission for Europe.

A *mineral resource* is a concentration or occurrence of material of intrinsic economic interest in or on the earth's crust, or deposit, in such a form, quality and quantity that there are reasonable prospects for eventual economic extraction. The location, quantity, grade, geological characteristics and continuity of a mineral resource are known, estimated or interpreted from specific geological evidence and knowledge. Mineral resources are subdivided, in order of increasing geological confidence, into inferred, indicated and measured categories. Portions of a deposit that do not have reasonable prospects for eventual economic extraction are not included as mineral resources.

An *inferred mineral resource* is that part of a mineral resource for which tonnage, grade and mineral content can be estimated with a low level of confidence. It is inferred from geological evidence and assumed but not verified geological and/or grade continuity, and based on information gathered through appropriate techniques from locations such as outcrops, trenches, pits, workings and drill holes which is limited or of uncertain quality and/or reliability.

An *indicated mineral resource* is that part of a mineral resource for which tonnage, densities, shape, physical characteristics, grade and mineral content can be estimated with a reasonable level of confidence. It is based on exploration, sampling and testing information gathered through appropriate techniques from locations such as outcrops, trenches, pits, workings, and drill holes. The locations are too widely or inappropriately spaced to confirm geological continuity and/or grade continuity but are spaced closely enough for continuity to be assumed.

A *measured mineral resource* is that part of a mineral resource for which tonnage, densities, shape, physical characteristics, grade and mineral content can be estimated with a high level of confidence. It is based on detailed and reliable exploration, sampling and testing information gathered through appropriate techniques from locations such as outcrops, trenches, pits, workings, and drill holes. The locations are spaced closely enough to confirm geological and/or grade continuity.

Ore reserves are the economically mineable parts of an indicated or measured mineral resource. Ore reserves take account of diluting materials and allowances for losses that may occur when the material is mined. Appropriate assessments, which may include feasibility studies, have been carried out on the deposit and include consideration of and modification by realistically assumed mining, metallurgical, economic, marketing, legal, environmental, social and governmental factors. These assessments establish that at the time of reporting extraction is reasonably justified.

A *probable ore reserve* is the economically mineable part of an indicated and, in some circumstances, a measured mineral resource.

A *proved ore reserve* is the economically mineable part of a measured mineral resource.

## BUSINESS

### Overview of the Group

The Group is an international, vertically-integrated metals and mining company that sells steel and mining products to customers across the world. According to Metal Bulletin, the Group was the world's 15th largest producer of crude steel in 2007, by volume of production. The Group is a full production cycle operation which includes iron ore and coal mining enterprises, steel mills and rolled product plants as well as downstream production and distribution businesses. The Group's production facilities are geographically diversified, with locations in Russia, the United States, Italy, France, Ukraine, the United Kingdom and Kazakhstan. With a focus on high value-added products in attractive niche markets and a successful track record of acquiring and integrating high-quality assets in the United States and Europe, the Group's corporate strategy is to improve its position as a leading global steel company in terms of profitability, with a vertically-integrated, low-cost business structure.

Following a reorganisation of the Group's management structure in April 2008, the Group comprises three business divisions: the Russian Steel Division, Severstal International, and Severstal Resources.

***Russian Steel Division.*** The Russian Steel Division produced approximately 16.4 percent of the total production of Russian crude steel in 2007, making it the third largest producer of crude steel products in Russia by volume of production in that year, in each case according to Chermet Corporation. The Russian Steel Division comprises three segments: the Russian Steel segment, Metalware and Izhora Pipe Mill.

- The Russian Steel segment consists primarily of the Group's steel production facilities in Cherepovets (the "**Cherepovets Steel Plant**"), high-grade automotive galvanising facilities at Severgal and Rolling Mill 5000, which the Group believes to be Russia's only rolling mill that produces 4.8 metre-wide high-quality hot-rolled plates, as well as various supporting functions for trading, maintenance and transportation. With total steelmaking capacity of 13.2 million tonnes of crude steel per year as at 31 December 2007, the Russian Steel segment produced 11.9 million tonnes of crude steel and 10.8 million tonnes of finished steel in 2007.
- Metalware comprises Severstal-Metiz's wire drawing and metalware manufacturing businesses in Russia, Ukraine and the United Kingdom. With total metalware production of 1.0 million tonnes, in 2007, Severstal-Metiz's production represented approximately 34.4 percent of domestic Russian metalware production, based on data from the Association of Metalware Producers of Russia, and approximately 33.2 percent of Ukrainian metalware production, based on data from the Association of Metalware Producers of Ukraine.
- The Izhora Pipe Mill comprises a large-diameter pipe mill in Russia. With total pipemaking capacity of 0.6 million tonnes as at 31 December 2007, Izhora Pipe Mill produced 0.3 million tonnes in 2007.

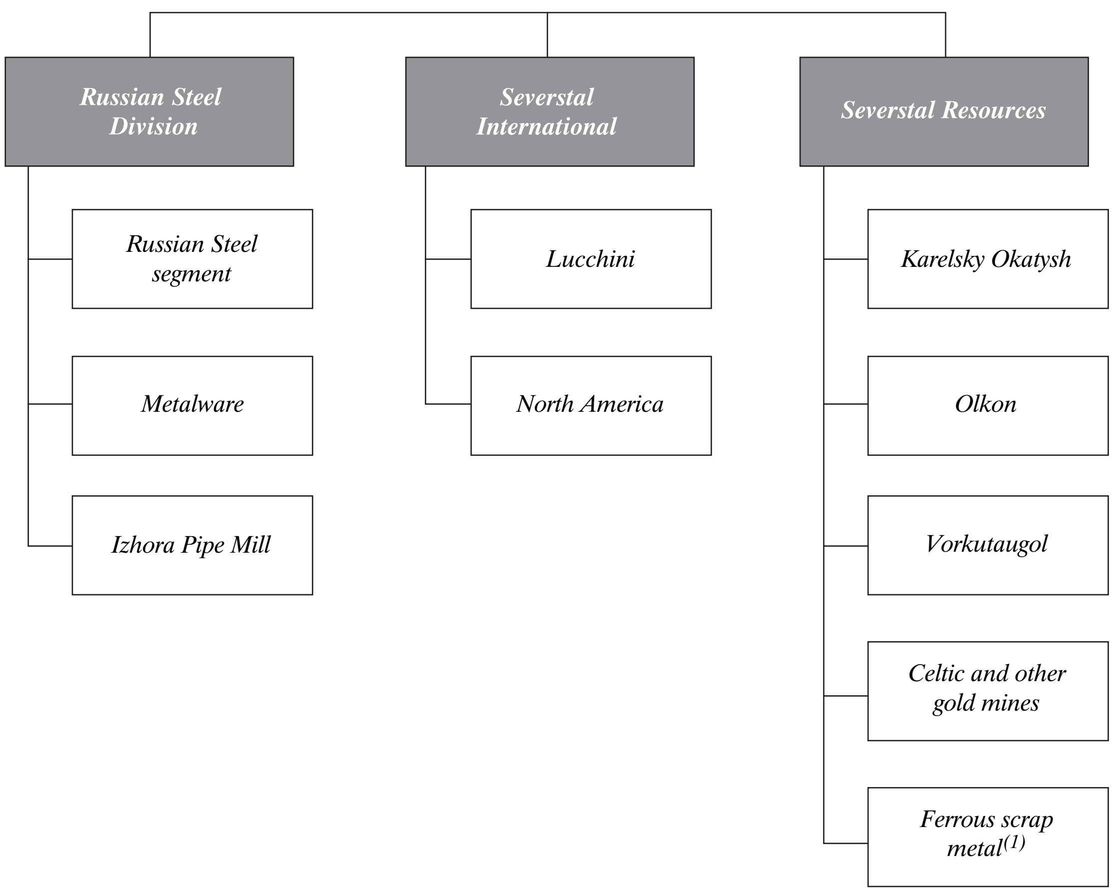
***Severstal International.*** Severstal International comprises two segments: North America and Lucchini.

- According to the Group's estimates, North America was the fourth largest integrated steel producer by volume of production in the United States in 2007. North America comprises Severstal North America, which is located in Dearborn, Michigan close to a large number of US steel customers, including several major automotive customers; SeverCorr, located in Columbus, Mississippi; and Sparrows Point steel plant, located in Baltimore, Maryland. In addition, the Group is in the process of acquiring further assets in the United States. See "— Recent Developments". North America currently has a total crude steelmaking capacity of 8.1 million tonnes per year, including the capacity of the recently acquired Sparrows Point steel plant and SeverCorr, which has been consolidated into the Group's financial results since January 2008. In 2007, prior to the acquisition of the Sparrows Point steel plant and excluding SeverCorr's production which was being ramped up upon commissioning of the plant, North America's total steel production was approximately 2.0 million tonnes of crude steel and 2.5 million tonnes of finished steel.
- Lucchini is one of the largest European producers of special quality long products by volume of production, based on the Group's estimates. Lucchini has several plants and service centres throughout Europe, with steelmaking capacity of approximately 4 million tonnes of crude steel per year, and total production in 2007 of approximately 3.6 million tonnes of crude steel. It operates in niche markets such as automotive, rails and wire rod. Lucchini comprises the Piombino business unit and the Ascometal business unit. Piombino is a well-known European producer of rails, bars and high-quality wire rods, and Ascometal is a well-known producer of high-quality, tailored products,

such as ingots, billets, blooms, bars, wire rod and drawn wire. Until its disposal in the second quarter of 2007, Lucchini also consisted of the Sidermeccanica business unit, a well-known European producer of rolling stock materials.

***Severstal Resources.*** Severstal Resources consists primarily of two iron ore complexes, Karelsky Okatysh and Olkon, and one coal mining complex, Vorkutaugol, each in northwest Russia, as well as gold mining assets in east Russia and in Kazakhstan and a ferrous scrap metal recycling business operating in northwest and central Russia. Severstal Resources was the second largest producer of iron ore pellets and coking coal (before accounting for the sale of the Kuzbassugol mining complex) in Russia in 2007, according to RudProm and CDU TEK, respectively. With the capacity to supply all of the current iron ore and hard coking coal needs of the Russian Steel Division, Severstal Resources forms the basis of the Group's balanced and vertically-integrated business model. With a focus on high value-added products, such as export quality iron ore pellets and coking coal concentrate, Severstal Resources had a total output of 14.7 million tonnes of iron ore and 9.4 million tonnes of coal in 2007. Severstal Resources estimates that, as at 31 December 2007, it had iron ore reserves and resources of approximately 710 million tonnes and 962 million tonnes, respectively, and coal reserves and resources of approximately 276 million tonnes and 27 million tonnes, respectively, based a report issued by IMC Consulting Ltd dated 14 August 2006, prepared in accordance with JORC reporting standards, adjusted for actual production since 1 January 2006, and as further adjusted for the disposal of the Kuzbassugol mining complex (consisting of the Berezovskaya and Pervomayskaya mines) in April 2008 as if it had occurred on 31 December 2007.

*The Group's Business Divisions*




Note:

(1) It is currently expected that with effect from 1 August 2008, management responsibility for the scrap operations is to be transferred to the Russian Steel Division.

The Group originally consisted of its core Russian steelmaking business, which was state-owned until its privatisation in 1993. Since that time, the Group has expanded by identifying attractive acquisition opportunities and by consolidating all of the steel and mining assets of the Group's controlling shareholder into its business. In addition to acquiring numerous production facilities in Russia, the Group acquired substantially all of the principal steelmaking and finishing assets of US steel producer Rouge Steel, subsequently renamed Severstal North America, in 2004. In June 2006, the Group acquired controlling interests in OAO Karelsky Okatysh, OAO Olkon, OAO Vorkutaugol, OAO Mine Vorgashorskaya, OAO Mine Pervomaiskaya and OAO Mine Berezovskaya, the last two of which were disposed of in the second quarter of 2008. On 2 October 2006, the Group acquired a controlling interest in European steel producer Lucchini SpA and in May 2007, increased its stake in Lucchini to 79.82 percent. In 2007, the Group purchased two gold mining operations in Russia, as well as gold mining licences in Russia. In 2008, the Group completed the acquisition of Celtic Resources Holdings plc, a company with subsidiaries holding gold mining assets in Kazakhstan. In January 2008, the Group acquired a controlling interest in SeverCorr, a steel mill in Columbus, Mississippi. In May 2008, the Group acquired Sparrows Point LLC, a steel plant located in Baltimore, Maryland ("**Sparrows Point**"). Also in May 2008, the Group made an offer to acquire all of the outstanding shares of common stock of Esmark Incorporated ("**Esmark**"), a manufacturer and distributor of flat rolled and other steel products in the United States. In July 2008, the Group acquired WCI Steel, which operates a steel mill in Warren, Ohio, after entering into an agreement to purchase it in May 2008. The Company is the ultimate parent company of the Group.

For more information, see "— History and Development of the Group" and "— Recent Developments".

## COMPETITIVE STRENGTHS

The Group has developed a variety of competitive strengths, which it believes provide it with a greater resilience, compared to some of its competitors, to the cyclical nature of the steel industry and a basis on which to build its position as a global metals and mining company.

### Vertically-Integrated Business with Access to Iron Ore and Coal

The Group is a vertically-integrated steel producer operating on a global scale. Its facilities span the full production cycle from iron ore and coal mining operations to steel mills and rolled product plants as well as downstream production and distribution businesses. Its mining operations in Russia, conducted by the Severstal Resources division, provide supplies of iron ore and coal to its production facilities in Russia, but also have the capacity to supply iron ore to its European operations.

Severstal Resources was the second largest producer of iron ore pellets and coking coal (before accounting for the sale of the Kuzbassugol mining complex) in Russia in 2007, according to RudProm and CDU TEK, respectively. Currently, Severstal Resources has the capacity to provide approximately 100 percent of the iron ore and hard coking coal requirements of the Russian Steel Division's steel operations and in 2007, the Russian Steel Division's steel operations procured approximately 74 percent and 75 percent of its iron ore and coal requirements from Severstal Resources, respectively. Severstal Resources' deposits have technical characteristics enabling it to produce a relatively wide range of products for customers in the metallurgical industries, in addition to the Group's steel operations. Its deposits of iron ore and coal are significant, with estimated mine lives extending ten years and beyond.

The Group's North American business units source the majority of their raw materials from domestic suppliers under a variety of arrangements aimed at ensuring a reliable long-term supply of raw materials at competitive prices, with the balance being purchased in the spot markets. The Group's primary plant at the Lucchini business unit, Piombino, sourced approximately 69 percent of its carbon coke requirements from its own coke ovens in 2007.

The vertically-integrated nature of the Group also allows it to limit its exposure to raw material price fluctuations and increase efficiencies.

### Geographically Diversified Business with a Broad Range of Products

The Group's production facilities are geographically diversified, with locations in Russia, the United States, Italy, France, Ukraine, the United Kingdom and Kazakhstan. The Group's largest steel production facilities, located in Cherepovets in northwest Russia, provide it with access to the growing Russian, CIS and Eastern European steel markets. Further, the Group believes that, as a result of its presence in Europe and the United States, it also benefits from greater access to the mature European and North American markets for high-quality and niche steel products. In this regard, its recent acquisition of Sparrows Point, WCI Steel, and, if successfully completed, Esmark (see "— Recent Developments") in the United States and the commissioning of the newly constructed SeverCorr mini-mill in Columbus, Mississippi are expected to enhance its presence in the North American steel market and enable it to increase sales and realise production synergies. SeverCorr also provides the Group with greater access to the growing steel markets in the south of the United States, to balance the Group's presence in the mature steel markets in the north. The global diversified nature of the Group has also enabled it to benefit from the sharing of industry know-how and best practices across business divisions. The Group also believes that its broad range of products has allowed it to meet demand for steel products in each of the markets in which the Group operates.

**Low Cost Producer**

Russia is one of the lowest cost regions for steel production worldwide. With its largest production facilities located in northwest Russia, the Group benefits from relatively low-cost supplies of electricity and natural gas, as well as transportation, given the proximity of its production facilities to producers of raw materials in that region, major steel-consuming markets in the central European part of Russia, and the ports of the St. Petersburg region. In addition to these cost advantages, as one of the largest producers of steel in Russia, the Group benefits from economies of scale in production and negotiating power with its suppliers, including third party suppliers of raw materials. In order to maintain its cost competitiveness, the Group has made and continues to make significant capital expenditures in upgrading its facilities to increase productivity and improve the energy efficiency, as well as optimising the size of its labour force. For example, in 2007 the Group's largest steel production facility, located in Cherepovets, was estimated to be approximately 45 percent self-sufficient in terms of its own generation and consumption of electricity, and the Group plans to further increase the plant's level of energy self-sufficiency (see "— Strategy — Pursue Lower-Cost Steel Production").

**Investment in Modernisation and Advanced Technological Processes**

The Group has invested heavily in modernisation programmes at its main steel production facilities and mining facilities in Russia, as well as its steel production facilities in the United States and Europe, expanding production and achieving operational efficiencies. In 2006 and 2007, the Group's capital expenditure at its three business divisions amounted to approximately US$2,877 million and it currently intends to invest an additional US$16.3 billion from 2008 to 2012 as part of its capital expenditure programme.

The Group has sought to adopt new technological processes when operationally convenient to do so, such as the introduction of pulverised coal injection ("**PCI**") technology into blast furnace "C" at Severstal North America's Dearborn facility during the recent major refurbishments of that blast furnace. In addition to modernisation, the Group has built on existing strengths in advanced technological processes, particularly in the automotive and long products markets where, for example, Lucchini's Ascometal business unit is a recognised market leader in special bar quality ("**SBQ"**) products. As a result, the Group believes that it is well-positioned in high value-added and niche product markets, in addition to its other steel and metalware products from its modern production facilities.

**Experienced Management Team**

The Group's senior management team combines extensive steel and resources industry knowledge with international management and financial expertise, including valuable insight gained from the five independent non-executive directors on the board of directors. At an operational level, the Group has developed, and continues to refine, a management structure that is focused on improving accountability, clarifying responsibilities and streamlining information reporting and decision-making. Backed by international experience and advanced business qualifications, the management team's ability to improve the performance of the Group's assets is evidenced by the increased operating efficiency and profitability of the Cherepovets Steel Plant in recent years. Further, the team's ability to evaluate, negotiate and close complex acquisitions has also been shown recently with Severstal International's acquisition of the Sparrows Point production facilities and WCI Steel (see "— Recent Developments"). These transactions involved lengthy negotiations with a range of stakeholders, including complex discussions with labour unions, often in a competitive tender. Further, the management team has a proven track record of turning around underperforming assets, such as Lucchini and Severstal North America's Dearborn facility where significant operating improvements have been achieved, albeit in favourable market conditions.

**Strong Corporate Governance**

As a global metals and mining company, the Group seeks to adhere to international corporate governance standards. In addition to half of its board of directors being independent, according to UK standards of independence, the Group has established committees of its board of directors in accordance with the UK Combined Code on Corporate Governance and has implemented other measures aimed at promoting transparency and good corporate governance. These measures include internal control procedures and internal audit functions, publishing quarterly financial statements prepared in accordance with IFRS, publishing regular production updates, and requiring the approval of two-thirds of the board of directors for acquisitions with a value in excess of US$500 million and any transaction with a value of more than 10 percent of the book value of the Company's assets.

## STRATEGY

The Group's corporate strategy is to build upon and improve its position as a leading global steel company in terms of profitability, with a vertically-integrated, low-cost business structure. To successfully implement this strategy, the Group intends to do the following:

**Focus on High-Demand Products in Russia**

The Group views the Russian market for steel products as providing significant growth potential. Accordingly, the Group plans to continue to invest in its production facilities in Russia in order to increase production capacity, particularly of long products, pipes, sections and other products used in the construction and infrastructure industries, where demand has been strong and is expected by the Group to increase further. In this regard, the Group has started construction of a new pipe mill close to its main Russian steelmaking facilities in Cherepovets, which is currently expected to be completed in 2009. It also plans to commence the production of heavy structural long products at the Cherepovets Steel Plant, as well as to build two mini-mills in central Russia, each with a capacity of approximately 1 million tonnes of finished long products per year, the first of which is expected to be completed in 2010.

Growth in demand from customers in the oil and gas, ship-building and machinery industries is also a focus of the Group in Russia. For customers in these industries, the Group plans to continue to focus on providing a high standard of customer service, including the customisation of products, the supply of premium quality products and just-in-time deliveries, with a view to differentiating itself from other producers in Russia. To this end, the Group plans to leverage the experience of its operations in Europe and North America. The Group also intends to leverage its North American experience to further develop the Group's high-quality automotive steel products in Russia to meet the requirements of foreign car manufacturers operating in Russia. The Group believes that demand for these niche products is set to grow significantly in the medium and long-term.

**Optimisation of the Group's Operations in the United States**

Following the successful acquisition of Sparrows Point and WCI Steel in 2008, and if completed, the acquisition of Esmark (see "— Recent Developments"), the Group plans to focus on optimising and integrating the operations of the facilities acquired with the existing production facilities of Severstal North America and SeverCorr. The Group also plans to consolidate its presence in the growing steel markets in the south of the United States, with the construction of a second phase at SeverCorr, bringing its total production capacity to approximately 3.0 million tonnes of finished products per year. The Group believes that the geographical locations and product lines of these production facilities are complementary. The Group believes that in addition to having a more diverse customer-base and range of products than in the past, its operations in the United States should also benefit from synergies, including knowledge and technology transfers, aggregated purchasing, logistics and other overhead items, and optimised scheduling and production. Increasing the profitability of the entities acquired will also be a focus of the Group's management as well as securing greater reliable long-term supplies of raw materials, in relation to which the Group is considering the acquisition of coal mining assets in the United States (see "— Recent

Developments"). In addition, the Group plans to invest in upstream and downstream opportunities that are consistent with reducing costs and marketing value-added products.

**Pursue Lower-Cost Steel Production**

The Group plans to continue to pursue a strategy of lower-cost steel production in relation to its Russian operations (in comparison to global cost levels in steel production), as well as in relation to its European and US operations (in comparison to regional cost levels in steel production). The Group believes that this can be achieved by a combination of capital expenditure on production facilities, energy efficiency improvements and labour productivity gains. The Group's capital expenditure programme includes various projects to improve operational efficiencies and to reduce raw material consumption, such as the planned upgrades to blast furnaces at the Cherepovets Steel Plant to implement PCI technology and reduce the consumption of coal as was recently implemented at blast furnace "C" at Severstal North America's Dearborn facility. The Group plans to improve energy efficiency, including internal electricity generation capacity, is to be improved through measures including the planned construction of a 155 megawatt power generation facility in Cherepovets, currently expected to be completed by the end of 2012, and additional electricity generation at Sparrows Point. The Group plans to continue to focus on optimising the size of its labour force, particularly in Russia, as well as seeking to maintain its relationships with labour unions.

**Organic Growth and Disciplined Acquisitions Strategy**

The Group plans to grow the size of its operations by both organic growth and a disciplined acquisitions strategy focused on acquiring businesses that have the potential to provide synergies and earnings growth, or are of strategic importance for the Group. Currently, the Group's organic growth is expected to come from the construction of the second phase at SeverCorr, which is expected to double that facility's production capacity, together with growth in its Russian steelmaking operations (see "— Focus on High-Demand Products in Russia"). The Group also plans to consider growth opportunities within its mining operations, including by expanding production capacities at its existing mines and by developing new mining deposits.

The Group's acquisition strategy in the steel industry is primarily focused on the CIS and the United States (see also "— Recent Developments"), although as the United States market is relatively mature and consolidated, opportunities in that market are not expected to arise frequently. The Group may also acquire or develop steel operations in regions expected to provide high levels of growth in demand, particularly where low-cost sources of raw materials and other production inputs are readily available. As regards raw materials, the Group plans to seek additional sources of raw materials to enhance its existing vertical integration in Russia and to provide greater certainty of supply for the Group's operations in other markets, including by seeking access to raw materials within the countries in which it operates and elsewhere, particularly in locations with relatively low-cost mining operations and with convenient access to international markets.

In this regard, in May 2008 in connection with an acquisition of a minority stake in Mano River Resources Inc, the Group agreed to acquire a 61.5 percent stake in African Iron Ore Group Ltd, a company involved in the Putu Range iron ore project in eastern Liberia, subject to certain conditions. Through this acquisition, if successfully completed, the Group plans to explore and develop iron ore deposits, with a view to extracting iron ore for export to North America and European markets (see also "— Recent Developments"). Further, the Group is considering the acquisition of coal mining assets in the United States, aimed at securing a long-term supply of coal to its expanded operations in the United States (see also "— Optimisation of the Group's Operations in the United States" and "— Recent Developments"). The Group also plans to expand its mining operations by actively participating in the consolidation of the Russian/CIS iron ore and coking coal industries as well as participating in "greenfield" projects in Russia and neighbouring countries, and forming alliances with mining majors.

**HISTORY AND DEVELOPMENT OF THE GROUP**

The Group's predecessor, Cherepovets Metallurgical Works, produced its first cast iron in 1955. Cherepovets Metallurgical Works was 100 percent state-owned until it was privatised in 1993 in accordance with the State Programme for the Privatisation of State and Municipal Enterprises in the Russian Federation. The newly privatised entity, the Company, was registered as an open joint stock company in the city of Cherepovets on 24 September 1993. Since 1993, the Group has expanded to include steel operations in North America and Europe and a number of different businesses, including companies engaged in the mining of iron ore, coal, gold and other minerals, the procurement of scrap, pipe manufacturing, metalware production, the manufacturing of steel furniture and kitchenware, construction and repair.

A brief summary of the historical development of the Group's current business divisions, the Russian Steel Division, Severstal International and Severstal Resources, is set forth below.

**Russian Steel Division**

The Russian Steel Division is the result of a series of acquisitions and disposals in the Group's most important market.

***Russian Steel segment.*** In 2000, the Group purchased Hot Rolling Mill 5000 ("**Mill 5000**"), from OAO United Heavy Machinery. The Group believes that Mill 5000 is the only mill of its kind in Russia that produces 4.8 metre-wide high-quality hot-rolled plates for large-diameter pipes.

In 2001, the Group and Arcelor formed the Severgal joint venture, which has a focus on high-quality galvanised auto body sheet products. The Group completed the construction of a new facility for the production of polymer-coated steel products, which began operations on the Cherepovets site in December 2005. In July 2006, the Group completed the construction of the Izhora Pipe Mill, a project designed to produce large-diameter 18-metre-length pipes with three-layered anti-corrosion coating that meet the requirements of domestic and international gas and oil customers, and which is supplied with rolled steel from Mill 5000, located nearby. Other than at the Izhora Pipe Mill, the Group believes large-diameter pipes of this length are not currently produced in Russia. In May 2007, the Group acquired Arcelor Mittal's 25 percent stake in the Severgal joint venture, taking the Group's stake in Severgal to 100 percent. In July 2007, the Group commenced the development of the first of two mini-mills in Russia, currently expected to be completed in 2010. In June 2007, the Group commenced the development of a new pipe mill on a site close to Cherepovets (the "**Sheksna Pipe Mill**"), which upon its completion, currently expected in 2009, is to produce pipes primarily for the construction industry.

***Repair and maintenance.*** In 2006, the Group repurchased from the Controlling Shareholder a controlling stake in certain engineering, machine-building and repair and maintenance companies, including OOO SSM-Tyazhmash, OAO Domnaremont and OAO Metallurgremont for US$60.8 million. This purchase price was not significantly different from the amounts received by the Group for the disposal of these entities in 2004 to the Controlling Shareholder.

***Trading and transportation.*** In 2007, the Group established LLC Severstal-Ukraine to be a distributor in Ukraine, and began expanding its distribution operations in Belarus through ZAO SeverstalBel. The Group holds controlling interests in both of these entities. In 2007, the Group acquired ZAO Neva-Metall and ZAO Neva-MetallTrans, stevedoring and shipping logistics entities at the port of St. Petersburg from Transportation Investments Holding Limited.

***Metalware.*** Now the principal operating company of the Group's metalware segment, Severstal-Metiz was created through a series of acquisitions throughout the last decade. In 1996, the Group purchased a 32.99 percent stake in Cherepovets Steel Rolling Plant ("**ChSPZ**"), a large Russian metalware producer. The Group increased its stake in ChSPZ to 88.8 percent in December 2005. In 2003, the Controlling Shareholder purchased a controlling stake in OAO Orlovsky Steel Rolling Mill ("**OSPAZ**"), and subsequently transferred a portion of its interest to the Group, resulting in the Group holding a 19 percent stake in OSPAZ. In 2004, the Controlling Shareholder purchased a controlling interest in OAO Volgograd Steel Rolling Mill ("**VSPKZ-PROM**"). In January 2005, the Group acquired a 100 percent stake in ZAO Severstal-Metiz from the Controlling Shareholder. In 2005, the Group transferred its interests in OSPAZ and ChSPZ to Severstal-Metiz. Also in 2005, the principal assets and liabilities previously-owned by VSKPZ-PROM were transferred to Severstal-Metiz.

In February 2006, the Group acquired a 60 percent ownership interest in the Ukrainian wire and metalware producer OAO Dneprometiz ("**Dneprometiz**"). In the second quarter of 2008, the Group acquired an additional 34.6 percent stake in Dneprometiz, bringing its total shareholding to approximately 94.6 percent.

In April 2006, the Group acquired a 100 percent stake in British wire producer Carrington Wire Ltd ("**Carrington**"). In 2007, the Group also acquired the remaining interests in the Policher joint venture, a wire producer with production facilities in Cherepovets and Orel.

**Severstal International**

Severstal International is the result of a series of acquisitions over the last four years.

***North America.*** North America was created when the Group acquired substantially all of the assets of Rouge Steel in January 2004. Rouge Steel had been in the steel manufacturing business since the early 1920's, first as a division of Ford and later as a subsidiary of Ford. In 1989, Ford sold Rouge Steel. Difficult market conditions in the United States steel market beginning in 1998 were exacerbated by production outages related to a powerhouse explosion and a fire at one of Rouge Steel's joint ventures. This caused significant operating losses and put considerable pressure on Rouge Steel's liquidity. In October 2003, Rouge Steel filed for bankruptcy protection under Chapter 11 of the United States Bankruptcy Code. Subsequently, substantially all of its steelmaking assets were acquired by the Group for US$260 million in cash and the assumption of US$113 million of liabilities.

In 2005, the Group entered into the SeverCorr joint venture with an entity beneficially owned by the Controlling Shareholder and others. Construction of the SeverCorr plant began in October 2005. The construction of the 1.5 million tonne mini-mill has essentially been completed and the facility is operating at near target capacity. The plant is a technologically advanced flat rolled steel mini-mill, and which the Group believes is the only plant in the southern United States with the capability to cast finished sheet widths of 72 inches. Also, based on publicly available information, the Group believes it is the only electric arc furnace ("**EAF**") plant in the world designed to make exposed automotive steels. SeverCorr has a total production capacity of 1.5 million tonnes of hot-rolled, cold-rolled, galvanised and galvannealed sheet per year. In January 2008, the Group acquired a controlling interest in SeverCorr and consolidated it into the Group's Financial Statements. In April 2008, the Group's stake in SeverCorr increased to 87.7 percent, on a fully-diluted basis, after some of the minority interests were bought-out.

In May 2008, the Group acquired the Sparrows Point plant in Baltimore, Maryland for US$810 million and the assumption of, according to the Group's estimates, approximately US$50 million of healthcare-related liabilities. The plant has its own sinter facility, which produces sinter, a raw material in the ironmaking process at Sparrows Point. The product line includes slabs, hot-rolled, cold-rolled, coated zinc and zinc-aluminium products as well as tin coated steel. Sparrows Point's crude steel production capacity is 3.4 million tonnes per year.

For recent developments relating to North America, see also "— Recent Developments".

***Lucchini.*** In April 2005, the Group acquired a 19.99 percent stake in the European steel producer Lucchini SpA, and the Controlling Shareholder acquired a 41.92 percent stake. Accordingly, the Controlling Shareholder obtained an aggregate 61.91 percent voting control of Lucchini SpA. In May, June and November 2005, the Controlling Shareholder acquired an additional 8.9 percent of Lucchini SpA, giving it a total share holding of 70.81 percent. On 2 October 2006, the Group acquired a controlling stake in Lucchini SpA and in May 2007, the Group increased its stake to 79.82 percent. In the second quarter of 2007, Lucchini disposed of the Sidermeccanica business unit to an entity connected to the Lucchini family for approximately €127.8 million (approximately US$172.5 million at the time of the sale).

**Severstal Resources**

Severstal Resources is the result of a series of acquisitions and disposals over the last 12 years.

Through a series of share purchases from 1994 to 1999, the Group and the Controlling Shareholder acquired a combined stake of 52 percent of the share capital of OAO Karelsky Okatysh ("**Karelsky Okatysh**"), an iron ore pellet producer. In 1995, the Group acquired OAO Olkon ("**Olkon**"), an iron ore producer in the Murmansk region. In 2001, the Controlling Shareholder, together with MMK, purchased a 51.7 percent stake in OAO Kuzbassugol, a Russian coal-mining company that includes the Pervomayskaya Mine and the Berezovskaya Mine, in which the Controlling Shareholder and MMK held equal shares. During 2001 and 2002, the Group and the Controlling Shareholder acquired approximately 16 percent of the shares of OAO Vorkutaugol ("**Vorkutaugol**"), another Russian coal producer that includes the Vorgashorskaya Mine, through various private and market purchases.

In 2002, MMK sold its 25.85 percent stake in OAO Kuzbassugol to the Controlling Shareholder and, in 2003, the two main shareholders of OAO Kuzbassugol, the Controlling Shareholder and the MDM Group, agreed to divide the business. The MDM Group received those coal mines previously held by OAO Kuzbassugol that produce coal suitable for energy generation and the Controlling Shareholder received the MDM Group's shares in OAO Kuzbassugol, which was left with those coal mines producing coal suitable for coke production.

Also in 2003, the Group purchased shares in certain coal-mining assets in the Komi Republic and purchased a 39.8 percent stake in Vorkutaugol in a public auction held by the Russian Government. This stake was subsequently resold to the Controlling Shareholder at cost.

In June 2006, the Group acquired controlling interests in Karelsky Okatysh, Olkon, Vorkutaugol and OAO Kuzbassugol.

Over a period of years up until 2007, the Group acquired several ferrous scrap metal yards in Russia, including an acquisition of a group of companies called Vtorchermet St Petersburg ("**Vtorchermet**").

In October 2007, the Group acquired all of the shares in OOO Nerungri-Metallic ("**Nerungri-Metallic**") and ZAO Rudnik Aprelkovo ("**Aprelkovo**"), each being a Russian gold-mining company operating one mine. In addition, in 2007, the Group acquired three gold mining licences for sites in east Russia in public auctions from the relevant government authorities.

In 2008, the Group completed the acquisition of Celtic Resources Holdings plc, a company with subsidiaries holding gold mining assets in Kazakhstan ("**Celtic**") for a total consideration of US$308.6 million. In April 2008, the Group sold the Kuzbassugol mining complex ("**Kuzbassugol**"), consisting of the Berezovskaya and Pervomayskaya mines, to Arcelor Mittal for US$652 million. The Group has also recently increased its shareholding in each of Karelsky Okatysh and Olkon to a level over 95 percent with an intention to increase it further to 100 percent by way of a minority squeeze-out allowed by Russian law. The Group's shareholding in Vorkutaugol remains below 95 percent which is insufficient for a squeeze-out under Russian law.

## RECENT DEVELOPMENTS

### WCI Steel

In July 2008, the Group acquired the outstanding equity of WCI Steel, which operates a steel mill in Warren, Ohio, for a total cash consideration of approximately US$140 million plus the assumption of, according to the Group's estimates, approximately US$285 million of liabilities and the repayment of debt in an additional amount of approximately US$274.9 million, including payments connected with the redemption of certain senior secured notes of WCI Steel referred to below. WCI Steel's product line comprises custom and commodity flat rolled steel products, including hot-rolled, cold-rolled and galvanised steel. WCI Steel has an estimated production capacity of approximately 1.85 million tonnes of crude steel per year and produced approximately 1.0 million tonnes of crude steel in 2007. The Group believes that WCI Steel's product line, which includes high-carbon and alloy products, and its geographical location close to some of the Group's existing customers and operations, should provide a range of advantages to the Group's US operations in addition to the increased capacity the acquisition gives to the Group in the US market for flat products. The Group's preliminary estimate of the capital expenditure that would be required at WCI Steel for the period from 2008 to 2012 is approximately US$175 million.

In connection with the acquisition, WCI Steel has called for the redemption of the US$100 million aggregate principal amount outstanding of its 8 percent senior secured notes due 2016. Notice of the redemption has been mailed to record holders of such notes and the notes are expected to be redeemed in August 2008.

Recently, an unsuccessful bidder for WCI Steel, together with certain existing minority shareholders of WCI Steel, brought proceedings against WCI Steel, the Company and another member of the Group, seeking an injunction to prevent the completion of the acquisition of WCI Steel by the Group. The plaintiffs alleged that the board of directors of WCI Steel breached its fiduciary duties by, among other matters, not accepting the unsuccessful bidder's bid. The proceedings did not assert any claims against the Company or the other member of the Group. A hearing was held on 27 June 2008, at the conclusion of which the court denied the plaintiffs' application for a preliminary injunction, thereby permitting completion of the acquisition.

**Esmark**

On 30 May 2008, the Group commenced an all cash US$17 per share offer to acquire all of the outstanding shares of common stock of Esmark, a manufacturer and distributor of flat rolled and other steel products in the United States. Initially, the Group's offer was not supported by Esmark's board of directors. However, on 25 June 2008, the Group entered into an agreement with Esmark in connection with which the Group has increased the purchase price in the tender offer to US$19.25 per share in cash and Esmark's board of directors has recommended that Esmark's shareholders tender their shares to the Group. The expiration date of the tender offer has been extended to 10:00 am, New York City time, 4 August 2008. The offer and related transactions contemplated by the agreement are subject to certain customary closing conditions. The Group has entered into an agreement with Esmark's majority shareholder to tender its shares in the tender offer. The Group has also entered into an agreement that satisfies the successorship clause of the United Steelworkers' collective bargaining agreement. If the acquisition is successfully completed, the Group will acquire all of Esmark's business, including Wheeling-Pittsburgh Steel Corporation, Esmark Steel Services Group, Inc and the remaining 50 percent interest in Mountain State Carbon, LLC, a blast furnace coking coal production joint venture with the Group.

The Group's operating and restructuring plan for Esmark, upon successful completion of the acquisition, includes a five-year capital investment programme and is designed to derive value from Esmark through operational improvements, including the maximisation and optimisation of production at the EAF, upgrades to enhance the quality and capacity of the hot strip mill, improvements of the downstream operations, and leveraging synergies and geographical alignment between the Group's other assets in the United States. The Group believes that its combined operations in the United States, including Esmark, would create one of North America's leading producers of flat rolled steel, further expanding the Group's product offerings to its customers in a market that has displayed consistent demand for high quality steel.

The acquisition of Esmark, if successfully completed, is expected to provide the Group with substantial synergies with its current US operations at the Dearborn facility, SeverCorr, Sparrows Point and WCI Steel. Full ownership of Mountain State Carbon, LLC is also expected to increase the Group's vertical integration with raw materials in the United States. In addition, Esmark's service centres and corrugated sheet production facilities are expected to enhance the Group's operations in the US by allowing it to reach more customers and add value to its steel products.

Following completion of the tender offer, subject to the terms and conditions set forth in the offer to purchase, the Group intends to consummate a second-step merger where all remaining Esmark stockholders will receive the same cash price paid in the tender offer, subject to any available appraisal rights under Delaware law. If the offer is accepted at the revised offer price of US$19.25 per share, the total purchase price for all of the outstanding shares of common stock of Esmark would be approximately US$775 million. The Group has also purchased Esmark's aggregate US$110 million term loan facilities from Essar Steel Holdings Limited ("**Essar Steel**"). The Group has, on behalf of Esmark, paid Essar Steel certain other termination and change of control fees and prepayment penalties in connection with certain existing arrangements between Esmark and Essar Steel, including a US$25 million termination fee and a US$20.25 million payment in lieu of the exercise by Essar Steel of its conversion rights related to the term loan facilities referred to above.

**Mano River Resources Inc/African Iron Ore Group**

In May 2008, the Group entered into arrangements to acquire a minority stake in Mano, a company focused on the exploration and development of iron ore, diamonds and gold in west Africa, listed on the London Stock Exchange's Alternative Investment Market and on the TSX-Venture Exchange in Canada. The acquisition price was approximately US$4 million. The Group has also agreed to acquire a 61.5 percent stake in African Iron Ore Group Ltd, a company currently majority-owned by Mano and involved in the Putu Range iron ore project in eastern Liberia, for approximately US$37.5 million, subject to certain conditions, including Mano converting its exploration licence into a mineral development agreement with the government of Liberia.

**Potential Coal Mining Acquisitions**

The Group is considering the strategic acquisition of coal mining assets in the United States. After completing the assessment of potential acquisition targets, the Group may decide to submit a bid on one or more coal mining assets in the near term, possibly as early as July 2008. If the Group were to submit any such bids, and if one or more of the relevant acquisition targets were successfully acquired, the aggregate purchase price for such assets could be material to the Group's financial condition and results of operations. However, there can be no assurance that any such bids will be made or, if made, that any such acquisitions of coal mining assets will be successfully completed.

**RUSSIAN STEEL DIVISION**

The Russian Steel Division produced approximately 16.4 percent of the total production of Russian crude steel in 2007, making it the third largest producer of crude steel products in Russia by volume of production in that year, in each case according to Chermet Corporation. The Russian Steel Division comprises three segments: (i) the Russian Steel segment which consists primarily of steel production facilities at the Cherepovets Steel Plant, high-grade automotive galvanising facilities at Severgal and Rolling Mill 5000, which the Group believes is Russia's only rolling mill that produces 4.8 metre-wide high-quality hot-rolled plates, as well as various supporting functions for trading, maintenance and transportation; (ii) Metalware with its wire drawing and metalware manufacturing business in Severstal-Metiz; and (iii) the Izhora Pipe Mill, a large-diameter pipe mill. With total steelmaking capacity of 13.2 million tonnes of crude steel per year as at 31 December 2007, the Russian Steel segment produced 11.9 million tonnes of crude steel and 10.8 million tonnes of finished steel in 2007. With a total estimated metalware production capacity of in excess of 2 million tonnes per year as at 31 December 2007, Metalware produced 1.0 million tonnes in 2007, which represented approximately 34.4 percent of domestic Russian metalware production, based on data from the Association of Metalware Producers of Russia, and approximately 33.2 percent of Ukrainian metalware production, based on data from the Association of Metalware Producers of Ukraine. With total pipemaking capacity of 0.6 million tonnes as at 31 December 2007, Izhora Pipe Mill produced 0.3 million tonnes in 2007.

The Russian Steel Division's primary steel production facilities are the Cherepovets Steel Plant, located in Cherepovets, in northwest Russia, approximately 600 kilometres from Moscow and approximately 450 kilometres from St. Petersburg. The Russian Steel segment also includes a heavy plate mill in Kolpino, which is approximately 26 kilometres from St. Petersburg. The Izhora Pipe Mill is adjacent to Kolpino. Metalware operates out of multiple sites across Russia, Ukraine and the UK. These locations give the Russian Steel Division strategic proximity to river ports and railways, providing logistically favourable access to raw material sources and customers.

**Facilities**

The Russian Steel Division's steel production facilities at the Cherepovets Steel Plant are fully integrated, occupying approximately 30 square kilometres, with coking, sintering, blast furnaces, steel making, casting and hot and cold rolling facilities. The Russian Steel Division's downstream operations are at Severgal and the Izhora Pipe Mill, which are facilities for the production of galvanised coils and large-diameter pipes, respectively. Its wire drawing and metalware facilities are located on three sites in Russia, one site in Ukraine and one site in the UK.

The hot phase at the Cherepovets Steel Plant consists of a coke plant; a sintering plant; five blast furnaces; three oxygen converters; two vacuum degassers; two EAFs; three open-hearth furnaces; seven continuous casting lines; a cogging mill; a continuous billet mill; two hot strip mills and a heavy plate mill. The cold phase at the Cherepovets Steel Plant consists of three continuous picking lines, two cold rolling mills and annealing facilities, two tempering mills, two lines for dynamo steel, two galvanising lines, two cold profile tending lines, one colour coating line and six pipe rolling mills. There are also automotive grade galvanising facilities at Severgal and a large-diameter pipe rolling mill at the Izhora Pipe Mill. The Russian Steel Division also has wire drawing and metalware facilities in Russia in Cherepovets, Orel and Volgograd, as well as the Dneprometiz plant in Ukraine and the Carrington plant in the UK.

The following table sets forth the Russian Steel Division's actual output in 2005, 2006 and 2007 and equipment, capacity and utilisation rate by unit as at 31 December 2007.

*Steel Production Facilities, Russian Steel Division — Output, Capacity and Utilisation Rate by Unit*

| | Actual output | | | As at 31 December 2007 | | Utilisation rate in 2007 |
|---|---|---|---|---|---|---|
| | 2005 | 2006 | 2007 | Equipment | Capacity | |
| | *(million tonnes)* | | | | *(million tonnes per year)* | *(percent)* |
| **Russian Steel Segment** | | | | | | |
| ***Cherepovets Steel Plant*** | | | | | | |
| Coking plant | 4.20 | 4.22 | 4.63 | 7 batteries | 4.7 | 98.5 |
| Sintering plant | 8.34 | 8.55 | 8.68 | 8 machines | 8.7 | 99.8 |
| Blast furnace facilities | 7.98 | 8.20 | 8.76 | 5 furnaces | 9.0(1) | 97.3 |
| Basic oxygen furnaces | 8.48 | 8.04 | 8.32 | 3 furnaces | 9.5 | 87.6 |
| EAFs | 1.43 | 1.95 | 2.05 | 2 furnaces | 2.1 | 97.6 |
| Open-hearth furnaces | 0.90 | 1.30 | 1.50 | 3 furnaces | 1.6 | 93.8 |
| Continuous casters | 9.93 | 9.97 | 10.37 | 7 casters | 11.1 | 93.4 |
| Hot-rolling mills | 7.64 | 7.95 | 8.27 | 4 mills | 8.9 | 93.0 |
| *Of which finished products* | 4.90 | 5.00 | 5.38 | | | |
| Cold-rolling mills | 2.42 | 2.61 | 2.57 | 2 mills | 2.8 | 91.8 |
| *Of which finished products* | 1.82 | 2.01 | 2.00 | | | |
| Continuous pickling lines | 2.79 | 3.06 | 2.97 | 3 lines | 3.2 | 92.8 |
| Hot-dip galvanising lines | 0.60 | 0.60 | 0.57 | 2 lines | 0.6 | 95.0 |
| Section rolling mills | 1.59 | 1.91 | 2.03 | 3 mills | 2.4 | 84.6 |
| Cold roll-forming lines | 0.15 | 0.17 | 0.18 | 1 line | 0.2 | 90.0 |
| Pipe rolling mills | 0.19 | 0.24 | 0.25 | 7 mills | 0.3 | 83.3 |
| ***Severgal*** | | | | | | |
| Galvanising line | — | 0.27 | 0.40 | 1 line | 0.4 | 100.0 |
| **Izhora Pipe Mill** | | | | | | |
| Pipe mill | — | 0.01 | 0.30 | 1 line | 0.6 | 50.0 |
| **Metalware** | | | | | | |
| ***Severstal-Metiz*** | | | | | | |
| Metalware | 0.82 | 1.10 | 1.05 | N/A | 2.5 | 42.0 |

Note:

(1) Blast furnace 3, with a capacity of 1.9 million tonnes per year, was not operating as at 31 December 2007 due to a scheduled reconstruction, which is expected to be completed in 2010.

***Cherepovets Steel Plant.*** The Cherepovets Steel Plant produces almost all of the Russian Steel Division's crude steel. The facilities' total production capacity is 13.2 million tonnes of crude steel per year, as at 31 December 2007.

*Blast furnace facilities.* There are five blast furnaces at the Cherepovets Steel Plant, with an estimated current combined capacity of 10.9 million tonnes per year. Blast Furnace 5 was fully refurbished in October 2006 and has a capacity of 4.2 million tonnes per year. Blast Furnace 4, which recommenced operation in December 2005 after refurbishment and recommissioning, has an installed capacity of 2.3 million tonnes per year. Blast Furnaces 1 and 2, the oldest furnaces, have an installed capacity of 1.2 million tonnes each per year. Blast Furnace 3 has a capacity of 1.9 million tonnes per year and is currently undergoing reconstruction, to increase its capacity and efficiency, which is expected to be completed in 2010.

*Basic oxygen furnaces, EAFs and open-hearth furnaces.* Crude steel is produced at the Cherepovets Steel Plant in three basic oxygen furnaces ("**BOF**"), with a combined capacity of 9.5 million tonnes per year; two EAFs, with a combined capacity of 2.1 million tonnes per year; and three open-hearth furnaces, with a combined capacity of 1.6 million tonnes per year, which it intends to decommission by 2015.

*Hot-rolling mills.* The Cherepovets Steel Plant's hot-rolling mills consist of three hot-rolling shops, with a combined capacity of 8.9 million tonnes per year, taking into account the shop's production layout, as at 31 December 2007.

Hot-rolling Shop 1 is equipped with two combined semi-continuous mills. Mill 2800, which has a capacity of 600,000 tonnes per year, produces thick plates with a thickness of 6.35 to 50 millimetres, which serve as feedstock for Mill 1700, which has a capacity of 1.4 million tonnes per year. Mill 1700 produces sheet with a thickness of 0.8 to 8 millimetres and is equipped with four coilers, with a capacity of 2.0 million tonnes per year.

Hot-rolling Shop 2 is equipped with Mill 2000, a continuous wide-sheet mill with a capacity of 6.0 million tonnes per year and includes four reheating furnaces and length and width-cutting machines. Mill 2000 is operated on a fully-automated basis and produces sheet with a thickness of 1.2 to 16 millimetres.

Hot-rolling Shop 3 is equipped with Mill 5000, a heavy plate mill located in Kolpino. Mill 5000 produces wide quarto plate for shipbuilding, and strips for pipe manufacturing, including as feedstock for the Izhora Pipe Mill. Mill 5000 has a capacity of 850,000 tonnes per year.

*Cold-rolling mills.* The Cherepovets Steel Plant has two cold-rolling mills, with a combined capacity of 2.8 million tonnes per year including a four-stand continuous rolling Mill 1700 and a five-stand continuous rolling Mill 1700. The cold-rolling mills produce cold-rolled sheet with a thickness of 0.25 to 3.2 millimetres. The cold-rolling mills operate together with two tempering mills, a set of bell-type annealing furnaces and slitting and cutting lines.

*Continuous pickling lines and hot-dip galvanising lines.* The Cherepovets Steel Plant has three pickling lines, with a combined capacity of 3.2 million tonnes per year, and two hot-dip galvanising lines with zinc and alumozinc coating, with a combined capacity of 600,000 tonnes per year.

*Section rolling mills.* The Cherepovets Steel Plant has three section rolling mills: a medium-section Mill 350, with a capacity of 1.0 million tonnes per year; a small-section Mill 250, with a capacity of 504,000 tonnes per year; thermo-strengthening equipment and a wire rod Mill 150, with a capacity of 850,000 tonnes per year.

*Cold roll-forming line.* The Cherepovets Steel Plant's cold roll-forming line produces a range of different shaped profiles: closed profile, S-shape profile, E-shape profile, trough-shape profile, angle profile and others and has a combined capacity of 200,000 tonnes per year.

*Pipe rolling mills.* The Cherepovets Steel Plant also has seven pipe rolling mills that can produce pipes with circular, oblong and semi-oblong, square and rectangular cross sections in a wide range of sizes. The seven pipe rolling mills have a combined capacity of 300,000 tonnes per year.

***Severgal.*** Located on the site of the Cherepovets Steel Plant, Severgal produces high-quality galvanised auto body sheet products. In commercial operation since December 2005, the galvanising plant has a capacity of 400,000 tonnes per year. Severgal can produce galvanised-steel sheet with a thickness of 0.4 to 2.0 millimetres and a width of 900 to 1,850 millimetres. The plant produces steel sheet products coated with zinc-iron alloy. Severgal's production for 2007 was approximately 402,287 tonnes. Severgal is strategically located close to several major domestic automotive "greenfield" production facilities, including Nissan and Toyota in St. Petersburg, and Volkswagen in Kaluga.

***Izhora Pipe Mill.*** The Izhora Pipe Mill is the Russian Steel Division's large-diameter pipe mill for the oil and gas industry. The mill is designed to produce pipes meeting the requirements of domestic and international customers, including OAO Gazprom ("**Gazprom**") and OAO Transneft ("**Transneft**") as well as others.

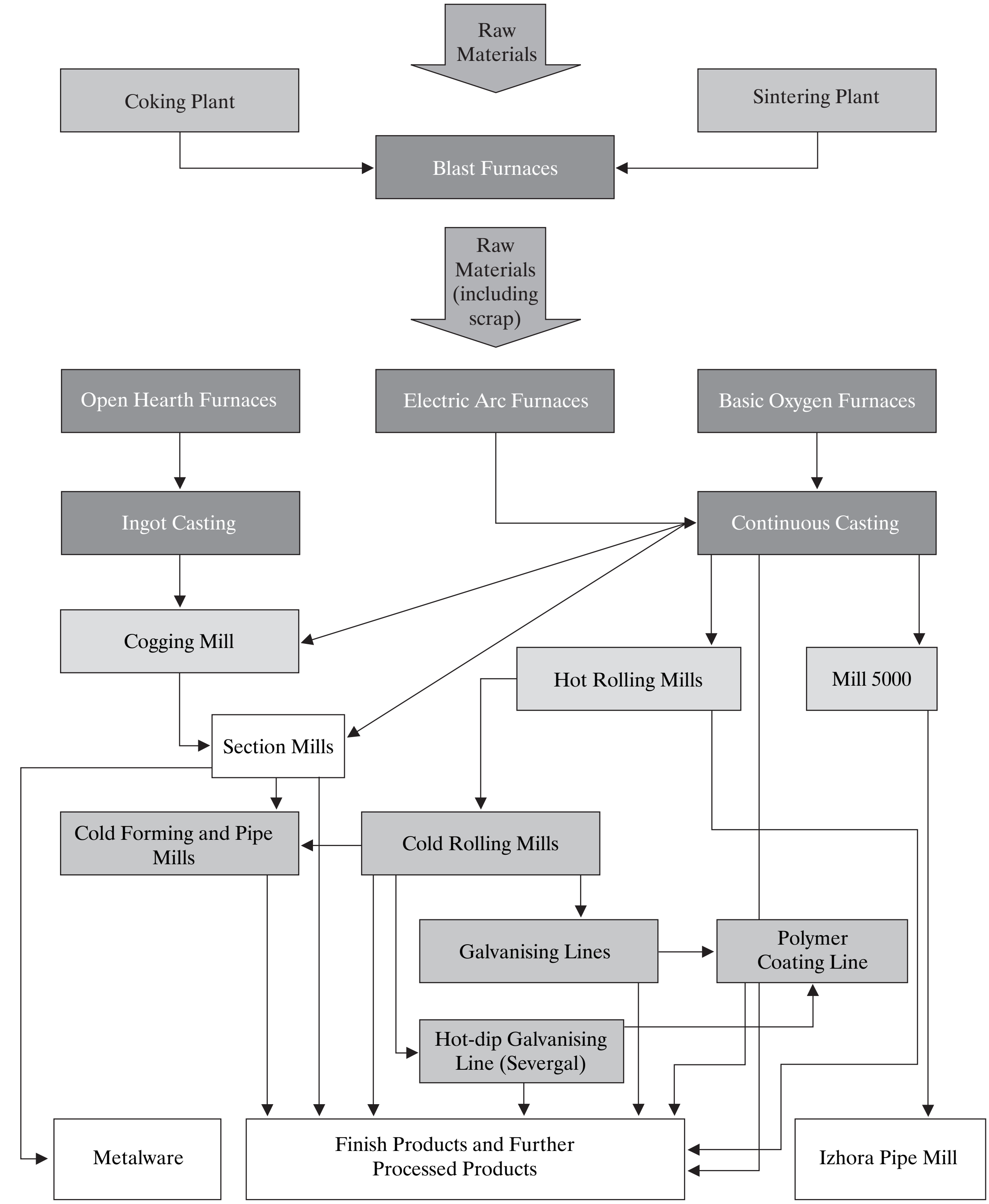
The construction of the Izhora Pipe Mill in Kolpino, next to Mill 5000, included three-layered anti-corrosion coating technology and was completed in July 2006. Mill 5000 was modified to produce strips manufactured by its steel segment to feed the Izhora Pipe Mill. When fully utilised, the Izhora Pipe Mill is expected to reach a production of 600,000 tonnes per year of large-diameter pipes with three-layered anti-corrosion coating, diameters ranging from 610 millimetres to 1420 millimetres and 18.3 metres in length. Other than at the Izhora Pipe Mill, the Group believes that large-diameter pipes of this length are not currently produced in Russia. The project was financed through a mixture of internal and external financing.

***Metalware.*** Metalware is comprised of Severstal-Metiz, which is a subsidiary of the Group and forms part of the Russian Steel Division. The Group believes Severstal-Metiz to be a leading downstream wire drawing and metal processing business in Russia. In 2007, Severstal-Metiz's production represented approximately 34.4 percent of domestic Russian metalware production, based on data from the Association of Metalware Producers of Russia, and approximately 33.2 percent of Ukrainian metalware production, based on data from the Association of Metalware Producers of Ukraine.

Severstal-Metiz operates wire drawing and metal processing operations in Cherepovets, Orel and Volgograd. In 2006, the Group acquired the Carrington plant in the UK and the Dneprometiz plant in Ukraine, both of which are included in Metalware and are held by subsidiaries of Severstal-Metiz. Severstal-Metiz currently produces more than 26,000 products, including rod, nails, cold-drawn steel, steel rope, netting and fastenings and currently has a total maximum production capacity of more than 2.4 million tonnes per year.

**Steel Production Process**

The following diagram illustrates the principal steps in the Russian Steel Division's main steel production processes.




The Russian Steel segment continuously seeks to improve the efficiency of the steel production process with the implementation of an asset modernisation programme and decommissioning of the remaining open-hearth furnaces, the ingot casting lines and cogging facilities.

Currently, the steelmaking process at the Cherepovets Steel Plant begins with coal being fed into the coking plant and iron ore concentrate and other materials being fed into the sintering plant to produce coke and sinter, respectively.

The mix of sinter, pellets and coke is then fed into the blast furnaces, which operate continuously. During the blast furnace process, the charge is converted into pig iron. Liquid slag, which remains after smelting, is also removed from the blast furnaces. When cooled, the slag is crushed at the slag-processing facilities and is then sold domestically by the Russian Steel Division as road-construction material. Gas produced by the blast furnaces is captured and recycled to produce heat.

The molten pig iron is transported to the BOF shop and to the remaining open-hearth furnaces and EAFs in railway ladle cars. The basic oxygen steelmaking process is autogenous, or self-sufficient in terms of energy.

The two EAFs at the Cherepovets Steel Plant, each with a capacity of 150 tonnes per heat, do not need to be charged with molten pig iron, and can be charged with "cold" material, normally steel scrap, recycled goods made from steel which have reached the end of their useful life and solid pig iron. The current proportion of scrap metal used in the EAFs is approximately 80 percent. Other forms of raw materials may be used, including pig iron from the blast furnaces that has been cast and allowed to go cold. Molten steel produced by the EAFs can either undergo secondary steelmaking or be transported to the continuous caster.

Approximately 89 percent of the liquid steel is fed from the furnaces into the continuous casting machines to produce slabs and billets. Continuous casting is the most effective casting process with the lowest metal consumption per tonne of rolled products and saves approximately 70 kilograms of steel per tonne compared to ingot casting. The slabs are further rolled at the hot-rolling mills into sheet and coils.

The remaining liquid steel is poured into bloom ingots. The ingots are then treated in the cogging mill to produce rolled billets for hot-rolled section steel of various types. Some of this steel is then fed into the profile-bending machines and pipe rolling mills.

Additional processing methods related to cold-rolling further improve the surface characteristics of the steel. These additional processing methods include pickling, hydrogen annealing and tempering. Some cold-rolled sheet is galvanised, which involves applying a coat of zinc and aluminium, and some is further polymer coated.

***Quality control.*** The Russian Steel Division has established comprehensive quality-control systems at each stage of its production cycle. The Russian Steel Division currently operates a total quality management ("**TQM**") system at each of its steel production facilities, which involves organising employees in quality teams. Established in the converter shop at the Cherepovets Steel Plant in 2000, these teams are now in place at all of the Russian Steel Division's shops. The Russian Steel Division uses the European Foundation for Quality Management model for TQM and also employs techniques of benchmarking performance to best practice and statistical process control, which the Russian Steel Division began in 2001. The main objective of these techniques is to improve the quality of steel by improving technological process parameters. The current quality-control systems are carried out by an internal quality control division with further support provided by SGS Vostok Limited, a French-based quality surveyor, during transportation and loading.

Lloyd's Register has completed several audits of a number of its steel products within the Russian Steel Division and has extended its quality-management certificate of compliance with standard ISO 9001:2000 to 31 December 2008. In May 2005, some of the Russian Steel Division's steel products were certified according to the ISO TS 16949-2002 automobile standard until 31 December 2008.

The quality-control measures employed by the Russian Steel Division have enabled it to maintain a range of products that meet the high standards required in the United States, Germany, the United Kingdom, Japan and other markets in addition to the modernised Russian oil and pipeline industries. A range of products produced by the Russian Steel Division have been certified by the Marine Register of the Russian Federation, Lloyd's Register, the American Bureau of Shipping, Norske Veritas, Germanischer Lloyd, Bureau Veritas and the Russian River Register. In 2001, the Russian Steel Division received several certificates attesting to the quality of the production output at Mill 5000. The Russian Steel Division's steel products are supplied to various offshore oil and gas development projects.

Severstal-Metiz's three plants in Russia have Management Quality Systems corresponding to the requirements of International Standard ISO 9001. Severstal-Metiz also has a series of certificates attesting to the quality of its products, including welded wire, powder wire, electrodes, ropes and railway fasteners. Severstal-Metiz has quality standard certification under International Standard ISO/TS 16949:2002.

**Products**

***Crude steel products.*** With total crude steel production of 11.9 million tonnes in 2007 and crude steel production capacity of 13.2 million tonnes per year, the Russian Steel Division's utilisation rate was approximately 90 percent.

The following table sets forth the Russian Steel Division's production of crude steel in 2005, 2006 and 2007, as well as the estimated aggregate production of crude steel in Russia and the Russian Steel Division's estimated share of production.

*Crude Steel Production — Russian Steel Division*

| Year | Russian Steel Division | Estimated aggregate production of crude steel in Russia | Russian Steel Division's estimated share of production in Russia |
|---|---|---|---|
| | *(million tonnes)* | | *(percent)* |
| 2005 | 10.8 | 64.87 | 16.7 |
| 2006 | 11.3 | 69.31 | 16.3 |
| 2007 | 11.9 | 72.39 | 16.4 |

Source: Chermet Corporation.

***Semi-finished products.*** Semi-finished products are intermediary products from the production process and represent generic steel products that have not yet been rolled for a specific application. The Group classifies the following products as "semi-finished", which are normally not classified as "saleable goods": (i) steel ingots or steel slabs from continuous casting; and (ii) billets from the continuous billet mill prior to treatment in the rolling mills.

***Finished steel products.*** Most of the Russian Steel Division's crude steel production is further processed into finished steel products, which include flat and long products. Flat products include hot-rolled and cold-rolled sheet, plates and coils. Long products include hot-rolled sections, cold-formed shapes and pipes.

The following table sets forth the Russian Steel Division's production by product category in 2005, 2006 and 2007.

*Production by Product — Russian Steel Division*

| | Year ended 31 December | | |
|---|---|---|---|
| | 2005 | 2006 | 2007 |
| | | (thousand tonnes) | |
| **Russian Steel Segment Steel Products**[(1)] | | | |
| Semi-finished products | 925 | 537 | 731 |
| Hot-rolled sheet and plate | 4,898 | 5,001 | 5,382 |
| Cold-rolled sheet | 2,418 | 2,613 | 2,568 |
| Hot-rolled sections | 1,594 | 1,913 | 2,025 |
| **Total** | **9,835** | **10,064** | **10,706** |
| *Some of the above products are then processed into:* | | | |
| Other tubes and pipes formed shapes | 343 | 408 | 430 |
| Galvanised and other metallic coated sheet | 600 | 699 | 735 |
| Colour-coated sheet | — | 148 | 230 |
| **Metalware** | | | |
| Metalware products | 826 | 1,104 | 1,047 |
| **Izhora Pipe Mill** | | | |
| Pipe products | — | 12 | 299 |

Note:

(1) Includes internal consumption and/or products used for further processing.

*Hot-rolled sheet and plate.* Hot-rolled flat products include heavy-gauge plate and light-gauge hot-rolled sheet produced from ordinary and high-quality carbon steel, low-alloy strengthened steel and clad steel. Clad steel includes two and three-ply steel combined with a corrosion-resistant or wear-resistant ply.

The Russian Steel Division produces hot-rolled plate with a maximum thickness of 450 millimetres, up to 4,800 millimetres in width and 20,000 millimetres in length, as well as coils for rerolling of up to 36 tonnes. Heavy-gauge plate is used to manufacture pipes, oil and gas tanks, ships, bridge structures and railway cars. Light-gauge hot-rolled sheet has a minimum thickness of 0.8 millimetres and is used for welded pipe and tubing, automotive parts, small-size shapes, channels and profiles.

*Cold-rolled sheet.* A cold-rolled flat product consists of cold-rolled sheet and coils with a thickness of 0.25 to 3.2 millimetres and is up to 1,620 millimetres in width. Cold-rolled sheet, which has a greater plasticity and a better surface quality than hot-rolled sheet, has various uses, including the manufacture of automotive body-panels and home appliances. In addition, cold-rolled products serve as feedstock for the Russian Steel Division's galvanised and roll-formed products.

The Russian Steel Division is able to produce sophisticated steel grades for pipe manufacturing as well as high-quality steel with a very low level of impurities (sulphur content of less than 0.025 percent and a phosphorus content of less than 0.05 percent). The Russian Steel Division believes that the large-diameter pipes that the Izhora Pipe Mill manufactures are not currently produced elsewhere in Russia. Other goods manufactured by the Russian Steel Division include civil construction goods and associated products.

*Other tubes and pipes, formed shapes.* A cold-rolled flat product consists of cold-rolled sheet and coils with a thickness of 0.25 to 3.2 millimetres and is up to 1,620 millimetres in width. Cold-rolled sheet, which has a greater plasticity and a better surface quality than hot-rolled sheet, has various uses, including the manufacture of automotive body-panels and home appliances. In addition, cold-rolled products serve as feedstock for the Russian Steel Division's galvanised and roll-formed products.

*Galvanised and other metallic coated sheet.* The Russian Steel Division produces over 250 types of carbon and low-carbon steel roll-formed shapes, including perforated, close-welded square and rectangular sections. Profiles with rectangular and square cross sections are widely used in the agricultural machine-building, civil construction and automotive industries. Cold-formed sections also include a wide range of pipes and construction and furniture materials.

*Coated/galvanised products.* The Russian Steel Division produces aluminium-coated and galvanised products, including those produced for the automotive industry by Severgal. The Russian Steel Division believes that demand from international automotive manufacturers will increase demand for galvanised products. Due to the strict requirements of automotive plants outside Russia, the Russian Steel Division has focused on improving the quality of its products significantly and has developed new grades of products (for example, products with an alumino-silicon coating and high-strength steels) to meet the demands of automotive customers. The Russian Steel Division has benefited from Severstal North America's experience in manufacturing high-quality galvanised products for the automotive industry.

*Hot-rolled sections.* Hot-rolled steel sections are produced from ordinary carbon steel, high carbon steel, low-alloy steel, structural alloy steel and include equal and unequal angles, hexagonal shapes, round bars, steel strips, wire rods and reinforcement bars.

***Other steel products.*** Civil construction goods include a wide range of products such as door hinges, window butts, steel tiles and others. Associated products include a wide range of by-products (for example, chemical products including benzol and green vitriol, blast furnace and converter slag and other by-products of the metallurgical process). These products are purchased by customers in the agricultural, chemical and construction industries. The Russian Steel Division also provides various ancillary services to customers, primarily rolling services.

***Metalware.*** Severstal-Metiz's factories in Russia focus on the manufacture of long products, such as low carbon and high carbon wire rods, nails, cold-drawn steel, steel rope, netting and fastenings. Severstal-Metiz comprises three sites in Russia: the Cherepovets site, the Orel site and the Volgograd site, located in northwest Russia, central Russia and the Povolzhie region of Russia, respectively. It has an additional site in each of the Ukraine and the UK. Each of the locations in Russia and Ukraine are dynamically developing regions with a high concentration of industrial and consumer-type customers. In addition to enjoying significant geographic coverage, Severstal-Metiz operates in all of the basic segments of the Russian metalware product market as the products manufactured at the respective plants complement each other. Dneprometiz produces wire and certain other processed products at its production facilities located in Ukraine. In 2007, Dneprometiz had a total production of approximately 126,000 tonnes. Carrington had a total production of approximately 129,000 tonnes of wire in 2007 and supplied more than 50 countries worldwide.

***Large-diameter pipes.*** The Izhora Pipe Mill produces large-diameter pipes with three-layered anti-corrosion coating, diameters ranging from 610 millimetres to 1,420 millimetres and 18.3 metres in length, aimed at domestic customers in the gas industry, as well as domestic oil customers and some export customers.

**Supply Chain**

The principal raw materials used by the Russian Steel Division to produce steel include iron ore concentrate and pellets, coking coal, limestone and dolomite, non-ferrous metal and ferro-alloys and metal scrap. The Russian Steel Division maintains a minimum two-week reserve of all the main raw materials used in their production process. This reserve is normally increased to approximately three weeks during the winter to compensate for any potential break in supply due to bad weather and for increased consumption rates experienced during the colder weather. In addition, during the winter, the stocks of ferro-alloys and scrap are increased to one and three months, respectively.

The Russian Steel Division's steel production energy requirements include water, gas, electricity and steam.

***Raw materials.*** Severstal Resources has the capacity to provide approximately 100 percent of the iron ore and coal requirements of the Russian Steel Division's steel operations. In 2007, the Russian Steel Division's steel operations procured approximately 74 percent of its iron ore, concentrate and pellets, and 75 percent of its coal requirements from Severstal Resources, purchasing its remaining requirements from third-party sources. The Group believes that the use of third-party sources for iron ore requirements ensures the security and reliability of the Russian Steel Division's iron ore supplies. The Russian Steel Division's sources a portion of its coal requirements from third-party suppliers due to its requirements for coal with different mineral contents and chemical features.

The Cherepovets Steel Plant's raw materials requirements account for approximately 100 percent of the Russian Steel Division's total raw material requirements.

The following table sets forth a breakdown of the raw materials consumed by the Cherepovets Steel Plant in 2006 and 2007.

*Consumption of Raw Materials — Cherepovets Steel Plant*

| Raw materials | Year ended 31 December 2006 | 2007 |
|---|---|---|
| | *(thousand tonnes, except as otherwise noted)* | *(thousand tonnes, except as otherwise noted)* |
| Iron ore (concentrate and pellets) | 11,852.0 | 12,673.8 |
| Coal | 6,006.2 | 6,656.8 |
| Metal scrap | 3,591.3 | 3,541.0 |
| Ferro-alloys and non-ferrous metals | 187.3 | 201.7 |

*Iron ore and pellets.* The smelting process at the Russian Steel Division's blast furnace facilities requires 30 percent of the feedstock to be in the form of iron ore pellets, the majority of which are sourced from Severstal Resources. Iron ore concentrate and pellets are supplied to the Russian Steel Division's steel operations on the basis of contracts that are reviewed and renegotiated on an annual basis. All of the Russian Steel Division's operations contracts with its iron ore suppliers, including those with Severstal Resources, are concluded on an arm's-length basis. The Russian Steel Division's quality control of the iron ore supplies involves verifying suppliers' quality certificates and monitoring the moisture content, iron content and weight of the ore concentrate at laboratories located at each of the production facilities located within the Russian Steel Division's operations. On a case by case basis, contract arrangements provide for price adjustments depending on the quality of the concentrate.

The Cherepovets Steel Plant's iron ore requirements account for approximately 100 percent of the Russian Steel Division's total iron ore requirements.

The following table sets forth a breakdown of the iron ore consumed by the Cherepovets Steel Plant by supplier in 2006 and 2007.

*Consumption of Iron Ore Concentrate and Iron Ore Pellets — Cherepovets Steel Plant*

| Supplier | Year ended 31 December 2006 | 2007 |
|---|---|---|
| | *(million tonnes)* | |
| **Iron ore concentrate** | | |
| Olkon | 4.35 | 4.38 |
| Kovdorsky GOK | 2.95 | 3.03 |
| Yakovlevskaya Ruda | — | 0.26 |
| Other | 0.34 | — |
| **Iron ore pellets** | | |
| Karelsky Okatysh | 4.21 | 5.00 |

*Coal.* The Russian Steel Division meets nearly all of its annual coke supply requirements from its own coke batteries, using coal purchased from Severstal Resources.

The Russian Steel Division has long-standing relationships with its key coal suppliers, which consist primarily of companies in Severstal Resources, in particular Vorkutaugol. Vorkutaugol has been supplying coal to the Russian Steel Division and its predecessors for over 40 years. Geographically, the Cherepovets Steel Plant is closer to Vorkutaugol than Vorkutaugol's other customers.

All contracts with the Russian Steel Division's coal suppliers, including those with Severstal Resources, are concluded on an arm's-length basis and may be suspended if suitable coal can be purchased from alternative suppliers at lower prices. Contracts are generally concluded for a term of one year, with the intention of ensuring continuity, security and reliability of supplies. Payment under these contracts is made on delivery.

The Cherepovets Steel Plant's coal requirements account for approximately 100 percent of the Russian Steel Division's total coal requirements.

The following table sets forth a breakdown of the coal consumed by the Cherepovets Steel Plant by supplier in 2006 and 2007.

*Consumption of Coal — Cherepovets Steel Plant*

| | Year ended 31 December | |
|---|---|---|
| **Supplier** | **2006** | **2007** |
| | *(million tonnes)* | |
| Vorkutaugol[(1)] | 3.54 | 3.96 |
| Kuzbassugol[(1)] | 0.88 | 1.07 |
| Sibuglemet | 0.92 | 0.50 |
| Prokopyevskugol | 0.23 | 0.10 |
| Mechel | 0.13 | 0.64 |
| Other | 0.30 | 0.39 |

Note:

(1) Vorkutaugol is part of the Group. Kuzbassugol was part of the Group until its disposal in April 2008.

*Scrap.* The Russian Steel Division is a significant consumer of scrap in Russia and sources its scrap on a spot basis from smaller suppliers and on a contract basis for larger volumes.

The Russian Steel Division has its own scrap-processing facilities that allow it to utilise a wide range of sizes of steel scrap. These facilities include special cutting and packaging lines for processing the scrap so that it is ready for use in the smelting process. Scrap is sourced both externally, from companies that collect scrap metal, and internally, by using amortisation scrap, which is fixed assets that were cut up and melted down at the end of their useful lives, and production waste. Scrap is used in all steel-melting processes; the average proportion of scrap metal in the metal charge used in the smelting process ranges from approximately 30 percent in the oxygen converter and open-hearth furnace shops to close to 80 percent in the electric arc shop.

In 2007, the Russian Steel Division processed approximately 4.6 million tonnes of scrap, of which 3.5 million tonnes were purchased and 1.1 million tonnes were internally sourced from the Cherepovets Steel Plant.

It is currently expected that with effect from 1 August 2008, management responsibility for the scrap operations is to be transferred to the Russian Steel Division from Severstal Resources. See also "— Severstal Resources". The Group believes that the scrap operations more appropriately fit within the Russian Steel Division, particularly given the planned construction of two mini-mills, the first of which is currently expected to be completed in 2010, and the resulting significant increase in the consumption of scrap metal (see "— Capital Expenditure Programme").

*Other raw materials.* The Russian Steel Division sources limestone from its open-pit limestone mines located in the northern part of the Vologda region in Russia, approximately 250 kilometres from Cherepovets.

A wide range of ferro-alloys is also used in the steelmaking process. Non-ferrous metals, such as zinc, manganese and aluminium, are employed primarily in the production of higher value-added steel products, such as galvanised sheet. The Russian Steel Division sources most of its ferro-alloy requirements from third-party suppliers under annual contracts.

The Russian Steel Division also imports certain raw materials, such as ferro-alloys and refractory materials, from France, Austria, China and Ukraine. Contracts are typically for a term of one year, with prices being fixed on a quarterly basis, or adjusted monthly by reference to market rates. Prices for non-ferrous metals are generally linked to the London Metal Exchange prices for such metals.

***Energy.*** The Russian Steel Division's electricity requirements total approximately 6.9 billion kilowatt hours per year. In 2007, 44.9 percent of these electricity requirements were provided by two on-site power stations owned by the Russian Steel Division. The two power stations have a total installed capacity of approximately 446 megawatts. The power stations generate electricity by burning natural gas and waste by-products from the steel mill's production process, such as coke breeze, blast-furnace gas and coke-oven gas. Recycling waste by-products creates significant cost savings. As a result, the Russian Steel Division uses a relatively low amount of energy coal to generate electricity at its facilities. The Russian Steel Division covers its remaining electricity requirements through direct contracts to buy electricity in the Russian wholesale electricity market, typically with a term of one year.

The Cherepovets Steel Plant's energy requirements account for a substantial portion of the Russian Steel Division's total energy requirements.

The following table sets forth a breakdown of the energy consumption of the Cherepovets Steel Plant in 2006 and 2007.

*Consumption of Energy — Cherepovets Steel Plant*

| | Year ended 31 December | |
|---|---|---|
| **Energy consumption** | **2006** | **2007** |
| Electricity (millions of kilowatt hours)(1) | 6,529.9 | 6,887.1 |
| Natural gas (million cubic metres) | 2,590.0 | 2,642.5 |
| Diesel and fuel oil (thousands of tonnes) | 48.3 | 49.6 |

Note:

(1) Cherepovets Steel Plant's electricity generation facilities generated 2,825.3 million kilowatt hours and 3,092.6 million kilowatt hours in 2006 and 2007, respectively, the majority of which was used by the plant, and some of which was used by other production facilities or lost in transmission. The plant purchased 3,756.4 million kilowatt hours and 3,848.6 million kilowatt hours in 2006 and 2007, respectively.

As shown in the table above, the Cherepovets Steel Plant, and therefore the Russian Steel Division, purchases a significant amount of electricity from third-party suppliers in addition to the amount it produces internally. Prices for electricity in the Russian market have continued to increase and further increases are expected in line with the significant capital expenditure requirements of the Russian electricity industry. If prices from third-party suppliers remain high and if it is economically feasible to do so, the Russian Steel Division would consider constructing additional generating units, and it is currently developing plans to build a third power station on the site of the Cherepovets Steel Plant.

To generate heat, the steelmaking facilities within the Russian Steel Division use blast-furnace gas. The gas used is sufficient to meet all of the heat requirements of the Russian Steel Division, with surplus heat being sold to local utilities.

Natural gas and fuel oil also form part of the Russian Steel Division's energy requirements. Natural gas is used as a heat source in the open-hearth furnaces, blast furnaces, reheating lines and power plants.

The power plants within the Russian Steel Division operate a combined cycle. These plants burn gases, including natural gas, to generate steam for electricity and burn by-product coal breeze from the coking plants to supplement hot water and industrial steam output. The Russian Steel Division's power plants use fuel oil only in emergencies.

The Russian Steel Division purchases its natural gas from a subsidiary of Gazprom, the national gas supplier, under a five-year contract expiring in 2012 primarily at prices established by the Russian Federal Tariff Service. Affiliates of Gazprom, LukOil and TNK-BP supply fuel oil, typically under contracts with a term of one year, with a price determined monthly.

**Capital Expenditure Programme**

The Russian Steel Division's capital expenditure in 2006 and 2007 was approximately US$691.9 million and approximately US$548.1 million, respectively, most of which was spent on new projects as well as on the repair and modernisation of its existing steel operations. The Russian Steel Division's capital expenditure programme is designed to increase productivity and efficiency, effect environmental upgrades, replace and refurbish major equipment, and develop its product mix further to produce higher-quality, value-added products, including galvanised steel and cold-rolled products. New products under development include tube-making strips, such as X-70 and X-100 API-class strength steel for large-diameter pipelines; heavy plates for a shipbuilding project to be rolled by the 2800 and 5000 rolling mills; hot-dip galvanised sheets for automotive exposed parts and IF-steels; new-class carbon and low-alloyed steels with increased corrosion-resistant and low-temperature-resistant properties; long products of A 500C class for construction applications.

As a result of the capital expenditure programme, modern processing technology and equipment from leading suppliers to the steel industry, including Fuchs, LOI and Siemens, have been installed at the Russian Steel Division's facilities.

The Russian Steel Division's total capital expenditure from 2008 to 2012 is expected to be approximately US$8.8 billion, as set forth in the following table.

*Estimated Capital Expenditure Requirements from 2008 to 2012 — Russian Steel Division*

| Facilities | Estimated cost |
|---|---|
| | *(US$ millions)* |
| **Cherepovets Steel Plant** | |
| Coking plant | 383 |
| Sintering plant | 83 |
| Blast furnace shop | 1,061 |
| Converter shop | 268 |
| Hot-rolling shop | 938 |
| Cold-rolling shop | 133 |
| Capital maintenance | 2,744 |
| Transportation facilities | 95 |
| Other, including infrastructure projects | 701 |
| **Total** | **6,406** |
| **Severgal, Izhora Pipe Mill and Severstal-Metiz** | 649 |
| **Mini-mills** | 1,502 |
| **Other projects** | 194 |
| **Total** | **8,751** |

***Cherepovets Steel Plant.*** Capital expenditure planned at the Cherepovets Steel Plant is primarily as follows:

*Blast furnace facilities.* Blast Furnace 3 was decommissioned at the end of 2006 for refurbishment, and is expected to remain out of operation until 2010. Blast Furnaces 3, 4 and 5 are scheduled to have pulverised coal injection technology installed, to be completed by 2011. Reconstruction of the hot blast stoves in Blast Furnace 5 is also planned, as well as the decommissioning of Blast Furnace 2. Coke batteries 4 and 7 are to be refurbished from 2011 to 2012 and from 2009 to 2011, respectively.

*Converter shop.* The capital expenditure programme is to be used for improving the quality of output, to enable the production of new products, such as X-70 and X-100 API-class strength steel. Continuous Casting Machine 2 is to be fully reconstructed and the other continuous casting machines are to be modernised. A pig iron desulphurisation unit and dust-treatment equipment are also to be installed. This is expected to increase the combined capacity of the continuous casters and the quality of the product.

*Flat rolling facilities.* Automated systems and sheet-straightening machines are to be installed and heating facilities refurbished. Mill 5000 is also to be modernised and expanded to produce high-quality strips for large-diameter pipes and other applications which, when completed, are expected to increase the capacity of Mill 5000 to 850,000 tonnes per year.

Pickling lines 1 and 3 are to be renovated to provide facilities for 100 percent of hydrochloric pickling and to increase the capacity of the pickling lines to 3.6 million tonnes per year in aggregate. The cold-rolling equipment is to be refurbished to increase the rolling mill's production capacity from 2.8 million tonnes per year to 3.2 million tonnes per year by 2011.

*Energy-generating facilities.* The capital expenditure programme aims to increase the reliability of gas and energy supplies to the major production shops. This is expected to include the commissioning of two air-separating units in the oxygen shop to increase the production of converter steel and introduction of an automatic control and management system for energy resources, lower level of energy management. To supply steam and treated water to Severgal, the water-treatment station at the Cherepovets Steel Plant is expected to be refurbished and a steam boiler constructed. In addition, it is planned that the power-generating equipment will be modernised. Variable frequency drive installation and cooling-tower refurbishment are also planned. In 2007, the Group entered into a loan agreement with EBRD, which was amended in March 2008, for an aggregate principal amount of €600 million, the proceeds of which will to be used to finance some of these planned projects.

*Capital maintenance.* The capital expenditure on capital maintenance is primarily aimed at sustaining the production facilities at the Cherepovets Steel Plant as the useful life of the facilities expires and planned significant overhauls are required.

*Transportation facilities.* Capital expenditure on transportation facilities in the Russian Steel Division are also planned, including the development of its internal railway infrastructure and the purchase of coil delivery ramps and locomotives.

*Other facilities.* Capital expenditure in downstream facilities within the Russian Steel Division are also planned, including the construction of the Sheksna Pipe Mill and service centres in Russia, aimed at increasing the production and distribution of high-value added products. The Sheksna Pipe Mill is expected to be completed by the end of 2009, at an estimated cost of approximately US$110 million. The pipe mill is to have a capacity of 250,000 tonnes per year and is to be located close to the Cherepovets Steel Plant, from which it will obtain raw materials. The pipe mill is to supply products for use in the Russian construction industry, an industry which has grown significantly in Russia in recent years.

***Severgal, Izhora Pipe Mill and Severstal-Metiz.*** Severgal and Izhora Pipe Mill are new assets and are not expected to require significant additional capital expenditure in the near future. Severstal-Metiz has implemented capital expenditure programmes to enhance the efficiency of its assets and has formed a long-term development strategy. Its annual capital expenditure in 2007 was approximately US$30 million. The capital expenditure programmes include the development of M20-M30 fasteners, PC strands production, and operational optimisation programmes at the Volgograd plant.

***Mini-mills.*** The Russian Steel Division plans to construct two mini-mills in Russia, each with a planned capacity of approximately 1 million tonnes of finished long products per year. In July 2007, development commenced on the first of these mini-mills, to be built in the Saratov region in Russia, which is currently expected to be completed in 2010 at an estimated cost of approximately US$571 million. The second mini-mill is to be built in central Russia, and for which a suitable location is currently being sought. These production facilities are to be located close to growing markets for steel products, primarily from the construction industry, as well as markets for scrap metal, the primary raw material for their EAFs.

### Research and Development

The Russian Steel Division has pursued research and development initiatives with Russian universities and research institutes. Such initiatives include a research and development centre for cokemaking and ironmaking and studies for oil and gas pipe and shipbuilding steel applications.

The Russian Steel Division is also conducting cold-rolled products research initiatives, including the development of new kinds of strips and pipes not currently produced in Russia, development of more durable autosheet, research to increase the efficiency of the manufacturing process for sheet for the motor industry, optimisation of chemical compound and technological parameters for improvement of surface quality and reduction of expenses in the production of cold-rolled sheet and development of technological bases and optimum parameters for the production of hot-dip galvanised steel for the automotive industry.

### Sales and Marketing

#### *Russian Steel segment*

The Russian Steel segment sells its products in both export and Russian domestic markets. The Russian Steel segment views the Russian domestic market as strategically important and has implemented a long-term programme designed to broaden its customer base and develop its relationship with various key customers. In the export markets, the Russian Steel segment aims to sell products for which there is low demand in Russia, and sales are made predominantly on a spot-market basis.

The following table sets forth the sales by market for the Russian Steel segment in 2006 and 2007.

*Sales by Market — Russian Steel Segment*[(1)]

| | Year ended 31 December | | | |
|---|---|---|---|---|
| **Market** | **2006** | | **2007** | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Russian domestic sales | 6,707 | 66.4 | 7,466 | 68.6 |
| Export sales | 3,387 | 33.6 | 3,424 | 31.4 |
| **Total** | **10,094** | **100.0** | **10,890** | **100.0** |

Note:

(1) Includes intersegmental sales.

The following table sets forth the sales by industry sector for the Russian Steel segment in 2006 and 2007.

*Sales by Industry Sector — Russian Steel Segment*[(1)]

| | Year ended 31 December | | | |
|---|---|---|---|---|
| **Industry sector** | **2006** | | **2007** | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Steel industry | 878 | 8.7 | 703 | 6.5 |
| Automotive | 965 | 9.6 | 922 | 8.5 |
| Pipemaking | 2,057 | 20.4 | 2,504 | 23.0 |
| Construction | 256 | 2.5 | 356 | 3.3 |
| White goods | 103 | 1.0 | 81 | 0.7 |
| Machine building | 419 | 4.1 | 413 | 3.8 |
| Shipbuilding | 104 | 1.0 | 64 | 0.6 |
| Railway industry | 118 | 1.2 | 143 | 1.3 |
| Trading and regional distribution[(2)] | 5,194 | 51.5 | 5,704 | 52.3 |
| **Total** | **10,094** | **100.0** | **10,890** | **100.0** |

Notes:

(1) Includes intersegmental sales.

(2) Regional distribution includes sales to large-scale warehouses, regional supply agencies and traders.

***Russian domestic sales.*** The Russian Steel segment continues to regard Russia as its most important market, which is characterised by lower transportation costs for delivery to customers. This market has certain advantages, including the ability to realise higher profit margins, high demand from domestic industries that rely on a stable supply of steel products and the ability to develop long-term strategic alliances with customers. As domestic sales have higher profit margins than export sales, the Russian Steel segment aims to increase its share of domestic sales in the future. In 2007, the share of domestic sales increased to approximately 69 percent of its total sales by volume.

*Customers.* The Russian Steel segment's most important customers are the pipe-manufacturing and automotive sectors. Since 2007, the Russian Steel segment has also attached an increasing importance to the growing construction and construction materials sectors, which include a number of important customers located in the European part of Russia, as well as to the large customers emerging in the developing economies of several CIS countries.

Almost all of the Russian Steel segment's domestic sales are made by the Cherepovets Steel Plant, either directly to an end customer or to trading and distribution entities (see also "— Distribution"). The following paragraphs briefly describe the main end customers to which the Cherepovets Steel Plant sells and not sales to trading and distribution entities, as this category deals with end customers on an ad-hoc basis as opportunities arise, often selling single quantities of product to single-time customers.

The pipe manufacturing sector accounted for approximately 26 percent of the Cherepovets Steel Plant's total domestic sales by volume in 2007 and approximately 23 percent in 2006. The Cherepovets Steel Plant's principal customers in the pipe manufacturing sector are the Vyksa and Chelyabinsk pipe plants. The Cherepovets Steel Plant sold more than 2 million tonnes of different products to domestic customers in this sector in 2007. The Cherepovets Steel Plant is able to produce sophisticated steel grades for pipe manufacturing as well as high-quality steel with a very low level of impurities, namely, a sulphur content of less than 0.025 percent and a phosphorus content of less than 0.05 percent.

The Russian automotive sector accounted for approximately 11 percent of the Cherepovets Steel Plant's total domestic sales by volume in 2006, decreasing to approximately 9 percent in 2007, reflecting in part a reduction in the competitiveness of domestic car producers. The Cherepovets Steel Plant's key customers in the domestic automotive sector are GAZ, AutoVAZ and UAZ. The Cherepovets Steel Plant sold approximately 730,000 tonnes of steel products to the automotive sector in Russia in 2007. Due to the strict requirements of automotive plants, especially those outside Russia, the Russian Steel segment has focused on improving the quality of its products significantly and has developed new grades of products (for example, products with an alumino-silicon coating and high-strength steels) to meet the demands of customers and has benefited from Severstal North America's experience in manufacturing high-quality galvanised products for the automotive industry.

*Key customer management.* The Russian Steel segment has identified 11 key domestic customers as part of a project to work in close co-ordination with customers in strategically important sectors, including such large accounts as OMK, OAO Volzhsky Pipe Plant, Chelyabinsk pipe plant, AutoVAZ, UAZ, GAZ and Caterpillar. The Russian Steel segment works with these customers as part of its "key account management" process, managed by a dedicated team which includes the development of new products and leads to further innovations both for the customer and the Russian Steel segment. Services for such customers include the construction of consignment warehouses in different regions and quarterly product-quality co-ordination, overseen by representatives of both the Group and the relevant customer. Sales by the Cherepovets Steel Plant to such customers account for a substantial portion of the Russian Steel segment's total sales.

*Distribution.* The Russian Steel segment's domestic sales are made to regional and other distributors, directly to end-users, or through ZAO Trading House Severstal Invest ("**TD Severstal Invest**"), an entity controlled by the Controlling Shareholder, outside of the Group.

The regional distribution of the Russian Steel segment's products involves the delivery of steel products to large warehouses, regional supply agencies, and traders from which they are distributed to a wide range of customers (including small businesses and the public). The Russian Steel segment sold approximately 3.7 million tonnes and 3.0 million tonnes of steel products to this group of Russian customers in 2007 and 2006, respectively.

The Russian Steel segment also sells a considerable amount of its production volume (approximately 750,000 tonnes in 2007) to domestic customers through TD Severstal Invest.

Export sales are conducted entirely through the Russian Steel segment's export trading subsidiaries.

*Products.* The Russian Steel segment's domestic sales are dominated by hot-rolled sheet and sections, which accounted for approximately 72 percent of total domestic sales by volume in 2007. Higher value-added products such as cold-rolled and coated sheet are also very significant, making up approximately 22 percent of total domestic sales by volume in 2007.

The following table sets forth the domestic sales by product for the Russian Steel segment in 2006 and 2007.

*Domestic Sales by Product — Russian Steel Segment[(1)]*

| **Product** | **Year ended 31 December** | | | |
|---|---|---|---|---|
| | **2006** | | **2007** | |
| | *(thousand tonnes)* | *(percent of domestic sales by volume)* | *(thousand tonnes)* | *(percent of domestic sales by volume)* |
| Semi-finished products | 7 | 0.1 | 36 | 0.5 |
| Hot-rolled strip and plate | 2,809 | 41.9 | 3,419 | 45.8 |
| Cold-rolled sheet | 963 | 14.4 | 909 | 12.2 |
| Galvanised and other metallic coated sheet | 607 | 9.1 | 556 | 7.4 |
| Colour coated sheet | 132 | 2.0 | 201 | 2.7 |
| Long products | 1,801 | 26.9 | 1,931 | 25.9 |
| Others tubes and pipes, formed shapes | 340 | 5.0 | 376 | 5.0 |
| Metalware products | 48 | 0.6 | 38 | 0.5 |
| **Total** | **6,707** | **100.0** | **7,466** | **100.0** |

Note:

(1) Includes intersegmental sales.

*Contracts.* The Russian Steel segment has developed an approach to contractual relations with its Russian domestic customers that is relatively new in Russia. Contracts are concluded on a quarterly, semi-annual, annual or 15-month basis depending on the customer. Factors determining the length of the contract include, for example, relationship history, industry and significance of the customer in its industry. Contracts also include a flexible system of discounts and rebates that provides for adjustments to the contract price on the basis of product tonnage, timing of payment and other contractual terms.

Contracts for key customers usually have a duration of approximately three months, after which the price may be renegotiated, and may include other customised terms.

The Russian Steel segment seeks prepayments from certain customers, including new customers and those companies who are considered to be at risk financially. In 2007, prepayments accounted for less than 10 percent of the Russian Steel segment's sales by value. The remainder of contracts require settlement within a range of five to thirty days from delivery (accounting for approximately 58 percent of sales by value in 2007) and combined settlements (accounting for approximately 35 percent of sales by value in 2007). The Russian Steel segment offers credit to a number of key customers of up to thirty days under bank guarantees. This flexibility of contract and credit terms has generated a significant competitive advantage for the Russian Steel segment, allowing it to forge closer ties with customers and to react more effectively to changes in market conditions. In recent years, the Russian Steel segment has experienced relatively low levels of bad debts.

***Export sales.*** In line with its strategy of focusing on the Russian domestic market, the Russian Steel segment's export sales strategy is, on the whole, oriented towards identifying spot markets of steel products.

*Customers.* The Russian Steel segment also focuses on a number of export customers irrespective of the fact that sales to such customers do not represent a substantial proportion of total export sales. These customers are often targeted for other strategic reasons, for example, to establish relationships with the customer, particularly where the customer is likely to establish or has recently established operations in Russia or where the Russian Steel segment aims to gain further exposure to sophisticated customers with complex specification requirements.

The Russian Steel segment's primary export customers are companies in the automotive industry, such as Fiat, Ford Motor Company, General Motors Corporation, Renault, Greif (formerly Van Leer), Philips, Merloni and Electrolux, for which it produces galvanised sheet steel with a high-quality surface and other high-quality products.

*Distribution.* The Russian Steel segment conducts its export sales primarily through two export-trading subsidiaries, Severstal Export GmbH and AS Severstallat, as well as through LLC Severstal-Ukraine and ZAO SeverStalBel. This system has enabled the Russian Steel segment to increase the efficiency of its export operations by minimising its reliance on intermediaries in the sales process and, therefore, reducing its distribution costs.

Severstal Export GmbH is the marketing centre for the Russian Steel segment's sales operations in the export markets, excluding the Baltic States, which are covered by AS Severstallat. Handling export operations through one centre has allowed the Russian Steel segment to achieve cost savings through lower administrative expenses, to benefit from large volumes and to eliminate intermediaries from the distribution chain.

AS Severstallat has been the Russian Steel segment's export agent in the Baltic region since its formation in 1992. Although the Russian Steel segment has direct contracts with certain customers in the Baltic market, the majority of sales contracts, primarily with shipbuilding companies, are entered into through AS Severstallat. AS Severstallat is currently a joint venture between Severstal Trade, which owns 50.5 percent, and local partners, not affiliated with the Russian Steel segment, and was originally established in 1992. AS Severstallat was founded to manage the transportation of the Russian Steel segment's products for export sale through the Baltic countries and at Baltic ports. Changes in railway tariffs led to AS Severstallat's reorganisation in 2001. AS Severstallat now operates as an export agent, a customer-oriented regional service centre and a producer of metal products for Baltic countries and elsewhere in Northern and Eastern Europe. It conducts a variety of businesses, including direct metal sales, a cutting service for coils and the production of long products and pipes.

Both of the Russian Steel segment's export trading companies are responsible for the day-to-day management of export operations, with monitoring provided by the Russian Steel segment's sales department in collaboration with the trading companies described above. This system provides a higher degree of control over export operations and ensures that these operations are aligned with the Russian Steel segment's long-term strategy.

*Products.* The Russian Steel segment's export sales are predominantly flat products, with hot-rolled products and cold-rolled products accounting for approximately 62 percent of sales by volume in 2007. Semi-finished products are also a significant part of total sales, due to strong cost advantages in the merchandise slab market.

The following table sets forth the export sales by product for the Russian Steel segment in 2006 and 2007.

*Export Sales by Product — Russian Steel Segment[(1)]*

| Product | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2006 | | 2007 | |
| | *(thousand tonnes)* | *(percent of export sales by volume)* | *(thousand tonnes)* | *(percent of export sales by volume)* |
| Semi-finished products | 570 | 16.8 | 845 | 24.7 |
| Hot-rolled strip and plate | 1,850 | 54.6 | 1,602 | 46.8 |
| Cold-rolled sheet | 607 | 17.9 | 509 | 14.9 |
| Galvanised and other metallic coated sheet | 87 | 2.6 | 195 | 5.7 |
| Colour coated sheet | 11 | 0.3 | 27 | 0.8 |
| Long products | 121 | 3.6 | 120 | 3.5 |
| Others tubes and pipes, formed shapes | 131 | 3.9 | 119 | 3.4 |
| Metalware products | 10 | 0.3 | 7 | 0.2 |
| **Total** | **3,387** | **100.0** | **3,424** | **100.0** |

Note:

(1) Includes intersegmental sales.

***Metalware***

Severstal-Metiz sells its products in both international and domestic markets, with the majority of sales being domestic sales.

The following table sets forth the sales by market for Metalware in 2006 and 2007.

*Sales by Market — Metalware[(1)]*

| Market | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2006 | | 2007 | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Domestic sales[(2)] | 870.5 | 78.9 | 622.2 | 59.4 |
| Export sales[(3)] | 233.1 | 21.1 | 425.4 | 40.6 |
| **Total** | **1,103.6** | **100.0** | **1,047.6** | **100.0** |

Notes:

(1) Includes intersegmental sales.

(2) Domestic sales includes sales in Russia and Belarus.

(3) Export sales are sales outside of Russia and Belarus.

***Domestic sales.*** Severstal-Metiz continues to regard Russia as its most important market, which is characterised by lower transportation costs for delivery to customers from its Russian production facilities. This market has certain advantages, such as significant demand from the domestic construction industry and greater profit margins, compared with export markets. Historically, sales in Belarus have not been a significant part of Severstal-Metiz's domestic sales.

Severstal-Metiz's most important Russian customers are in the construction industry and the mass market, which consists primarily of small and medium-sized businesses, housing and communal services providers and as well as individuals. The construction industry accounted for approximately 24 percent of Severstal-Metiz's total domestic sales by volume in 2007. Due to the absence of significant consolidation in the construction industry, Severstal-Metiz's customer base is large. The mass market accounted for approximately 23 percent of Severstal-Metiz's domestic sales by volume in 2007. In addition, sales to the railway, automotive and machine building industries accounted for approximately 12 percent, 8 percent and 7 percent, respectively, of domestic sales by volume in 2007.

The largest part of Severstal-Metiz's domestic sales is high-carbon products, such as ropes and steel wire, as well as low-carbon wire, which together accounted for approximately 59 percent of total domestic sales by volume in 2007.

Severstal-Metiz's Russian customers purchase on a range of contractual terms, varying from point-of-sale transactions to long-term contracts of typically three, six or twelve months duration and depending also on factors such as the customer's history and the industry. Severstal-Metiz typically seeks prepayments from certain customers, including new customers and those who are considered to be at risk financially. A flexible system of discounts and rebates may also be given according to product tonnage, timing of payment and other matters.

***Export sales.*** The main international markets into which Severstal-Metiz sells are those in the CIS, as well as Europe. Its customers are generally in similar industries to those in the Russian market. Severstal-Metiz conducts its export sales primarily through Dneprometiz, which sells primarily to customers in the Ukraine, and Carrington, which sells primarily to customers in the UK.

In 2007, Severstal-Metiz's export sales amounted to approximately 425 thousand tonnes of metalware.

***Izhora Pipe Mill***

In 2007, the first year of significant production, Izhora Pipe Mill sold approximately 95 percent of its sales by volume in the Russian domestic market. The Izhora Pipe Mill's largest customer is the oil and gas industry, and in particular, Gazprom, Transneft and Novatek, sales to whom represented approximately 94 percent of the mill's sales by volume in 2007. Sales are made directly to customers, with a contractual term of typically one year.

## Severstal International

Severstal International consists of two segments, North America and Lucchini.

### North America

North America comprises the Group's operations in the United States. North America consists of Severstal North America, SeverCorr and Sparrows Point. The Group has recently acquired WCI Steel (see "— Recent Developments") and has commenced an offer to acquire all of the outstanding shares of common stock of Esmark (see "— Recent Developments").

#### *Severstal North America*

Severstal North America's production facility is located in Dearborn, Michigan ("**Dearborn**"). This location gives Severstal North America strategic proximity to major automotive customers, Great Lakes waterways and to three large railroads in North America, providing logistically favourable access to raw materials and to customers. Dearborn has a crude steel production capacity of 3.2 million tonnes per year, assuming blast furnace "B", which is currently being rebuilt and is expected to be re-commissioned by the end of 2009, is operational. Dearborn's product line includes hot-rolled, cold-rolled and galvanised steel. These products — and in particular the value-added products such as high strength, high-carbon and low-alloy steel — are largely targeted at the automotive industry.

Severstal North America has three joint ventures and an associate, each established with US companies, for the purpose of expanding its product line:

- Double Eagle Steel Coating Company, a 50 percent joint venture with US Steel, with a capacity of 800,000 tonnes per year ("**Double Eagle**");
- Spartan Steel Coating, LLC, a 48 percent joint venture with Worthington Steel of Michigan, with a capacity of 544,000 tonnes per year ("**Spartan Steel**"). Spartan Steel produces hot-dip galvanised sheet steel for automotive and service customers. Severstal North America supplies 100 percent of the substrate to Spartan Steel and sells 80 percent of Spartan Steel's production;
- Mountain State Carbon, LLC, a 50 percent joint venture between SNA Carbon, LLC (a wholly-owned subsidiary of Severstal North America) and Wheeling-Pittsburgh Steel Corporation ("**Mountain State Carbon**"). Mountain State Carbon is a metallurgical coke producer; and
- Delaco Processing, LLC, an associate owned 49 percent by Severstal North America and 51 percent by Delaco Supreme Tool and Gear Company ("**Delaco Processing**"). Delaco Processing specialises in longitudinal slitting of steel coils and is capable of slitting steel coils with a width of up to 1,892 millimetres.

#### *SeverCorr*

SeverCorr is a steel mill which employs the latest and, in some aspects, unique steelmaking technology provided by SMS Demag AG, with a production capacity of 1.5 million tonnes of finished products per year, and produces a full range of flat rolled products, including exposed automotive steel. Built in Columbus, Mississippi, SeverCorr has access to major railroads and highways. Because of the large number of car stamping and assembly facilities in the area close the SeverCorr site, it has a strategic location to supply its high-end steel products to the expanding industries in the southern part of the United States and northern parts of Mexico. The mill covers more than 305,000 square metres and features a melt shop, thin slab caster, six-stand hot mill, five-stand tandem cold mill and a hot-dip galvanising line. The Group currently plans to increase production at SeverCorr to approximately 3.0 million tonnes of finished products per year after completing a second construction phase ("**Phase II**"), which is expected to occur in 2010, with a production ramp-up anticipated to commence in late 2009. From January 2008, SeverCorr was consolidated into the Group's financial statements.

***Sparrows Point***

Sparrows Point is an integrated steel plant on the East Coast of the United States. The plant has its own deep water port and rail connection to both north-south and east-west rail networks. The plant has the third largest blast furnace in North America, which was completely relined in 1999 and has a crude steel production capacity of 3.4 million tonnes per year. Sparrows Point has its own sinter facility, which produces sinter, a raw material in the ironmaking process. The production facilities include two flexible and modern straight mould continuous casters and one modern cold mill, with a continuous pickle line coupled to the tandem mill, which was commissioned in 2000. Sparrows Point's product line consists of slabs (including 12-inch plate), hot-rolled, cold-rolled, coated zinc and zinc-aluminium products as well as tin coated steel. Sparrows Point has a self-contained tin mill, three active on-site hot-dip galvanising lines and its own on-site 120 megawatt power generation facility.

***Facilities***

North America's main production facilities at Severstal North America, SeverCorr and Sparrows Point are set forth below.

Severstal North America is focused primarily on high-quality flat products and has a production capacity at its Dearborn facility of 3.2 million tonnes of crude steel per year, assuming blast furnace "B", which is currently being rebuilt and is expected to be re-commissioned by the end of 2009, is operational. Severstal North America's Dearborn facility is fully integrated and is located on an industrial site adjacent to Ford's stamping, engine, frame, paint and assembly plants. These operations consist of two operating blast furnaces (although due to an accident on 5 January 2008, blast furnace "B" has been shut down and is expected to be re-commissioned by the end of 2009), two BOF vessels, two ladle refining facilities, one vacuum degassing facility, two continuous casters, one hot strip mill, three pickle lines, one tandem mill, one temper mill, a hot-dip galvanising line at Spartan Steel and an electrogalvanising line at Double Eagle. It also has a steel-slitting facility at Delaco Processing and a coke facility at Mountain State Carbon. These facilities enable Severstal North America to produce high-quality, flat-rolled carbon steel products consisting of hot-rolled, cold-rolled and galvanised steel.

SeverCorr is a "greenfield" project involving the construction of a mini-mill with a current production capacity of 1.5 million tonnes of finished products, located in Columbus, Mississippi. SeverCorr's operations consist of a DC arc furnace, which produces 150 tonne heats; a ladle metallurgy furnace; a vacuum tank degasser; and a thin-slab caster directly coupled to a six-stand hot strip mill via a tunnel reheat/equalising furnace. Finishing facilities include a coupled pickle line with a five-stand tandem cold reduction mill, hydrogen batch annealing furnaces, a temper mill and a hot-dip galvanising line. The facility serves a growing manufacturing industry in the southern United States. The facility has access to both rail and interstate truck routes for fast delivery to more than twelve targeted states and northern Mexico. The Group plans to increase the production capacity at SeverCorr to approximately 3.0 million tonnes of finished products per year after completing Phase II, which is currently expected to occur in 2010. The steelmaking operation and hot mill commenced operations in August 2007, with the first coil shipped in September 2007. As production commenced only at the end of 2007, production information for SeverCorr is unavailable for 2007.

Sparrows Point has flexible production capabilities, focused on construction, packaging, and semi-finished products, with a crude steel production capacity of 3.4 million tonnes per year. Sparrows Point operations consist of a sinter plant, one operating blast furnace, two BOFs, two straight mould continuous casters, one hot strip mill, one continuous pickler linked tandem mill, three active hot-dip galvanising lines, one hydrogen batch anneal, one temper/tension mill, and a self-contained tin mill operation. The tin mill operation consists of one pickle line, one tandem line, one continuous anneal line, batch anneal, two temper mills, and two plating lines. These facilities enable Sparrows Point to produce a wide range of products that serve multiple markets on the east coast and southeast of the US. The plant's deep water port and access to the Atlantic Ocean allow it to export to European markets.

The following table sets forth Severstal North America's actual output in 2005, 2006 and 2007 and equipment, capacity and utilisation rate by sub-segment as at 31 December 2007.

*Steel Production Facilities, Severstal North America — Output, Capacity and Utilisation Rate by Unit*

| Production facility | Actual output | | | As at 31 December 2007 | | Utilisation rate in |
|---|---|---|---|---|---|---|
| | 2005 | 2006 | 2007 | Equipment | Capacity | 2007 |
| | | (million tonnes) | | | (million tonnes) (as at 31 December 2007) | (percent) |
| **Dearborn** | | | | | | |
| Blast furnaces[(1)] | 2.272 | 2,119 | 1.656 | 2 furnaces | 3.096 | 53 |
| Basic oxygen furnace | 2.753 | 2.618 | 2.042 | 2 vessels | 3.200 | 64 |
| Continuous caster | 2.670 | 2.547 | 1.979 | 2 cc-3 strands | 3.266 | 61 |
| Vacuum degassing facility | 0.688 | 0.576 | 0.388 | 1 facility | 3.200 | 12 |
| Ladle refining facilities | 2.572 | 2.619 | 2.042 | 2 facilities | 3.200 | 64 |
| Hot strip mill | 2.870 | 2.746 | 2.521 | 1 mill | 3.311 | 76 |
| Pickle lines | 1.427 | 1.200 | 1.209 | 3 lines | 1.451 | 83 |
| Tandem mill | 1.372 | 1.213 | 1.191 | 1 mill | 1.361 | 88 |
| Temper mill | 0.801 | 0.679 | 0.656 | 1 mill | 0.816 | 80 |
| **Spartan Steel** | | | | | | |
| Hot-dip galvanising line[(2)] | 0.348 | 0.338 | 0.410 | 48 percent of 1 line | 0.544 | 75 |
| **Double Eagle** | | | | | | |
| Electrogalvanising line[(3)] | 0.304 | 0.262 | 0.266 | 50 percent of 1 line | 0.789 | 34 |
| **Delaco Processing** | | | | | | |
| Steel slitting facility[(4)] | 0.09 | 0.067 | 0.075 | 49 percent of facility | 0.108 | 69 |
| **Mountain State Carbon** | | | | | | |
| Coke production facility[(5)] | 0.155 | 0.670 | 1.021 | 50 percent of coke batteries | 1.111 | 92 |

Notes:

(1) Blast furnace "C" was completely rebuilt in 2007 causing the furnace to be down for 98 days, which resulted in a decrease in production in the facility's primary operations as well as downstream operations. The capacity indicated includes the capacity of blast furnace "B", which is currently being rebuilt and is expected to be re-commissioned by the end of 2009, and the recently rebuilt and expanded blast furnace "C".

(2) Owned through Spartan Steel. Under the Spartan Steel joint venture agreements, Severstal North America supplies 100 percent of the substrate material and markets a minimum of 80 percent of the output. Through good operating practices and as a result of the 2006 upgrade to the furnace and cooling capability, Spartan Steel was able to increase its capacity. The actual output shown in the table is Severstal North America's share of total production.

(3) Owned through Double Eagle. Under the Double Eagle joint venture agreements, Severstal North America receives 50 percent of the coating line time, the actual output of which is shown in the table.

(4) Owned through Delaco Processing. Under the Delaco Processing joint venture agreements, Severstal North America owns 49 percent of the steel slitting facility.

(5) Owned through Mountain State Carbon. Under the Mountain State Carbon joint venture agreements, Severstal North America owns 50 percent of the facility and sells 50 percent of the output.

***Dearborn.*** Severstal North America's Dearborn facility includes blast furnaces and steel making, casting and hot and cold rolling facilities.

*Blast furnaces.* Blast furnace "C" has a working volume of approximately 1,800 cubic metres and a capacity to produce approximately 2.2 million tonnes of crude steel per year. In 2007, blast furnace "C" was completely rebuilt and modernised causing it to be shut down for 98 days, during which Severstal North America experienced decreased hot metal and slab production. During the period from January to April 2008, blast furnace "C" has operated at approximately 63 percent capacity. However, after the completion of the PCI and cold blast blower projects in 2008, the furnace is expected to run at close to 100 percent of its design capacity.

Blast furnace "B" has a working volume of approximately 800 cubic metres. Due to an accident which occurred on 5 January 2008 and involved significant damage to the furnace, it was shut down. Severstal North America evaluated various options to either repair or rebuild the furnace, and decided to completely rebuild it. It is currently expected that the rebuilt blast furnace will be operational by the end of 2009. During that time, Severstal North America estimates that the lost production will be approximately 1,300,000 tonnes of crude steel. Severstal North America's property damage and business interruption insurance will cover the majority of the replacement cost and of the losses from the decrease in production (subject to certain deductibles under the relevant policies). The cause of the accident is currently under investigation. As a result of the decrease in crude steel production, the Dearborn facility's downstream production operations are working at a reduced output and are expected to do so for the remainder of the period during which blast furnace "B" is not operational, as it is not economical to purchase slabs from other sources for rolling at these facilities.

*Steelmaking facilities.* The Dearborn facility has two 236 tonne converter BOF vessels and two slab continuous casting machines. One is a twin strand, straight mould machine with a metallurgical length of 26.5 metres, and the other is a single strand, straight mould machine with a metallurgical length of 23.5 metres.

*Rolling facilities.* The Dearborn facility's hot strip mill has three walking beam furnaces, four roughing stands and seven finishing stands. It has a capacity of 3.3 million tonnes per year.

The Dearborn facility has three pickle lines, two of which have maximum line speeds of 305 metres per minute and a maximum coil weight of 22.7 tonnes. The third line has a maximum line speed of 762 metres per minute and a maximum coil weight of 25 tonnes. The total capacity of the pickle lines is 1.5 million tonnes per year.

The tandem cold mill is a four stand by four high mill. The maximum line speed is 975 metres per minute and the maximum coil weight is 27.2 tonnes. It has a capacity of 1.4 million tonnes per year.

The Dearborn facility's temper mill is one stand, four-high design. The maximum rolling speed is 858 metres per minute and the maximum coil weight is 27.2 tonnes. The temper mill has a capacity of 0.8 million tonnes per year.

The Dearborn facility has two annealing processes: hydrogen batch annealing and hydrogen-nitrogen ("**HN**") batch annealing. The hydrogen batch annealing facility consists of 26 bases with 17 furnaces and a stacking height of 5.28 metres. The HN batch annealing facility has 86 bases with 34 furnaces and a stacking height of 3.95 metres. The primary fuel used for both annealing processes is natural gas.

***Spartan Steel hot-dip galvanising line.*** Severstal North America owns 48 percent of a hot-dip galvanising line through a joint venture with Worthington Steel of Michigan. Spartan Steel produces hot-dip galvanised sheet steel sold to unexposed automotive and service centre customers. Spartan Steel has improved its capacity through good management practices and a 2006 upgrade of the furnace and cooling capability. Spartan Steel currently states its capacity as 544,000 tonnes. Severstal North America sells approximately 80 percent of the output.

***Double Eagle electrogalvanising line.*** Severstal North America owns 50 percent of an electrogalvanising line through a joint venture with US Steel. Double Eagle has a capacity of 789,000 tonnes per year, approximately one-half of which is dedicated to Severstal North America. This facility has 42 plating cells and can coat on one or two sides at a thickness of 0 to 100 grams per square metre. The facility can coat the substrate with either pure zinc or a zinc-iron alloy.

***Delaco Processing slitter.*** Delaco Processing, an associate owned 49 percent by Severstal North America and 51 percent by Delaco Supreme Tool and Gear Company, operates a steel slitting facility capable of processing coils up to 1,829 millimetres wide and up to 27 tonnes in weight and creating slit widths as low as 35 millimetres.

***Mountain State Carbon.*** Severstal North America owns 50 percent of a coke facility in West Virginia, Mountain State Carbon, through a joint venture with Wheeling-Pittsburgh. Mountain State Carbon produces approximately 1 million tonnes of coke per year.

***SeverCorr.*** SeverCorr includes an EAF and steelmaking, casting and hot-rolling and cold-rolling facilities.

*EAF.* The single EAF has a total furnace capacity of 240 tonnes, with a rated capacity of 1.5 million tonnes per year.

*Steelmaking facilities.* SeverCorr includes a Ladle Metallurgy Furnace ("**LMF**") which aims to maximise productivity through composition control, temperature adjustment, desulfurisation and steel cleanliness enhancement. The principal objective of the vacuum degasser is to produce the very low carbon levels necessary for producing interstitial-free steels for critical exposed automotive grades, as well maintaining low nitrogen levels. Continuous casting is a single-stand, thin-slab caster coupled directly via a tunnel furnace with the six-stand hot strip mill.

*Rolling facilities.* The current six-stand hot strip mill has a design rating that is in excess of 2.7 million tonnes per year. The directly coupled pickle line and five-stand tandem cold mill complex has the capability to produce both pickled and oiled products, as well as cold reduced strip. The total capacity of the continuous three-stage hydrochloric acid pickle line is slightly more than 1.1 million tonnes per year.

SeverCorr's tandem cold mill is a single stand, four-high design. It has a capacity of 544,310 tonnes per year.

The continuous hot-dip galvanising and galvannealing line is designed to coat cold-rolled strip for exposed automotive and appliance applications. It has a design capacity of 408,233 tonnes per year.

When Phase II is complete, the SeverCorr plant is expected to produce 3.0 million tonnes of hot-rolled, hot-rolled pickled and oiled, cold-rolled and hot-dip galvanised/galvannealed steels for customers in a number of industries.

***Sparrows Point.*** Sparrows Point includes one blast furnace, steelmaking, casting, hot and cold rolling facilities, coating lines and a tin mill.

*Blast furnace.* Blast furnace "L" is the third largest blast furnace in the western hemisphere with a diameter of 13.5 metres. The "#7 Strand" sinter plant has a capacity of 3.2 million tonnes per year and the blast furnace has a capacity of 3.4 million tonnes per year.

*Steelmaking facilities.* Sparrows Point has two BOF vessels with a heat capacity of 236 tonnes and two one-strand straight-mould slab casters with a combined capacity of 3.35 million tonnes per year

*Hot rolling facilities.* The hot strip mill has two modern walking-beam reheat furnaces with extractors, a reversing rougher with vertical edgers, an R-5 one-pass rougher, a hot coilbox and six finishing strands. The capacity is 2.7 million tonnes per year.

The Group believes that Sparrows Point has one of the most modern cold mills of its size in North America. It has full cold-rolling capabilities with hydrogen annealing and skin passing technology, with a pickle line coupled to the five-stand tandem mill. Its capacity is 1.3 million tonnes per year.

*Coating lines.* Sparrows Point has four coating lines, three of which are presently in operation. The operating coating lines can produce galvanised or galvalume coatings and have a combined capacity of 599,000 tonnes.

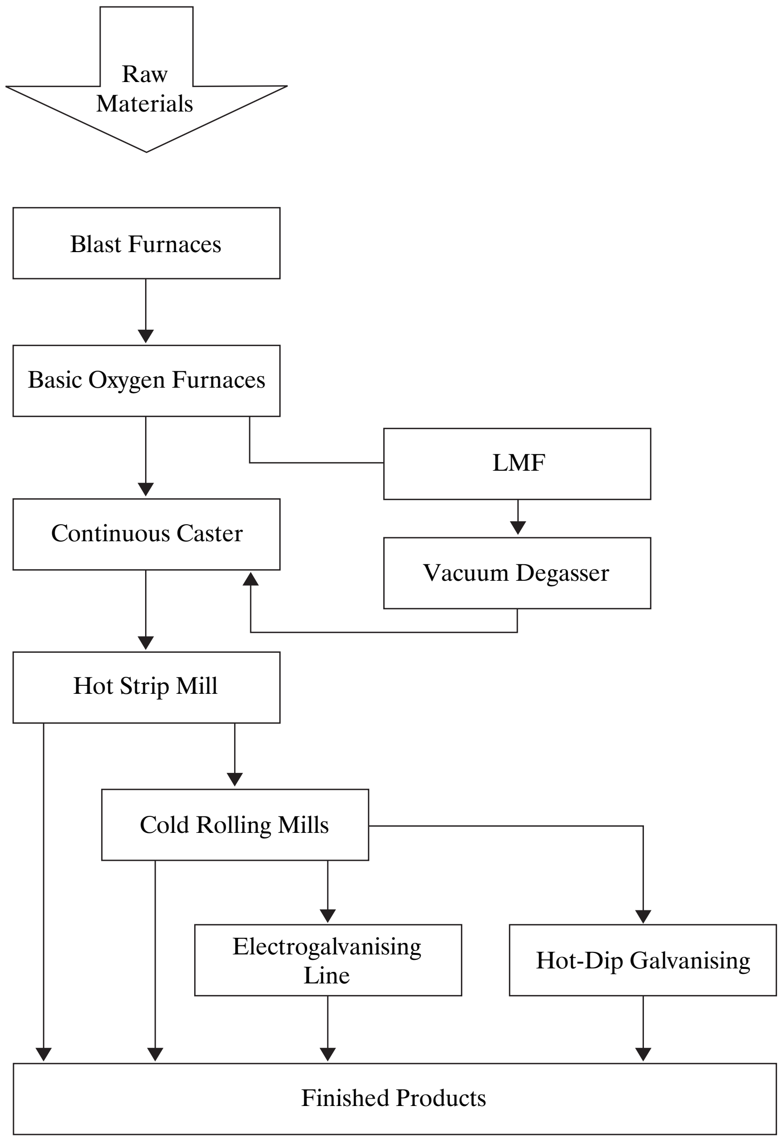
*Tin mill facilities.* Sparrows Point has self-contained tin mill facilities, including a pickler, a tandem cold mill, a continuous anneal line, a batch anneal facility, a temper mill/duo mill, a halogen plating line and a MSA plating line, that can produce approximately 500,000 tonnes of tin mill product annually. Sparrows Point's tin mill production includes drawn and ironed can stock, which, in Sparrows Point's experience, is the most quality demanding product in the domestic US tin mill product market.

Sparrows Point has 160 miles of its own rail tracks, which it uses for internal transportation of steel products. External rail services are provided by CSX and Norfolk Southern railroads, to whose networks Sparrows Point's internal rails connect.

Roll grinding services are supplied by Bethlehem Roll Technologies (a joint venture in which Mittal Steel holds a partial equity interest) under a contract which expires at the end of 2013.

***Production Process***

***Severstal North America.*** The following diagram illustrates the principal steps in Severstal North America's production process as at 31 December 2007:



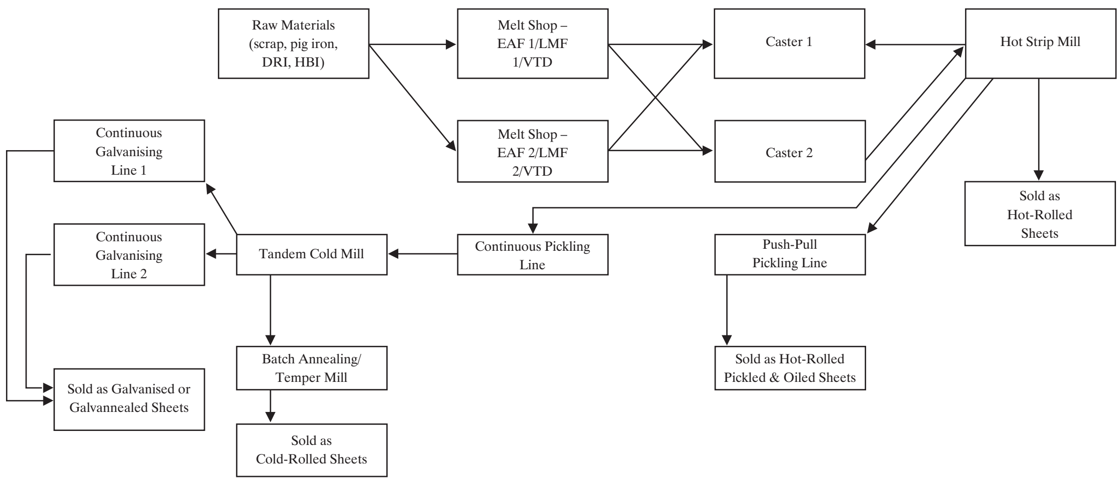

The steelmaking process at Severstal North America begins with iron ore pellets and coke being fed into the blast furnaces, which operate continuously. During the blast furnace process, the charge is converted into pig iron. The pig iron sinks to the bottom of the blast furnace and is tapped off for further processing. Liquid slag, which remains after smelting, is also removed from the blast furnaces.

Once cooled, slag is sold to a slag processing facility to be used for a variety of products, including railroad track ballast, roadway base and bulk concrete additive. Gas produced by the blast furnaces is captured and a portion is reused for the blast furnace stoves and the remainder is sold to DIG, a cogeneration power plant and affiliate of CMS Energy Corporation ("**CMS Energy**"). Molten pig iron, which is a component of the metal charge used in the production of steel in Severstal North America's BOF, is transported to the BOF in 145 tonne railway torpedo cars. The pig iron is poured into charging ladles and then into the BOF vessel. In addition to pig iron, the metal charge consists of scrap metal in various forms, such as loose and packaged purchased scrap and internally generated scrap.

The molten steel is then fed from the BOF into the continuous casting machines to produce slabs that are then rolled at the hot strip mill into coils. The continuous caster facility is equipped with two straight mould continuous casting machines. Severstal North America's hot strip mill is able to produce coiled sheet of a thickness ranging from 1.9 to 9.6 millimetres with a coil weight of up to 27 tonnes. Part of the hot strip mill production is sent to Severstal North America's cold rolling mills. These mills produce coiled sheet of a thickness ranging from 0.5 to 2.3 millimetres. Additional processing methods related to cold-rolling may be used to further improve the surface characteristics of the steel, including pickling, annealing and sheet-tempering.

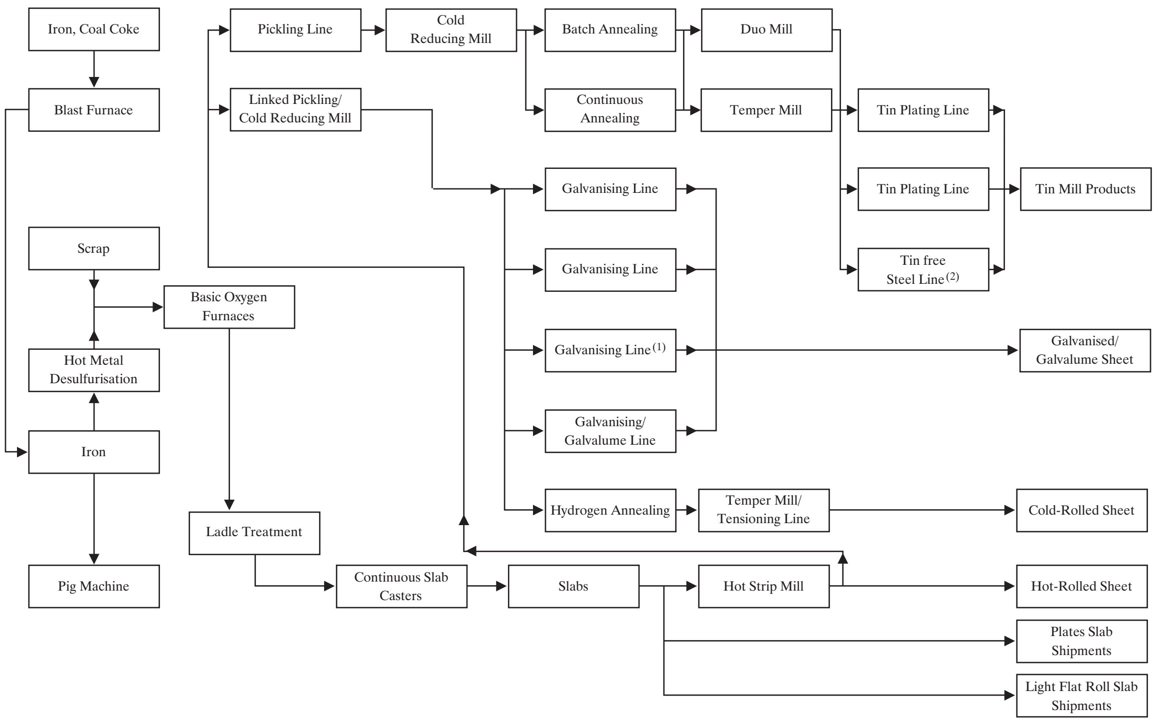
Some of the cold-rolled sheets are galvanised at Spartan Steel or Double Eagle.

***SeverCorr.*** The following diagram illustrates the principal steps in SeverCorr's production process as at 31 December 2007:




Production begins at the melt shop in the EAF where the raw materials, consisting of hot briquetted iron ("**HBI**"), pig iron and scrap metal, are melted for steel production. At the LMF, steel chemistry is tested for and adjusted by the addition of alloys. The ladle is then taken to the caster and emptied into the tundish where molten steel solidifies. A solid strand of steel is cut and individual slabs enter the funnel furnace. The slabs move through the furnace and are processed in the hot rolling mill. Once strips are processed at the hot rolling mill, reduced strip is cooled by sprays on the runout table. Cooled strip is then coiled at the coiler and then sent out to the coil yard. This is the first point where finished goods are produced. Coils could be sold at this time as hot rolled bands or processed further through the pickling line. Coils that come through a pickling line are pickled and oiled for added protection. Once processed, they could be sold as hot rolled pickled and oiled or can be processed further through the tandem cold mill. At the tandem cold mill the coils go through a cold reduction process which hardens the coil. At this stage, the coil can be sold as cold rolled full hard or can be processed further through the annealing and galvanising lines. Through annealing, coils that have lost most of their ductility and become very hard through the cold reduction process are processed to become softer and regain almost all of their original chemical properties. Coils are not considered finished goods once they are annealed until they have gone through the temper mill to correct shape deformation caused by the annealing process and to finish the surfaces of the coils. At the galvanising line coils are coated according to customer specifications. At this point coils could be sold as galvanised coils.

***Sparrows Point.*** The following diagram illustrates the principal steps in Sparrows Point's production process:




Notes:

(1) Idled in 2002

(2) Idled in 2004

Sparrows Point is located on the tidewater area of Baltimore, Maryland where raw materials are received either by water and/or rail for charging into a single blast furnace. The products produced from this blast furnace are pig iron that is either sold or, in most cases, moved downstream for the production of low to medium carbon and high strength steel grades. The slag which is a bi-product of the blast furnace is sold primarily for the manufacture of concrete.

The pig iron that is consumed internally is charged into one of two BOF vessels with cold scrap to start the refining process to convert the pig iron into steel. Once refined, the steel is ready to be transported to one of two straight mould casters which can cast up to 2.1 metres or 2.6 metres depending upon which caster machine is utilised. Based on the excess steel producing capacity, slabs are sold directly off the caster for plate and strip conversion or in most incidences further processed downstream in the hot strip mill.

The hot mill consists of two walking beam furnaces, a reversing roughing mill, coil box and two down coilers. The 250 millimetres thick slabs are rolled to 1.5 millimetres to 12.5 millimetres thick with a maximum width of 1,540 millimetres. Sparrows Point sells hot-rolled sheet and hot-rolled pickled and oiled sheet, which are pickled and oiled by an outside contractor. Of the material further processed internally, the hot bands will either go to the continuously linked pickler-tandem mill in the cold mill or to the non-linked pickler-tandem mill in the tin mill.

For the hot bands that are processed in the continuously linked pickler-tandem mill, the coils are reduced from the hot band thickness to the desired cold-rolled thickness in one operation. The range of thicknesses of the cold-rolled product is between 0.35 millimetres and 2.5 millimetres. The cold-rolled product will be sold as either full hard (non-annealed product) or as fully processed annealed material.

In addition to being sold as cold-rolled product, the cold reduced full hard coils are also the substrate used for the hot-dipped coatings of zinc for galvanised and zinc-aluminium for galvalume. Both of these coated products are produced in thicknesses of between 0.35 millimetres and 1.9 millimetres.

In addition to hot-rolled, cold-rolled and/or coated products produced at Sparrows Point, hot bands will be processed in the tin mill. The tin mill receives coils from the hot mill and will pickle and cold reduce coils in two separate operations. The coils produced from the tandem mill are full hard and are sold as full hard or will be annealed as a continuous or a box annealed product, temper passed and then electrolytically plated with tin. The tin mill products are in thicknesses of between 0.20 millimetres and 0.70 millimetres.

***Quality Control.***

***Severstal North America.*** Severstal North America has implemented the TS16949 quality management system and updated its certification to this internationally recognised technical specification in July 2007. Certification to this specification is required to directly supply the automotive industry. Severstal North America has successfully completed the necessary surveillance audits since July 2007 to maintain certification and the benefits of the TS16949 technical specification.

***SeverCorr.*** SeverCorr in the process of an assessment and certification to ISO/TS, which is currently expected to be completed by the end of 2008. UL, a certification agency who certifies products to certain specifications, is currently in the process of assessing and certifying SeverCorr's laboratories, a process which is expected to be completed in 2008. In addition, SeverCorr is currently devising a process for gaining ISO/TS 16949 certification for all product types. ISO/TS 16949 represents current minimum requirements requested of suppliers by most of the major automotive original equipment manufacturers ("**OEM**") worldwide, including General Motors, Chrysler, Ford, Renault, BMW, Volkswagon, PSA Peugeot Citroen and Fiat.

***Products***

***Severstal North America.***

*Crude steel products.* Severstal North America's production of crude steel in 2005, 2006 and 2007 was 2,753 thousand tonnes, 2,618 thousand tonnes and 2,042 thousand tonnes, respectively.

*Finished steel products.* Most of Severstal North America's crude steel production is further processed into finished steel products, including: hot-rolled sheet, cold-rolled sheet, hot-dip galvanised and electrogalvanised sheets and high-carbon, high-strength low-alloy, alloy and specialty steel sheets.

The following table sets forth the Severstal North America's production by product category in 2005, 2006 and 2007.

*Production by Product — Severstal North America*

| | Year ended 31 December | | |
|---|---|---|---|
| **Product** | **2005** | **2006** | **2007** |
| | | *(thousand tonnes)* | |
| Hot-rolled strip and plate | 1,470 | 1,397 | 1,185 |
| Cold-rolled sheet | 811 | 544 | 468 |
| Galvanised and other metallic coated sheet, *consisting of:* | | | |
| Electrogalvanised sheet | 304 | 263 | 262 |
| Hot-dip galvanised sheet | 348 | 384 | 471 |

*Hot-rolled strip and plate.* Severstal North America's hot-rolled sheet products are available in low carbon, high strength low alloy, structural, high carbon and alloy grades. Hot-rolled sheet can be further processed by Severstal North America into cold-rolled sheet, hot-dip galvanised sheet and electrogalvanised sheet steel. Severstal North America produces hot-rolled sheet with a thickness of 1.8 to 11.9 millimetres and width of 1,574 millimetres. Hot-rolled sheet steel is used to manufacture many automotive parts such as wheels, suspension arms, intrusion beams, and clutch plates as well as non automotive end uses such as welded pipe and tubing.

*Cold-rolled sheet.* Severstal North America's cold-rolled sheet is produced from precisely manufactured hot-rolled sheet, cold reduced to the desired thickness on the tandem cold reduction mill. The resulting cold-rolled full-hard sheet can be further processed through annealing furnaces to produce a fully processed product, which is generally temper rolled to minimise fluting or coil breaks, impart hardness (temper), a suitable surface texture, and flatness.

Severstal North America produces cold-rolled coils with a thickness of 0.6 to 2.3 millimetres and a width up to 1,549 millimetres. Cold-rolled sheet has various uses, including the manufacture of automotive parts, lighting fixtures, white goods, and tubing. In addition, cold rolled products serve as a substrate for Severstal North America's galvanised products.

*Electrogalvanised sheet.* Severstal North America's electrogalvanised sheet steel is produced from cold-rolled sheet steel that is electrolytically coated with zinc or zinc-iron alloy, and is used primarily for exposed automotive body panels. Electrolytic zinc and zinc-iron alloy sheet is available with a range of coating weights up to 100 grams/square metre per side. These products are available with various coating types: one-side coated with zinc; one-side coated with zinc-iron alloy; two-side coated with zinc or two-side coated with zinc-iron alloy to various differential-coating weights. Severstal North America produces electrogalvanised sheet with a thickness of 0.6 to 1.6 millimetres and a width up to 1,549 millimetres.

*Hot-dip galvanised sheet.* Severstal North America's hot-dip galvanised sheet is manufactured by passing sheet steel through a molten bath of zinc. A product coated with zinc or iron-zinc alloy can be produced from either a cold rolled or hot rolled sheet substrate. Hot-dip galvanised sheet steel provides a barrier of resistance to steel oxidation. Severstal North America produces hot-dipped sheets with a thickness of 0.6 to 4.0 millimetres and a width up to 1,549 millimetres. Hot-dip galvanised sheet steel is used for automotive parts, as well as non-automotive products such as residential and commercial doors, roofing, ductwork, and grain bins.

***SeverCorr.***

*Crude steel products.* SeverCorr produced 0.322 million tonnes of crude steel for the three months ended 31 March 2008, or approximately 21 percent of capacity.

*Finished steel products.* SeverCorr's crude steel production is further processed into finished steel products, including hot-rolled sheet, cold-rolled sheet and hot-dip galvanised sheet steel. SeverCorr produces the following steel grades: commercial steel ("**CS**"), drawing steel ("**DS**"), deep drawing steel ("**DDS**"), extra deep drawing steel ("**EDDS**") or interstitial free ("**IF**"), structural steel ("**SS**"), high strength low allow ("**HSLA**"), and low, medium and high carbon steels.

In the three months ended 31 March 2008, SeverCorr produced 198 thousand tonnes of hot-rolled strip and plate, 43 thousand tonnes of cold-rolled sheet, and 52 thousand tonnes of galvanised sheet.

***Sparrows Point.***

*Finished steel products.* Sparrows Point produces hot-rolled sheet, cold-rolled sheet, hot-dip galvanised/galvannealed sheet, tin plate and semi-finished slabs.

*Hot-rolled strip and plate.* Sparrows Point's hot-rolled sheet is available in commercial, drawing, structural and high-strength low-alloy grades. This product is sold to converters, service centres and automotive customers or further processed into cold-rolled sheet steel or tin mill products.

*Cold-rolled sheet.* Sparrows Point's cold-rolled sheet is available in commercial, drawing, deep drawing, structural and high-strength low-alloy grades. This product is primarily sold to service centres but is also used by customers in the construction and container markets as well as converters and OEMs. Cold-rolled sheet can be further processed into galvanised or galvalume products.

*Galvanised sheet.* Sparrows Point's hot-dip galvanised sheet is available in commercial, forming and structural grades. These products are primarily used in the construction industry.

*Tin plate.* Sparrows Point's tin plate product includes both single and double reduced products. This product is used for food cans, paint cans, aerosol cans, pails and oil filter shells.

*Semi-finished slabs.* Sparrows Point's slabs are produced in a range of grades and are primarily sold to other domestic steel producers for further processing.

***Supply Chain***

***Raw materials.***

***Severstal North America.*** The principal raw materials used by Severstal North America to produce steel include iron ore pellets, coke, limestone and dolomite, non-ferrous metal and ferro-alloys and metal scrap. Severstal North America does not maintain a minimum reserve of raw materials with the exception of iron ore pellets, which are delivered by ship. The Great Lakes shipping channels are typically closed during the period from January through March, and accordingly, Severstal North America accumulates a three-month supply of iron ore pellets by the end of each year to sustain production during the winter months. Other raw materials are generally delivered by rail and by road. Energy requirements for Severstal North America include electricity, steam and natural gas.

The following table sets forth a breakdown of the raw materials consumed by Severstal North America's Dearborn facility in 2006 and 2007. The decrease in the facility's consumption of raw materials (other than slabs) and energy in 2007 was primarily due to the reduction in production resulting from the closure of blast furnace "C" for 98 days, during which time it was completely rebuilt and modernised (see "— Facilities — Dearborn — Blast furnaces").

*Consumption of Raw Materials — Severstal North America, Dearborn facility*

| Raw materials | Year ended 31 December 2006 | 2007 |
|---|---|---|
| | *(thousand tonnes except as otherwise noted)* | *(thousand tonnes except as otherwise noted)* |
| Iron ore pellets | 3.373 | 2,565 |
| Coke | 1,061 | 810 |
| Metal scrap | 922 | 731 |
| Ferro-alloys and non-ferrous metals | 23 | 20 |
| Fluxes | 164 | 131 |
| Purchased slabs | 401 | 556 |
| Other materials | 32 | 22 |

*Iron ore and pellets.* Iron ore is purchased exclusively from Cleveland-Cliffs Sales Company, an affiliate of Cleveland-Cliffs Inc, pursuant to a long-term contract, at a competitive price set annually by reference to then current market price, expiring at the end of 2022. Severstal North America has committed to purchase all of its iron ore requirements from Cleveland-Cliffs Sales Company through this period, including a minimum volume of 2.5 million tonnes per year from 2010 to 2022. Severstal North America is expected to consume approximately 3.5 million tonnes of iron ore per year in 2008 and 2009. Annual consumption is anticipated to increase to approximately 4.8 million tonnes following the re-commissioning of blast furnace "B" in late 2009.

*Coke.* In 2007, Severstal North America received approximately 500,000 tonnes of coke from its Mountain State Carbon joint venture. After modernisation of Mountain State Carbon's largest battery, Severstal North America believes that two thirds of its metallurgical coke needs for the operation of blast furnace "C" will be met by its Mountain State Carbon joint venture. Severstal North America has entered into long-term agreements with Sun Coke and DTE Energy to acquire most of the balance of the coke required to operate its blast furnaces. If additional volume is required, it will be purchased on a spot market basis.

*Scrap.* Scrap is purchased from companies that collect scrap metal and is generated internally from Severstal North America production processes. Approximately 20 percent of the BOF vessel charge is scrap and the remaining 80 percent is liquid iron. Severstal North America also uses scrap-processing services, which allows Severstal North America to process a wide range of sizes and quality of steel scrap. Such services include special cutting and packaging lines for processing the scrap so that it is ready for use in the smelting process. Although there have been sharp increases in market prices of steel scrap in both the United States and international markets in recent years, Severstal North America believes that its strategic location in a region with significant sources of prime automotive scrap brings it an advantage in transport costs. Severstal North America launched a scrap blending programme in the fourth quarter of 2007. This programme allows for the replacement of prime scrap bundles with non-prime grades to reduce costs. Non-prime grades of scrap currently account for approximately 25 percent of the total scrap, compared with approximately 5 percent in 2006 and in the first three quarters of 2007.

*Purchased slabs.* Severstal North America purchases slabs (semi-finished products) in order to produce incremental hot sheet products. In 2006, Severstal North America purchased 401,000 tonnes of slabs, all of which were from Lucchini. In 2007, Severstal North America purchased a total of 540,000 tonnes from Lucchini, USS Mon-Valley Works, NLMK, COSIPA, and CST. In 2008, Severstal North America plans to purchase approximately 83,000 tonnes, all of which are expected to be purchased at spot market prices, pursuant to supply contracts. Of this amount, approximately 68,000 tonnes are expected to be from USS Mon-Valley Works and 15,000 tonnes are expected to be from Lucchini. The expected decrease in purchases of slabs in 2008, compared to 2007, is primarily due to the depreciation of the US dollar compared to the euro, making it uneconomical for Severstal North America to purchase and roll slabs to compensate for the reduction in crude steel production at Dearborn as a result of the closure of blast furnace "B" in January 2008 (see "— Facilities — Dearborn — Blast furnaces").

*Other raw materials.* Severstal North America purchases metallic and non-metallic alloys and fluxes from domestic producers and brokers. Pricing for ferro-alloys is generally set by contracts that are one to three months in duration. Prices have increased in recent months as demand has strengthened. The Group believes that prices increases have also reflected power shortages in major alloy producing countries.

***SeverCorr.*** SeverCorr's raw materials consist of inbound scrap, HBI and direct reduced iron, which total 1.6 million tonnes per year. Total carbon use is approximately 32 thousand tonnes per year, while total lime and dolomite use is approximately 64 thousand tonnes per year. Jefferson Iron is the major supplier of scrap. Stena Metal Inc. supplies pig iron and HBI.

***Sparrows Point.*** Sparrows Point purchases iron ore primarily from IOC and Vale pursuant to contracts in place for 2008 and 2009, respectively. The balance of its iron ore requirements are purchased in the spot market. Approximately 20 percent of the coke required by Sparrows Point is purchased from Sun Coke's Haverhill and Jewell facilities under contracts that extend through to 2018. The balance of Sparrows Point's current coke requirements are purchased under short-term contracts with several suppliers. Sparrows Point is currently investigating several options for the procurement of the balance of its long-term coke requirements.

***Energy***

***Severstal North America.*** *Electricity.* Severstal North America's electricity requirements total approximately 0.6 million megawatt-hours per year. Electricity is purchased from DTE Energy, a local public utility, under two contracts, expiring in 2013 and 2016, which provide for firm power at a competitive price, and interruptible power at a lower rate. Severstal North America purchases steam from CMS ERM LLC, an affiliate of DIG, under a 15-year contract. Prices are fixed for each year during the contract term in accordance with a negotiated schedule and are lower than current market prices. Under this contract, DIG is required to purchase 100 percent of Severstal North America's available blast furnace gas. The contract extends through 2015 with an option to renew for an additional 15 years. In early 2008, Severstal North America received approximately US$177 million from CMS Energy, an affiliate of DIG, for the termination of an electricity supply arrangement that was otherwise to extend until 2030. The termination was at the request of Severstal North America's supplier and the lump sum payment broadly compensates Severstal North America for the differential in price it is likely to have to pay to another supplier for the duration of the original arrangement.

The following table sets forth a breakdown of the energy consumed by Severstal North America's Dearborn facility in 2006 and 2007:

| Energy consumption | Year ended 31 December | |
|---|---|---|
| | 2006 | 2007 |
| | *(thousand tonnes except as otherwise noted)* | *(thousand tonnes except as otherwise noted)* |
| Electricity (millions of kilowatt hours) | 656.6 | 623.5 |
| Steam (thousands of MLbs) | 2,384 | 1,980 |
| Natural gas (1,000 cubic metres) | 476,001 | 219,994 |

*Natural gas.* Severstal North America purchases natural gas at prevailing market prices from a variety of natural gas suppliers. In 2006 and 2007, Severstal North America purchased natural gas primarily in the spot market. Severstal North America has achieved significant natural gas consumption reductions due to the modernisation of its hot strip mill reheat furnaces. Additional consumption reductions are expected to be achieved when the PCI project is finalised in 2008.

***SeverCorr.*** *Electricity.* Electricity is provided by the Tennessee Valley Authority. Monthly power demand is 250 megawatts, with an estimated consumption of approximately 152 million kilowatt hours per month. The main utilities (other than water) are natural gas, oxygen, nitrogen, and hydrogen.

*Natural gas.* Natural gas is the source of heat in different areas of the facility, including in the melt shop (EAF, LMF, vacuum tank degasser, caster and boiler), the hot mill tunnel furnace, and the cold mill. Natural gas is supplied to the facility by Atmos Energy.

***Capital Expenditure Programme***

***Severstal North America.*** Severstal North America's capital expenditure in 2006 and 2007 was approximately US$82.8 million and approximately US$483.3 million, respectively. Severstal North America has plans for capital expenditure of approximately US$1,232.8 million at Dearborn, Double Eagle and Spartan Steel between 2008 and 2012. The capital expenditure programme is designed to replace or refurbish major equipment, increase productivity and efficiency, make environmental improvements, improve product quality and develop Severstal North America's product mix.

Severstal North America's modernisation programme is in progress with several projects completed to date, including the modernisation and expansion of Severstal North America's largest blast furnace in 2007, the installation of a secondary emission control system at the BOF, which allowed it to use lower-priced scrap and meet increasingly stringent environmental standards, the installation of a straight mould conversion at the continuous caster, which is expected to ensure the production of high-quality slabs for the automotive market, and upgrades to the hot strip mill reheat furnace, which have allowed Severstal North America to significantly reduce natural gas consumption.

Two major projects are currently underway:

- the construction of a new pickle line and tandem cold mill, which is expected to decrease operating costs and allow Severstal North America to produce steel products that are expected to be required by its automotive customers in the future. The commissioning of the line is expected in mid 2009; and
- the construction of a new exposed hot-dip galvanising line, expected to be commissioned in late 2009.

The following table sets forth the estimated capital expenditure requirements from 2008 to 2012 for Severstal North America.

*Estimated Capital Expenditure Requirements from 2008 to 2012 — Severstal North America*

| Operating facility | Estimated cost |
|---|---|
| | *(US$ millions)* |
| Blast furnaces | 313.7 |
| BOF | 80.4 |
| Continuous caster/LMF | 12.4 |
| Hot strip mill | 69.9 |
| Coupled pickle line and tandem mill/cold mill | 438.7 |
| Hot-dip galvanising line | 252.5 |
| Joint ventures and other (including expenditure on environmental, quality, safety and systems improvements) | 65.2 |
| **Total** | **1,232.8** |

***SeverCorr.*** SeverCorr's capital expenditure programme is primarily the completion of its two-phased construction project, scheduled to occur between 2008 and 2010:

- Phase I construction, which included the construction of 1.5 million tonnes of steelmaking capacity and a hot strip mill, a pickling line tandem cold mill facility, a batch anneal, a temper mill, and a galvanising line; and
- Phase II construction, which will include the construction of an additional 1.5 million tonnes of steelmaking capacity, a second pickling line, more annealing capacity, a second galvanising line.

Phase II is currently estimated to cost approximately US$500-550 million.

***Sparrows Point.*** The Group plans to invest up to US$500 million to modernise Sparrows Point over the next five years. As Sparrows Point has only recently been acquired, detailed plans for capital expenditure have not yet been finalised. However, capital expenditure is likely to be targeted at refurbishing parts of the blast furnace and upgrading finishing lines, as well as performing required capital maintenance. The Group plans to construct a natural gas co-generation power facility to significantly decrease Sparrows Point's dependence on local suppliers of electricity.

***Research and Development***

Severstal North American has partnered with Ford, GM, Daimler-Chrysler and other major automotive companies to pursue various research and development projects. Such projects include efforts to provide value-added customer support in addressing cost, vehicle weight and materials performance and research in vehicle manufacturing efficiency, weight reduction and material durability. The annual cost of research and development is not significant.

***Sales and Marketing***

***Severstal North America.*** Severstal North America sells its products primarily in the domestic US market.

The following table sets forth the sales by market for Severstal North America in 2006 and 2007.

*Sales by Market — Severstal North America*

| Market | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2006 | | 2007 | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Domestic US sales | 2,307 | 87.1 | 2,114 | 90.8 |
| Export sales | 342 | 12.9 | 213 | 9.2 |
| **Total** | **2,649** | **100.0** | **2,327** | **100.0** |

*Customers.* The majority of steel customers are located within 350 miles of Severstal North America's facility. Severstal North America believes this proximity to its customers enables it to provide focused customer service and logistical support. Severstal North America's ten largest customers in the aggregate accounted for approximately 68 percent of sales by volume in 2007. In 2007, there were no customers who accounted for more than 25 percent of sales by volume.

The following table sets forth the sales by industry sector for Severstal North America in 2006 and 2007.

*Sales by Industry Sector — Severstal North America*

| Industry sector | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2006 | | 2007 | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Automotive | 966 | 36.5 | 1,064 | 45.7 |
| Non-automotive end users | 46 | 1.7 | 24 | 1.0 |
| Converters | 860 | 32.5 | 478 | 20.6 |
| Service centres | 777 | 29.3 | 761 | 32.7 |
| **Total** | **2,649** | **100.0** | **2,327** | **100.0** |

*Distribution.* Severstal North America distributes its steel products principally through its own sales organisation. Severstal North America' sales department is headquartered in Dearborn, Michigan with a small number of representatives working from off-site locations.

*Products.* Severstal North America believes its focus on value-added products and services differentiates it from its competitors. Through its joint ventures, Double Eagle and Spartan Steel, Severstal North America produces galvanised steel. It also produces high-carbon, alloy and other specialty steels that are used primarily by automotive customers for engine, transmission and drive train parts, seat components and clutch plates. Some non-automotive customers use these value-added steels for specialised agricultural equipment, plough discs, lawnmower blades and bearings.

The following table sets forth the sales by product for Severstal North America in 2006 and 2007.

*Sales by Product — Severstal North America*

| Product | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2006 | | 2007 | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Hot-rolled strip and plate | 1,424 | 53.7 | 1,179 | 50.7 |
| Cold-rolled sheet | 582 | 22.0 | 435 | 18.7 |
| Galvanised and other metallic coated sheet | 643 | 24.3 | 713 | 30.6 |
| **Total** | **2,649** | **100.0** | **2,327** | **100.0** |

*Contracts.* In 2007, in excess of half of Severstal North America's sales by volume were under long-term contracts. Sales to most non-automotive customers are done at spot prices, which are determined by market demand each month.

***SeverCorr.*** SeverCorr sells its products primarily in the domestic US market. Although sales commenced in 2007, full-scale production at SeverCorr did not commence until 2008, and as a result, the majority of sales have occurred only in 2008.

*Customers.* SeverCorr's customers are in a range of markets, including automotive, appliance, building products, containers, office furniture, pipe and tube, and service centres. SeverCorr has a relatively diversified customer-base, with only one customer accounting for more than 10 percent of sales by volume and no customers accounting for more than 25 percent of sales by volume, in each case in the three months ended 31 March 2008.

*Distribution.* SeverCorr distributes its products using third-party transport providers by barge (approximately 20 percent), rail (approximately 40 percent) and truck (approximately 40 percent).

*Products.* SeverCorr produces only flat-rolled products, including hot-rolled, hot-rolled pickled and oiled, cold-rolled full hard, cold-rolled annealed and tempered, galvanised, and galvannealed products.

In the three months ended 31 March 2008, SeverCorr sold approximately 219 thousand tonnes of hot-rolled sheet, 49 thousand tonnes of cold-rolled sheet and 57 thousand tonnes of galvanised sheet.

**Lucchini**

Lucchini is the second largest steel group in Italy and was, in 2007, one of the largest European producers of special quality steel long products by production volume according to the Group's estimates. It has several plants and service centres throughout Europe, with steelmaking capacity of approximately 4 million tonnes of crude steel per year, and total production in 2007 of approximately 3.6 million tonnes of crude steel. It has more than 1,000 customers in niche markets such as automotive, rails, bearings, springs and wire rod.

Lucchini's main production facilities are located in Italy (Piombino, Trieste, Condove and Lecco) and in France (Hagondange, Les Dunes and Fos sur Mer). This broad geographic spread of facilities gives Lucchini strategic access to a combination of sea, rail and road as means for receiving raw material supplies and transporting its goods.

Lucchini comprises the Piombino business unit, producing rails, bars and high-quality wire rod, and the Ascometal business unit, producing high-quality, tailored products, such as ingots, billets, blooms, bars, wire rod and drawn wire. Until its disposal in the second quarter of 2007, Lucchini also consisted of the Sidermeccanica business unit, a well-known European producer of rolling stock materials. Sidermeccanica was sold to an entity connected to the Lucchini family for approximately €127.8 million (approximately US$172.5 million at the time of the sale). Sidermeccanica primarily manufactures wheels and axels for the railway industry, which the Group considered to be a separate market and not a core part of Lucchini's operations.

***Facilities***

***Piombino.*** The Piombino business unit comprises the following main production facilities.

*Piombino plant.* The Piombino plant is the Piombino business unit's largest plant and is located in Piombino, near Livorno. It has an overall production capacity of 2.5 million tonnes of crude steel and 1.8 million tonnes of long products per year (assuming both of its blast furnaces are operational). This plant's production facilities include one coke oven battery with 45 ovens and a capacity of 430,000 tonnes per year, one blast furnace with a capacity of 2.7 million tonnes of hot metal per year, three BOFs and four continuous casting machines: one for slab casting with a capacity of 850,000 tonnes per year and three for billet and bloom casting of various sizes and shapes. The rolling facilities include one rolling mill for rails, one for wire rod and two for bars. The plant is located near a seaport and has its own dock with loading equipment for all types of raw materials and finished products.

*Lecco plant.* The Lecco plant is a wire-rod plant located in Lecco, and consists of a single rolling mill with a production capacity of 330,000 tonnes per year. The Lecco plant uses billets produced at the Piombino plant.

*Trieste plant.* The Trieste plant focuses solely on the production of high-quality hot metal and pig iron and has an installed capacity of 800,000 tonnes per year. The Trieste plant consists of one coke oven battery, one sintering plant, and two blast furnaces, each with a capacity of 400,000 tonnes per year. One of the blast furnaces that produces hot metal was idled in 2002 in connection with the dismantling of the steel work plant, and is not in regular use. The blast furnace is used primarily as a back-up facility for times when the other blast furnace is undergoing maintenance.

*Condove plant.* The Condove plant, located in Condove near Turin, focuses on the production of cold finishing bars and has an installed capacity of approximately 70,000 tonnes of cold finishing bars per year.

***Ascometal.*** Ascometal is a well-known European long specialty steel manufacturer and operates four integrated EAF-based plants, two cold finishing centres and a distribution centre in France. Ascometal's facilities are strategically located near scrap collection and processing centres. Ascometal has a production capacity of 1.2 million tonnes of special bar quality steel. The facilities are sophisticated and have been reconfigured and recalibrated to various manufacturing processes to produce specialised products to meet specific needs of customers, giving Ascometal what Lucchini believes is an unparalleled range of products.

***Sidermeccanica.*** Until its disposal in the second quarter of 2007, Lucchini also consisted of the Sidermeccanica business unit, a well-known European producer of rolling stock materials.

The following table sets forth Lucchini's actual output in 2005, 2006 and 2007.

*Steel Production Facilities, Lucchini — Output by Unit*

| Plant | Year ended 31 December 2005 | 2006 | 2007 |
|---|---|---|---|
| | (thousand tonnes) | | |
| ***Piombino*** | | | |
| *Piombino plant* | | | |
| Coking plant | 415 | 467 | 432 |
| Blast furnace | 2,198 | 2,025 | 2,117 |
| Continuous casting (steel prod.) | 1,883 | 2,185 | 2,295 |
| Rolling mills, including the Lecco plant (finished goods) | 1,134 | 1,434 | 1,525 |
| *Trieste plant* | | | |
| Coking plant | 417 | 415 | 414 |
| Blast furnace | 423 | 401 | 417 |
| ***Ascometal*** | | | |
| Continuous casting + ingots (steel prod.) | 1,154 | 1,172 | 1,179 |
| Rolling mills (finished goods) | 970 | 965 | 965 |

### *Products*

Lucchini believes it is a European leader of long specialty steel products, including round bars, rolled blooms and billet and flat products and is a leading Italian producer of high-quality wire rod, including drawing wire rod, cold heading steel and welding steel. Lucchini estimates that it had approximately a 12 percent European market share and an 80 percent domestic Italian market share for rails and rail stocks in 2007.

***Hot-rolled products.*** Lucchini produces more than 1,200 sizes and cross-sections of over 1,200 different brands and qualities, including wire rod, rolled billets, round bars, square bars and slabs. These products are used for a variety of applications, including automotive, mechanical and manufacturing industries, construction and infrastructure, electrical household appliances and the railway sector.

***Cold transformed products.*** Lucchini manufactures drawn, peeled, ground or shaved products and re-rolled strips. These products are used within the automotive and mechanical industries and are characterised by a high degree of customisation, reliability and product finish.

***Semi-finished products.*** Lucchini manufactures goods intended for rolling long products made of quality and specialty steels (billets, blooms and ingots), for direct stamping (billets and blooms) and for the production of forged items (ingots) and rolling flats (slabs).

The main users of these products are foundries and the iron and steel industry. Ingots are used by the utilities, aerospace, offshore, shipbuilding, petrochemical and infrastructure industries.

### *Supply Chain*

The principal raw materials used at Piombino are coking coal, iron ore concentrate, iron ore pellets, coke, scrap and ferro-alloys. The main raw materials required by Ascometal are scrap and ferro-alloys. The energy requirements used by Piombino and Ascometal include natural gas and electricity.

The raw materials and energy requirements of the Piombino Plant and the Trieste Plant, which are the only plants within Lucchini that produce hot metal, account for a substantial portion of Lucchini's total raw materials and energy requirements, respectively.

The following table sets forth a breakdown of the raw materials and energy use by the Piombino plant in 2006 and 2007.

*Consumption of Raw Materials and Energy — Piombino Plant*

| Raw materials and energy consumption | Year ended 31 December 2006 | 2007 |
|---|---|---|
| | *(thousand tonnes except as otherwise noted)* | *(thousand tonnes except as otherwise noted)* |
| **Raw materials** | | |
| Coal | 869 | 832 |
| Iron ore pellets | 3,221 | 3,334 |
| Coke | 224 | 300 |
| Metal scrap | 222 | 253 |
| Ferro-alloys | 38 | 44 |
| **Energy consumption** | | |
| Electricity (millions of kilowatt hours) | 783 | 788 |
| Natural gas (1,000 cubic metres) | 93,131 | 109,944 |

The following table sets forth a breakdown of the raw materials and energy use by the Trieste plant in 2006 and 2007.

*Consumption of Raw Materials and Energy — Trieste Plant*

| Raw materials and energy consumption | Year ended 31 December 2006 | 2007 |
|---|---|---|
| | *(thousand tonnes except as otherwise noted)* | *(thousand tonnes except as otherwise noted)* |
| **Raw materials** | | |
| Coal | 521 | 503 |
| Iron ore pellets | 636 | 640 |
| Coke | 0 | 6 |
| Ferro-alloys | 0.5 | 0.2 |
| **Energy consumption** | | |
| Electricity (millions of kilowatt hours) | 100 | 103 |
| Natural gas (1,000 cubic metres) | 57,121 | 61,998 |

***Raw materials.*** The raw materials used by Lucchini vary across its operations and include iron ore, coal, scrap and ferro-alloys.

*Piombino.* Iron ore and coal are purchased from third parties and from Severstal Resources, in the case of iron ore pellets, in each case primarily under annual contracts, as well as some spot price purchases. Coking coal is sourced mainly from Australia, Canada and the United States. Approximately 69 percent of metallurgical coke requirements are currently produced internally, at the Piombino and Trieste sites, with the remainder sourced from Italy or imported from China.

Prior to 2006, iron ore pellets were imported solely from Brazil, Venezuela and Canada. Since 2006, Severstal Resources has supplied a material quantity of pellets annually and in 2007, supplied approximately 25 percent of the iron ore consumed by Lucchini.

The majority of Piombino's coke is produced internally. The scrap required by Piombino is supplied mainly by local and international traders. Ferroalloys are purchased on both national and international markets, leveraging volume bundles with Ascometal.

*Ascometal.* For scrap, Ascometal relies on a network consisting of a large number of suppliers. To benefit from volume discounts, ferro-alloys are purchased by bundling orders (where possible) with Piombino.

***Energy.*** The Piombino operations purchase natural gas from ENI. Enel supplies approximately 50 percent of Piombino's electricity requirements, the remaining 50 percent being provided by power plants fuelled by gas recycled from Piombino's own plant operations. The Piombino plant sells gas to three different power plants in the local area. The Trieste plant sells coke oven and blast furnace gas to a local power plant.

Ascometal purchases its electricity and natural gas from Electricite de France and Gaz de France, respectively. The Le Cheylas (Allevard) plant produces electricity through hydraulic production facilities which it sells entirely to Réseau de Transport d'Électricité (RTE).

***Logistics.*** Lucchini benefits from the strategic geographic locations of its major plants and uses a combination of sea, rail and road as means for transporting its goods. Lucchini relies more heavily on sea for supplies and on trucks for distribution.

*Piombino.* The logistics for the Piombino plant are primarily organised through a seaport with a deep harbour, allowing mooring of ships up to 72,500 tonnes (with partial trans-shipping in the harbour up to 60,000 tonnes) for a maximum draught of 11.9 metres. The Piombino plant also has three berths for the delivery of goods by ships of up to 30,000 tonnes with maximum draught of 9.2 metres. The total carrying capacity of these berths is 100,000 tonnes of goods delivered per month. The rail capacity allows the plant to deliver approximately 60,000 tonnes per month and road capacity allows the delivery of 80,000 tonnes per month. The Trieste plant has its own berth for discharging raw materials and loading coke, pig iron and iron ore. The plant also has a seaport with a maximum draught of 12.62 metres, which is used by Panamax vessels. The railway and road transportation capacities of the plant are approximately 15,000 and 10,000 tonnes per month, respectively.

*Ascometal.* Ascometal uses a combination of road shipments, railway shipments and sea shipments to transport its products to its customers and receive its raw material shipments.

***Capital Expenditure Programme***

Lucchini's capital expenditure in 2006 and 2007 was approximately US$126.7 million and approximately US$199.3 million, respectively. Lucchini has developed a capital expenditure programme with planned capital expenditures of approximately US$2.2 billion from 2008 to 2012, to be funded by operating cash flows and long-term debt finance. This programme includes investment and optimisation programmes intended to target cost savings, to expand steel production, to diversify production into hot-rolled products, and to improve the quality of long products.

The following table sets forth Lucchini's estimated capital expenditure requirements from 2008 to 2012.

*Estimated Capital Expenditure Requirements from 2008 to 2012 — Lucchini*

| **Business unit** | **Estimated cost** |
|---|---|
| | ***(US$ millions)*** |
| Piombino | 1,510.3 |
| Ascometal | 650.7 |
| **Total** | **2,161.0** |

*Piombino.* Lucchini invested heavily in capital improvements at the Piombino plant between 1998 and 2002. The blast furnace was completely relined and is not scheduled for relining again until 2009. In addition, a new 45-coke oven battery was installed and has an expected lifetime of at least 20 years. Several additional investments have been made at the steel plant and the rolling mill.

Additional capital expenditures of approximately US$1,510 million are planned at Piombino from 2008 to 2012 and are aimed at commencing the production of hot rolled coils and increasing the output capacity of the blast furnace, as well as at reducing costs, improving the product mix and optimising coke and gas usage which is expected to increase steel production to 3.1 million tonnes of crude steel per year. Specific uses for this expenditure are expected to include:

- the installation of a flat rolling mill in order to produce the product portfolio as finished products;
- the improvement of safety and environmental standards;

- the upgrading of production equipment for high-margin long products such as round and flat bars and wire rod; and
- an intensive maintenance programme to improve the production reliability and efficiency.

*Ascometal.* In the past few years, capital expenditures have allowed Ascometal to dedicate each production unit to one specific product line and to improve overall finishing capacities. Additional capital expenditures of approximately US$651 million are planned at Ascometal from 2008 to 2012 and are concentrated mainly on product mix improvements and reductions of production costs and reductions of environmental impacts. Specific uses for this expenditure are expected to include:

- the installation of a continuous casting machine at the Fos sur Mer plant;
- the optimisation of the steel shop at the Hagondange plant and improvements in the productivity of the EAF at the melt shop at the Fos sur Mer plant; and
- investments in a big bar finishing and a wire rod mill at the Fos sur Mer plant.

***Research and Development***

Ascometal has established a Centre of Excellence for Research and Development Activities ("**CREAS**") in Hagondange for the development of new bar and wire rod steel applications. CREAS' annual budget in 2008 is approximately US$8 million. All research and development projects at CREAS are led specifically by trained individuals and include sales and production professionals in the core teams.

***Sales and Marketing***

Lucchini has more than 1,000 customers in its core markets in Italy, France and Germany. Lucchini sells its Piombino products primarily in the Italian domestic market and nearly half of its Ascometal products in the French domestic market. Lucchini's main objectives include maintaining and strengthening its cost leadership position in Italy and Western Europe and expanding into new, high-growth markets such as Eastern Europe and the Far East. Lucchini has commercial offices in Zurich, Barcelona, New York, Singapore and Düsseldorf and exports its products to more than 60 countries.

Lucchini has centralised sales and marketing departments. In 2006 and 2007, in excess of 80 percent of Lucchini's sales by volume were sold in Europe, predominantly in Italy, with a significant proportion of the remainder being sold in North America.

***Piombino***

*Customers.* Piombino had a customer base of approximately 800 customers in 2007. Its four largest steel customers, including Italian railway network operator Rete Ferroviania Italiana SpA ("**RFI**"), Severstal North America and Italian steel maker ILVA, accounted for approximately 25 percent of Piombino's sales by volume in 2007.

Piombino targets its sales of rails predominantly at the domestic Italian market, with the largest customers being the entities involved in the high-speed Italian rail network and maintaining standard infrastructure facilities. Fifteen percent of rails are replaced each year as the average life of a rail is five to 15 years. Contractual arrangements with customers are usually annual. The current fixed-price contract with RFI was signed in September 2007 for a term of one year, with an option for RFI to extend the term until December 2008.

In 2007, Piombino's main customers for slabs were ILVA and North America's Severstal North America business unit. See also "— North America — Supply Chain — Raw materials — Severstal North America".

The following table sets forth the sales by industry sector for Piombino in 2006 and 2007.

*Sales by Industry Sector — Piombino*[(1)]

| Industry sector | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2006 | | 2007 | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Steel industry | 830 | 32.6 | 810 | 31.0 |
| Automotive | 62 | 2.4 | 92 | 3.5 |
| Bearings | 160 | 6.3 | 154 | 5.9 |
| Construction | 123 | 4.8 | 98 | 3.8 |
| Machine building | 160 | 6.3 | 137 | 5.2 |
| Railway | 388 | 15.3 | 437 | 16.7 |
| Trading and regional distribution | 208 | 8.2 | 277 | 10.6 |
| Other | 612 | 24.1 | 605 | 23.3 |
| **Total** | **2,543** | **100.0** | **2,610** | **100.0** |

Note:

(1) Includes intersegmental sales.

*Products.* Piombino's sales are dominated by wire rod, slabs, rails and bars. Piombino estimates that it has approximately an 8 percent market share by volume of special niche product sales and a 38 percent market share by volume of value-added product sales in 2007.

The following table sets forth the sales by product for Piombino in 2006 and 2007.

*Sales by Product — Piombino*[(1)]

| Product | Year ended 31 December | | | |
|---|---|---|---|---|
| | 2006 | | 2007 | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Hot metal and pig iron | 387 | 15.2 | 419 | 16.1 |
| Steel products | | | | |
| Semi-finished products | 737 | 29.0 | 681 | 26.1 |
| Long products | 1,109 | 43.6 | 1,190 | 45.6 |
| Rails | 276 | 10.8 | 288 | 11.0 |
| Other steel products | 34 | 1.4 | 32 | 1.2 |
| **Total** | **2,543** | **100.0** | **2,610** | **100.0** |

Note:

(1) Includes intersegmental sales.

***Ascometal.***

Ascometal has a well-established, stable customer base and generates the majority of its sales under yearly contracts.

*Customers.* In 2007, Ascometal had approximately 600 customers. Ascometal's sales by volume. Ascometal's main customers are leaders in their respective industries. They include Peugeot SA, Thyssen Krupp and GKN in the automotive industry; Fag/Ina, Euroball and VM Tubes in the bearings industry; Sogefi, Thyssen Krupp and Styria in the automotive springs industry; and Mechanical V&M Tubes, Valdunes and IMS in the mechanical engineering industry.

Ascometal's contracts include provisions to adjust the relevant price based on variations of scrap price and fluctuations in prices of alloying elements used during the relevant period of time. Since the beginning of

2004, when the price of scrap increased substantially, the surcharge mechanism has been adopted by all major European EAF steel producers, resulting in improved margin protection.

The following table sets forth the sales by industry sector for Ascometal in 2006 and 2007.

*Sales by Industry Sector — Ascometal*

| **Industry sector** | **Year ended 31 December** | | | |
|---|---|---|---|---|
| | **2006** | | **2007** | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Automotive | 425 | 43.5 | 427 | 42.7 |
| Bearings | 185 | 18.9 | 183 | 18.3 |
| Machine building | 211 | 21.6 | 229 | 22.9 |
| Railway | 57 | 5.8 | 70 | 7.0 |
| Other | 100 | 10.2 | 90 | 9.1 |
| **Total** | **978** | **100.0** | **999** | **100.0** |

*Products.* Ascometal's sales are dominated by bars, which accounted for approximately 66 percent of its sales by volume in 2007. Other high-quality, tailored products, such as drawn wire, ingots, flat bars and billets, account for Ascometal's remaining sales. Ascometal estimates that it has approximately a 53 percent market share by volume of special niche product sales and a 21 percent market share by volume of value-added product sales.

The following table sets forth the sales by product for Ascometal in 2006 and 2007.

*Sales by Product — Ascometal*

| **Product** | **Year ended 31 December** | | | |
|---|---|---|---|---|
| | **2006** | | **2007** | |
| | *(thousand tonnes)* | *(percent of sales by volume)* | *(thousand tonnes)* | *(percent of sales by volume)* |
| Bars (less than 80 millimetres) | 368 | 37.6 | 353 | 35.3 |
| Bars (greater than 80 millimetres) | 282 | 28.8 | 305 | 30.5 |
| Wire and drawn | 79 | 8.1 | 79 | 7.9 |
| Ingots and billets | 72 | 7.4 | 72 | 7.2 |
| Flat bars | 53 | 5.4 | 68 | 6.8 |
| Billets (rolled) | 124 | 12.7 | 122 | 12.3 |
| **Total** | **978** | **100.0** | **999** | **100.0** |

### Severstal Resources

Severstal Resources consists primarily of two iron ore complexes and one coal mining complex in northwest Russia, as well as three gold mining complexes in east Russia and in Kazakhstan, and a ferrous scrap metal recycling business operating in northwest and central Russia. Severstal Resources was the second largest producer of iron ore pellets and coking coal (before accounting for the sale of Kuzbassugol) in Russia in 2007, according to RudProm and CDU TEK, respectively. With the capacity to supply all of the current iron ore and coal needs of the Russian Steel Division, Severstal Resources forms the basis of the Group's balanced and vertically-integrated business model. With a focus on high value-added products, such as export quality iron ore pellets and coking coal concentrate, Severstal Resources had a total output of 14.7 million tonnes of iron ore and 9.4 million tonnes of coal in 2007. In aggregate, higher value-added products, such as iron ore pellets and coking coal concentrate, represented more than 60 percent of Severstal Resources' total production by volume in 2007.

Commencing in 2007, Severstal Resources acquired gold mines and licences and several ferrous scrap metal recycling businesses, resulting in it becoming, according to its own estimates for 2008, one of Russia's four largest gold producers and a leading collector of scrap metal in northwest Russia. It is currently expected that with effect from 1 August 2008, management responsibility for the scrap operations is to be transferred to the Russian Steel Division.

Severstal Resources comprises five mining complexes in Russia and one in Kazakhstan:

- Karelsky Okatysh, located in the Karelia Republic, produces iron ore pellets and has an annual capacity of 11.4 million tonnes and estimated JORC iron ore reserves and resources of approximately 560 million tonnes and 723 million tonnes, respectively;
- Olkon, located in the Murmansk region of Russia, produces iron ore concentrate and has an annual capacity of 5 million tonnes and estimated JORC iron ore reserves and resources of approximately 149 million tonnes and 239 million tonnes, respectively;
- Vorkutaugol, located in the Komi Republic, produces coke and steam coal and has an annual capacity of 12.2 million tonnes and estimated JORC coal reserves and resources of approximately 276 million tonnes and 27 million tonnes, respectively;
- Nerungri-Metallic, located in the Republic of Sakha-Yakutia, produces gold and is expected to have an annual output of approximately 1.35 tonnes (approximately 43,000 ounces);
- Aprelkovo, located in the Chita Region, produces gold and is expected to have an annual output of approximately 1.25 tonnes (approximately 40,000 ounces); and
- Celtic, located in Kazakhstan, produces gold and is expected to have an annual output of approximately 2.9 tonnes (approximately 95,000 ounces).

In April 2008, the Group sold Kuzbassugol, consisting of the Berezovskaya and Pervomayskaya mines, to Arcelor Mittal for US$652 million. Kuzbassugol was not considered to be of strategic importance for the supply of coal to the Russian Steel segment's steelmaking operations and the Group was able to achieve what it believes to be a fair price for the sale.

Severstal Resources estimates that, as at 31 December 2007, it had iron ore reserves and resources of approximately 709 million tonnes and 962 million tonnes, respectively, and coal reserves and resources (calculated as if the disposal of Kuzbassugol had occurred on 31 December 2007) of approximately 276 million tonnes and 27 million tonnes, respectively. All data relating to Severstal Resources' reserves and resources relating to iron ore and coal summarised in "— Severstal Resources" are calculated by reference to estimates provided by IMC Consulting Ltd in its report dated 14 August 2006, which was prepared in accordance with JORC reporting standards, reduced by actual production since 1 January 2006, and also accounting for the disposal of Kuzbassugol.

At expected rates of operation, audited JORC reserves of iron ore and coking coal are estimated to be sufficient for at least ten years of operation. Severstal Resources believes it will be able to achieve significant reserve extension potential (increasing life of mine to at least 23 years; see "— Reserves and Resources") through conversion of resources into reserves and acquisition of adjacent reserves.

**Facilities**

***Karelsky Okatysh.*** Karelsky Okatysh is located in Kostomuksha in the Karelia Republic in the northwest of Russia. It mines low-grade magnetite-quartzite ores and produces high-quality iron ore pellets with an iron content of 63 to 65 percent. Karelsky Okatysh operates four major deposits that have an estimated life of 33 years based on the Group's estimates of JORC reserves plus expected reserves extension. The average iron content of the reserves at Karelsky Okatysh is approximately 29 percent. The opening of a new mine at the Korpanga deposit in 2007 as well as the efficiency improvements that have been made at the Kostomuksha operation, have boosted the production capacity of Karelsky Okatysh to 36 million tonnes of run of mine ("**ROM**") ore per year.

The most valuable production asset of Karelsky Okatysh is its large pelletiser. It enables valorisation of fines into pellets (pellets trade at a premium to fines). The pelletiser has three production lines, each with a capacity of up to 4 million tonnes per year, although actually output is currently limited by the capacity of the concentrator. The Group believes that output capacity could be increased to the full 12 million tonnes per year with relatively minor investments and operational debottlenecking of the concentrator.

*Kostomuksha.* The arch shaped Kostomuksha deposit consists of three sections, with a total strike extent of 13,000 metres. The depth of the open pit at its largest section reaches 400 metres below sea level with a stripping ratio of 1.15 in 2007. The iron content in the ore is medium (29 percent total iron, 24 percent iron magnetite). However, it is well suited for relatively simple magnetic beneficiation and the deposit produces high-quality fines (68 percent iron) and pellets (65 percent iron). The Kostomuksha deposit has a capacity of 24 million tonnes of ROM ore at 29 percent iron per year.

*Korpanga.* In 2007, a mine opened at the Korpanga deposit, which consists of east and west sections. It is an isoclinal synform that has been refolded into a plunging anticline along a northeast-southwest axis. The west and east sections form the two flanks of the plunging anticline, and have respective strike lengths of 3,800 metres and 3,000 metres. The ore qualities at Korpanga are similar to the Kostomuksha deposit. The Korpanga deposit has added 7.5 million tonnes of ROM ore at 28 percent iron per year.

Extracted ore is delivered to the beneficiation plant by railway. The beneficiation plant is located seven kilometres from Central Section and 25 kilometres from Korpanga. The current design capacity of the beneficiation plant is 10.4 million tonnes of concentrate (representing 28 million tonnes of input ore). The Group believes that this capacity could be increased to 11.7 million tonnes per year by 2010 with a relatively minor amount of investment. The planned investment would include installation of dry magnetic separation equipment at the open pits to reduce the waste feed into the crushers. The plant beneficiation consists of two crushing lines and 12 beneficiation circuits with primary magnetic and secondary gravitational separation equipment.

***Olkon.*** Olkon is located in the Murmansk region in northwest Russia. It mines low-grade magnetite-quartzite ores and produces high-quality iron ore concentrate. Currently, ore mining is carried out in five open pits: Olenegorsky, Kirovogorsky, Baumansky, XVth Anniversary of October and Komsomolsky in conjunction with the new site at the Olenegorsky underground mine, which was built in 2005. The deposit has an estimated life of 23 years based on the Group's estimates of JORC reserves plus expected reserves extension.

There are 137 million tonnes of ore within the existing boundary of the open pit and the remainder will be mined from new underground mines that will extend the current open pits. The average iron content in the Olkon reserves is 27 percent total iron, 22 percent iron magnetite. Olkon produces iron ore concentrate with an average iron content of 65.7 percent. The average stripping ratio was 1.2 in 2007 but will decline due to the increase in underground mining. The original design capacity at Olkon was 12 million tonnes of ore per year. This was increased to 14.0 million tonnes per year in 2007. A further increase to approximately 16 million tonnes is planned once the underground mines are fully operational. The ore from the Kirovogorsky, Baumansky, XVth Anniversary of October and Komsomolsky pits is delivered to the beneficiation plant by railway, between 11 and 15 kilometres. The beneficiation plant has a production of 4.6 million tonnes of concentrate. It consists of two crushing lines and 10 beneficiation circuits with primary magnetic and secondary gravitational separation equipment. The plant capacity has recently been increased to 5.0 million tonnes of concentrate.

***Vorkutaugol.*** The Vorkutaugol and Vorgashorskaya mines are located near the town of Vorkuta, in the Komi Republic in northeast Russia. The Vorkutaugol and Vorashorskaya mines are separate legal entities but are integrated operations from a production perspective. The mining area of Vorkutaugol consists of five underground mines, with an estimated life of 38 years based on the Group's estimates of JORC reserves plus expected reserves extension, and one open pit located within the Vorkutinskoye deposit. The Vorkutinskoye deposit covers an area of 280 square kilometres and is in the form of a basin with outcrops around the perimeter, dipping towards the centre of the deposit. The Vorgashorskaya mine is located on the adjacent Vorgashorskaya coal deposit approximately 25 kilometres northeast of Vorkuta. Premium grades of coking coal concentrate account for a high proportion of the Vorkutaugol reserves.

There are three principal seams currently under operation at the Vorkutinskoye deposit. Two of the seams, Triple and Fourth seam, are between 1.5 and 2.5 metres and are suitable to be extracted by conventional longwall shears. Fifth seam is 0.8 metres thick and is currently extracted by a longwall shear, primarily for degasification of the two thicker seams. However, with the near-term introduction of plough technology, the Group expects the operating economies of the mining operation at Fifth seam to improve significantly.

The concentrate produced by Vorkutaugol is of high-quality, with a majority of output being a premium grade category, medium volatility, high fluidity coking coal concentrate.

There is only one seam of workable thickness at the Vorgashorskaya mine. The total seam thickness is between 2.7 metres and 3.0 metres. The mine has two high-productivity faces, with an annual production capacity of approximately 4.6 million tonnes (on a ROM basis). Some ROM coals are processed at the central Pechorskaya plant.

There are currently three washing facilities in Vorkuta (Severnaya — located at the Severnaya mine, Vorkutinskaya — located at the Vorkutinskaya mine and central Pechorskaya) with a total capacity of approximately 11.1 million tonnes (on a ROM basis) per year. In addition, the washing facilities at the Cherepovets have an additional production capacity of 1.8 million tonnes per year. The washing process reduces ash content to 8-9 percent, enabling the production of concentrate with a high market value. Coking coal concentrate from Vorkutaugol can be used directly in coke batteries. The most valuable coal is washed on the site at Vorkuta. Middlings are currently shipped and washed in Cherepovets.

***Nerunigri-Metallic.*** Nerunigri-Metallic is a gold mine operating on the Tabornoye gold deposit located in the Republic of Sakha-Yakutia, in east Russia. The gold reserves registered on the state register amount to approximately 15 tonnes of Category C1 and Category C2, in aggregate, and in excess of 70 tonnes of Category P1 and Category P2, in aggregate. The mine is an open-pit mine and uses heap leaching processing technology, with an estimated annual output of approximately 1.35 tonnes (43,000 ounces) of gold.

***Aprelkovo.*** Aprelkovo is a gold mine operating on the Pogromnoye gold deposit located in the Chita Region, in east Russia. The gold reserves registered on the state register amount to approximately 25 tonnes of Category C1 and Category C2, in aggregate. The mine is an open-pit mine and uses heap leaching processing technology, with an estimated annual output of approximately 1.25 tonnes (40,000 ounces) of gold.

***Celtic.*** Celtic consists of two gold mines, which Severstal Resources treats for management purposes as one mining complex, on the Suzdal deposit and the Zherek deposit in northeast Kazakhstan. Refractory-rich sulphide ores are mined at the Suzdal deposit and processed with bio-oxidation and leaching technology. The mine is expected to have an annual output of approximately 2.9 tonnes (95,000 ounces) of gold.

***Scrap metal.*** Severstal Resources' ferrous scrap metal operations consist of collection, processing and sales. Collection and processing facilities are located primarily in northwest Russia. Scrap is collected through a network of collections points and processed at several main facilities, the largest of which is located in St Petersburg. Severstal Resources also acts as a broker for sales of scrap.

**Reserves and Resources**

At expected rates of operation, the Group estimates that Severstal Resources' audited reserves and resources of iron ore and coal are sufficient for at least ten years of iron ore and coking coal production. The table below shows the Group's life of mine estimation based on the report issued by IMC Consulting Ltd dated 14 August 2006, which was prepared in accordance with internationally accepted standards set forth in the JORC code (including expected reserves extension through conversion of resources into reserves and acquisition of adjacent reserves), adjusted for actual production since 1 January 2006, and accounting for the disposal of Kuzbassugol in April 2008 (see also "Presentation of Financial and Other Information — Mining Reserves" and "Industry — Mining Industry — International Reporting Methodologies").

*Estimated Reserves and Resources — Severstal Resources*

| Mine | JORC reserves, as at 1 January 2006[1] | Adjusted JORC reserves, as at 31 December 2007[2] | JORC resources[3] | Expected reserves extension (based on resources confirmation[4]) | Expected reserves extension (based on adjacent reserves acquisition[5]) | Estimated total reserves (Adjusted JORC reserves plus reserves extension) | Life of mine, years[6] (based on adjusted JORC reserves) | Life of mine, years[6] (based on total reserves estimation) |
|---|---|---|---|---|---|---|---|---|
| | *(thousand tonnes)* | | | | | | | |
| Karelsky | | | | | | | | |
| Okatysh . . . . | 614,920 | 560,364 | 723,278 | 295,991 | 332,500 | 1,188,855 | 16 | 33 |
| Olkon . . . . . . . | 176,678 | 149,244 | 239,004 | 59,751 | 130,000 | 338,995 | 10 | 23 |
| Vorkutaugol[7] . . | 298,463 | 275,625 | 26,850 | 13,425 | 124,430 | 413,480 | 25 | 38 |

Source: Group estimates and IMC Consulting Ltd (see Notes).

Notes:

(1) Proved plus probable, based on the report of IMC Consulting Ltd dated 24 August 2006, which estimated JORC reserves as at 1 January 2006.

(2) Estimated JORC reserves are based on the JORC reserves contained in the report of IMC Consulting Ltd dated 24 August 2006, which estimated JORC reserves as at 1 January 2006, reduced for actual production since 1 January 2006, until 31 December 2007.

(3) JORC resources are based on the report of IMC Consulting Ltd dated 24 August 2006, which the Group estimates have not changed materially.

(4) Estimation based on JORC resources volume (calculated as 25 percent to 50 percent of JORC resources).

(5) Estimation based on adjacent reserves volume under Russian classification (calculated as 30 percent to 50 percent of the A+B+C1 categories).

(6) Life of mine calculation formula: Life of mine = business plan forecast period + ((reserves — business plan forecast mining volume)/ mining volume of the forecast's last year of mining).

(7) Includes licences owned by Vorkutaugol and Vorgashorskaya legal entities.

## Products

Severstal Resources produces a high proportion of premium products, such as iron pellets from iron ore and coking coal concentrate from coal, for domestic and international customers. In 2007, iron pellets constituted 68 percent of Severstal Resources' production of iron ore, and coking coal concentrate constituted 61 percent of its coal production. In 2010, Severstal Resources expects that iron pellets will still constitute 70 percent of Severstal Resources' production of iron ore and that coking coal concentrate will increase to 70 percent of total coal production.

The following table sets forth Severstal Resources' volumes of extraction and production in 2005, 2006 and 2007.

*Volumes of Extraction and Production — Severstal Resources*

| Item[1] | Year ended 31 December 2005 | 2006 | 2007 |
|---|---|---|---|
| | *(millions of tonnes)* | | |
| Coking coal . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 1.8 | 2.0 | 1.8 |
| Coking coal concentrate . . . . . . . . . . . . . . . . . . . . . . . . . . . | 3.9 | 5.6 | 5.8 |
| Steam coal . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 1.2 | 2.0 | 1.8 |
| Iron ore concentrate . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 4.0 | 4.5 | 4.7 |
| Iron ore pellets . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | 8.9 | 9.4 | 10.0 |
| Scrap metal[2] . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . . | — | — | 0.8 |

Notes:

(1) No material production of gold occurred in 2007 at Severstal Resources' gold mines (see "— Facilities").

(2) Amount is only for processed and assorted scrap.

*Coking coal and coking coal concentrate.* Vorkutaugol's two main products are premium hard coking coal, in concentrate form, and semi-soft coking coal, in concentrate form, with an ash content of 8-9 percent.

*Steam coal.* Vorkutaugol also produces steam coal. It is sold to local heating and power plants in the Komi region, as well as other industrial customers, with some quantity exported to customers in Europe.

*Iron ore concentrate.* Olkon produces iron ore fines with an iron content of 65.7 percent. Currently these fines are shipped only to the Russian Steel Division where they are used as sinter feed, before being blended with coke and loaded into the blast furnace.

*Iron ore pellets.* Karelsky Okatysh produces iron ore pellets. These have an iron content of 65.0 percent for non-fluxed and 63.2 percent for fluxed pellets. Pellets are a high value-added iron ore product, as they can be used directly in the blast furnace without intermediate sintering. They also ensure optimal coke consumption in the furnace and significantly reduce the carbon dioxide emissions in the furnace operation.

*Scrap metal.* Severstal Resources' ferrous scrap metal operations collect a range of scrap metals, which are sold as raw materials for EAFs, oxygen converters and casting mills.

**Supply Chain**

***Raw materials.*** Raw materials used by Severstal Resources include petroleum products, liquid explosives and metallic raw materials and supplies.

Petroleum products are the largest raw material type consumed by Severstal Resources. In order to take advantage of economies of scale, Severstal Resources has centralised the purchasing of items that are used in all of its operations. Purchases of petroleum products are centralised and made pursuant to annual contracts, some of which include credit terms, with several large suppliers, such as Gazprom, TNK-BP and LukOil. Suppliers are selected on the basis of the competitiveness of their commercial terms. Actual prices are determined on a monthly basis with a subset of the suppliers chosen from the wider group, based on their offer for that month. In respect of the year 2007, a total of 11 contracts were entered into with petroleum suppliers; however, no more than five to seven suppliers actually supply petroleum products in any given month. The purchasing of metal-based raw materials, cables, conveyor belts and explosives is also centralised.

Following a competitive tender process, Karelsky Okatysh signed a six-year contract for the supply of liquid explosives with one of the market leaders, UEE. Under the contract, a new manufacturing plant for liquid explosives was constructed in Kostomuksha. A similar contract was entered into by Olkon with ZAO Dyno Nobel Russia and a new manufacturing plant is currently under construction. Contracts for the supply of metallic raw materials and supplies are signed annually, while prices are fixed on a quarterly basis.

Severstal Resources expects that during the next ten years it will have a raw materials surplus. Severstal Resources believes that such a surplus would provide it with enhanced stability in terms of raw material supplies and enable it to meet potential future production growth.

***Energy.*** Severstal Resources' energy requirements constitute approximately 21 percent of its total supply chain requirements in 2007 and include electricity purchased from local energy producers, typically under annual contracts, with prices fixed for the duration of the term.

**Capital Expenditure Programme**

In recent years, Severstal Resources has replaced all of its major equipment for both its underground operations and open pit mines, and in 2006 and 2007, its capital expenditure was approximately US$350.9 million and approximately US$394.0 million, respectively.

Further capital improvements are currently underway at each of Severstal Resources' mining assets, with a planned total capital expenditure of approximately US$3.0 billion from 2008 to 2012. These projects are designed to further modernise equipment, increase the production of premium products, stabilise the mix of products, optimise degasification systems, utilise coal-mine methane, develop new iron ore and coal reserves, improve cost efficiency and expand extraction and beneficiation capacities.

In carrying out its capital expenditure programme, Severstal Resources plans to improve its internal processes for sourcing supplies, including by consolidating purchasing and seeking to enter long-term contracts with key suppliers, such as with suppliers of heavy machinery.

The following table sets forth Severstal Resources' estimated capital expenditure requirements from 2008 to 2012.

*Estimated Capital Expenditure Requirements from 2008 to 2012 — Severstal Resources*

| Asset | Estimated cost |
|---|---|
| | *(US$ millions)* |
| Karelsky Okatysh | 745 |
| Olkon | 379 |
| Vorkutaugol | 1,002 |
| Gold mining assets | 488 |
| Scrap metal assets | 166 |
| Other | 224 |
| **Total** | **3,004** |

***Karelsky Okatysh.*** The estimated capital expenditure requirements at Karelsky Okatysh between 2008 and 2012 are approximately US$745 million. Planned improvements include:

- expansion of ore extraction, beneficiation, and pelletising capacities;
- upgrade of concentration facilities;
- selective debottlenecking projects; and
- addition of dry magnetic separation and flotation at the beneficiation plant.

Overall, the planned improvements are expected to result in full utilisation of the pelletiser and to increase long-term production of pellets by approximately 14 percent against 2007 production levels, from 10.0 million tonnes in 2007 to an estimated 11.4 million tonnes by 2012.

***Olkon.*** The estimated capital expenditure requirements at Olkon between 2008 and 2012 are approximately US$379 million. Planned improvements include:

- construction of two additional underground mines;
- improvements at the existing open pit at Komsomolsky; and
- improvements in the capacity of railroads.

Overall, the planned improvements are expected to increase the production output to 5.0 million tonnes of iron ore concentrate per year by 2012.

***Vorkutaugol.*** The estimated capital expenditure requirements at Vorkutaugol between 2008 and 2012 are approximately US$1,002 million. Planned improvements include:

- replacement of obsolete mining equipment with equipment of improved efficiency;
- surface and underground mine infrastructure development; and
- various investments in mine safety measures.

Overall, the planned improvements are expected to maintain the average production output at 7.7 million tonnes of coking coal concentrate per year to 2012.

***Gold mining assets.*** The estimated capital expenditure requirements in connection with gold mining assets between 2008 and 2012 are approximately US$488 million. The capital expenditure is expected to consist of expenditure at the existing mines in Russia and Kazakhstan to improve productivity, the development of deposits under the mining licences acquired in 2007, and the acquisition of additional licences and other gold mining assets.

***Scrap metal assets.*** The estimated capital expenditure requirements in the ferrous scrap metal business between 2008 and 2012 are approximately US$166 million. The capital expenditure is expected to consist of the acquisition of, and construction of, new scrap collection points in the European part of Russia, as well as capital expenditure on existing processing facilities.

**Sales and Marketing**

Severstal Resources sells its products internally within the Group as well as to the international and Russian domestic markets. Severstal Resources aims to maintain its domestic market share and expand its international market share with high-quality pellets and coking coal concentrate.

*Customers.* Within the Group, Severstal Resources sells iron ore and coking coal to the Russian Steel Division and iron ore pellets to Lucchini. In 2007, Severstal Resources' total iron ore and coal sales were 24.8 million tonnes, of which 15.4 million tonnes were sold to the Russian Steel Division and Lucchini, 6.6 million tonnes were sold domestically and 2.8 million tonnes were exported.

Severstal Resources' total sales were 9.9 million tonnes of iron ore pellets and 5.8 million tonnes of coal concentrate in 2007. In 2007, Severstal Resources met the full demand for pellets by the Russian Steel Division. Severstal Resources estimates that its total production of pellets and coal concentrate in 2012 will be substantially in excess of demand by the Russian Steel Division and Lucchini for such products, with total production of pellets and coal concentrate increasing to 11.9 million tonnes and 5.4 million tonnes, respectively, with estimated 2010 demand by the Russian Steel Division amounting to 4.7 million tonnes of pellets and 3.1 tonnes of coking coal concentrate and demand by Lucchini amounting to 0.8 million tonnes of pellets.

Severstal Resources plans to continue selling iron ore and coal to the Cherepovets Steel Plant and currently covers 100 percent of the Cherepovets Steel Plant's production needs in pellets and hard coking coal and in excess of half of its needs in iron ore concentrate.

Severstal Resources' main customers are domestic Russian and European steel producers. Severstal Resources' largest domestic customers, other than the Russian Steel Division, are Evraz, NLMK and Tulachermet. Major European customers include Corus and Arcelor Mittal. Additionally, smaller amounts of coal are also being sold to stand-alone coking companies and power plants.

Of Severstal Resources' exports by volume in 2007, 38 percent were sold to Ukraine, 28 percent to the UK, 13 percent to Finland, 11 percent to the Czech Republic, 4 percent to Denmark, 3 percent to Bulgaria and 3 percent to Turkey, excluding sales to Lucchini and other related parties.

*Products.* Severstal Resources' sales are dominated by iron ore pellets, which accounted for approximately 40 percent sales by volume in 2007. Coking coal concentrate and coking coal together accounted for approximately 32 percent of sales by volume. Iron ore concentrate accounted for approximately 19 percent of sales by volume, while all other products represented 9 percent of Severstal Resources' sales by volume.

The following table sets forth sales by product for Severstal Resources in 2005, 2006 and 2007.

*Sales by Product[(1)] — Severstal Resources*

| Product | Year ended 31 December 2005 | 2006 | 2007 |
|---|---|---|---|
| | | *(million tonnes)* | |
| Iron ore pellets | 8.8 | 9.5 | 9.9 |
| Iron ore concentrate | 3.9 | 4.5 | 4.6 |
| Coking coal concentrate | 5.0 | 5.4 | 5.8 |
| Coking coal | 1.8 | 1.2 | 2.2 |
| Steam coal | 1.8 | 3.5 | 2.3 |
| **Total** | **21.3** | **24.1** | **24.8** |

Note:

(1) Includes intersegmental sales.

*Contracts.* Severstal Resources operates through direct contracts with customers. Usually contracts with domestic customers have a one-year duration, after which both the volume and price may be reviewed. The majority of export sales are made through one to three-year contracts, with price changes annually. Severstal Resources contracts on an annual basis with Corus as its largest export buyer, and intends to increase the amount of sales organised under annual fixed price contracts in the future. It also intends to offer combined pellet and coking coal concentrate contracts for its main international customers.

At present, Severstal Resources enters into most contracts on a FOB or FCA delivery basis; however in the future, it intends to gradually move to CPT/CIF contracts. Because Severstal Resources ships large volumes, it is often able to negotiate discounts on freight and rail fees, thereby increasing the margin on its sales.

## COMPETITION

The following table sets forth some of the competitors of the Group in the global steel industry.

*Competitors of the Group — Global Steel Industry*

| Company | Year ended 31 December 2006 |
|---|---|
| | *(million tonnes)* |
| Estimated worldwide production | 1250.6 |
| *Including:* | |
| — Arcelor Mittal | 117.2 |
| — Nippon Steel Corporation | 34.7 |
| — JFE Steel Corporation | 32.0 |
| — POSCO | 30.1 |

Source: IISI

### Russian Steel Division

Both the Russian and the international steel markets are highly competitive due to increased consolidation. Primary competitive factors include product sophistication, quality, price, payment terms and customer service. In addition, the development of new technologies has reduced the capital costs associated with steel production and led to increased competition from new entrants to the industry with lower capital requirements. The steel industry also competes with producers of materials that offer an alternative to traditional steel products, such as aluminium or plastic. To withstand this competition, the Group has consistently invested both in new facilities, allowing it to produce lower cost, higher quality and more sophisticated products, as well as in management systems and personnel. The Group has also steadily moved the Russian Steel Division further down the value-chain, producing higher-value-added, differentiated products and establishing closer relations with end-users in the export markets. The Group believes that the domestic market share of finished steel products held by the Russian Steel segment, being the Russian Steel Division's primary steelmaking business unit, has increased from approximately 69 percent in 2006 to 71 percent in 2007 and that it is likely to achieve a further increase in market share in 2008.

The Russian Steel segment's key competitors in the Russian domestic markets for flat-rolled steel products are MMK and NLMK. The major competitors in the market for steel sections and specialised products, such as heavy sections, include Evraz and Mechel.

The following table sets forth the principal competitors of the Russian Steel segment in the Russian crude steel market.

*Principal Competitors of the Russian Steel segment — Russian Crude Steel Market*

| Company | Year ended 31 December 2005 | 2006 | 2007 |
|---|---|---|---|
| | *(thousands of tonnes)* | | |
| Evraz | 13,800 | 15,331 | 14,065 |
| MMK | 11,394 | 12,268 | 13,264 |
| Russian Steel segment | 10,821 | 11,293 | 11,867 |
| NLMK | 8,469 | 9,126 | 9,057 |
| Mechel | 5,190 | 5,444 | 5,579 |

Source: Chermet Corporation.

The Russian market is characterised by intensifying competition for customers, raw materials, capital and experienced personnel. The Russian Steel Division's relative cost advantage is of lesser importance in the domestic market as the major domestic competitors, to a varying extent, enjoy similar low cost factors and have access to captive raw materials. In terms of volume, the Group believes that the Cherepovets Steel Plant is one of the two largest steel complexes in the CIS based on production data published by the Chermet Corporation and is one of the most modern and technically sophisticated. The plant has a captive supply of high-quality raw materials, allowing it to ensure a favourable cost baseline even as compared to the largest domestic competitors. The Russian Steel Division's ongoing goal of achieving quality and technical sophistication has also allowed it to gain strong positions in the strategically important pipe manufacturing sector. The Group believes that the Izhora Pipe Mill, with a production capacity of 600,000 tonnes per year, is the only domestic manufacturer of 18-metre-length large-diameter pipe.

Finally, the Russian Steel Division's relative market strength is underpinned by its proactive marketing strategy, which has allowed it to forge long-term relationships with key domestic customers in the pipe production and automotive sector.

**Severstal International**

***North America***

In the North American markets for flat-rolled steel products served by Severstal North America, SeverCorr and Sparrows Point, competition comes from both domestic producers and international sources. The major domestic suppliers are Arcelor Mittal, US Steel, and Nucor, each with a significant market share, with the remainder of the supply from a number of smaller producers and imported steel. Shipments of steel products are heavily influenced by transportation and logistics expenses and most shipments are made within 300 miles of the production facility. In the automotive industry, there are four major steel producers, one of which is Severstal North America, together with Arcelor Mittal, US Steel and AK Steel, all of which are integrated producers, with the capability to produce the highly-engineered and high-quality flat rolled products required for automotive parts.

***Lucchini***

Lucchini's range of locations gives Lucchini strategic access to a combination of sea, rail and road as means for receiving raw material supplies and transporting its goods. Lucchini estimates that it has a favourable market position in rails, with approximately a 12 percent share of the European market and approximately 80 percent share of the domestic Italian market, and a significant domestic market share for wire rod; and that Ascometal has a strong and well-established presence in the long specialty steels market, which is a well-consolidated niche market with relatively high barriers to entry.

According to the Group's estimates, the European market for rails was approximately 2 million tonnes in 2007, with Voest Alpine, Corus and Arcelor Mittal holding significant market shares. The European market for wire rod was estimated to be approximately 11 million tonnes in 2007, with Arcelor Mittal and Saarsahl holding the most significant shares. The European market for bars was estimated to be approximately 12 million tonnes in 2007, with significant market shares being held by Lucchini, Ovako and Corus.

**Severstal Resources**

The Group believes that Severstal Resources is favourably positioned on the global cost curve for both iron ore and coking coal, with strong competitive positions in the domestic markets and in its core export markets of northern and eastern Europe. This is evident in respect of the pellets produced at Karelsky Okatysh and coking coal concentrate produced at Vorkutaugol — the two assets with stronger orientation towards the export market and higher-value added products.

Severstal Resources has a strong market position in the Russian iron ore and coking coal markets. The following tables set forth the principal competitors of Severstal Resources in the Russian markets for coking coal and iron ore.

*Principal Competitors of Severstal Resources — Russian Coking Coal Market*

| Producer of coking coal | Year ended 31 December 2007 |
|---|---|
| | *(estimated percentage of Russian production, 72.9 million tonnes)* |
| Raspadskaya *(affiliated with Evraz)* | 18.6 |
| Severstal Resources(1) | 14.7 |
| Yuzhny Kuzbass *(owned by Mechel)* | 11.9 |
| Sibuglemet (*independent producer*) | 11.9 |
| Yuzhkuzbassugol *(affiliated with Evraz)* | 10.2 |
| Yakutugol *(owned by Mechel)* | 9.6 |
| KRU *(independent producer)* | 6.9 |
| Other | 16.2 |

Source: CDU TEK.

(1) Includes Kuzbassugol production.

*Principal Competitors of Severstal Resources — Russian Iron Ore Market*

| Producer of iron ore (concentrate, pellets or lump) | Year ended 31 December 2007 |
|---|---|
| | *(estimated percentage of Russian production, 93.5 million tonnes)* |
| Metalloinvest | 39.2 |
| Severstal Resources | 15.5 |
| Evraz | 15.1 |
| NLMK | 14.3 |
| Kovdor *(independent producer)* | 5.7 |
| Mechel | 5.2 |
| Other | 5.0 |

Source: RudProm.

The Russian coking coal market is less consolidated than the Russian iron ore market, with high competition in low quality coking coals. Severstal Resources' key competitors in this market include Evraz, Mechel and Sibuglemet. Severstal Resources believes that its location provides it with an advantage over its competitors in the Kuzbass region, which is located over 2,000 kilometres away from the major purchasers of coking coal in the Russian market.

Based on RudProm and CDU TEK industry data, Severstal Resources believes it faces less competition in the iron ore pellets market, compared to the coking coal market. Severstal Resources' main competitor in the Russian iron ore pellets market is Metalloinvest, which delivered approximately 7.7 million tonnes of pellets and 8.2 million tonnes of iron ore concentrate into the Russian domestic market in 2007. Other large producers are Evraz, NLMK and Mechel who predominantly supply iron ore to their own steelmaking operations. The only significant company importing iron ore into the Russian market is the Kazakh producer SSGPO. In 2007, SSGPO exported approximately 5.7 million tonnes of pellets and 6.3 million tonnes of iron ore concentrate into the Russian iron ore market, mostly to MMK.

## EMPLOYEES

The following table sets forth the average number of the Group's employees (full-time equivalents) by business division in 2006 and 2007:

| Business division | 2006 | 2007 |
|---|---|---|
| Russian Steel Division | 61,300 | 60,518 |
| North America[(1)] | 2,171 | 2,165 |
| Lucchini[(2)] | 6,029 | 6,595 |
| Severstal Resources[(3)] | 30,639 | 27,905 |
| **Total** | **100,139** | **97,183** |

Notes:

(1) Excludes employees at SeverCorr and at Sparrows Point, which was acquired in 2008.

(2) Excludes employees at Sidermeccanica, which was disposed of in 2007.

(3) Includes employees at Kuzbassugol, which was disposed of in 2008.

### Russian Steel Division

The reduction in employee numbers between 2006 and 2007 for the Russian Steel Division was the result of increased labour efficiency and changes in staff numbers occurring in the ordinary course of business. This reduction was partially offset by an expansion of the repairs and maintenance services parts of the division, as well as the acquisition of the stevedoring and shipping logistics entities at the port of St. Petersburg and the ramp-up of production at the Izhora Pipe Mill. The Russian Steel Division is currently reviewing its labour structure to ensure it is optimal. A three-year collective bargaining agreement was concluded between the Group and the Mining and Metallurgical Trade Union in 2007 in respect of employees at the Cherepovets Steel Plant, which provides, among other matters, that wages may be renegotiated when the price of a basket of goods increases by at least 5 percent. Since 1996, the Russian Steel Division has experienced no material labour disputes, strikes or employee legal actions. The Russian Steel Division considers its employee relations to be good.

The majority of employees of the Russian Steel Division are entitled to a lump-sum payment on retirement, which is based on their average salary and number of years of service, as well as monthly fixed payments.

### Severstal International

#### *North America*

***Severstal North America.*** A significant reduction in the number of hourly employees has been achieved, which has increased productivity and reduced overall labour cost. In 2007, the Group and the International Union, United Automobile, Aerospace and Agricultural Implement Workers of America ("**UAW**") successfully negotiated a five-year collective bargaining agreement which will expire on 31 March 2012 and is competitive in total compensation and benefits cost with other fully integrated steel makers in the United States. Additionally, the collective bargaining agreement provides for the sharing of business information, timely response and collaborative resolution of issues affecting workplace performance.

Severstal North America maintains defined contribution pension plans for its salaried and hourly employees and post-retirement health care plans, which cover substantially all of its employees and are operated on a pay-as-you-go basis. No assets have been segregated and restricted to provide for retiree medical benefits under the plans. Under the terms of the collective bargaining agreement, Severstal North America's obligation under the post-retirement health care plan is capped at the 2009 rate. Any further increase in health care costs as a result of future health care trend rate increases is to be borne by the plans' beneficiaries.

***SeverCorr.*** Currently, SeverCorr employs 551 employees, which is expected to increase to approximately 665 after the completion of Phase II. There is a competitive incentive plan in place that encourages high production levels with a limited number of workers. SeverCorr maintains a defined contribution pension plan for its salaried and hourly employees as well as health care plans, which cover all of its employees.

***Sparrows Point.*** As at 31 December 2007, Sparrows Point had 2,452 employees. The contract with the United Steelworkers ("**USW**") union includes minimal labour grades (5) with expanded job duties that provide increased workplace flexibility and employee empowerment consistent with new industry standards. The contract covers 100 percent of the hourly workforce until August 2008. Sparrows Point employees participate in 401(k) plans. Sparrows Point maintains health insurance and life insurance programmes for both its USW and salaried employees. For active USW employees of Sparrows Point, there is a retiree insurance benefit plan that has a co-insurance of 25 percent. Active USW employees of Sparrows Point also participate in the Steelworker Pension Trust (multi-employer plan) rather than a defined benefit plan.

***Lucchini***

The average number of employees at Lucchini in 2007 was 6,595, consisting of 3,204 at Piombino and 3,391 at Ascometal, excluding employees at Sidermeccanica, which was disposed of in 2007. Lucchini launched several initiatives at Piombino during 2005 to improve the quality of human resources, such as exchange programmes with other parts of the Group to promote expertise sharing.

**Severstal Resources**

Severstal Resources expects its restructuring and headcount reduction programme to lead to a headcount of approximately 24,500 by the end of 2008, but which is likely to increase to approximately 25,700 in 2010 driven by anticipated production increases, particularly in the gold mining and ferrous scrap metal businesses. The headcount reductions are expected to arise from higher productivity through increased use of capital equipment, employee training and optimisation of organisational structures.

Severstal Resources has entered into collective bargaining agreements in respect of employees at Karelsky Okatysh, expiring at the end of 2010, and Olkon, expiring in May 2010. In respect of Vorkutaugol, Severstal Resources is a party to a regional collective agreement, expiring at the end of 2010.

Under Russian legislation, Severstal Resources is obliged to make monthly pension contributions to the state pension fund on behalf of all of its employees. Contributions are calculated according to a regressive scale related to employees' actual compensation. Currently, Severstal Resources does not have any material accrued liabilities in respect of their contributions to the state pension fund. In addition to the contributions made to the state pension fund, Severstal Resources has obligations in respect of social programmes under collective workplace agreements, which include providing life and workplace insurance, medical insurance and voluntary pension contributions.

**HEALTH, SAFETY AND ENVIRONMENT**

Each of the Group's business divisions operate health and safety management systems which apply a systematic approach to establishing work processes that preserve and enhance their employees' ability to work effectively and safely and are in compliance with applicable legal requirements.

Each of the Group's business divisions monitors its compliance with applicable environmental regulations and standards. Each of the Group's business divisions have been and continue to be the subject of claims, litigation and other proceedings relating to environmental matters.

**Russian Steel Division**

In 2006, there were 86 industrial accidents in the Russian Steel segment, declining in 2007 to 67. In January 2008, a fire at blast furnace 5 at the Cherepovets Steel Plant resulted in one casualty. In 2007, there were 30 accidents at Metalware. No data is available for industrial accidents at Metalware in 2006. No accidents at Izhora Pipe Mill were reported in 2006 or 2007. The Group estimates that its total expenditure on industrial safety measures at the Cherepovets Steel Plant in 2007 amounted to approximately US$5.1 million, compared to approximately US$4.4 million in 2006. This expenditure was made on items such as safety clothing, boots and other personal safety equipment and improving working conditions.

**Severstal International**

*North America*

***Severstal North America.*** Severstal North America believes that it was the first integrated steel mill in the United States to certify their health and safety programme to an international ISO standard (OHSAS 18001). The mill has successfully maintained this certification through independent semi-annual surveillance audits and a recertification audit in March 2008. Recordable injury, lost workday case and lost time accident rates in 2007 improved over 2003 levels by 79.73 percent, 46.41 percent and 74.18 percent, respectively. The site's five-year goal is to achieve zero accidents. The 2008 safety improvement programmes include employee safety awareness training for all employees, supervisor safety leadership training, safety compliance audits, cardinal safety rules, daily management safety briefings, senior management safety walks and electronic safety concern tracking systems to ensure timely closure on identified issues. The Severstal OSHAS 18001 programme also defines mill-specific continuous improvement programmes to address priority issues identified through annual hazard assessments. The key to the OHSAS safety management system is to raise safety issues at all levels of the operating units and increase ownership and personal accountability among all employees.

On 5 January 2008, an accident occurred at blast furnace "B" at Severstal North America's Dearborn facility (see "— North America — Facilities — Dearborn — Blast furnaces"), which resulted in one injury. The cause of the accident is currently under investigation.

***SeverCorr.*** In 2007, SeverCorr's Occupational Health and Safety Administration ("**OSHA**") Total Recordable Incident Rate ("**TRIR**") was 4.8, compared to a Steel Industry Standard Rate of 5.4, and SeverCorr's Days Away Restricted Transfer ("**DART**") was 2.8, compared to a Steel Industry Standard Rate of 2.9. SeverCorr has improved its safety performance by performing behavioural safety audits, frequent site wide accident/incident communication, and various other improved operating procedures.

***Lucchini***

In 2006, there were 248 industrial accidents at Lucchini, declining in 2007 to 187. In the case of particular problems or special requirements, Lucchini's plants can make use of external, specialist support. For example, each plant has an external specialist in charge of industrial medicine who, with the support of a paramedic, provides for the medical service of all the personnel. In addition, first aid services are available at each plant and comprise a first aid room properly equipped for medical treatments and overseen by a medical doctor and an ambulance equipped with basic medical aids. The Group believes Lucchini's health and safety systems allow Lucchini to define work processes, to preserve and improve workers' ability to work effectively and safely and to take prompt decisions to correct unsafe working conditions.

Lucchini's Ascometal business unit maintains safety and monitoring procedures at each production site exposure to hazardous substances, such as asbestos. However, certain employees have alleged that they were exposed to asbestos in the course of employment and have developed diseases as a result, and have brought claims before the French social security tribunals. While Ascometal vigorously defends itself against such actions, the Group believes that, even if such claims are resolved adversely to Ascometal, this would not result in a material liability for the Group. At 31 December 2007, Ascometal had created a €9,914 thousand reserve in respect of potential asbestos-related liabilities pertaining to claims of which it was aware at such date.

**Severstal Resources**

The number of industrial accidents at Severstal Resources was 271 for 2007, 504 for 2006 and 810 for 2005. Severstal Resources made health and safety investments of approximately US$9.9 million in 2007, US$6.4 million in 2006 and US$1.7 million in 2005. Karelsky Okatysh, Vorkutaugol and Olkon are accredited under the international occupational health and safety standard, OHSAS 18001. Severstal Resources believes that its "safety for all" programme is unique in Russia in its scale and the number of participants, and has been effective in reducing the number of incidents in recent years.

In June 2007, at the Vorkutaugol mining complex, there was an explosion and fire, which resulted in ten casualties. The investigation into the accident, conducted by the relevant authorities, concluded that the accident resulted primarily from the particular geological conditions and other of the mine. Severstal Resources paid voluntary compensation to the families of the miners who died and was not prosecuted or fined in connection with the accident.

## INSURANCE

The Group's business divisions maintain a level of insurance commensurate with the standards of other leading steel companies in the markets in which it operates.

### Russian Steel Division

The Russian Steel Division maintains a level of insurance covering the property, plant and equipment at the Russian Steel Division (for replacement value as assessed by the Moscow subsidiary of American Appraisal Inc.) commensurate with the standards of other international and domestic steel companies and has business interruption insurance cover ranging from fixed costs to full gross profits, depending on the plant, for interruption periods of up to 12 months' indemnity.

The Russian Steel Division does not purchase full insurance for third-party liability in respect of property or environmental damage.

Third-party insurance services are provided to the Russian Steel Division by Russian insurers, which include Sheksna Insurance Company ("**Sheksna**"), which was previously owned by the Group and divested in 2004. All risks covered by policies issued by Sheksna are reinsured, with approximately 70 percent to 95 percent reinsured in the international market and the remainder with domestic insurers.

### Severstal International

#### *North America*

North America maintains a level of insurance covering its property, plant and equipment commensurate with the standards of other leading steel companies in the United States. North America's insurance covers direct damage and business interruption, including loss of profits up to specified limits. North America also maintains a level of insurance for injury, property damage and other related third-party risks. In January 2008, there was an accident at blast furnace "B" at Severstal North America's Dearborn facility, in respect of which claims under property and business interruption insurance have been made. See "— Severstal International — North America — Facilities".

#### *Lucchini*

Lucchini has adopted an insurance programme that includes all Lucchini group companies. The insurance policies have been reinsured in the international re-insurance market. Lucchini also has a risk management policy whose main target is to monitor and focus on critical risk areas and propose alternative solutions through insurance or other means. Both risk management and risk transfer strategies are carried out through services of Willis Italia, the risk management consultant and insurance broker member of Willis Group.

### Severstal Resources

Severstal Resources maintains a level of insurance commensurate with the standards of other large mining companies in Russia. In particular, it fully insures the property, plant and equipment of Karelsky Okatysh and Olkon at actual value (ACV). These assets also have limited business interruption insurance covering the direct costs of an interruption, including lost profit and incurred fixed costs of operation. Employees are insured against accidents.

Insurance coverage in respect of property, plant and equipment at the coalmines is on a partial basis, and does not include business interruption insurance. Procedures are being put in place to ensure insurance coverage for all newly built major facilities. All employees are insured against accidents that occur within the workplace. Severstal Resources does not have comprehensive insurance for third party liability in respect of property or environmental damage. Insurance services are provided to Severstal Resources by

Sheksna. All risks covered by policies purchased from Sheksna are reinsured on international markets, with Munich Re serving as lead re-insurer.

### Legal

Each of the Group's business divisions has been and continues to be the subject of legal proceedings and adjudications from time to time, which are incidental to the Group's business. The Group is not aware of any governmental, legal, or arbitration proceedings (including any such proceedings which are pending or threatened of which the Group is aware), during the last 12 months, which may have, or have in the recent past, significant effects on the Group's financial position or profitability.

## MANAGEMENT

### ANNUAL GENERAL SHAREHOLDERS' MEETING

The annual general shareholders' meeting is the Company's highest governing body and has exclusive powers to take certain decisions by a vote of the ordinary shares represented at the meeting. The powers of the Company's shareholders, acting through the general shareholders' meeting, are derived from, and their scope is limited to, the powers set forth in the Federal Law dated 26 December 1995 No. 208-FZ "On Joint Stock Companies", as amended ("**Federal Law on Joint Stock Companies**"), and the Company's charter. Voting at a general shareholders' meeting is generally based on the principle of one vote per ordinary share, with the exception of the election of the Board of Directors, which must be done through cumulative voting. Ordinarily, a majority vote of the voting shares present at a general shareholders' meeting is required for a decision of the general shareholders' meeting to be valid. However, a three-quarters majority vote of the voting shares present at a general shareholders' meeting is required to approve certain decisions.

Issues for which a majority vote is required include:

- the number of members of the Board of Directors, and the election and dismissal of its members;
- the election and dismissal of the Internal Audit Commission;
- the approval of the Company's independent auditor;
- the increase of the Company's share capital by way of an increase in the nominal value of the Company's shares;
- the reduction of the Company's share capital by way of the repurchase of part of the Company's shares for the purpose of decreasing the total number of outstanding shares and the cancellation of the acquired or repurchased shares;
- the approval of the Company's annual reports and financial statements;
- the declaration and payment of dividends;
- the splitting and consolidation of the Company's shares;
- the approval of interested party transactions in cases provided for by the Federal Law on Joint Stock Companies;
- the approval of the Company's participation financial and industrial groups, associations and other unions of commercial organisations;
- the approval of internal regulations in relation to management bodies of the Company; and
- other issues as provided by the Federal Law on Joint Stock Companies and the Company's charter.

Issues for which a three-quarters majority vote is required include:

- amendments to the Company's charter;
- the reorganisation of the Company;
- the liquidation of the Company, appointment of the liquidation commission and approval of the interim and final liquidation balances;
- the number, nominal value and type of authorised shares, and the rights attached to those shares;
- the approval of major transactions in cases provided for by the Federal Law on Joint Stock Companies;
- the acquisition by the Company of issued shares in cases provided for by the Federal Law on Joint Stock Companies;
- any issue of shares, or securities convertible into shares, by a closed subscription;
- the reduction of the Company's share capital by way of a reduction of the nominal value of the Company's shares;
- the increase of the Company's share capital by placement of additional shares by means of a closed subscription;

- the increase of the Company's share capital by issuing additional ordinary shares by means of an open subscription if the ordinary shares to be additionally issued would constitute over 25 percent of the total number of ordinary shares issued prior to such additional issue; and
- the issue of securities convertible into ordinary shares by means of an open subscription if the shares into which the securities would be converted would constitute over 25 percent of the total number of ordinary shares issued prior to such issue.

A quorum for a general shareholders' meeting of the Company is achieved if the holders of more than 50 percent of the issued outstanding voting shares are attending in person or by proxy. If a 50 percent quorum is not achieved, the quorum shall be at least the holders of 30 percent of the issued outstanding voting shares are attending (in person or by proxy) a meeting duly reconvened to consider the same agenda.

The annual general shareholders' meeting must be convened by the Board of Directors between 1 March and 30 June of each year, and the agenda must include the following items:

- election of the members of the Board of Directors;
- approval of the annual report, balance sheet and profit and loss statement;
- approval of the distribution of profits and losses;
- approval of the appointment of an independent auditor; and
- election of the Internal Audit Commission.

A shareholder owning, individually or collectively with other shareholders, at least 2 percent of the issued voting shares may propose items for the agenda of the annual general shareholders' meeting and may nominate candidates to the Board of Directors and the Internal Audit Commission. Any agenda items or nominations must be submitted to the Company no later than 60 calendar days after the end of the financial year.

Extraordinary general shareholders' meetings may be convened by the Board of Directors on its own motion or at the request of the Internal Audit Commission, the independent auditor or any shareholder owning, individually or collectively with other shareholders, at least 10 percent of the issued voting shares at the date of the request.

A general shareholders' meeting may be held in person or by absentee ballot. A general shareholders' meeting held in person involves the adoption of resolutions by the general shareholders' meeting through the personal attendance of the shareholders or their authorised representatives for the purpose of discussing and voting on issues on the agenda, provided that if the ballot is mailed to shareholders for participation at a meeting convened in such form, the shareholders may complete and mail the ballot back to the company without personally attending the meeting. A general shareholders' meeting held by absentee ballot involves the determination of shareholders' opinions on the issues on the agenda by means of a written poll.

The following issues cannot be decided by absentee ballot:

- the election of the members of the Board of Directors;
- the election of the Internal Audit Commission;
- the approval of the appointment of an independent auditor; and
- the approval of the annual report, balance sheet and profit and loss statement, and the distribution of profits and losses.

**Notice and Participation**

All shareholders entitled to participate in a general shareholders' meeting must be notified of the meeting, whether the meeting is to be held in person or by absentee ballot, no fewer than 30 days prior to the date of the meeting, and such notification shall specify the agenda for the meeting. However, if election of the members of the Board of Directors is on the agenda of an extraordinary general shareholders' meeting, shareholders must be notified at least 70 days prior to the date of the meeting. Only those items that are set forth in the statutory notice to shareholders may be considered at a general shareholders' meeting. According to the Company's charter, the notice to the shareholders can be sent to the shareholders by registered post or delivered by hand. The Company must also publish the notice in the Russian newspapers "Cherepovetsky Metallurg" and "Rossiyskaya Gazeta".

The list of persons entitled to participate in a general shareholders' meeting is to be compiled on the basis of the data in the Company's register of shareholders on the date specified by the Board of Directors. The list of persons entitled to participate in a general shareholders' meeting may not be compiled earlier than the date of adoption of the resolution to hold such meeting and may not be more than 50 days before the date of the meeting or, in the case of an extraordinary general shareholders' meeting to elect the Board of Directors, 85 days before the date of the meeting.

Generally, the right to participate in a general shareholders' meeting may be exercised by a shareholder as follows:

- by personal attendance;
- by proxy;
- by absentee ballot; or
- by delegating the right to vote using the absentee ballot to a duly authorised representative.

**BOARD OF DIRECTORS**

Pursuant to the Federal Law on Joint Stock Companies and the Company's charter, the Board of Directors (the "**Board of Directors**") is responsible for the general management of the Company and its operations, except with respect to matters reserved to the exclusive competence of the general shareholders' meeting.

The members of the Board of Directors are elected at the annual general shareholders' meeting through a system of cumulative voting for the period until the next annual general shareholders' meeting (except if re-election of the Board of Directors is required by an extraordinary general shareholders' meeting). Only natural persons (as opposed to legal entities) are entitled to sit on the Board of Directors. Members of the Board of Directors are not required to be shareholders of the Company. As provided by law, the Company's charter requires that the entire Board of Directors retire and stand for re-election at each annual general shareholders' meeting, and that a new Board of Directors be elected through cumulative voting. Under cumulative voting, each shareholder may cast an aggregate number of votes equal to the number of shares it holds multiplied by the number of persons to be elected to the Board of Directors, and the shareholder may give all such votes to one candidate or spread them between two or more candidates.

All directors may be removed as a group without cause at any time before their term expires by a majority vote of shareholders participating in a general shareholders' meeting. Persons elected to the Board of Directors may be re-elected an unlimited number of times.

The Federal Law on Joint Stock Companies generally prohibits the Board of Directors from acting on issues that fall within the exclusive competence of the general shareholders' meeting of the Company. According to the Federal Law on Joint Stock Companies and the Company's charter, the Board of Directors has the power to perform the general management and, among other things, it has the power to:

- determine the Company's business priorities;
- convene annual and extraordinary general shareholders' meeting of the Company, other than in certain cases provided by law;
- approve the agendas of general shareholders' meetings of the Company;
- determine the record date for compilation of the list of persons having the right to participate in the general shareholders' meetings and pass resolutions on certain other issues in connection with the preparation for, and holding of, general shareholders' meetings;
- resolve to issue bonds and other securities in accordance with applicable law;
- determine the value of property and of the placement and repurchase price of the Company's securities in accordance with applicable law;

- acquire shares, bonds and other securities issued by the Company other than in situations reserved to the exclusive competence of the general shareholders' meeting;
- decide on the policy of appointment and remuneration of the Company's chief executive officers, including the general director and make recommendations with respect to such policy and the early termination of its powers;
- make recommendations on the amount of remuneration and compensation to be paid to the Internal Audit Commission and on the independent auditor's fee;
- make recommendations on the amount of dividends to be paid and the procedure for the payment thereof;
- decide on the utilisation of the Company's reserve and other funds;
- establish and close down the Company's branches and representative offices;
- approve major and interested party transactions in accordance with applicable law;
- approve the appointment of the Company's registrar and the terms of, as well as the termination of, the registrar's appointment;
- approve transactions with a value exceeding 10 percent of the book value of the Company's assets;
- approve the acquisition of (i) shares or participatory interests or the rights to dispose of them or (ii) fixed assets or intangible assets, if the total value of any such transaction is more than US$500 million; and
- review of the consolidated budget of the Group and submission of recommendations related to such budget.

The number of members of the Board of Directors is approved by the general shareholders' meeting and must be equal to 10 members. A meeting of the Board of Directors has a quorum if at least half of its members are present. Some decisions (such as increases in the share capital and approvals of major transactions) require the unanimous agreement of all members of the Board of Directors. Decisions on approval of transactions with a value exceeding 10 percent of the book value of the Company's assets and transactions with a total value over US$500 million are to be adopted by a two-thirds majority of the total number of directors, excluding any retired directors.

As at 25 July 2008, the active membership of the Board of Directors (the business address of each of which is Ulitsa Mira 30, Cherepovets, Vologda Region, 162600 Russia, and the telephone of which is +7 8202 530 909) is as follows:

| Name | Year of Birth | Current position/biography and outside memberships | Since |
|---|---|---|---|
| Christopher Clark . . . . . . . . | 1942 | Independent Chairman of the Board of Directors, Member of Nomination and Remuneration.<br><br>Mr. Clark is a graduate in metallurgy from Trinity College, Cambridge and the Brunell University of London. His career spanned 40 years at Johnson Matthey plc, a specialty chemical and precious metals Group, where he served as Chief Executive Officer in 1998-2004. Since 2004, Mr. Clark has held a number of non-executive positions.<br><br>Mr. Clark's outside activities include the following:<br>• Associated British Ports (Chairman of the Board of Directors);<br>• Urenco Limited (Chairman of the Board of Directors); and<br>• Wagon plc (Chairman of the Board of Directors). | 2006 |

| Name | Year of Birth | Current position/biography and outside memberships | Since |
|---|---|---|---|
| Alexey A. Mordashov | 1965 | Member of the Board of Directors; Chief Executive Officer of the Group, Member of Nomination and Remuneration Committee.<br><br>Mr. Mordashov is a graduate of the Leningrad Institute of Engineering and Economics. He has worked at the Group since 1988. He has also served as the Chief Economist and later as the Deputy Head of the Planning Department. Between 1992 and 1996, Mr. Mordashov was the Group's Finance Director. He was the Group's General Director from 1996 to 2002.<br><br>Mr. Mordashov's outside activities include the following:<br>• OAO AB Russia (Member of the Board of Directors);<br>• ZAO Alliance — 1420 (Chairman of the Board of Directors);<br>• OOO Capital (General Director);<br>• OOO Algoritm (General Director);<br>• ZAO Laguna-Delta (General Director);<br>• OAO Sveza (Chairman of the Board of Directors);<br>• OAO Terraprof (General Director);<br>• OOO Severstal-Holding (Chairman of the Board of Directors);<br>• OAO Power machines (Chairman of the Board of Directors); and<br>• ZAO Severstal Group (General Director). | 1996 |
| Martin Angle | 1950 | Independent Director, Chairman of the Audit Committee<br><br>Mr. Angle is a graduate of the University of Warwick in physics. He is also a Chartered Accountant, a Member of the Securities Institute and a Fellow of the Royal Society of Arts. He was an Operational Managing Director of Terra Firma Capital Partners and a director of various of its portfolio companies, including positions as Executive Chairman for Waste Recycling Group and Deputy Chairman for the Le Méridien hotel group.<br><br>Mr. Angle's outside activities include the following:<br>• Savills plc (Member of the Board of Directors);<br>• Dubai International Capital LLC (Member of the Board of Directors);<br>• The National Exhibition Group (Chairman);<br>• Celerant Consulting (Chairman); and<br>• Warwick Business School (Board of Directors). | 2006 |

| Name | Year of Birth | Current position/biography and outside memberships | Since |
|---|---|---|---|
| Ronald Freeman . . . . . . . . . | 1939 | Independent Director, Member of the Audit Committee.<br><br>Mr. Freeman is a graduate of Lehigh University and Columbia Law School. Between 1991 and 1997, he served as the Head of the Banking Department of the European Bank for Reconstruction and Development (EBRD). Prior to that, he worked in the Citigroup investment business. Mr. Freeman is a member of the New York Bar.<br><br>Mr. Freeman's outside activities include the following:<br><br>• Moscow-based Troika Dialog Investment Bank (Member of the Board of Directors; Consulting Partner);<br><br>• Polish Telecom (Supervisory Board);<br><br>• Imagine Group Holdings Ltd. (Member of the International Advisory Council);<br><br>• Volga Gas (member of the Board of Directors);<br><br>• KAMAZ Inc. (member of the Board of Directors); and<br><br>• UK/US Fulbright Commission (Commissioner, Co-Chairman). | 2006 |
| Anatoly N. Kruchinin . . . . . | 1960 | Member of the Board of Directors; Chief Executive Officer of Cherepovets Steel Plant<br><br>Mr. Kruchinin is a graduate of the Ivanovo Energy Institute. He began his career with the Group in 1982. He was Head of the Group's Energy Division between 1993 and 1999. He was appointed the Group's Commercial Director in 1999. In 2002, he was appointed Executive Director, assuming the functions of the general director of the Group.<br><br>Since December 2006, he has been the Chief Executive Officer of Cherepovets Steel Plant.<br><br>Mr. Kruchinin's outside activities include the following:<br><br>• OOO Severstal-Mebel (Chairman of the Board of Directors);<br><br>• OOO Severstal-Emal (Chairman of the Board of Directors); and<br><br>• ZAO Torgovy Dom Severstal-Invest (Chairman of the Board of Directors). | 1999 |
| Peter Kraljic . . . . . . . . . . . . | 1939 | Independent Director; Member of the Audit and Strategy Committee.<br><br>Mr. Kraljic is a graduate of the University of Ljubljana and Polytechnic University in Hannover, Germany. He also holds a masters degree in business management from the INSEAD business school in France. | 2006 |

| Name | Year of Birth | Current position/biography and outside memberships | Since |
|---|---|---|---|
| | | He is a Director Emeritus at McKinsey & Company, where he spent 32 years and held a number of senior positions until his retirement in 2002. His experience focused on the chemical, pharmaceutical, automotive assembly, steel and aluminium sectors. He was also a member of McKinsey's Personnel Development Committee and managed McKinsey's activities in France and Germany.<br><br>Mr. Kraljic has also led economic growth and job creation projects in Germany and Brazil.<br><br>Mr. Kraljic's outside activities include the following:<br><br>• Business School Bled (member of Advisory Board); and<br><br>• LEK d.d., Slovenia (member of Advisory Board). | |
| Vadim A. Makhov . . . . . . . | 1972 | Member of the Board of Directors; Chairman of Severstal North America and Vice Chairman of Lucchini, Chairman of the Strategy Committee.<br><br>Mr. Makhov is a graduate of the State Management Academy. He has been with the Group since 1994. He has worked as Head of the Economic Research Laboratory at the Group, Head of the Strategic Planning Department and Deputy General Director for Strategic Planning. Mr. Makhov has been Strategic Planning Director since 1998. In 2002, he was appointed Deputy General Director of ZAO Severstal Group for Strategic Planning and Development of Business.<br><br>From December 2004, he served as Deputy Chief Executive Officer of the Group for Strategy and Business Development. In 2007, he was appointed Deputy Chief Executive Officer of the Group for Strategy and Business Development. | 1998 |
| Mikhail V. Noskov . . . . . . . | 1963 | Member of the Board of Directors of the Group.<br><br>Mr. Noskov is a graduate of the Moscow Institute of Finance. He worked for the International Moscow Bank between 1989 and 1993. He has also worked at Credit Suisse (Moscow) as Head of Trade Finance. Between 1997 and 1998, he served as Head of Corporate Finance at the Group. He was appointed Finance Director in 1998. Since 2002, Mr. Noskov has been Deputy General Director of ZAO Severstal Group for Finance and Economics. In January 2007, he was appointed Deputy Chief Executive Officer for Finance and Economics of the Group.<br><br>Mr. Noskov's outside activities include the following:<br><br>• OOO Media-Holding REN-TV (Member of the Board of Directors);<br><br>• OAO "Bank VTB North-west" (Member of Advisory Board); | 1998 |

| Name | Year of Birth | Current position/biography and outside memberships | Since |
|---|---|---|---|
| | | • OAO Sveza (Member of the Board of Directors);<br>• ZAO "National Media Group" (Member of the Board of Directors); and<br>• Non governmental superannuation fund "Stalfond" (Member of Advisory Board). | |
| Rolf Stomberg . . . . . . . . . . | 1940 | Independent Director, Chairman of the Nomination and Remuneration Committee.<br>Mr. Stomberg is a graduate of Hamburg University. He held executive positions with British Petroleum (BP) as a managing director and a chief executive officer of BP's refining and marketing business.<br>Mr. Stomberg's outside activities include the following:<br>• Lanxess AG (Chairman of the Supervisory Board); and<br>• Smith & Nephew plc (Senior Independent Director). | 2006 |
| Gregory Mason . . . . . . . . . | 1952 | Member of the Board of Directors.<br>Mr. Mason is a graduate of the Naval University of St. Petersburg and is a registered professional engineer in the United States. Mr. Mason joined the Group in 2004 and, in 2006, he was appointed as Chief Operating Officer of the Group. In 2008, he was also appointed as the Chief Executive Officer of Severstal International. Prior to joining the Group, Mr. Mason was the managing partner at Metal Strategies, an international metals industry management consulting firm. His other previous positions include roles as a Vice President of Detroit Steel Company, Technical Director of Caparo Steel, Steelmaking Technology Director at Davy International and Chief Engineer at KRUPP Industries (a division of KRUPP Stahl). | 2008 |

There are no current or potential conflicts between the private interests and duties of the members of the Board of Directors or the General Director and the duties of those officers to the Company.

In the previous five years, no member of the Board of Directors has been convicted of any fraudulent offence; served as a director, partner, founder or senior manager of any organisation that has been the subject of any bankruptcies, receiverships or liquidations; was subject to any official public incrimination or sanctions by statutory or regulatory authorities, including designated professional bodies, or has been disqualified by a court from acting as a director of an issuer or from acting in the management or conduct of the affairs of any issuer.

### General Director

The General Director of the Company is the Company's executive body that carries out the day-to-day management of the Company.

The General Director, elected by the general shareholders' meeting for a three-year term, is entitled to act on behalf of the Company without a power of attorney. The following matters are within the competence of the General Director:

- the implementation of current and future programmes of the Company;
- the performance of the routine management of the Company's operations;

- the representation of the Company's interests both in Russia and abroad;
- performance of the resolutions adopted by the general shareholders' meeting and the Board of Directors;
- the adoption of regulations on sub-divisions of the Company and on various subjects of the Company's business activities;
- employment of the Company's staff;
- the issuance of powers of attorney on behalf of the Company;
- the entry into transactions on behalf of the Company;
- the general management of the Company's assets (the value of which does not exceed 10 percent of the assets of the Company); and
- the issuance of orders and instructions binding upon all subordinated officers and employees of the Company.

Mr. Alexey A. Mordashov, the controlling shareholder of the Company and a member of the Board of Directors, was elected by shareholders as the General Director on 15 June 2007 for a three-year term.

### External Auditors and Internal Audit Commission

As required by Russian law, the Company's financial and economic activities are monitored by the Company's Internal Audit Commission (a body established by the general shareholders' meeting of the Company) and the Company's Chief Accountant.

ZAO KPMG conducts the statutory audit of the Company's stand-alone accounts produced under Russian Accounting Standards. The appointment of ZAO KPMG as the statutory auditors of the Company is approved by the annual general shareholders' meeting.

Audits of the Company's financial and economic performance are conducted by the Internal Audit Commission on the basis of the Company's annual results, but may also be carried out at any time on the initiative of the Internal Audit Commission or at the request of the general shareholders' meeting, the Board of Directors or any shareholder owning a total of at least 10 percent of the Company's voting shares.

The Internal Audit Commission prepares a report on the basis of the results of the audit. The report should contain confirmation of the authenticity of data included in financial reports, accounts and other financial documents of the Company, and set forth breaches of procedures for conducting accounting operations and financial reporting established by applicable Russian laws.

The Internal Audit Commission's report must be submitted to the Board of Directors no later than 45 days prior to the annual general shareholders' meeting in accordance with Regulations on Internal Audit Commission. In accordance with the Company's charter, the Internal Audit Commission consists of three members. They are elected at the annual general shareholders' meeting and their incumbency lasts until the date of the next annual general shareholders' meeting.

The present members of the Internal Audit Commission are:

| Name | Position |
|---|---|
| Mr. Roman Antonov | Deputy Head of the Internal Audit Department |
| Mr. Timur Bayazitov | Head of the Risk Management Department |
| Mr. Alexei Guryev | Head of the Internal Audit Department |

### Audit Committee

The Audit Committee of the Board of Directors is responsible for evaluating candidates for the position of the Group's auditor, evaluating auditors' reports, evaluating the Group's internal control and risk management procedure, analysing the system for the approval of unusual transactions and making suggestions for improvement to the Board of Directors.

The Audit Committee consists of three Independent Directors. At least one member of the Audit Committee shall have recent, relevant and sufficient experience in the financial area, as well as skills reasonably required for financial statements and business risks analysis and financial management skills. No senior executive of the Company may be a member of the Audit Committee.

The Audit Committee consists of three members of the Board of Directors: Mr. Freeman, Mr. Kraljic and Mr. Angle. The Audit Committee is chaired by Mr. Angle.

### Remuneration and Nomination Committee

The Remuneration and Nomination Committee of the Board of Directors is responsible for assisting the Board of Directors in engaging qualified experts in managing the Company and creating the incentives necessary to ensure their successful work in the Company.

The Remuneration and Nomination Committee consists of three members. At least two members of the Remuneration and Nomination Committee, including the Chairman of the Committee, shall be Independent Directors who are not senior executives of the Company.

The Remuneration and Nomination Committee consists of three members of the Board of Directors: Mr. Stomberg, Mr. Clark and Mr. Mordashov. The Remuneration and Nomination Committee is chaired by Mr. Stomberg.

### Strategy Committee

The Strategy Committee of the Board of Directors is responsible for formulating and submitting to the Board of Directors its recommendations in relation to the development of the Company's business priorities and its growth strategy, including preparation of measures contributing to improvement of the Company's business on a long-term basis. The Strategy Committee shall assist the Board of Directors in implementing the Board's resolutions regarding the Company's development strategy.

The Strategy Committee shall consist of three members one of which shall be an Independent Director who is not a senior executive of the Company.

The Strategy Committee will consist of three members of the Board of Directors. Currently, the Strategy Committee has two members: Mr. Makhov and Mr. Kraljic. A third member is expected to be selected in the future. The Strategy Committee is chaired by Mr. Makhov.

### Compensation of Senior Managers, Executive Officers and Directors

The aggregate amount of compensation paid by the Company to its senior managers as a group (currently 25 persons) in 2007 was US$57.2 million (including salary and other cash compensation paid during 2007) and was US$44.5 million in 2006. This group includes members of the Board of Directors, the Chief Executive Officer of the Group and his deputies, and the Chief Executive Officers of the Group's business divisions. Senior managers also received benefits in kind, including life insurance and real estate insurance from the Company.

Members of the Board of Directors do not receive compensation for service as directors nor is any director a party to any service contract with the Company or any of its subsidiaries where such contract provides for benefits upon termination of employment.

## PRINCIPAL SHAREHOLDERS

The table below sets forth certain information regarding the ownership of the Company as at 3 July 2008, according to the Company's share register:

| Shareholder | Percentage of shares |
|---|---|
| Frontdeal Limited(1) | 36.8 |
| OOO Kapital(1) | 23.1 |
| OOO Deutsche Bank(2) | 15.3 |
| OOO Algoritm(1) | 13.1 |
| Unifirm Limited(1) | 3.2 |
| ZAO Depository-Clearing Company | 1.2 |
| NP National Depository Centre | 1.5 |
| Other minority shareholders | 6.0 |
| **Total** | **100.0** |

Notes:

(1) The ultimate shareholder of Frontdeal Limited, OOO Kapital, OOO Algoritm and Unifirm Limited is Mr. Alexey Mordashov, the Group's chief executive officer and a member of the Board of Directors.

(2) OOO Deutsche Bank is the custodian for Deutsche Bank Trust Company Americas, the Depositary for the Company's Global Depositary Receipts programme.

The Company placed global depositary receipts ("**GDRs**"), which were admitted to trading on the London Stock Exchange on 14 November 2006. Each GDR represents one ordinary share.

As at 3 July 2008, approximately 82.373 percent of the Company's share capital was indirectly controlled by Mr. Alexey Mordashov, the Group's chief executive officer and a member of the Board of Directors. At such date, 0.007 percent of the Company's shares was controlled by members of the Board of Directors through the GDRs representing such shares.

## RELATED PARTY TRANSACTIONS

*The following is a summary of the Group's most significant transactions with related parties for the three months ended 31 March 2008 and the years ended 31 December 2007, 2006 and 2005. For further details of these transactions, see Note 15 to the Annual Financial Statements and Note 5 of the Interim Financial Statements.*

In the ordinary course of its business, the Group has engaged, and continues to engage, in transactions with parties that are under common control with the Group or that are otherwise related parties to the Group. Transactions with entities under common control with the Group constitute transactions with parties that have the same beneficial owners as the Company, or who are also members of the Board of Directors. See "Principal Shareholders". Other than the transactions with entities under common control described herein, the Group did not engage in any transactions with members of its Board of Directors during the period under review.

The Group has transactions with related parties in respect of sales, purchases, financing and other types of transactions. Because of the varying ownership percentages of its Controlling Shareholder in such related parties, as well as other factors, there may be incentives for transactions between the Group and its related parties to be effected on other than arm's-length terms, which could result in subsidies or other transfers of value and could have a material adverse effect on the Group's business, results of operations and financial condition.

The following related parties and their transactions are considered to be significant to the Group. The scope of related party transactions entered into by the Group as reflected in the Annual Financial Statements were similar to those entered into by the Group in the three months ended 31 March 2008.

### SALES

As disclosed in the Interim Financial Statements, the Group's sales to related parties totalled US$164.6 million for the three months ended 31 March 2008. As disclosed in the Annual Financial Statements, the Group's sales to related parties totalled US$701.9 million, US$725.7 million and US$665.6 million for the years ended 31 December 2007, 2006 and 2005, respectively.

The Group has strict credit criteria that not all its customers can meet. In these cases, TD Severstal Invest, an intermediary which is controlled by the Controlling Shareholder, provides financial assistance to the customer by purchasing from the Group in accordance with the stipulated credit terms and selling to the end user on terms that it can afford. For this service the intermediary normally adds a financial charge to the market prices charged by the Group. The EBITDA margin of such intermediary typically varies from 2 to 7 percent, depending on market conditions. Sales of steel products to TD Severstal Invest totalled approximately US$112.0 million for the three months ended 31 March 2008 and US$548.2 million, US$516.7 million and US$349.0 million for the years ended 31 December 2007, 2006 and 2005, respectively.

The remaining related party sales include, *inter alia*, sales of steel products to a Russian automotive manufacturing group and sales to other related party trading companies.

### PURCHASES

As disclosed in the Interim Financial Statements, the Group's purchases from related parties totalled US$129.4 million for the three months ended 31 March 2008. As disclosed in the Annual Financial Statements, the Group's purchases from related parties totalled US$674.7 million, US$1,143.5 million and US$705.1 million for the years ended 31 December 2007, 2006 and 2005, respectively.

The Group has the following major categories of purchases from related parties: transport services, materials and equipment.

#### Transport Services

During 2005, 2006 and 2007, transport services were provided through ZAO Severstaltrans, ("**Severstaltrans**"), which was at that time a related party due to a 50 percent ownership by the Controlling Shareholder. In April 2007, the Controlling Shareholder sold the ownership interest in Severstaltrans, and in September 2007, the Controlling Shareholder terminated his membership on the board of directors of Severstaltrans. Accordingly, since October 2007, transport services, which continue to be provided by Severstaltrans and its affiliates (now operating under a different name) to the Group, have not been treated as related party transactions. Total purchases from Severstaltrans treated as related party transactions for the nine months ended 30 September 2007 were US$427.6 million and for the years ended 31 December 2006 and 2005 were US$510.2 million and US$214.0 million, respectively.

**Purchases from Associates and Joint Ventures**

Purchases from associates and joint ventures totalled US$47.7 million the three months ended 31 March 2008 and US$220.7 million, US$141.6 million and US$85.4 million for the years ended 31 December 2007, 2006 and 2005, respectively, and comprised purchases by Severstal North America from Double Eagle Steel Coating company, Spartan Steel Coating LLC, Delaco Processing LLC and Mountain State Carbon LLC. Such transactions were undertaken as part of Severstal North America's normal business operations and are expected to continue in the foreseeable future.

**Purchases of Raw Materials and Equipment**

Certain purchases of raw materials and construction equipment by Severstal Resources were centralised within certain related parties to increase control over the mining operations. Such purchases ceased in 2006.

### Financing

The Group's cash flows have been used, from time to time, to finance the acquisition and development of various companies. In particular, the acquisition of shares in Lucchini by the Controlling Shareholder was financed through loans issued by the Group.

### Additional Information

For additional information and certain financial statement amounts with respect to various related party transactions for the years ended 31 December 2007, 2006 and 2005 and the balances as at such date, refer to the following parts of the Annual Financial Statements:

Consolidated balance sheet
Consolidated income statement
Notes to the Annual Financial Statements:
Note 5 — Staff costs
Note 8 — Financing
Note 12 — Short-term financial investments
Note 14 — Related party balances
Note 20 — Investment in associates and joint ventures
Note 21 — Long-term financial investments
Note 28 — Subsidiaries, associates and joint ventures
Note 31 — Segment information

For relevant disclosures for the three months ended 31 March 2008 and 2007 and the balances as of those dates, refer to the corresponding parts of the Interim Financial Statements, and in particular the following:

Note 4 — Related party balances
Note 5 — Related party transactions
Note 8 — Segmental information — Income statement

## REGULATORY MATTERS

### Regulation of the Steel and Mining Industries in Russia

Russia has not enacted any specific legislation governing the operation of the steel industry and the business of steel-manufacturing companies. The production, sale and distribution of steel in the Russian Federation is regulated by general civil legislation and special legislation relating to quality standards, industrial safety, environmental and other rules.

On 5 September 2002, the Russian Government approved the "Plan of Measures for Development of the Russian Steel Industry until 2010", (the "**Plan**"). The Plan proposes measures supporting voluntary certification of steel products and promotion of innovation in the industry, reduction of import duties on high-tech machinery, financing of research and development in the steel industry, investment in new technologies and professional development and social protection of the industry's workforce.

Furthermore, the Ministry of Industry and Energy (subsequently reorganised into the Ministry of Industry and Trade) on 29 May 2007 approved the "Strategy for Development of Metal Manufacture Industry of the Russian Federation for the Period till 2015" (the "**Strategy**"). The Strategy, *inter alia*, outlined the key trends and factors relevant for the development of national ferrous and non-ferrous metallurgy and determined that innovative growth would be the priority for improving competitive strength of national manufacturers.

The Federal Law "On Technical Regulation" No. 184-FZ dated 27 December 2002 (the "**Technical Regulation Law**"), introduced new rules relating to the development, enactment, application and enforcement of obligatory technical requirements and the development of voluntary standards relating to manufacturing processes, operations, storage, transportation, selling and utilisation.

The Technical Regulation Law supersedes the Laws of the Russian Federation "On Certification of Goods and Services" No. 5151-1 dated 10 June 1993 and "On Standardisation" No. 5154-1 dated 10 June 1993 and will be followed by the revision of existing legislation and technical rules falling within the scope of its regulation. Under the Technical Regulation Law, technical rules and regulations relating to industrial safety and environmental protection can be enacted only by federal laws, decrees of the president and resolutions of the government.

#### Federal, Regional and Local Regulatory Authorities Governing the Steel Industry

At the federal level, regulatory authority over the steel industry is divided primarily between the Ministry of Industry and Trade and the Ministry of Natural Resources and Ecology. The Ministry of Industry and Trade is responsible for the development of governmental policy in and regulation of, the industry. In addition, it regulates Russian exports and imports of steel products and coordinates intergovernmental negotiations relating to export and import regulations. Prior to 5 June 2008, the latter functions were performed by the Ministry of Economic Development and Trade, subsequently reorganised as the Ministry of Economic Development. The Ministry of Natural Resources and Ecology is responsible for the development of governmental policy and regulation in the sphere of natural resources, including subsoil.

The federal ministries in Russia are not responsible for compliance control or management of state property and provision of services, which are directed by the federal services and the federal agencies, respectively. The federal services and agencies that are relevant to the Group's activities include:

- The Federal Service for Environmental, Technological and Nuclear Supervision, which sets procedures for, and oversees compliance with, industrial safety and environmental rules and issues licences for certain industrial activities and activities relating to safety and environmental protection.
- The Federal Agency for Subsoil Use, which organises auctions and issues licences for subsoil use and approves design documentation for subsoil production activities.
- The Federal Agency for Technical Regulation and Metrology, which determines and oversees levels of compliance with obligatory state standards and technical regulations.

Aside from the above federal executive bodies, which are directly involved in regulating and supervising the steel sector in Russia, there are a number of other federal regulators that, together with their structural sub divisions, have authority over general issues relevant to the Russian steel industry, such as defence, internal affairs, security, border services, justice, tax enforcement, rail transport and other matters.

Generally, regional and municipal authorities with jurisdiction over the specific territory in which a steel-producing enterprise is located have authority in certain matters, in particular with regard to land-use allocations.

**Licensing of Operations**

The Group is required to obtain numerous licences, authorisations and permits from Russian governmental authorities for its operations. The Federal Law "On Licensing of Certain Types of Activities" of 8 August 2001 as amended (the "**Licensing Law**"), as well as other laws and regulations, set forth the activities subject to licensing and establish procedures for issuing licences. In particular, some of the Group's Russian companies need to obtain licences, permits and approvals of executive authorities to carry out certain activities, including, *inter alia*:

- the use of subsoil, which is described in more detail below in "— Subsoil Licensing";
- the collection, utilisation, deactivation, transportation and disposing of hazardous waste;
- the storage, utilisation and distribution of explosives for industrial use (three different licences);
- the operation of complexes containing radioactive substances;
- medical operations;
- educational services; and
- transportation activities.

These licences are usually issued for a period of five years and in most cases may be extended upon application by the licensee. Licences for carrying out of certain types of geological survey may be issued for a period of 10 years. Licences for the use of natural resources may be issued for shorter or longer periods. In particular, licences for the use of subsoil water resources may be issued for periods of up to 25 years, although the Group's licences extend from three to five years. Certain types of licences may also have unlimited terms.

The requirements imposed by regulatory authorities may be costly and time-consuming, which may result in delays in the commencement or continuation of exploration or production operations. Accordingly, the licences that the Group needs may not be issued in a timely fashion, or may impose requirements that restrict its ability to conduct its operations or to do so profitably.

As part of the Group's obligations under licensing regulations and the terms of its licences and permits, the Group must comply with numerous industrial standards, employ qualified personnel, maintain certain equipment and a system of quality controls, monitor operations, maintain and make appropriate filings and, upon request, submit specified information to the licensing authorities that control and inspect their activities.

**Subsoil Licensing**

In Russia, mining minerals requires a subsoil licence with respect to an identified mineral deposit, as well as the right (through ownership, lease or other right) to use the land where such licensed mineral deposit is located. In addition, as discussed above, operating permits are required with respect to specific mining activities.

The licensing regime for use of subsoil for geological research, exploration and production of mineral resources is established primarily by the Federal Law of the Russian Federation "On Subsoil" No. 2395-1 dated 21 February 1992, as amended, (the "**Subsoil Law**"). The procedure for subsoil use licensing, as well as certain rules of exploration and production of mineral resources was established by Resolution of the Supreme Soviet of the Russian Federation on 15 July 1992, as amended, (the "**Licensing Regulation**").

There are two major types of licences: (1) an exploration licence, which is a non-exclusive licence granting the right of geological exploration and assessment within the licence area, and (2) a production licence, which grants the licensee an exclusive right to produce minerals from the licence area. In practice, many of the licences are issued as combined licences, which grant the right to explore, assess and produce minerals from the licence area.

There are two major types of payments with respect to the use of subsoil: (1) periodic payments for geological exploration under the Subsoil Law and (2) the minerals extraction tax under the Tax Code. Failure to make these payments could result in the suspension or termination of the subsoil licence.

***Issuance of subsoil licences.*** Subsoil licences are issued by the Federal Agency for Subsoil Use. Most of the currently existing production licences owned by companies derive from (1) pre-existing rights granted during the Soviet era and up to the enactment of the Subsoil Law to state-owned enterprises that were subsequently reorganised in the course of post-Soviet privatisations; or (2) tender or auction procedures held in the post-Soviet period. The Subsoil Law and the Licensing Regulation set out the major requirements relating to such tenders and auctions.

Amendments to the Subsoil Law, passed in August 2004, significantly changed the procedure for awarding exploration and production licences, in particular abolishing the joint grant of licences by federal and regional authorities. Under the 2004 amendments, production licences and combined exploration and production licences are awarded by tender or auction conducted by the Federal Agency for Subsoil Use. While the auction or tender commission may include a representative of the relevant region, the separate approval of regional authorities is no longer required in order to issue subsoil licences. The winning bidder in the tender is selected on the basis of the submission of the most technically competent, financially attractive and environmentally sound proposal that meets published tender terms and conditions. At the auction, the success of the bid is determined by the attractiveness of the financial proposal.

The Subsoil Law allows for production licences to be issued without a tender or auction procedure only in limited circumstances, such as instances when a mineral deposit is discovered by the holder of an exploration licence at its own expense during the exploration phase. In those circumstances, as a matter of practice, the production licence will be issued to the holder of the exploration licence, but, legally, the right of the holder of the exploration licence to receive the production licence in the event of discovery is not guaranteed.

Regional authorities may issue production licences for “common” mineral resources, such as clay, sand or limestone. A recipient of a licence from a regional authority is also usually granted rights to use the land surrounding the licence area.

***Extension of subsoil licences.*** The term of any subsoil licence is set forth in the licence and runs from the date the licence is registered. Prior to January 2000, exploration licences could have a maximum term of five years, production licences a maximum term of 20 years, and combined exploration, assessment and production licences a maximum term of 25 years. After amendment of the Subsoil Law in January 2000, exploration licences may still have a maximum term of five years (except for exploration licences in relation to inland sea waters, territorial sea and continental shelf which may be issued for a period of up to 10 years); production licences may have a one-year term in a limited number of special cases, but are generally granted for a term of the expected operational life of the field based on a feasibility study; and combined exploration, assessment and production licences can be issued for the term of the expected operational life of the field based on a feasibility study. These amendments did not affect the terms of licences issued prior to January 2000, but permit licensees to apply for extensions of such licences for the term of the expected operational life of the field in accordance with the amended Subsoil Law.

The Subsoil Law permits a subsoil licensee to request an extension of a production licence in order to complete the production from the subsoil plot covered by the licence or the procedures necessary to vacate the land once the use of the subsoil is complete, provided the user complies with the terms and conditions of the licence and the relevant regulations.

In order to extend a subsoil licence, a company must file an application with the federal authorities to amend the licence. The Order of the Ministry of Natural Resources No. 439-r, dated 31 October 2002, requires that the following issues be considered by the relevant governmental authorities when determining whether to approve an amendment: (1) the grounds for the amendments, with specific information as to how the amendments may impact payments by the licensee to the federal and local budgets; (2) compliance of the licensee with the conditions of the licence; and (3) the technical expertise and financial capabilities that would be required to implement the conditions of the amended licence.

In practice, the factors that may affect a company's ability to obtain the approval of licence amendments include its compliance with the licence terms and conditions and its management's experience and expertise relating to subsoil issues, including experience in amending licences.

***Maintenance and termination of subsoil licences.*** A licence granted under the Subsoil Law is generally accompanied by a licensing agreement. The licensing agreement sets out the terms and conditions for the use of the subsoil licence. Prior to the August 2004 amendments, the relevant regional authority, the Ministry of Natural Resources and the licensee were each party to a licence agreement. Under the August 2004 amendments, only the Federal Agency for Subsoil Use and the licensee are parties to licence agreements.

Under a licensing agreement, the licensee makes certain environmental, safety and production commitments, including extracting annually an agreed target amount of reserves; conducting agreed mining and other exploratory and development activities; protecting the environment in the licence areas from damage; providing geological information and data to the local authorities; submitting on a regular basis formal progress reports to regional authorities; making all obligatory payments when due and commitments with respect to social and economic development of the region. When the licence expires, the licensee must return the land to a condition, which is adequate for future use. Most of the conditions set out in a licence are based on mandatory rules contained in Russian law, and licence agreements are generally not negotiable. The Group expects that it will be able to meet the commitments set forth in its licensing agreements.

The fulfilment of a licence's conditions is a major factor in the good standing of the licence. If the subsoil licensee fails to fulfil the licence's conditions, upon notice, the licence may be terminated by the licensing authorities. However, if a subsoil licensee cannot meet certain deadlines or achieve certain volumes of exploration work or production output as set forth in a licence, it may apply to amend the relevant licence conditions, though such amendments may be denied.

The Subsoil Law and other Russian legislation contain extensive provisions for licence termination. A licensee can be fined or the licence can be limited, suspended or terminated for the reasons noted above, for repeated breaches of the law, upon the occurrence of a direct threat to the lives or health of people working or residing in the local area, or upon the occurrence of certain emergency situations. A licence may also be limited, suspended or terminated for violations of "material" licence terms. Although the Subsoil Law does not specify which terms are material, failure to pay subsoil taxes and failure to commence operations in a timely manner have been common grounds for suspension or termination of licences. Consistent underproduction and failure to meet obligations to finance a project would also likely constitute violations of material licence terms. In addition, certain licences provide that the violation by a subsoil licensee of any of its obligations may constitute grounds for limiting, suspending or terminating the licence.

If the licensee does not agree with a decision of the licensing authorities, including a decision relating to a licence limitation, suspension or termination or the refusal to reissue an existing licence, the licensee may appeal the decision through administrative or judicial proceedings. In certain cases of termination, the licensee has the right to attempt to cure the violation within three months of its receipt of notice of the violation. If the issue has been resolved within such a three-month period, no termination or other action may be taken.

Licences may be transferred only under certain limited circumstances that are identified in the Subsoil Law, including the reorganisation or merger of the licence holder or in the event that an initial licence holder transfers its licence to a legal entity in which it has at least a 50 percent ownership interest, provided that the transferee possesses the equipment and authorisations necessary to conduct the exploration or production activity that is covered by the transferred licence.

**Land Use Rights**

Land use rights are needed and granted for the portions of the licence area actually being used, including the plot being mined, access areas and areas where other mining-related activity is occurring.

Under the Land Code of the Russian Federation of 25 October 2001, as amended, (the "**Land Code**"), legal entities may generally have the rights of ownership or lease with regard to land plots in the Russian Federation.

A majority of land plots in the Russian Federation are owned by federal, regional or municipal bodies, which can sell or lease land to private users.

Legal entities may also have a so-called "right of perpetual use" of land plots, provided such type of title was obtained by them prior to the enactment of the Land Code; however, the Federal Law on Introduction of the Land Code of 25 October 2001, with certain exceptions, requires legal entities using land plots on the ground of the right of perpetual use to purchase or to lease the respective land plot from the relevant federal, regional or municipal authority by 1 January 2010.

The Group's mining subsidiaries (composing Severstal Resources) generally have a right of perpetual use of their plots or have entered into long-term lease agreements. A land use lessee has a priority right to enter into a new land lease agreement with a lessor upon the expiration of a land lease. In order to renew a land lease agreement, the lessee must apply to the lessor (usually state or municipal authorities) for a renewal prior to the expiration of the agreement. Any lease agreement for a period of one year or more must be registered with the relevant state authorities.

**Environmental Considerations**

The Group is subject to laws, regulations and other legal requirements relating to the protection of the environment, including those governing the discharge of substances into the air and water, the management and disposal of hazardous substances and waste, the clean-up of contaminated sites, flora and fauna protection and wildlife protection. Issues of environmental protection in Russia are regulated primarily by the Federal Law "On Environmental Protection" No. 7-FZ of 10 January 2002, as amended, (the "**Environmental Protection Law**"), as well as by a number of other federal and local legal acts.

***Pay-to-pollute.*** The Environmental Protection Law establishes a "pay-to-pollute" regime administered by federal and local authorities. The Federal Service for Environmental, Technological and Nuclear Supervision has established standards relating to the permissible impact on the environment and, in particular, limits for emissions and disposal of substances, waste disposal and resource extraction. A company may obtain approval for exceeding these statutory limits from the federal or regional authorities, depending on the type and scale of environmental impact. As a condition to such approval, a plan for the reduction of the emissions or disposals must be developed by the company and cleared with the appropriate governmental authority. Fees are assessed on a sliding scale for both the statutory or individually approved limits on emissions and effluents and for pollution in excess of these limits: the lowest fees are imposed for pollution within the statutory limits, intermediate fees are imposed for pollution within the individually approved limits, and the highest fees are imposed for pollution exceeding such limits. Payments of such fees do not relieve a company of its responsibility to take environmental protection measures and undertake restoration and clean-up activities.

***Environmental approval.*** Any activities that may affect the environment are subject to state ecological approval by federal authorities in accordance with the Federal Law "On Ecological Expert Examination" No. 174-FZ of 23 November 1995, as amended. Conducting operations that may cause damage to the environment without state ecological approval may result in the negative consequences described in "— Environmental liability".

***Enforcement authorities.*** The Federal Service for the Supervision of the Use of Natural Resources, the Federal Service for Environmental, Technological and Nuclear Supervision, the Federal Service for Hydrometrology and Environmental Monitoring, the Federal Agency on Subsoil Use, the Federal Agency on Forestry and the Federal Agency on Water Resources (along with their regional branches) are involved in environmental control, implementation and enforcement of relevant laws and regulations. The federal government and the Ministry of Natural Resources and Ecology are responsible for co-ordinating the activities of the regulatory authorities in this area. Such regulatory authorities, along with other state authorities, individuals and public and non-governmental organisations, also have the right to initiate lawsuits for the compensation of damage caused to the environment. The statute of limitations for such lawsuits is 20 years.

***Environmental liability.*** If the operations of a company violate environmental requirements or cause harm to the environment or any individual or legal entity, a court action may be brought to limit or ban these operations and require the company to remedy the effects of the violation. Any company or employees that fail to comply with the requirements of applicable environmental laws and regulations may be subject to administrative and/or criminal liability. Courts may also impose clean-up obligations on violators in lieu of or in addition to imposing fines. The Group has, in the past, been subject to enforcement actions, fines and, in some cases, court actions in relation to breaches of environmental regulations by the entities currently comprising the Russian Steel Division and Severstal Resources. Although none of these court actions and fines has had, individually or in aggregate, a material adverse effect on the Group, its business and results of operations, there can be no assurance that any such court actions or fines will not have a material effect on the Group in the future.

Subsoil licences generally require certain environmental commitments. Although these commitments can be substantial, the penalties for failing to comply and the clean-up requirements are generally low.

**Health and Safety**

Due to the nature of the Group's business, much of its activity is conducted at industrial sites by large numbers of workers, and workplace safety issues are of significant importance to the operation of these sites.

The principal law regulating industrial safety is the Federal Law "On Industrial Safety of Dangerous Industrial Facilities" No. 116-FZ of 21 July 1997, as amended, (the "**Safety Law**"). The Safety Law applies, in particular, to industrial facilities and sites where certain activities are conducted, including sites where lifting machines are used, where alloys of ferrous and non-ferrous metals are produced and where certain types of mining are done. The Safety Law also contains a comprehensive list of dangerous substances and their permitted concentration, and extends to facilities and sites where these substances are used.

There are also regulations that address safety rules for coal mines, the production and processing of ore, the blast-furnace industry, steel smelting, alloy production and nickel production. Additional safety rules also apply to certain industries, including metallurgical and coke chemical enterprises, and the foundry industry.

Any construction, reconstruction, liquidation or other activities in relation to regulated industrial sites is subject to a state industrial safety review. Any deviation from project documentation in the process of construction, reconstruction and liquidation of industrial sites is prohibited unless reviewed by a licensed expert and approved by the Federal Service for Environmental, Technological and Nuclear Supervision.

Companies that operate such industrial facilities and sites have a wide range of obligations under the Safety Law and the Labour Code of Russia effective 1 February 2002, as amended, (the "**Labour Code**"). In particular, they must limit access to such sites to qualified specialists, maintain industrial safety controls and carry insurance for third-party liability for injuries caused in the course of operating industrial sites. The Safety Law also requires these companies to enter into contracts with professional wrecking companies or create their own wrecking services in certain cases, conduct personnel training programmes, create systems to cope with and inform the Federal Service for Environmental, Technological and Nuclear Supervision of accidents and maintain these systems in good working order.

In certain cases, companies operating industrial sites must also prepare declarations of industrial safety which summarise the risks associated with operating a particular industrial site and measures the company has taken and will take to mitigate such risks and use the site in accordance with applicable industrial safety requirements. Such declaration must be adopted by the chief executive officer of the company, who is personally responsible for the completeness and accuracy of the data contained therein. The industrial safety declaration, as well as a state industrial safety review, are required for the issuance of a licence permitting the operation of a dangerous industrial facility.

The Federal Service for Environmental, Technological and Nuclear Supervision has broad authority in the field of industrial safety. In case of an accident, a special commission led by a representative of the Federal Service for Environmental, Technological and Nuclear Supervision conducts a technical investigation of the cause. The company operating the hazardous industrial facility where the accident took place bears all costs of an investigation. The officials of the Federal Service for Environmental, Technological and Nuclear

Supervision have the right to access industrial sites and may inspect documents to ensure a company's compliance with safety rules. The Federal Service for Environmental, Technological and Nuclear Supervision may suspend or terminate operations or impose administrative liability.

Any company or individual violating industrial safety rules may incur administrative and/or civil liability, and individuals may also incur criminal liability. A company that violates safety rules in a way that negatively impacts the health of an individual may also be obligated to compensate the individual for lost earnings, as well as health-related damages.

**Investments in Russian Companies of Strategic Importance**

A new law "On the Order of Foreign Investments in the Companies of Strategic Importance for the Defence and Security of the State" No. 57-FZ (the "**Foreign Investment Law**") came into force in May 2008. The Foreign Investment Law establishes certain restrictions for foreign investments into Russian companies which are deemed strategically important for the defence and security of the Russian Federation (the "**Strategic Companies**"). The Foreign Investment Law provides for the list of activities that have strategic importance for the national defence and security. This list *inter alia* includes (a) exploration and production of subsoil of federal land plots and, generally, (b) activities of those companies that have a market share in a particular segment in excess of 35 percent. Under the Foreign Investment Law, an acquisition by a foreign investor of a direct or indirect control over a Strategic Company requires a permit of the competent state authority.

In the light of the novelty of this piece of legislation and in the absence of any reliable clarifications or guidance as to the scope of its effect, currently it is not possible to predict how the Foreign Investments law will be implemented in practice and to assess all potential consequences of its introduction.

**Competition and Mergers Control**

As at 26 October 2006 the new Federal Law on the Protection of Competition (the "**Competition Law**") became effective. A summary of the relevant provisions of the Competition Law is set out below, although investors should note that it is currently not entirely clear how such provisions will be applied in practice.

Under the Competition Law, an investor or several entities constituting "a group of entities and/or individuals" should obtain FAS clearance in the following cases in particular:

- for the initial acquisition of more than 25 percent of the voting shares in a joint stock company, or 33.3 percent of the participation interest in a limited liability company, provided that the acquirer did not have any shares (participation interest) in such company or had less than the above threshold before the acquisition;
- for the subsequent acquisition of the voting shares in a joint stock company or participation interests in a limited liability company such that the level of their holding of the company's shares (participation interest) passes the threshold of 50 percent or 75 percent of the voting shares in a joint stock company or 50 percent or 66.6 percent of the participation interests in a limited liability company;
- for the acquisition of production or intangible assets if the book value of such assets exceeds 20 percent of the production or intangible assets of the seller (transferor); or
- for the acquisition of rights to determine the conditions of the business of another entity.

A prior FAS clearance for an acquisition is required if (i) either the aggregate balance value of assets of the acquirer and the target and the companies of their respective groups exceeds RUR3 billion or the aggregate value of revenues of the same entities in the last calendar year exceeds RUR6 billion and, simultaneously, (ii) the aggregate value of assets of the target and the companies of its group exceeds RUR150 million or, alternatively, one of the entities mentioned above is entered in the Russian register of businesses with a market share exceeding 35 percent.

A post-completion notification on acquisition is required if (i) either the aggregate balance value of assets of the acquirer and the target and the companies of their respective groups exceeds RUR200 million or the aggregate value of revenues of the same entities in the last calendar year exceeds the same amount and, simultaneously, (ii) the aggregate value of assets of the target and the companies of its group exceeds RUR30 million or, alternatively, one of the entities mentioned above is entered in the Russian register of businesses with a market share exceeding 35 percent.

Intra-group transfers are no longer subject to prior approval by the FAS. However, intra-group transfers may be subject to post-completion notifications. For the purposes of a notification, one of the parties should file a "list of its group members" with the FAS not later than 1 month prior to completion. The list should specify the reasons for including each of the group members in the group.

The Competition Law expressly provides for its extraterritorial application to transactions which are made outside of Russia but lead, or may lead, to the restriction of competition in Russia and relate to assets located on the territory of Russia or to the shares (participation interests) in Russian companies or rights in relation to such companies.

As part of its competition-monitoring activities, the FAS keeps a register of companies that have more than a 35 percent share in a particular goods market. As a major Russian steel producer, the Company appears on the register in relation to certain types of steel products.

The FAS may rule that certain companies that appear on the register have a dominant position in the market. Such companies are subject to more rigorous governmental regulation including the imposition of price controls. The FAS ruled that the Company must maintain the price of the steel it sells to UAZ at a competitive level for a period of three years beginning from July 2001.

The Company, together with OAO MMK, was subject to a case brought by the FAS in connection with allegations of price fixing in the pipe industry. On 14 January 2004, the FAS (i) found the Company and OAO MMK guilty of violating anti-monopoly legislation by acting in concert in respect of the pricing of steel strips sold to pipe mills for the production of oil and gas pipes; and (ii) obliged both companies: (a) to stop such practices and to prevent any such violations in the future; and (b) for the next three years, to provide the FAS on a quarterly basis with detailed information on the pricing of such strips together with the economic rationale for any increase in prices of more than 5 percent. In March 2004, the Company filed an appeal against the decision of the FAS in the Moscow Arbitration Court, which ruled in favour of the Company and OAO MMK on 27 May 2004. This decision was confirmed further on 14 December 2004 by the Federal Arbitration Court of Moscow District, acting as a cassation court.

**Employment and Labour**

Labour matters in Russia are primarily governed by the Labour Code.

***Employment contracts.*** As a general rule, employment contracts for an indefinite term are concluded with all employees. Russian labour legislation expressly limits the possibility of entering into term employment contracts. However, an employment contract may be entered into for a fixed term of up to five years in certain cases where labour relations may not be established for an indefinite term due to the nature of the duties or the conditions of the performance of such duties as well as in other cases expressly identified by federal law.

An employer may terminate an employment contract only on the basis of the specific grounds enumerated in the Labour Code, including:

- liquidation of the enterprise or downsizing of staff;
- failure of the employee to comply with the position's requirements due to incompetence;
- systematic failure of the employee to fulfil his or her duties without a fair excuse;
- any single gross violation by the employee of his or her duties; and
- provision by the employee of false documents or misleading information prior to entry into the employment contract.

An employee dismissed from an enterprise due to downsizing or liquidation is entitled to receive compensation including a severance payment and, depending on the circumstances, salary payments for a certain period of time.

The Labour Code also provides protections for specified categories of employees. For example, except in cases of liquidation of an enterprise, an employer cannot dismiss minors, expectant mothers, mothers with a child under the age of three, single mothers with a child under the age of 14 or disabled child under the age of 18 or other persons caring for a child under the age of 14 or disabled child under the age of 18 without a mother.

Any termination by an employer that is inconsistent with the Labour Code requirements may be invalidated by a court, and the employee may be reinstated. Lawsuits resulting in the reinstatement of illegally dismissed employees and the payment of damages for wrongful dismissal are increasingly frequent, and Russian courts tend to support employees' rights in most cases. Where an employee is reinstated by a court, the employer must compensate the employee for unpaid salary for the period between the wrongful termination and reinstatement, as well as for mental distress.

***Work time.*** The Labour Code generally sets the regular working week at 40 hours. Any time worked beyond 40 hours per week, as well as work on public holidays and weekends, must be compensated at a higher rate. Annual paid vacation leave under the law is generally 28 calendar days. Employees who perform underground and open-pit mining works or other work in harmful conditions may be entitled to additional paid vacation ranging from six to 36 working days.

The retirement age in the Russian Federation is 60 years for males and 55 years for females. However, the retirement age for male miners who have worked in underground mines for at least 10 years, and females who have worked in underground mines for at least seven years and six months, is 50 years and 45 years, respectively. Persons who have worked as miners in open-pit mines and/or underground mines for at least 25 years may also retire, regardless of age.

***Salary.*** The minimum salary in Russia, as established by federal law, is calculated on a monthly basis and is RUR2,300 from 1 September 2007. Although the law requires that the minimum wage be at or above a minimum subsistence level, the current minimum wage is generally considered to be less than a minimum subsistence level.

***Strikes.*** The Labour Code defines a strike as the temporary and voluntary refusal of workers to fulfil their work duties with the intention of settling a collective labour dispute. Russian legislation contains several requirements for legal strikes. Participation in a legal strike may not be considered by an employer as grounds for terminating an employment contract, although employers are generally not required to pay wages to striking employees for the duration of the strike. Participation in an illegal strike may be adequate grounds for termination.

***Trade Unions.*** Although recent Russian labour regulations have curtailed the authority of trade unions, they still retain significant influence over employees and, as such, may affect the operations of large industrial companies in Russia. In this regard, the Group's management routinely interacts with trade unions in particular the Mining and Metallurgical Trade Union, in order to ensure the appropriate treatment of employees and the stability of its business. See "Business — Employees — Russian Steel Division."

The activities of trade unions are generally governed by the Federal Law on Trade Unions, Their Rights and Guaranties of Their Activity of 12 January 1996, as amended, (the "**Trade Union Law**"). Other applicable legal acts include the Labour Code of Russia, which provide for more detailed regulations relating to activities of trade unions.

The Trade Union Law defines a trade union as a voluntary union of individuals with common professional and other interests that is incorporated for the purposes of representing and protecting the rights and interests of its members. National trade union associations, which coordinate activities of trade unions throughout Russia, are also permitted.

As part of their activities, trade unions may:

- negotiate collective contracts and agreements such as those between the trade unions and employers, federal, regional and local governmental authorities and other entities;
- monitor compliance with labour laws, collective contracts and other agreements;
- access work sites and offices, and request information relating to labour issues from the management of companies and state and municipal authorities;

- represent their members and other employees in individual and collective labour disputes with management;
- participate in strikes; and
- monitor redundancy of employees and seek action by municipal authorities to delay or suspend mass layoffs.

Russian laws require that companies co-operate with trade unions and do not interfere with their activities. Trade unions and their officers enjoy certain guarantees as well, such as:

- legal restrictions as to rendering redundant employees elected or appointed to the management of trade unions;
- protection from disciplinary punishment or dismissal on the initiative of the employer without prior consent of the management of the trade union and, in certain circumstances, the consent of the relevant trade union association;
- retention of job positions for those employees who stop working due to their election to the management of trade unions;
- protection from dismissal for employees who previously served in the management of a trade union for two years after the termination of the office term; and
- provision of the necessary equipment, premises and transportation vehicles by the employer for use by the trade union free of charge, if provided for by a collective bargaining contract or other agreement.

If a trade union discovers any violation of work condition requirements, notification is sent to the employer with a request to cure the violation and to suspend work if there is an immediate threat to the lives or health of employees. The trade union may also apply to state authorities and labour inspectors and prosecutors to ensure that an employer does not violate Russian labour laws. Trade unions may also initiate collective labour disputes, which may lead to strikes.

To initiate a collective labour dispute, trade unions present their demands to the employer. The employer is then obliged to consider the demands and notify the trade union of its decision. If the dispute remains unresolved, a reconciliation commission attempts to end the dispute. If this proves unsuccessful, collective labour disputes are generally referred to mediation or labour arbitration.

The Trade Union Law provides that those who violate the rights and guaranties provided to trade unions and their officers may be subject to disciplinary, administrative and criminal liability. Although neither the Code of Administrative Delinquencies of Russia of 30 December 2001, nor the Criminal Code of the Russian Federation of 13 June 1996, currently has provisions specifically relating to these violations, general provisions and sanctions may be applicable.

**Trade Barriers and Anti-Dumping Regulations**

Steel-producing countries generally view their steel industries as strategically important and therefore requiring protection from foreign competition. In addition, the governments of some emerging economies employ non-market methods to try to protect and develop their steel industries, and, while those governments seek to achieve the desired balance in their economies between production levels and product mix and consumption, they may resort to protectionist measures against imports from third countries.

Exports of steel from Russia are primarily regulated by the Federal Law "On Fundamentals of State Regulation of Foreign Trade Activities" No. 164-FZ dated 8 December 2003 and bilateral agreements between Russia and its trading partners, including the United States, the EU and China, which establish minimum prices and/or quotas for the export from Russia to those markets of certain types of steel products. Russian exporters of steel products to the United States and the EU are required, in accordance with the bilateral agreements between Russia and the United States and the EU, respectively, to obtain a licence for those exports from the Russian Ministry of Economic Development and Trade.

***General.*** In general, the recent trend worldwide has been for the relaxation of import restrictions. The largest importers of the Company's products are countries in the EU and North America. Restrictive measures on imported steel introduced by certain Latin American countries have not affected the Company's business adversely, as the Company's exports have, for geographical reasons, been principally directed at markets in the EU and North America.

The Group believes that, due to Russia being granted "market economy" status by the EU and various countries, including the United States, South Africa and Brazil, it has become relatively easier for Russian steel producers to defend their interests in the course of anti-dumping and other trade proceedings, and the Group expects this trend to continue if Russia accedes to the WTO in the near future.

***United States.*** On 6 March 2002, the United States introduced safeguard measures in respect of steel imports, which resulted in the imposition of additional import duties (ranging from 8 percent to 30 percent) on steel products imported into the United States and restricted the import into the United States of most high value-added products, including those imported from Russia. These US measures resulted in a "domino" effect of similar safeguard measures in other regions, including the EU, Czech Republic, Brazil, Canada, Mexico, Venezuela, Chile, Colombia, Argentina, Thailand, India, Iran and China, each of which introduced measures to protect their own markets from "excessive" steel unable to enter the US market and led to a substantial decrease in sales to the United States by Russian steel producers during 2002 and 2003. On 5 December 2003, the United States revoked its 2002 safeguard measures.

As a result, Russian steel producers, including Russian Steel are currently able to operate in this market in accordance with the following two agreements, which limit Russian exports of metal products:

- A suspension agreement on hot-rolled cut-to-length steel plate, which establishes minimum prices without quotas based on information about the costs and expenses of Russian exporters. Russian exporters concluded this market economy cost-based agreement with the US Department of Commerce on 20 December 2002, replacing the non-market economy agreement that had been in force since 1997. Russian Steel and Metalware is the only exporter from Russia who is able to satisfy US Department of Commerce requirements and who sells hot-rolled cut-to-length steel plate into the US market;
- A suspension agreement on hot-rolled flat carbon-steel products, which established minimum prices and quotas. The quota for 2006 was 814,610 tonnes (of which the Company was allocated 330,997 tonnes). The quota for 2005 was 792,055 tonnes (of which the Company was allocated 330,171 tonnes). While these quotas have generally been enough to satisfy Russian producers' needs, the Company is restricted on sales of hot- rolled coils and thin sheets in the US market;
- In relation to steel products such as cold-rolled, galvanised and semi-finished steel and long products, Russian exporters have been operating in the US market without any restrictions on the import of these products since the expiry of the Comprehensive Steel Agreement on 11 July 2004; and
- Russia was granted "market economy" status by the United States with effect from 1 April 2002.

***EU.*** On 26 October 2007, the Russian Federation and the EU entered into an agreement regulating trade in certain steel products. This agreement established a quota for the export of Russian metals into the EU and superseded the previous quota system for the export of Russian metals, which had been in place since 1 December 1997 in the form of a bilateral agreement. This agreement and these quotas are referred to in a regulation issued by the European Council on 22 October 2007 on import of certain steel products from the Russian Federation.

*Quotas for Export of Russian Steel into the EU, 2007 and 2008*

| Products | Year ended 2008 (tonnes) | Year ended 2007 (tonnes) | Year ended 2006 (tonnes) |
|---|---|---|---|
| **SA. Flat products** | | | |
| SA1. Coils | 1,035,000 | 1,042,090 | 930,975 |
| SA2. Heavy plate | 275,000 | 270,820 | 195,358 |
| SA3. Other flat products | 595,000 | 565,770 | 399,485 |
| SA4. Alloyed products | 105,000 | 94,860 | 99,507 |
| SA 5. Alloyed quarto plates | 25,000 | 20,460 | 22,047 |
| SA 6. Alloyed cold-rolled and coated sheets | 110,000 | 105,000 | 102,597 |
| **SB. Long products** | | | |
| SB1. Beams | 55,000 | 55,800 | 46,072 |
| SB2. Wire rod | 324,000 | 275,000 | 176,993 |
| SB3. Other long products | 507,000 | 474,200 | 299,685 |
| **Total** | **3,031,000** | **2,904,000** | **2,272,719** |

On 31 October 2003, the EU terminated its anti-dumping investigation against imports of hollow sections originating from Russia and Turkey, without the imposition of any trade restrictions.

Russia was granted "market economy" status by the EU in November 2002.

**Anti-Dumping Proceedings**

The most significant anti-dumping proceedings against Russian steel exporters were initiated between 1996 and 2001 by the United States in respect of a wide range of hot-rolled and cold-rolled steel products. The Company actively participated, along with other Russian steel producers, in all those proceedings. In general, the granting of "market economy" status to Russia by the United States in April 2002 has led to a reduction in the anti-dumping measures imposed in the US market, benefiting, in particular, the ferrous metal industries. For example, the United States terminated the anti-dumping proceedings against imports of cold-rolled steel products, which it initiated on 21 June 1999 and 18 October 2001, and, since April 2002, the Company has incurred lower rates of duty in anti-dumping proceedings compared to rates from previous periods, for example, the 184 percent anti-dumping duty for Russian hot-rolled steel that the United States imposed in 1999. During 2004 and 2005, the Company participated in the sunset review of anti-dumping duty measures against Russian hot-rolled steel in the United States. Following this review, the United States decided on 14 April 2005 to retain these measures.

In 2004 and 2005, the following key decisions were made regarding Russian steel exporters by foreign government authorities:

- Expiration of the US-Russia Comprehensive Steel Agreement, which established quotas on various types of steel products such as cold-rolled, galvanised and semi-finished steel and long products, on 14 July 2004. Since that time, the Russian Steel Division and other Russian exporters have operated in the US market without any restrictions on these products.
- Termination of anti-dumping measures against hot-rolled and cold-rolled products in Canada.
- Termination of anti-dumping measures against electrical steel products in China.
- Suspension of anti-dumping measures against cold-rolled steel products in China.
- Termination of anti-dumping measures against cold-rolled steel products in South Africa, hot-rolled products in Indonesia and cold-rolled and long steel products in Colombia.
- Opening of US cut-to-length market through the establishment of minimum prices by the US Department of Commerce, as the result of co-operation between the Department and the Company.
- Possibility of the export of new grades of hot-rolled products within the framework of the US-Russia Suspension Agreement on hot-rolled flat carbon-steel products.

Currently, there are relatively few trade restrictions in force against exports from the Russian Federation in countries such as Venezuela, Colombia, Mexico, Argentina, Peru, Thailand and South Africa. These restrictions did not have and are not expected to have a material effect on the Company's business.

Meanwhile, a number of anti-dumping duty measures against Russian steel products expired after being in force for five years, including measures relating to grain-oriented electrical steel in China and cold-rolled steel in Colombia.

The Company, along with other Russian steel producers, continues to participate in those proceedings and reviews that it regards as important to its business. The Company intends to continue to participate actively in all inter- governmental consultations relating to Russian steel exports to the United States, the EU and other international markets.

## Regulation of the Steel and Mining Industries in the United States and Europe

### Overview

Steel and mining operations and activities in the United States and Europe are extensively regulated at both the federal and state level in the United States and at the national and local level in Europe. Federal, national, regional, state and local authorities in the United States and the EU regulate a variety of matters, including employee health and safety; royalties; permitting and licensing requirements; environmental impact assessment, planning and development; and environmental compliance (including, for example, compliance with the regulatory regimes governing waste and waste water treatment and disposal; waste transportation; emissions and discharges; protection of species and habitats; decommissioning, reclamation and restoration of properties used for mining or other activities; surface subsidence from underground mining and the effects that mining and other activities have on surface and/or groundwater quality and availability).

Activities and operations involved in the mining and steel production industries generate hazardous and non-hazardous wastes, effluent and emissions, require waste transportation and treatment, and have other environmental impacts which require various environment-related permits and approvals to be held or received. Licences may also be required for the abstraction of the relevant natural resources. Such permits and licences are subject, in certain situations or on the occurrence of certain events, to modification or addition of conditions (including monitoring, upgrading, improvement, decommissioning and aftercare requirements), or revocation by issuing authorities. The carrying out of such activities and operations is also subject to various restrictions and other requirements under environmental, health and safety laws. Violations of health and safety laws relating to a mine or a steel factory, or a failure to comply with the instructions of relevant health and safety authorities, man result in the temporary or permanent shutdown of steel or mining operations in the United States or Europe, as well as the imposition of fines, or penalties corrective procedures.

Steel and mining businesses in the United States and Europe are also required in many cases to prepare and present to national, federal, regional, state and/or local authorities information pertaining to the anticipated effect or impact that proposed exploration, mining or production activities may have upon the environment. The preparation and presentation of this information in many cases requires a substantial commitment of personnel and financial resources. In response to such presentations, the national, federal, regional, state and/or local authorities are empowered to determine that mining operations must suspended or decommissioned.

### Climate Change

In December 1997, in Kyoto, Japan, the signatories to the United Nations Convention on Climate Change established individual, legally binding targets to limit or reduce greenhouse gas emissions by developed nations in the period 2008-2012. This international treaty, known as the Kyoto Protocol, came into force in the Russian Federation on 16 February 2005. The Kyoto Protocol enables the emissions reductions to be achieved by a variety of means including emissions trading and investment in overseas emissions reduction projects. Russia is anticipated to offer opportunities in relation to such projects. The 181 states and the EU have ratified, accepted, accessed or approved the Protocol. Discussions are ongoing as to a possible successor to the Kyoto Protocol, with the aim of signing a new agreement in December 2009. It is currently unclear what emission reduction targets will be adopted, but in light of recent scientific and economic reports on the impact of climate change, these may be more stringent than those adopted in the Kyoto Protocol.

In a separate development, in July 2005 Australia, China, India, Japan, South Korea and the United States formed the Asia-Pacific Partnership on Clean Development and Climate. Members of the partnership intend to cooperate on the development and transfer of technology with a view to reducing greenhouse gas emissions.

Steel and mining operations in Europe and the United States are subject to laws, regulations and policies aimed at limiting or reducing greenhouse gas emissions. For example, in the EU, an increasingly stringent regulatory framework is being developed to achieve the EU's Kyoto Protocol commitments and to meet its own emissions reductions targets which affect, among other activities, coke ovens and steel plants. In the United States, California's recent legislative initiatives may indicate a trend towards a similarly stringent regulatory system. In addition, government entities and other organisations in Europe and the United States are actively investing in research projects aimed at reducing greenhouse gas emissions. In the past, such legislative and research initiatives have involved additional market regulatory measures such as emissions trading, switching to cleaner forms of energy and/or introducing emissions-curbing technologies.

## DESCRIPTION OF THE COMPANY

The Company's charter states in clause 4.1 that the main aim of the company is earning profits and using profits in the interest of the company.

The Company is an open joint stock company incorporated under the laws of the Russian Federation and domiciled in Cherepovets, Russia. The Company's registration number is 1023501236901 and its registered address is 30 Mira Street, Cherepovets, Vologodskaya oblast, 162600, Russian Federation. The telephone number of the Company's Moscow office is +7 495 540 7766.

# THE ISSUER

## General

The Issuer is a public limited liability company (*société anonyme*) of unlimited duration that is incorporated, exists and operates under the laws of Luxembourg, in compliance with the Companies' Act 1915, other applicable regulations and its Articles of Incorporation. The Issuer was incorporated on 11 May 2006 and is registered with the Luxembourg Trade and Companies' Register (*Registre de Commerce et des Sociétés*) under registration number B 116.975. The registered office of the Issuer is 2, Boulevard Konrad Adenauer, L-1115 Luxembourg, Grand Duchy of Luxembourg. The telephone number of the registered office of the Issuer is +35 242 122 462 and its fax number is +35 242 122 718. The Articles of Incorporation of the Issuer have been published in the *Mémorial, Journal Officiel du Grand Duché de Luxembourg, Recueil des Sociétés et Associations C-N° 1522* on 9 August 2006.

The Issuer is a special purpose vehicle and is operated for the purpose of issuing asset backed securities.

The Issuer has entered into an administrative services and domiciliation agreement on 12 May 2006 with Deutsche Bank Luxembourg SA, whereby Deutsche Bank Luxembourg SA provides in Luxembourg certain domiciliary, management, administrative, accounting and related services in relation to the Issuer's business.

The Issuer's share capital, as of the date of this Prospectus, is €31,000 divided into 310 registered shares with a par value €100, each of which is fully paid.

## Shareholders

Stichting Steel Capital Luxembourg, a Dutch company owns 309 shares in the Issuer and Stichting Participatie DITC Amsterdam, a Dutch company, owns 1 share.

Stichting Steel Capital Luxembourg is an organisation incorporated in the Netherlands having its registered office at Herengracht 450, 1017 CA Amsterdam. It is registered with the *handelsregister van de Kamers van Koophandel* of Amsterdam under number 34247473. The objectives of Stichting Steel Capital Luxembourg are, among others, to incorporate, manage and control shares in the share capital of the Issuer and to exercise all rights attached to such shares.

Stichting Participatie DITC Amsterdam is an organisation incorporated in the Netherlands, having its registered office at Herengracht 450, 1017 CA Amsterdam. It is registered with the *handelsregister van de Kamers van Koophandel* of Amsterdam under number 34148998. The objectives of Stichting Participatie DITC Amsterdam are, among others, to acquire and hold shares and to exercise all rights attached to such shares.

## Statutes

Article 4 of the Articles of Incorporation provides that the principal objects of the Issuer are the issue of loan participation notes for the purpose of financing loans to OAO Severstal and to its affiliates, the granting of security interests over its assets in relation to the issuance of the loan participation notes and the making of deposits at banks or with other depositaries.

The Issuer may further carry out any transaction, whether commercial or financial, which are directly or indirectly connected with its corporate object at the exclusion of any banking activity. In general, the Issuer may carry out any operation which it may deem useful or necessary to the accomplishment and the development of its corporate purpose.

## Management

The Issuer is managed by its board of directors (the "**Issuer's Board of Directors**"), who are appointed by the shareholders. The current directors of the Issuer are as follows:

| Name | Business Address |
|---|---|
| Mme. Anja Lakoudi | 2, Boulevard Konrad Adenauer L-1115 Luxembourg |
| Mme. Heike Kubica | 2, Boulevard Konrad Adenauer L-1115 Luxembourg |
| Mr. Rolf Caspers | 2, Boulevard Konrad Adenauer L-1115 Luxembourg |

The Issuer's directors do not perform any principal activities outside of the Issuer that are significant with respect to the Issuer.

There are no current or potential conflicts between the private interests and duties of the members of the Issuer's Board of Directors and the duties of those officers to the Issuer.

### Auditors

The Issuer's Statutory Auditor is Fiduciaire Patrick Sganzerla, 17 rue des jardiniers, L-1835 Luxembourg.

The Issuer has appointed ZAO KPMG to act as its external auditors. ZAO KPMG are professional auditors. ZAO KPMG are located at 18 Krasnopresnenskaya Naberezhnaya, Block C, Moscow, Russian Federation, as stated in their report appearing herein. ZAO KPMG are a member firm of the Audit Chamber of Russia (AchR) and the Institute of Professional Accountants of Russia (IPAR).

ZAO KPMG has no interest in the Issuer.

ZAO KPMG has audited the Issuer Financial Statements for the year ended 31 December 2007 and the eight months period ended 31 December 2006, which were prepared in accordance with International Financial Reporting Standards. ZAO KPMG's report appears elsewhere in this Prospectus.

### Financial Year

The Issuer's financial year begins on 1 January and ends on 31 December. The Issuer prepares and publishes annual audited non-consolidated financial statements.

### Other

The Issuer has published its financial statements in respect of its first financial years 2006 and 2007. A copy of the Issuer Financial Statements is set forth in on pages F-77 - F-89.

There has been no material adverse change in the financial position or prospects of the Issuer since 31 December 2007, the date of its last published audited financial statements.

The Issuer is not aware of any governmental, legal, or arbitration proceedings (including any such proceedings which are pending or threatened of which the Issuer is aware), during the last 12 months, which may have, or have in the recent past, significant effects on the Issuer's financial position or profitability.

## THE LOAN AGREEMENT

*The following is the text of the Loan Agreement to be entered into between the Issuer and the Company:*

**This Loan Agreement** is made on 25 July 2008 **between:**

**(1)** **OAO SEVERSTAL**, an open joint stock company established under the laws of the Russian Federation whose registered office is Ul. Mira 30, 162600 Cherepovets, Vologda Region, Russian Federation ("**Severstal**"); and

**(2)** **STEEL CAPITAL S.A.**, a *société anonyme* incorporated in Luxembourg with limited liability whose registered office is at 2, Boulevard Konrad Adenauer, L-1115 Luxembourg, registered with the Register of Commerce and Companies of Luxembourg under number B116975 (the "**Lender**", which expression, where the context so admits, includes any successor Lender pursuant to the terms of this Agreement and the Lender acting in its capacity as issuer of the agreed funding).

**Whereas**, the Lender has at the request of Severstal agreed to make available to Severstal a loan facility in the amount of U.S.$1,250,000,000 on the terms and subject to the conditions of this Agreement.

**Now it is hereby agreed** as follows:

### 1 Definitions and Interpretation

### 1.1 Definitions

In this Agreement (including the recitals), the following terms shall have the meanings indicated.

"**Account**" means the account in the name of the Lender with Citibank, N.A., London Branch, account number 11776797 (or such other account as may from time to time be agreed by the Lender with the agreed funding source pursuant to the agreed funding agreements and notified to Severstal in writing at least 5 Business Days in advance of such change);

"**Accounting Standards**" means IFRS, U.S. GAAP or any other internationally recognised set of accounting standards deemed equivalent to IFRS by the relevant regulators for the time being;

"**Advance**" means the advance to be made by the Lender under Clause 3 of the sum equal to the amount of the Facility, as from time to time reduced by prepayment;

"**Affiliate**" of any specified Person means (i) any other Person, directly or indirectly, controlling or controlled by or under direct or indirect common control with such specified Person or (ii) any other Person who is a director or officer (a) of such specified Person, (b) of any Subsidiary of such specified Person or (c) of any Person described in (i) above. For the purpose of this definition, "**control**" when used with respect to any Person means the power to direct the management and policies of such Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise; and the terms "**controlling**" and "**controlled**" have meanings correlative to the foregoing;

"**Agency**" means any agency, authority, central bank, department, government, legislature, minister, official or public statutory Person (whether autonomous or not) of, or of the government of, any state or supra-national body;

"**agreed funding**" shall mean the Indebtedness (including in the form of securities), Incurred to the agreed funding source;

"**agreed funding agreements**" shall mean any debt instrument or facility or guarantee thereof, trust deed, agency agreement or underwriting agreement entered into in connection with the agreed funding and any side or fee letters ancillary thereto;

"**agreed funding source**" shall mean any Person to whom the Lender owes any Indebtedness (including securities), which Indebtedness was Incurred to fund the Loan (including a designated representative or trustee of such Person or any assignee or transferee appointed in connection with the agreed funding source);

"**Agreement**" means this Agreement as originally executed or as it may be amended from time to time;

"**Asset Disposition**" means any sale, lease, transfer or other disposition (or series of related sales, leases, transfers or dispositions) by Severstal or any Subsidiary of Severstal, including any disposition by means of a merger, consolidation or similar transaction (each referred to for the purposes of this definition as a "**disposition**"), of:

(a) any shares of Capital Stock of a Subsidiary of Severstal (other than directors' qualifying shares or shares required by applicable law to be held by a Person other than Severstal or a Subsidiary of Severstal);

(b) all or substantially all the assets of any division or line of business of Severstal or any Subsidiary of Severstal; or

(c) any other assets of Severstal or any Subsidiary of Severstal outside of the ordinary course of business of Severstal or such Subsidiary,

other than, in the case of clauses (a), (b) and (c) above,

(i) a disposition by a Subsidiary of Severstal to Severstal or by Severstal or a Subsidiary of Severstal to a Subsidiary of Severstal;

(ii) a disposition of assets in a single transaction or a series of related transactions with a Fair Market Value of less than U.S.$20,000,000;

(iii) a disposition of cash or Temporary Cash Investments;

(iv) the creation of a Lien (but not the sale or other disposition of the property subject to such Lien);

(v) the licensing or sublicensing of rights to intellectual property or other intangibles in the ordinary course of business;

(vi) any disposition constituting or resulting from the enforcement of a Lien Incurred in compliance with Clause 10.1;

(vii) the sale, lease or other disposition of obsolete, worn out, negligible, surplus or outdated equipment or machinery or raw materials or inventory in the ordinary course of a Related Business;

(viii) the lease, assignment or sublease of any real or personal property in the ordinary course of business;

(ix) sales or other dispositions of assets or property received by Severstal or any Subsidiary of Severstal upon the foreclosure on a Lien granted in favour of Severstal or any Subsidiary of Severstal or any other transfer of title with respect to any ordinary course secured investment in default;

(x) the surrender or waiver of contract rights or the settlement, release, or surrender of contract, tort or other claims, in the ordinary course of the business; and

(xi) any disposition of Capital Stock, Indebtedness or other securities of a Subsidiary of Severstal;

"**Auditors**" means the auditors of Severstal's consolidated financial statements (prepared in accordance with applicable Accounting Standards) for the time being or, if they are unable or unwilling to carry out any action requested of them under this Agreement, such other internationally recognised firm of accountants as may be approved in writing by the Lender for this purpose;

"**Average Life**" means, as of the date of determination, with respect to any Indebtedness, the quotient obtained by dividing (1) the sum of the products of the numbers of years from the date of determination to the dates of each successive scheduled principal payment of such Indebtedness multiplied by the amount of such payment by (2) the sum of all such payments;

"**Business Day**" means a day on which (a) the London Interbank Market is open for dealings between banks generally, and (b) if on that day a payment is to be made hereunder, commercial banks generally are open for business in Luxembourg, New York City and Moscow;

"**Capital Lease Obligation**" means an obligation that is required to be classified and accounted for as a capital lease for financial reporting purposes in accordance with Accounting Standards, and the amount of Indebtedness represented by such obligation shall be the capitalised amount of such obligation determined in accordance with Accounting Standards; and the Stated Maturity thereof shall be the date of the last payment of rent or any other amount due under such lease prior to the first date upon which such lease may be terminated by the lessee without payment of a penalty;

"**Capital Stock**" means, with respect to any Person, any and all shares, interests, participations, rights to purchase, warrants, options, or other equivalents (however designated) of capital stock of a corporation and any and all equivalent ownership interests in a Person other than a corporation, in each case whether now outstanding or hereafter issued;

"**Central Bank**" means the Central Bank of the Russian Federation;

"**Closing Date**" means 29 July 2008 (or such later date not later than 12 August 2008 as may be agreed between the Lender and Severstal);

"**Consolidated Indebtedness**" means, as at the last day of the calendar quarter immediately preceding any date of determination (and without duplication), all Indebtedness of the Group outstanding on such former date, as would be shown on a consolidated balance sheet of the Group as at such date prepared in accordance with Accounting Standards to which the then most recent published audited consolidated financial statements of Severstal comply, as consistently applied;

"**Consolidated Interest Expense**" means, for any period, the total interest expense of Severstal and its Subsidiaries determined in accordance with applicable Accounting Standards as in effect from time to time, plus, to the extent not included in such total interest expense, and to the extent incurred by Severstal or its Subsidiaries, without duplication:

(a) interest expense attributable to Capital Lease Obligations other than interest expense attributable to a Capital Lease Obligation between or among Severstal and any Subsidiary of Severstal or between or among Subsidiaries of Severstal;

(b) amortisation of debt discount and debt issuance costs;

(c) capitalised interest;

(d) non cash interest expense;

(e) commissions, discounts and other fees and charges owed with respect to letters of credit and bankers' acceptance financing;

(f) net payments pursuant to Hedging Obligations to the extent such payments are characterised as interest expense under Accounting Standards; and

(g) dividends accrued in respect of all Disqualified Stock of Severstal and all Preferred Stock of any Subsidiary of Severstal, in each case, held by Persons other than Severstal or a Wholly Owned Subsidiary (other than dividends payable solely in Capital Stock (other than Disqualified Stock) of Severstal); provided, however, that such dividends will be multiplied by a fraction of the numerator of which is one and the denominator of which is one minus the effective combined tax rate of the issuer of such Preferred Stock (expressed as a decimal) for such period (as estimated by the chief financial officer of Severstal in good faith);

"**Consolidated Leverage Ratio**" as of any date of determination, means the ratio of (x) the aggregate amount of Consolidated Indebtedness outstanding on such date to (y) the aggregate amount of EBITDA for the period of the two most recent consecutive semi-annual periods ending prior to the date of such determination for which financial statements have been delivered under Clause 10.9, as determined in good faith by a responsible financial or accounting officer of Severstal; provided, however, that:

(a) if Severstal or any Subsidiary of Severstal has Incurred any Indebtedness since the beginning of such period that remains outstanding or if the Incurrence of Indebtedness giving rise to the need to calculate the Consolidated Leverage Ratio is an Incurrence of

Indebtedness, or both, Consolidated Indebtedness for such period shall be calculated after giving effect on a pro forma basis to such Indebtedness as if such Indebtedness had been Incurred on the first day of such period;

(b) if Severstal or any Subsidiary of Severstal has repaid, repurchased, defeased or otherwise discharged any Indebtedness since the beginning of such period or if any Indebtedness is to be repaid, repurchased, defeased or otherwise discharged (in each case other than Indebtedness Incurred under any revolving credit facility unless such Indebtedness has been permanently repaid and has not been replaced) on the date of the transaction giving rise to the need to calculate the Consolidated Leverage Ratio, the Consolidated Leverage Ratio shall be calculated on a pro forma basis as if such discharge had occurred on the first day of such period and as if Severstal or such Subsidiary had not earned the interest income actually earned during such period in respect of cash or Temporary Cash Investments used to repay, repurchase, defease or otherwise discharge such Indebtedness;

(c) if since the beginning of such period Severstal or any Subsidiary of Severstal shall have made any Asset Disposition, EBITDA for such period shall be reduced by an amount equal to EBITDA (if positive) directly attributable to the assets which are the subject of such Asset Disposition for such period, or increased by an amount equal to EBITDA (if negative), directly attributable thereto for such period;

(d) if since the beginning of such period Severstal or any Subsidiary of Severstal (by merger or otherwise) shall have made an Investment in any Subsidiary of Severstal (or any Person which becomes such a Subsidiary) or an acquisition of assets, including any acquisition of assets occurring in connection with a transaction requiring a calculation to be made hereunder, which constitutes all or substantially all of an operating unit of a business, EBITDA for such period shall be calculated after giving pro forma effect thereto (including the Incurrence of any Indebtedness) as if such Investment or acquisition had occurred on the first day of such period; and

(e) if since the beginning of such period any Person that subsequently became a Subsidiary of Severstal or was merged with or into Severstal or any Subsidiary of Severstal since the beginning of such period) shall have made any Asset Disposition, any Investment or acquisition of assets that would have required an adjustment pursuant to clause (c) or (d) above if made by Severstal or a Subsidiary of Severstal during such period, the Consolidated Leverage Ratio shall be calculated after giving pro forma effect thereto as if such Asset Disposition, Investment or acquisition had occurred on the first day of such period.

For purposes of this definition, whenever pro forma effect is to be given to an acquisition of assets and the amount of income or earnings relating thereto, the pro forma calculations shall be determined in good faith by a responsible financial or accounting officer of Severstal;

"**Consolidated Net Income**" means, for any period, the net income (loss) of Severstal and its consolidated Subsidiaries determined in accordance with the then applicable Accounting Standards ("net income"); provided, however, that there shall not be included in such Consolidated Net Income:

(a) any net income of any Person (other than Severstal) if such Person is not a Subsidiary of Severstal, except that:

  (i) subject to clause (d) below, Severstal's equity in the net income of any such Person for such period shall be included in such Consolidated Net Income up to the aggregate amount of cash actually distributed by such Person during such period to Severstal or a Subsidiary of Severstal as a dividend or other distribution (subject, in the case of a dividend or other distribution paid to a Subsidiary of Severstal, to the limitations contained in clause (c) below); and

  (ii) Severstal's equity in a net loss of any such Person for such period shall be included in determining such Consolidated Net Income, but only to the extent such loss has been funded with cash by Severstal or a Subsidiary of Severstal;

(b) any net income (or loss) of any Person acquired by Severstal or a Subsidiary of Severstal in a pooling of interests transaction (or any transaction accounted for in a manner similar to a pooling of interests) for any period prior to the date of such acquisition;

(c) any net income of any Subsidiary of Severstal if such net income is subject to restrictions, directly or indirectly, on the payment of dividends or the making of distributions by such Subsidiary (other than any Permitted Restriction), directly or indirectly, to Severstal, except that:

 (i) subject to clause (d) below, Severstal's equity in the net income of any such Subsidiary for such period shall be included in such Consolidated Net Income up to the aggregate amount of cash actually distributed by such Subsidiary during such period to Severstal or another Subsidiary as a dividend or other distribution (subject, in the case of a dividend or other distribution paid to another Subsidiary, to the limitation contained in this clause); and

 (ii) Severstal's equity in a net loss of any such Subsidiary for such period shall be included in determining such Consolidated Net Income;

(d) any net after tax gain (or loss) realised upon the sale or other disposition of any assets of Severstal, its Subsidiaries or any other Person, or any other net after tax gains or losses classified as extraordinary (including pursuant to any sale-and-leaseback arrangement) which are not sold or otherwise disposed of in the ordinary course of business and any gain (or loss) realised upon the sale or other disposition of any Capital Stock of any Person; and

(e) the cumulative effect of a change in accounting principles after the Closing Date,

in each case, for such period;

"**Currency Agreement**" means any foreign exchange contract, currency swap agreement or other similar agreement with respect to currency values.

"**Default**" means any event which is, or after notice or passage of time or after making any determination under this Agreement (or any combination of the foregoing) would be, an Event of Default;

"**Disqualified Stock**" means, with respect to any Person, any Capital Stock which by its terms (or by the terms of any security into which it is convertible or for which it is exchangeable at the option of the holder) or upon the happening of any event:

(a) matures or is mandatorily redeemable (other than redeemable only for Capital Stock of such Person which is not itself Disqualified Stock) pursuant to a sinking fund obligation or otherwise;

(b) is convertible or exchangeable at the option of the holder for Indebtedness or Disqualified Stock; or

(c) is mandatorily redeemable or must be purchased upon the occurrence of certain events or otherwise, in whole or in part,

in each case on or prior to the date which is six months after the Stated Maturity of the agreed funding; provided, however, that any Capital Stock that would not constitute Disqualified Stock but for provisions thereof giving holders thereof the right to require such Person to purchase or redeem such Capital Stock upon the occurrence of an "asset sale" or "change of control" occurring prior to the date which is six months after the Stated Maturity of the agreed funding shall not constitute Disqualified Stock if:

 (i) the "asset sale" or "change of control" provisions applicable to such Capital Stock are not more favourable to the holders of such Capital Stock than the terms applicable to the Notes and described under Clauses 10.2 and 10.3; and

(ii) any such requirement only becomes operative after compliance with such terms applicable to the Notes, including the purchase of any Notes tendered pursuant thereto.

The amount of any Disqualified Stock that does not have a fixed redemption, repayment or repurchase price will be calculated in accordance with the terms of such Disqualified Stock as if such Disqualified Stock were redeemed, repaid or repurchased on any date on which the amount of such Disqualified Stock is to be determined; provided, however, that if such Disqualified Stock could not be required to be redeemed, repaid or repurchased at the time of such determination, the redemption, repayment or repurchase price will be the book value of such Disqualified Stock as reflected in the most recent financial statements of such Person;

"**Dollars**", "**U.S. dollars**", "**US$**" and "**U.S.$**" mean the lawful currency of the United States of America;

"**EBITDA**" for any period means the sum of Consolidated Net Income plus the following to the extent deducted in calculating such Consolidated Net Income:

(a) all income tax expense and all revenue-based imputed tax expense of Severstal and its Subsidiaries;

(b) Consolidated Interest Expense;

(c) depreciation and amortisation expense of Severstal and its Subsidiaries (excluding amortisation expense attributable to a prepaid item that was paid in cash in a prior period); and

(d) all other non-cash charges of Severstal and its Subsidiaries (excluding any such non-cash charge to the extent that it represents an accrual of or reserve for cash expenditures in any future period unless such change is subsequently reversed) less, to the extent increasing Consolidated Net Income, all non-cash items of income of Severstal and its Subsidiaries (other than accruals of revenue by Severstal and its Subsidiaries in the ordinary course of business and other non-cash items to the extent they will result in the receipt of cash payments in any future period);

"**Environmental Laws**" means all laws, rules, regulations, ordinances, judgments, orders, decrees and agreements with, and licences, permits or franchises from, governmental entities, and all other regulatory restrictions (whether or not having the force of law) in existence at the date of this Agreement that (i) have been, are or may become applicable to Severstal or any of its Material Subsidiaries or any properties or business now owned, leased, occupied or operated by Severstal or any of its Material Subsidiaries and (ii) relate to the environment, health and safety, the use, possession, collection, storage, processing, treatment, emission, release, discharge, disposal, transfer or transport of Materials of Environmental Concern, or similar matters, or the remedying of any of the foregoing;

"**Event of Default**" has the meaning assigned to such term in sub-Clause 11.1;

"**Facility**" means the U.S.$1,250,000,000 term loan facility granted by the Lender to Severstal as specified in Clause 2;

"**Fair Market Value**" means, with respect to any asset or property, the price which could be negotiated in an arm's length, free market transaction, for cash, between a willing seller and a willing and able buyer, neither of whom is under undue pressure or compulsion to complete the transaction. Fair Market Value will be determined in good faith by the chief financial officer of Severstal, whose determination will be conclusive;

"**Group**" means Severstal and its Subsidiaries taken as a whole;

"**Guarantee**" means any financial obligation, contingent or otherwise, of any Person directly or indirectly guaranteeing any Indebtedness or other obligation of any other Person and any obligation, direct or indirect, contingent or otherwise, of such Person (a) to purchase or pay (or advance or supply funds for the purchase or payment of) such Indebtedness or other obligation of such other Person (whether arising by virtue of partnership arrangements, or by agreement to keep-well, to purchase assets, goods, securities or services, to take-or-pay or to maintain financial statement conditions or otherwise) or (b) entered into for purposes of assuring in any other manner the obligee of such Indebtedness or other obligation of the payment thereof or to protect such obligee against loss in respect thereof (in whole or in part); provided, however, that the term "**Guarantee**" will not include endorsements for collection or deposit in the ordinary course of business. The term "**Guarantee**" used as a verb has a corresponding meaning;

"**Hedging Obligations**" of any Person means the obligations of such Person pursuant to any Interest Rate Agreement or Currency Agreement;

"**IFRS**" means International Financial Reporting Standards (formerly International Accounting Standards) issued by the International Accounting Standards Board ("**IASB**") and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB (as amended, supplemented or re-issued from time to time);

"**Incur**" means issue, assume, Guarantee, incur or otherwise become liable for; provided, however, that any Indebtedness or Capital Stock of a Person existing at the time such Person becomes a Subsidiary (whether by merger, consolidation, acquisition or otherwise) or is merged into a Subsidiary will be deemed to be incurred or issued by such Subsidiary at the time it becomes or is so merged into a Subsidiary;

"**Indebtedness**" means any indebtedness, in respect of any Person for, or in respect of, moneys borrowed or raised including, without limitation, any amount raised by acceptance under any acceptance credit facility; any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument; any amount raised pursuant to any issue of Disqualified Stock; and any amount raised under any other transaction having the economic or commercial effect of a borrowing; and, without duplication of any of the foregoing, the amount of any liability in respect of any Guarantee or indemnity for any of the items referred to above. For the avoidance of doubt the following amounts shall not constitute "Indebtedness": (i) trade accounts payable, (ii) advances received from customers, (iii) operating lease liabilities, (iv) amounts payable to employees, (v) government grants, (vi) contingent liabilities other than with respect to items of Indebtedness described in the preceding sentence and (vii) other accounts payable and advances received, to the extent that such amounts described in sub-clauses (i) through (vii) arise in the ordinary course of business;

"**Interest Payment Date**" means 29 January and 29 July of each year, commencing on 29 January 2009;

"**Interest Period**" has the meaning assigned to such term in Clause 4.2;

"**Interest Rate Agreement**" means any interest rate swap agreement, interest rate cap agreement or other financial agreement or arrangement with respect to exposure to interest rates;

"**Investment**" in any Person means any direct or indirect advance, loan or other extensions of credit (including by way of guarantee or similar arrangement) (other than advances to customers in the ordinary course of business that are recorded as accounts receivable on the balance sheet of the lender) or capital contribution to (by means of any transfer of cash or other property to others or any payment for property or services for the account or use of others), or any purchase or acquisition of Capital Stock, Indebtedness or other similar instruments issued by such Person. If Severstal or any Subsidiary of Severstal issues, sells or otherwise disposes of any Capital Stock of a Person that is a Subsidiary of Severstal such that, after giving effect thereto, such Person is no longer a Subsidiary of Severstal, any Investment by Severstal or any Subsidiary of Severstal in such Person remaining after giving effect thereto will be deemed to be a new Investment at such time. The acquisition by Severstal or any Subsidiary of Severstal of a Person that holds an Investment in a third Person will be deemed to be an Investment by Severstal or such Subsidiary in such third Person at such time. Except as otherwise provided for herein, the amount of an Investment shall be its Fair Market Value at the time the Investment is made and without giving effect to subsequent changes in value;

"**Lien**" means any mortgage, pledge, encumbrance, easement, restriction, covenant, right-of-way, servitude, lien, charge or other security interest or adverse claim of any kind (including, without limitation, anything analogous to any of the foregoing under the laws of any jurisdiction and any conditional sale or other title retention agreement or lease in the nature thereof, including, but without limitation to, a Sale/Leaseback Transaction);

"**Loan**", at any time, means an amount equal to the aggregate principal amount of the Facility granted by the Lender pursuant to this Agreement and outstanding at such time;

"**Material Adverse Effect**" means a material adverse effect on (a) the business, operations, property, condition (financial or otherwise) or immediate prospects of Severstal or the Group; (b) Severstal's ability to perform or comply with its obligations under this Agreement or (c) the validity or enforceability of this Agreement or the rights or remedies of the Lender hereunder;

"**Material Subsidiary**" means, at any given time, a Subsidiary of Severstal which:

(a) has gross revenues representing 10 per cent. or more of the consolidated gross revenues of the Group; or

(b) has total assets representing 10 per cent. or more of the consolidated total assets of the Group,

in each case calculated on a consolidated basis in accordance with Accounting Standards to which the then most recent published audited consolidated financial statements of Severstal comply, as consistently applied.

Compliance with the conditions set out in paragraphs (a) and (b) above shall be determined by reference to the latest consolidated annual or, as the case may be, interim financial statements of that Subsidiary and the latest consolidated annual or, as the case may be, interim financial statements of the Group, provided, however, that a report based on the above criteria by the Auditors (if such report is requested by the Lender), that a Subsidiary is, or is not, a Material Subsidiary shall, in the absence of manifest error, be conclusive and binding on all parties;

"**Materials of Environmental Concern**" means any toxic, ignitable, corrosive, reactive, radioactive or caustic substance, and any other substance considered a pollutant, contaminant or hazardous or potentially hazardous substance or waste;

"**Non-recourse Project Financing**" means any financing of all or part of the costs of the acquisition, construction or development of any project if (i) the recourse of the Person or Persons providing such financing is limited to the project financed (and the direct owner of such project) and the revenues derived from such project as the principal source of repayment for the moneys advanced (it being acknowledged and agreed that equity contribution agreements (and related guaranties), subordinated debt obligations and equity pledges and similar arrangements, in each case, provided by or on behalf of the indirect owners of such project shall not result in such financing being considered recourse to such indirect owners) and (ii) the Person or Persons providing such financing have been provided with a feasibility study prepared by competent independent experts on the basis of which it is reasonable to conclude that such project would generate sufficient operating income to service substantially all Indebtedness Incurred in connection with such project;

"**Officers' Certificate**" means a certificate signed on behalf of Severstal by two officers of Severstal at least one of whom shall be the principal executive officer, principal accounting officer or principal financial officer of Severstal;

"**Permitted Liens**" means:

(a) Liens granted by Severstal or any of its Subsidiaries which are existing as at the date of this Agreement;

(b) Liens arising or created in connection with any Non-recourse Project Financing;

(c) Liens on any property, income or assets of a Person existing at the time that such Person is acquired, merged into or consolidated with Severstal or a Subsidiary of Severstal; provided that such Liens were not created in contemplation of such event and do not extend to any assets, income or property of Severstal or any Subsidiary of Severstal, other than the surviving Person and its Subsidiaries;

(d) Liens on assets, income or property acquired by Severstal or a Material Subsidiary existing prior to such acquisition; provided that such Liens were not created in contemplation of such acquisition and do not extend to any other assets, income or property (other than proceeds of such acquired assets or property);

(e) any Lien on any property or assets of Severstal or any Subsidiary of Severstal securing Indebtedness Incurred for the purpose of financing all or part of the acquisition, maintenance, repair or construction of such property or assets provided that (i) no such Lien shall extend to any other property or assets of Severstal or any of its Subsidiaries, (ii) the aggregate principal amount of all Indebtedness secured by Liens under this paragraph on such property or assets does not exceed the purchase price of such property or assets (including customs duties, transport, insurance, construction and installation costs and other incidental costs and expenses of purchase and any VAT or similar taxes thereon) and (iii) such Lien attaches to such property or assets concurrently with the maintenance or repair thereof or within 90 days after the acquisition or commencement of construction thereof, as the case may be;

(f) Liens Incurred, or pledges and deposits in connection with workers' compensation, unemployment insurance and other social security benefits, and leases, appeal bonds and other obligations of like nature in the ordinary course of business;

(g) Liens imposed by law, including, but without limitation to, mechanics', carriers', warehousemen's, materialmen's, suppliers' and vendors' Liens in the ordinary course of business;

(h) Liens for *ad valorem*, income or property taxes or assessments and similar charges which either are not delinquent or are being contested in good faith by appropriate proceedings for which Severstal has set aside in its books of account reserves to the extent required by Accounting Standards to which the then most recent published audited consolidated financial statements of Severstal comply, as consistently applied;

(i) easements, rights of way, restrictions (including zoning restrictions), reservations, permits, servitudes, minor defects or irregularities in title and other similar charges or encumbrances, and Liens arising under leases or subleases granted to others, in each case not interfering in any material respect with the business of Severstal or any of its Material Subsidiaries and existing, arising or Incurred in the ordinary course of business;

(j) (i) bankers' Liens in respect of deposit accounts, (ii) statutory landlords' Liens, (iii) deposits to secure the performance of bids, trade contracts, government contracts, leases, statutory obligations, surety and appeal bonds, performance and return-of-money bonds or liabilities to insurance carriers under insurance or self-insurance arrangements and other obligations of like nature (so long as, (X) with respect to items described in (ii) and (iii) above of this sub-Clause (j), such Liens do not secure obligations constituting Indebtedness for borrowed money and (Y) with respect to items described in (i), (ii) and (iii) above of this sub-Clause (j), such Liens are Incurred in the ordinary course of business), and (iv) Liens arising from any judgment, decree or other order which does not constitute an Event of Default;

(k) any Lien on the property, income or assets of Severstal or any of its Subsidiaries securing Indebtedness of Severstal or such Subsidiaries Incurred in an aggregate principal amount outstanding at any one time not to exceed 20 per cent. of the total assets of Severstal (determined by reference to the most recent publicly available consolidated annual or interim financial statements of Severstal prepared in accordance with Accounting Standards to which the then most recent published audited consolidated financial statements of Severstal comply as may be adopted from time to time by Severstal). For the avoidance of doubt this paragraph (k) does not include any Lien created in accordance with paragraphs (a) to (j) or (l) to (r) hereof;

(l) Liens upon, or with respect to, any present or future assets or revenues or any part thereof which are created pursuant to any repo transaction;

(m) Liens granted by a Subsidiary of Severstal in favour of Severstal or a Subsidiary of Severstal or by Severstal in favour of a Subsidiary of Severstal with respect to the property or assets, or any income or profits therefrom, of Severstal or such Subsidiary of Severstal, as the case may be;

(n) any Lien over any rights, title or interest in, to or under any Steel or Ferrous Metal Contract, including the receivables generated under any such Steel or Ferrous Metal Contract and all other monies and proceeds arising in connection with any such Steel or Ferrous Metal Contract, and any Lien over any bank accounts into which the receivables, monies and proceeds from any such Steel or Ferrous Metal Contract are paid or transferred (including (i) amounts standing to the credit of such bank accounts and (ii) any rights under any agreements establishing or opening such bank accounts);

(o) any Lien in respect of obligations arising under hedging agreements so long as the related Indebtedness is permitted to be Incurred under this Agreement and any such hedging agreement is not speculative;

(p) a right of set-off, right to combine accounts or any analogous right which any bank or other financial institution may have relating to any credit balance of any member of the Group;

(q) any Lien created in connection with the raising of any Indebtedness for working capital purposes; and

(r) any extension, renewal, replacement of or substitution for any Lien permitted by any of the preceding sub-Clauses (a) through (q); provided, however, that, such extension, renewal, replacement or substitution shall be no more restrictive in any material respect than the original Lien, with respect to Liens Incurred pursuant to this sub-Clause the principal amount secured has not increased and the Liens have not been extended to any additional property (other than proceeds of the property in question). For the purposes of this paragraph (r), a Lien created in renewal, replacement or substitution for an original Lien may be created either simultaneously or promptly after expiry or termination of such original Lien;

"**Permitted Restriction**" means any restriction or encumbrance on the ability of a Subsidiary of Severstal to pay dividends, return capital, make any other payment or distribution, or transfer assets to Severstal or its Subsidiaries (a) arising under a credit agreement or (b) in effect on the Closing Date with respect to a Subsidiary of Severstal and other restrictions with respect to such Subsidiary that are not materially less favourable to the agreed funding source than such restrictions in effect on the Closing Date;

"**Person**" means any individual, company, corporation, firm, partnership, joint venture, association, joint-stock company, trust, unincorporated organisation, government, or any agency or political subdivision thereof or any other entity;

"**Preferred Stock**", as applied to the Capital Stock of any Person, means Capital Stock of any class or classes (however designated) which is preferred as to the payment of dividends or distributions, or as to the distribution of assets upon any voluntary or involuntary liquidation or dissolution of such Person, over shares of any other class of Capital Stock of such Person;

"**Purchase Money Indebtedness**" means Indebtedness (including Capital Lease Obligations) (i) consisting of the deferred purchase price of property, conditional sale obligations, obligations under any title retention agreement, other purchase money obligations and obligations in respect of industrial revenue bonds or similar Indebtedness, in each case where the maturity of such Indebtedness does not exceed the anticipated useful life of the asset being financed, and (ii) Incurred to finance the acquisition by Severstal or a Subsidiary of Severstal of such asset, including construction, additions and improvements, in the ordinary course of business (including the cost of design, development, construction, acquisition, transportation, installation, improvement and migration of assets); provided, however, that (A) any Lien arising in connection with any such Indebtedness shall be limited to the specific asset being financed or, in the case of real property or fixtures, including additions and improvements, the real property on which such asset is attached, (B) such Indebtedness is Incurred within 180 days after such acquisition of such assets and (C) the aggregate principal amount of Purchase Money Indebtedness at any one time outstanding shall not exceed (x) the Fair Market Value of the acquired or constructed asset or improvement so financed or (y) in the case of an uncompleted constructed asset, the amount of the asset to be constructed, as determined on the date the contract for construction of such asset was entered into by Severstal or the relevant Subsidiary of Severstal (including, in each case, any reasonable related fees and expenses incurred in connection with such acquisition, construction or development);

"**Rate of Interest**" has the meaning assigned to such term in Clause 4.1;

"**Refinance**" means, in respect of any Indebtedness, to refinance, extend, renew, refund, repay, prepay, purchase, redeem, defease or retire, or to issue other Indebtedness in exchange or replacement for, such Indebtedness. "**Refinanced**" and "**Refinancing**" shall have correlative meanings;

"**Refinancing Indebtedness**" means Indebtedness that Refinances any Indebtedness of Severstal or any Subsidiary of Severstal existing on the Closing Date or Incurred in compliance with this Agreement, including Indebtedness that Refinances Refinancing Indebtedness; provided, however, that:

(a) such Refinancing Indebtedness has a Stated Maturity no earlier than the Stated Maturity of the Indebtedness being Refinanced;

(b) such Refinancing Indebtedness has an Average Life at the time such Refinancing Indebtedness is Incurred that is equal to or greater than the Average Life of the Indebtedness being Refinanced;

(c) such Refinancing Indebtedness has an aggregate principal amount (or if Incurred with original issue discount, an aggregate issue price) that is equal to or less than the aggregate principal amount (or if Incurred with original issue discount, the aggregate accreted value) then outstanding (plus fees and expenses, including any premium and defeasance costs) under the Indebtedness being Refinanced; and

(d) if the Indebtedness being Refinanced is subordinated in right of payment to the Loan, such Refinancing Indebtedness is subordinated in right of payment to the Loan at least to the same extent as the Indebtedness being Refinanced;

"**Related Business**" means any business of the type in which Severstal or any of its Subsidiaries was engaged on the Closing Date and any business related, ancillary or complementary to such business;

"**Repayment Date**" means 29 July 2013;

"**Reserved Rights**" has the meaning assigned to such term in the agreed funding agreements;

"**Rouble**", "**Ruble**", "**RUR**" and "**Rbs**" mean the lawful currency from time to time of the Russian Federation;

"**Sale/Leaseback Transaction**" means an arrangement relating to property now owned or hereafter acquired whereby Severstal or any Material Subsidiary of Severstal transfers such property to a Person and Severstal or such Material Subsidiary leases it from such Person;

"**Same-Day Funds**" means Dollar funds settled through the New York Clearing House Interbank Payments System or such other funds for payment in Dollars as the Lender may at any time reasonably determine to be customary for the settlement of international transactions in New York City of the type contemplated hereby;

"**Securities Act**" means the U.S. Securities Act of 1933;

"**Stated Maturity**" means, with respect to any security, the date specified in such security as the fixed date on which the final payment of principal of such security is due and payable, including pursuant to any mandatory redemption provision (but excluding any provision providing for the repurchase of such security at the option of the holder thereof upon the happening of any contingency unless such contingency has occurred);

"**Steel or Ferrous Metal Contract**" means any contract for the sale or delivery of any steel or steel products and ferrous metals (including iron ore and iron ore pellets), coke, coal, coke concentrate and gold (including contracts for sale, transportation or exchange and utilisation and pooling declarations or agreements), entered into from time to time between Severstal or any of its Subsidiaries and any other persons;

"**Subordinated Obligation**" means, with respect to a Person, any Indebtedness of such Person (whether outstanding on the Closing Date or thereafter Incurred) which is subordinate or junior in right of payment to the agreed funding source in respect of the agreed funding, pursuant to a written agreement to that effect;

"**Subsidiary**" of any specified Person means any corporation, partnership, joint venture, association or other business or entity, whether now existing or hereafter organised or acquired, (a) in the case of a corporation, of which more than 50 per cent. of the total voting power of the Voting Stock is held by such first-named Person and/or any of its Subsidiaries and such first-named Person or any of its Subsidiaries has the power to direct the management, policies and affairs thereof; or (b) in the case of a partnership, joint venture, association, or other business or entity, with respect to which such first-named Person or any of its Subsidiaries has the power to direct or cause the direction of the management and policies of such entity by contract or otherwise, if (in the case of each of (a) and (b)) in accordance with Accounting Standards to which the then most recent published audited consolidated financial statements of Severstal comply, as consistently applied, such entity would be consolidated with the first-named Person for financial statement purposes;

"**Temporary Cash Investments**" means any of the following:

(a) any investment in direct obligations of a member of the European Union, the Russian Federation, the United States of America or any agency thereof or obligations guaranteed by a member of the European Union, the Russian Federation, or the United States of America or any agency thereof;

(b) investments in demand and time deposit accounts, certificates of deposit and money market deposits with a maturity of one year or less from the date of acquisition thereof issued by a bank or trust company which is organised under the laws of the Russian Federation, a member of the European Union or the United States of America or any state thereof, and which bank or trust company has capital, surplus and undivided profits aggregating in excess of US$500,000,000 (or the foreign currency equivalent thereof) and has outstanding debt which is rated "BBB–" or "Baa3" (or such similar equivalent rating) or higher by at least one nationally recognised statistical rating organisation;

(c) repurchase obligations with a term of not more than 30 days for underlying securities of the types described in clause (a) above entered into with a bank meeting the qualifications described in clause (b) above;

(d) investments in commercial paper with a maturity of one year or less from the date of acquisition, issued by a corporation (other than an Affiliate of Severstal) organised and in existence under the laws of a member of the European Union, the United States of America or the Russian Federation with a rating at the time as of which any investment therein is made of "P 1" (or higher) according to Moody's Investors Service, Inc. or "A1" (or higher) according to Standard & Poor's Ratings Group;

(e) investments in securities with maturities of six months or less from the date of acquisition issued or fully guaranteed by any state, commonwealth or territory of a member of the European Union, the United States, or the Russian Federation or by any political subdivision or taxing authority thereof, and rated at least "BBB–" by Standard & Poor's Ratings Group or "Baa3" by Moody's Investors Service, Inc.; and

(f) investments in money market funds that invest substantially all their assets in securities of the types described in clauses (a) through (e) above;

"**U.S. Dollar Equivalent**" means with respect to any monetary amount in a currency other than U.S. dollars, at any time for determination thereof, the amount of U.S. dollars obtained by converting such foreign currency involved in such computation into U.S. dollars at the spot rate for the purchase of U.S. dollars with the applicable foreign currency as published in *The Wall Street Journal* in the "Exchange Rates" column under the heading "Currency Trading" on the date two Business Days prior to such determination;

"**U.S. GAAP**" means generally accepted accounting principles, standards and practices in the United States of America;

"**Voting Stock**" means, in relation to any Person, Capital Stock entitled (without the need for the occurrence of any contingency) to vote in the election of directors, managers or trustees thereof; and

"**Wholly Owned Subsidiary**" means a Subsidiary all the Capital Stock of which (other than directors' qualifying shares or shares of Subsidiaries required to be owned by third parties under applicable law) is owned by Severstal or one or more other Wholly Owned Subsidiaries.

**1.2 Other Definitions**

Unless the context otherwise requires, terms used in this Agreement which are not defined in this Agreement but which are defined in, or are defined by cross-reference to definitions in, or other provisions of, any agreed funding agreements, shall have the meanings assigned to such terms therein, **provided that** in the case of terms defined or references herein to documents to which Severstal is not a party, Severstal has been sent an up-to-date copy of such documents as soon as reasonably practicable (including any amendments thereto that may affect the meaning or interpretation of any such term or reference).

**1.3 Interpretation**

Unless the context or the express provisions of this Agreement otherwise require, the following shall govern the interpretation of this Agreement:

**1.3.1** all references to "Clause" or "sub-Clause" are references to a Clause or sub-Clause of this Agreement;

**1.3.2** the terms "hereof", "herein" and "hereunder" and other words of similar import shall mean this Agreement as a whole and not any particular part hereof;

**1.3.3** words importing the singular number include the plural and vice versa;

**1.3.4** all references to "taxes" include all present or future taxes, levies, imposts and duties of any nature and the terms "tax" and "taxation" shall be construed accordingly; and

**1.3.5** the table of contents and the headings are for convenience only and shall not affect the construction hereof.

**2 Facility**

**2.1 Facility**

On the terms and subject to the conditions set forth herein, the Lender hereby agrees to lend Severstal and Severstal hereby agrees to borrow from the Lender U.S.$1,250,000,000.

**2.2 Purpose**

The proceeds of the Advance will be used for (a) working capital and/or (b) general corporate purposes and/or (c) to finance acquisitions and/or to refinance Indebtedness, but the Lender shall not be concerned with the application thereof.

## 3 Drawdown

### 3.1 Drawdown

On the terms and subject to the conditions of this Agreement, on the Closing Date the Lender shall make the Advance to Severstal and Severstal shall make a single drawing in the full amount of the Facility.

### 3.2 Facility Fee

In consideration of the Lender making the Advance to Severstal, Severstal hereby agrees that it shall pay to the Lender, in Same-Day Funds, U.S.$12,488,429.53 (the "**Facility Fee**") constituting a fee in connection with, *inter alia*, the financing of the Loan, the arrangement of the Facility and the negotiation, preparation and execution of this Agreement and the other agreed funding agreements and other costs connected with and necessary for the establishment of the Facility and the provision of the Loan. Severstal shall pay the Facility Fee by 4.30 p.m. (London time) two Business Days prior to the Closing Date. The Lender shall promptly deliver an invoice to Severstal providing for the amount due. Following payment of the Facility Fee to the Lender by Severstal, Severstal and the Lender shall enter into and sign a delivery and acceptance act as provided in Clause 3.5. In the event that following payment of the Facility Fee by Severstal to the Lender, closing of the issue of the agreed funding does not take place in accordance with the agreed funding agreements, the Lender shall return the Facility Fee to Severstal less certain amounts to be deducted pursuant to arrangements entered into by Severstal in respect of the Loan in relation to costs due in such circumstances, within 3 Business Days of the determination of such amounts by the Lender (and the Lender shall determine such amounts as soon as reasonably practicable).

### 3.3 Disbursement

Subject to the conditions set forth herein, on the Closing Date the Lender shall transfer the amount of the Advance to Severstal's account as follows: Beneficiary: OAO Severstal, Russia, Vologda region, Cherepovets, Mira str. 30, INN 3528000597, Current account No: 40702840800020008507 with CJSC "CALYON RUSBANK Corporate and Investment Bank" Moscow Branch, SWIFT CRLYRU2P, Transit account No: 40702840300025008507, Corresponding Bank: CALYON NEW YORK, New York, NY, USA, SWIFT CRLYUS33, correspondent account: 01 25492 0001 00, or such other bank account that is notified in writing to the Lender by Severstal at least one Business Day prior to the Closing Date, in Same-Day Funds.

### 3.4 Ongoing Fees and Expenses

In consideration of the Lender (i) making available the Facility hereunder and (ii) maintaining and managing the Facility as a continuing facility and managing the Account, Severstal shall pay on demand to the Lender each year an amount equal to all ongoing fees and costs. Payments to the Lender referred to in this Clause 3.4 shall be made by Severstal promptly following receipt of the relevant invoice from the Lender. In addition, following each payment of such fees and expenses to the Lender by Severstal, Severstal and the Lender shall enter into and sign a delivery and acceptance act as provided in Clause 3.5.

### 3.5 Acts of Acceptance

In connection with all payments to be made by Severstal under Clauses 3.2, 3.4, 12 and 14.1, Severstal and the Lender shall, within 30 days of such payment becoming due or such indemnity claim having been made, as the case may be, execute a delivery and acceptance act (which Severstal shall prepare) with respect to the amounts to be paid by Severstal. Such delivery and acceptance acts shall specify (i) the net amount due, (ii) any applicable Russian income tax withholding, (iii) any applicable Russian value added tax and (iv) the resulting total amount inclusive of tax.

**4 Interest**

**4.1 Rate of Interest**

Severstal will pay interest in Dollars to the Lender on the outstanding principal amount of the Loan from time to time at the rate of 9.75 per cent. per annum (the "**Rate of Interest**").

**4.2 Payment**

Interest at the Rate of Interest shall accrue from day to day, starting from (and including) the Closing Date and shall be paid in arrear not later than 10.00 a.m. (New York City time) one Business Day prior to each Interest Payment Date. Interest on the Loan will cease to accrue from the due date for repayment thereof unless payment of principal due on such date is withheld or refused, in which event interest will continue to accrue (before or after any judgment) at the Rate of Interest to, but excluding, the date on which payment in full of the principal thereof is made. The amount of interest payable in respect of the Loan for any Interest Period shall be calculated by applying the Rate of Interest to the Loan, dividing the product by two and rounding the resulting figure to the nearest cent (half a cent being rounded upwards). If interest is required to be calculated for any other period, it will be calculated on the basis of a 360-day year consisting of 12 months of 30 days each and, in the case of an incomplete month, the number of days elapsed.

"**Interest Period**" means each period beginning on (and including) the Closing Date or any Interest Payment Date and ending on (but excluding) the next Interest Payment Date.

**5 Repayment and Prepayment**

**5.1 Repayment**

Except as otherwise provided herein, Severstal shall repay the Loan not later than 10.00 a.m. (New York City time) one Business Day prior to the Repayment Date.

**5.2 Prepayment in the event of Taxes or Increased Costs**

If, as a result of the application of or any amendments or clarification to, or change (including a change in interpretation or application) in, or determination under, the double tax treaty between the Russian Federation and Luxembourg or the laws or regulations of the Russian Federation or Luxembourg or of any political sub-division thereof or any authority therein having power to tax (each, a "**Taxing Jurisdiction**") or the enforcement of the security provided for in the agreed funding agreements, Severstal would thereby be required (i) to increase the payment of principal or interest or any other payment due hereunder as provided in Clause 6.2 or 6.3, or if (for whatever reason) Severstal would have to or has been required (ii) to pay additional amounts pursuant to Clause 8, and in any such case such obligation cannot be avoided by Severstal taking reasonable measures available to it, then Severstal may (without premium or penalty), upon not less than 30 days' notice to the Lender (which notice shall be irrevocable), prepay the Loan in whole (but not in part) at any time.

No such notice of prepayment shall be given earlier than 90 days prior to the earliest date on which Severstal would be obliged to pay such additional amounts or increase such payment if a payment in respect of the Loan were then due.

Prior to giving any such notice in the event of an increase in payment pursuant to Clause 6.2, Severstal shall deliver to the Lender an Officers' Certificate confirming that Severstal would be required to increase the amount payable, supported by an opinion of an independent tax adviser addressed to the Lender.

**5.3 Prepayment in the event of Illegality**

If, at any time, the Lender reasonably determines that it is or would be unlawful or contrary to any applicable law or regulation or regulatory requirement or directive of any agency of any state or otherwise for the Lender to allow all or part of the Loan or the agreed funding to remain outstanding or for the Lender to maintain or give effect to any of its obligations in connection with this Agreement or the agreed funding or the agreed funding agreements and/or to charge or receive or to be paid interest at the rate then applicable to the Loan (an "**Event of Illegality**"), then upon notice by the Lender to Severstal in writing, Severstal and the Lender shall consult in good faith as to a basis which eliminates the application of such Event of Illegality; provided, however, that the Lender shall be under no obligation to continue such consultation if a basis has not been determined within 30 days of the date on which it so notified Severstal. If such a basis has not been determined within the 30 days, then upon written notice by the Lender to Severstal, Severstal shall prepay the Loan in whole (but not in part) on the next Interest Payment Date or on such earlier date as the Lender shall (acting reasonably) certify to be necessary to comply with such requirements.

**5.4 Reduction of Loan upon Cancellation of agreed funding**

Severstal may from time to time deliver to the Lender evidence of agreed funding that has been repurchased, redeemed or cancelled, having an aggregate principal value of at least U.S.$1,000,000, together with an authorisation addressed to the agent of the Lender designated for such purpose, whereupon the Lender shall extinguish the principal amount of the Loan corresponding to the principal amount of such agreed funding for all purposes as of the date of such cancellation.

**5.5 Payment of Other Amounts**

If the Loan is to be prepaid by Severstal pursuant to any of the provisions of Clauses 5.2 or 5.3, Severstal shall, simultaneously with such prepayment, pay to the Lender accrued interest thereon to the date of actual payment and all other sums payable by Severstal pursuant to this Agreement in relation to the prepaid amount. For the avoidance of doubt, if the principal amount of the Loan is reduced pursuant to the provisions of Clause 5.4, then no interest shall accrue or be payable during the Interest Period in which such reduction takes place in respect of the amount by which the Loan is so reduced and Severstal shall not be entitled to any interest in respect of the cancelled agreed funding.

**5.6 Provisions Exclusive**

Severstal shall not prepay or repay all or any part of the amount of the Loan except at the times and in the manner expressly provided for in this Agreement. Severstal shall not be permitted to reborrow any amounts prepaid or repaid.

**6 Payments**

**6.1 Making of Payments**

All payments of principal, interest and other amounts (other than those in respect of Reserved Rights) to be made by Severstal under this Agreement shall be made unconditionally by credit transfer to the Lender not later than 10.00 a.m. (New York City time) one Business Day prior to each Interest Payment Date or the Repayment Date or the date of any payment (as the case may be) in Same-Day Funds to the Account, or as the agreed funding source may otherwise direct following the occurrence of a Relevant Event.

Severstal shall, before 10.00 a.m. (New York City time) on the second Business Day prior to each Interest Payment Date or the Repayment Date or such other date (as the case may be), procure that the bank effecting such payments on its behalf confirms to the party designated as principal paying agent by the agreed funding agreements by tested telex or authenticated SWIFT the payment instructions relating to such payment.

The Lender agrees with Severstal that it will not deposit any other monies into the Account and that no withdrawals shall be made from the Account other than as provided for and in accordance with the agreed funding agreements.

For the avoidance of doubt, the parties to any other agreed funding agreement are intended by the parties to this Agreement to have the right under the Contracts (Rights of Third Parties) Act 1999 to enforce the terms of this Clause 6.1.

**6.2 No Set-Off, Counterclaim or Withholding; Gross-Up**

All payments to be made by Severstal under this Agreement shall be made in full without set-off or counterclaim and (except to the extent required by law) free and clear of and without deduction for or on account of any taxes. If Severstal shall be required by applicable law to make any deduction or withholding from any payment under this Agreement for or on account of any such taxes, it shall, on the due date for such payment, increase the payment of principal or interest or any other payment due hereunder to such amount as may be necessary to ensure that the Lender receives a net amount in Dollars equal to the full amount which it would have received had payment not been made subject to such taxes, and shall promptly account to the relevant authorities for the relevant amount of such taxes so withheld or deducted and shall deliver to the Lender without undue delay evidence satisfactory to the Lender of such deduction or withholding and of the accounting therefor to the relevant taxing authority. If the Lender pays any amount in respect of such taxes (including penalties or interest) Severstal shall reimburse the Lender in Dollars for such payment on demand.

**6.3 Withholding on agreed funding**

Without prejudice to the provisions of Clause 6.2, if the Lender notifies Severstal that it has become obliged to make any withholding or deduction for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or on behalf of Luxembourg or any political subdivision or any authority thereof or therein having the power to tax from any payment which it is obliged to make under or in respect of the agreed funding, Severstal agrees to pay into the Account, no later than one Business Day prior to the date on which payment is due to the agreed funding source, such additional amounts as are equal to the additional amounts which the Lender would be required to pay in order that the net amounts received by the agreed funding source, after such withholding or deduction, will equal the respective amounts which would have been received by the agreed funding source in the absence of such withholding or deduction; provided, however, that the Lender shall immediately upon receipt from any paying agent of the Lender of any reimbursement of the sums paid pursuant to this provision, to the extent that the agreed funding source is not entitled to such additional amounts pursuant to the terms and conditions of the agreed funding, pay such additional amounts to Severstal (it being understood that neither the Lender nor any paying agent of the Lender shall have any obligations to determine whether the agreed funding source is not entitled to any such additional amount).

Any notification by the Lender to Severstal in connection with this Clause 6.3 shall be given as soon as reasonably practicable after the Lender becomes aware of any obligation on it to make any such withholding or deduction. The Lender shall, as soon as reasonably practicable following request by Severstal, provide Severstal with reasonable detail in writing as to the reasons for such withholding or deduction.

**6.4 Reimbursement**

**6.4.1** To the extent that the Lender subsequently obtains or uses any tax credit or allowance or other reimbursements relating to a deduction or withholding with respect to which Severstal has made a payment pursuant to this Clause 6, it shall pay to Severstal so much of the benefit it received as will leave the Lender in substantially the same position as it would have been in had no additional amount been required to be paid by Severstal pursuant to this Clause 6; provided, however, that the question of whether any such benefit has been received, and accordingly, whether any payment should be made to Severstal, the amount of any such payment and the timing of any such payment, shall be determined solely by the Lender, provided that the Lender shall notify Severstal promptly upon determination that it has received any such benefit. The Lender shall have the absolute discretion whether, and in what order and manner, it claims any credits or refunds available to it, and the Lender shall in no circumstances be obliged to disclose to Severstal any information regarding its tax affairs or computations.

**6.4.2** If as a result of a failure to obtain relief from deduction or withholding of any taxes referred to in Clause 6.2; (a) such taxes are deducted or withheld by Severstal and pursuant to Clause 6.2 an increased amount is paid by Severstal to the Lender in respect of such deduction or withholding, and (b) following the deduction or withholding of taxes as referred to above, Severstal applies on behalf of the Lender to the competent taxing authority for a withholding tax refund and such withholding tax is refunded or repaid by the relevant taxing authority to the Lender, the Lender shall as soon as reasonably practicable notify Severstal of the receipt of such withholding tax refund and promptly transfer the actually received amount of the withholding tax refund in the currency actually received and less any applicable cost to a bank account of Severstal specified for that purpose by Severstal.

**6.5 Representations of the Lender**

The Lender represents that, at the date hereof, (a) it is a company which is a resident of Luxembourg, is subject to taxation in Luxembourg on the basis of its registration as a legal entity, location of its board of directors or another similar criterion and it is not subject to taxation in Luxembourg merely on income from sources in Luxembourg or connected with property located in Luxembourg and it will be able to receive certification to this effect from the Luxembourg taxing authorities; (b) it does not have a permanent establishment in the Russian Federation; (c) it does not have any current intentions to effect, during the term of the Loan, any corporate action or reorganisation or change of taxing jurisdiction that would result in the Lender ceasing to be a resident of Luxembourg or ceasing to be subject to taxation in Luxembourg; and (d) it is not a holding company within the meaning assigned by specific laws of the Grand Duchy of Luxembourg governed by the law of 31 July 1929 and the decree of the Grand Duke dated 17 December 1938 (as repeated by the Grand Duchy of Luxembourg law dated 22 December 2006), nor a company in the Grand Duchy of Luxembourg governed by any similar tax law.

The Lender shall make reasonable and timely efforts to assist Severstal to obtain relief from withholding of Russian income tax pursuant to the double taxation treaty between the Russian Federation and Luxembourg, including, without limitation, its obligations under Clauses 6.6 and 6.9. The Lender makes no representation as to the application or interpretation of any double taxation treaty between the Russian Federation and Luxembourg.

**6.6 Notification and Substitution**

**6.6.1** The Lender agrees upon becoming aware of such, promptly to notify Severstal if it ceases to be tax resident in Luxembourg or opens a permanent establishment in Russia or if any of the representations set forth in Clause 6.5 are no longer true and correct.

**6.6.2** If the Lender ceases, as a result of the Lender's actions, to be tax resident in a jurisdiction for the purposes of a double taxation treaty between the Russian Federation and such jurisdiction, and such cessation results in Severstal being required to make payments pursuant to Clause 6.2, Clause 6.3 or Clause 8 then, except in circumstances where the Lender has ceased to be tax resident in such jurisdiction by reason of any change of law (as described in Clause 5.2) (including, without limitation, a change in a double taxation treaty or in such law or treaty's application or interpretation), Severstal may require the Lender to seek the substitution of the Lender as borrower of the agreed funding and as lender under this Loan Agreement. Severstal shall bear all costs and expenses relating to or arising out of such substitution.

**6.7 Evidence of Debt**

The entries made in the accounts of the Lender shall, in the absence of manifest error, constitute conclusive evidence of the existence and amounts of Severstal's obligations to pay amounts thereto, as recorded therein.

**6.8 Mitigation**

If at any time either party hereto becomes aware of circumstances which would or might, then or thereafter, give rise to an obligation on the part of Severstal to make any deduction, withholding or payment as described in Clauses 6.2 or 6.3, then, without in any way limiting, reducing or otherwise qualifying the rights of the Lender or Severstal's obligations under any of the above mentioned provisions, the Lender shall, upon becoming aware of the same, notify Severstal thereof and, in consultation with Severstal and to the extent it can lawfully do so and without prejudice to its own position, take all reasonable steps to remove such circumstances or mitigate the effects of such circumstances; provided that the Lender shall be under no obligation to take any such action if, in its reasonable opinion, to do so might reasonably be expected to have any adverse effect upon its business, operations or financial condition or might be in breach of any provision of the agreed funding agreements.

**6.9 Tax Treaty Relief**

The Lender shall at Severstal's cost, to the extent it is able to do so under applicable law including, without limitation, Russian laws, use commercially reasonable efforts to obtain and to deliver to Severstal, no later than 25 Business Days before the first Interest Payment Date and thereafter no later than 25 Business Days prior to the first Interest Payment Date in each calendar year, a certificate issued by the competent taxing authority in Luxembourg confirming that the Lender is a tax resident in Luxembourg. The Lender shall, at the request of Severstal and at Severstal's cost, to the extent it is able to do so under applicable law including, without limitation, Russian laws, from time to time use its commercially reasonable efforts to obtain and to deliver to Severstal any other information or additional application forms as may be needed to be duly completed and delivered by the Lender to enable Severstal to apply to obtain relief from deduction or withholding of Russian taxes or, as the case may be, to apply to obtain a tax refund if a relief from deduction or withholding of Russian taxes has not been obtained. The certificate and, if required, other forms referred to in this Clause 6.9 shall be duly signed by the Lender, if applicable, and stamped or otherwise approved by the competent taxing authority in Luxembourg, if applicable. Together with any such certificate, and, if required, other forms, the Lender shall deliver to Severstal a copy of the same, certified by a Luxembourg notary to be a true and up to date copy of the original document. Any such notary's certificate shall be apostilled or otherwise legalised. If a relief from deduction or withholding of Russian taxes under this Clause 6.9 has not been obtained and further to an application of Severstal to the relevant Russian taxing authorities the latter requests the Lender's rouble bank account details, the Lender shall at the request of Severstal (a) use its commercially reasonable efforts, at Severstal's cost, to procure that such rouble bank account of the Lender is duly opened and maintained, and (b) thereafter furnish Severstal with the details of such rouble bank account. Severstal and the Lender (using its best endeavours and in accordance with the law) agree that, should the Russian legislation regulating the procedure for obtaining relief from Russian income tax withholding or the interpretation thereof by the relevant competent authority change then the procedure referred to in this Clause 6.9 will be deemed changed accordingly.

**7 Conditions Precedent**

**7.1 Documents to be Delivered**

The obligation of the Lender to make the Advance shall be subject to the receipt by the Lender on or prior to the Closing Date of an executed copy of each of the following documents, each (other than sub-Clauses 7.1.4 and 7.1.5) dated the Closing Date, in form and substance satisfactory to the Lender:

**7.1.1** an opinion of Linklaters regarding issues of English and Russian law;

**7.1.2** an opinion of Freshfields Bruckhaus Deringer regarding issues of Russian law;

**7.1.3** an opinion of Arendt & Medernach regarding issues of Luxembourg law;

**7.1.4** a letter from Ernst & Young (CIS) B.V. regarding certain Russian tax matters; and

**7.1.5** written evidence that the persons mentioned in Clause 17.3.2(iv) have agreed to receive process in the manner specified herein.

**7.2 Further Conditions**

The obligation of the Lender to make the Advance shall be subject to the further conditions precedent that as at the Closing Date (a) the representations and warranties made and given by Severstal in Clause 9 shall be true and accurate as if made and given on the Closing Date with respect to the facts and circumstances then existing, (b) no event shall have occurred that constitutes, or that, with the giving of notice or the lapse of time, or both, would constitute, an Event of Default, (c) Severstal shall not be in breach of any of the terms, conditions and provisions of this Agreement and (d) the agreed funding agreements shall have been executed and delivered, (e) the Lender shall have received the full amount of the subscription moneys for the agreed funding and (f) the Lender shall have received in full the Facility Fee pursuant to Clause 3.2 hereof.

**8 Change in Law or Practices; Increase in Cost**

**8.1 Compensation**

In the event that after the date of this Agreement there is any change in or introduction of any tax, law, regulation, regulatory requirement or official directive (whether or not having the force of law but, if not having the force of law, the observance of which is in accordance with the generally accepted financial practice of financial institutions in the country concerned) or in the interpretation or application thereof by any person charged with the administration thereof and/or any compliance by the Lender in respect of the Loan or the Facility with any request, policy or guideline (whether or not having the force of law but, if not having the force of law, the observance of which is in accordance with the generally accepted financial practice of financial institutions in the country concerned) from or of any central bank or other fiscal, monetary or other authority, Agency or any official of any such authority, which:

**8.1.1** subjects or will subject the Lender to any taxes with respect to payments of principal of or interest on the Loan or any other amount payable under this Agreement (other than any taxes referred to in Clause 6.2, or any taxes referred to in Clause 6.3); or

**8.1.2** increases or will increase the taxation of or changes or will change the basis of taxation of payments to the Lender of principal of or interest on the Loan or any other amount payable under this Agreement (other than any taxes referred to in Clause 6.2 or any taxes referred to in Clause 6.3); or

**8.1.3** imposes or will impose on the Lender any other condition affecting this Agreement, the Facility or the Loan,

and if as a result of any of the foregoing:

(i) the cost to the Lender of making, funding or maintaining the Loan or the Facility is increased; or

(ii) the amount of principal, interest or other amount payable to or received by the Lender hereunder is reduced; or

(iii) the Lender makes any payment or foregoes any interest or other return on or calculated by reference to the gross amount of any sum receivable by it from Severstal hereunder or makes any payment or foregoes any interest or other return on or calculated by reference to the gross amount of the Loan, then subject to the following, and in each such case:

(a) the Lender shall, as soon as practicable after becoming aware of such increased cost, reduced amount or payment made or foregone, give written notice to Severstal together with a certificate describing in reasonable detail the introduction or change or request which has occurred and the country or jurisdiction concerned and the nature and date thereof and demonstrating the connection between such introduction, change or request and such increased cost, reduced amount or payment made or foregone, and all relevant supporting documents evidencing the matters set out in such certificates; and

(b) upon demand by the Lender to Severstal, Severstal, in the case of sub-Clauses (i) and (iii), shall on demand, pay to the Lender such additional amount as shall be necessary to compensate the Lender for such increased cost, and, in the case of sub-Clause (ii), at the time the amount so reduced would otherwise have been payable, pay to the Lender such additional amount as shall be necessary to compensate the Lender for such reduction, payment or forgone interest or other return provided however, that the amount of such increased cost, reduced amount or payment made or foregone shall be deemed not to exceed an amount equal to the proportion which is directly attributable to this Agreement.

**8.2 Mitigation**

In the event that the Lender becomes entitled to make a claim pursuant to Clause 8.1, then, without in any way limiting, reducing or otherwise qualifying the rights of the Lender or Severstal's obligations under the above mentioned provision, the Lender shall, upon becoming aware of the same, notify Severstal thereof and, in consultation with Severstal and to the extent it can lawfully do so and without prejudice to its own position, take all reasonable steps to remove such circumstances or mitigate the effects of such circumstances; provided that the Lender shall be under no obligation to take any such action if, in its reasonable opinion, to do so might reasonably be expected to result in a breach of any provision of the agreed funding agreements or the agreed funding.

**9 Representations and Warranties**

**9.1 Severstal's Representations and Warranties**

Severstal represents and warrants to the Lender, with the intent that such shall form the basis of this Agreement and shall remain in full force and effect, at the date hereof and shall be deemed to be repeated by Severstal on the Closing Date, that:

**9.1.1** it and each of its Material Subsidiaries is duly organised and incorporated and validly existing under the laws of its respective jurisdiction of incorporation and has the power and legal right to own its property, to conduct its business as currently conducted and in the case of Severstal only to enter into and to perform its obligations under this Agreement and to borrow the Advance; that it has taken all necessary corporate, legal and other action required to authorise the borrowing of the Advance on the terms and subject to the conditions of this Agreement and to authorise the execution and delivery of this Agreement and all other documents to be executed and/or delivered by it in connection with this Agreement, and the performance of this Agreement in accordance with its terms;

**9.1.2** this Agreement has been duly executed and delivered by and constitutes a legal, valid and binding obligation of Severstal enforceable in accordance with its terms, subject to applicable bankruptcy, insolvency, moratorium and other laws affecting creditors' rights generally, and subject, as to enforceability, (i) to general principles of equity (ii) to the fact that the gross-up provisions contained in Clauses 6.2 or 6.3 may not be enforceable under Russian law and (iii) with respect to the enforceability of a judgment, to the laws of the relevant jurisdiction where such judgement must be enforced and whether there is a treaty in force relating to the mutual recognition of foreign judgments;

**9.1.3** the execution, delivery and performance of this Agreement by Severstal will not conflict with or result in any breach or violation of (i) any law or regulation or any order of any governmental, judicial or public body or authority in the Russian Federation, (ii) the constitutive documents, rules and regulations of Severstal or any of its Material Subsidiaries, or (iii) any material agreement or other undertaking or instrument to which Severstal or any of its Material Subsidiaries is a party or which is binding upon Severstal or any of its Material Subsidiaries or any of their respective assets, nor result in the creation or imposition of any Liens on any of their respective assets pursuant to the provisions of any such agreement or other undertaking or instrument;

**9.1.4** all consents, licences, notifications, authorisations or approvals of, or filings with, any governmental, judicial and public bodies and authorities of the Russian Federation required by Severstal in connection with the execution, delivery, performance, legality, validity, enforceability, and admissibility in evidence of this Agreement have been obtained or effected and are and shall remain in full force and effect;

**9.1.5** no event has occurred that constitutes, or that, with the giving of notice or the lapse of time, or both, would constitute, an Event of Default or a default under any agreement or instrument evidencing any Indebtedness of Severstal or any Material Subsidiary (unless such default does not have a Material Adverse Effect), and no such event will occur upon the making of the Advance;

**9.1.6** there are no judicial, arbitral or administrative actions, proceedings or claims (including, but without limitation to, with respect to taxes) which have been commenced or are pending or, to the knowledge of Severstal, threatened, against Severstal or any of its Subsidiaries, the adverse determination of which could reasonably be expected to have a Material Adverse Effect;

**9.1.7** except for Liens of the types referred to in the definition of Permitted Liens in Clause 1.1, Severstal and each of its Material Subsidiaries has good title to its property (except where the failure to so have would not have a Material Adverse Effect) free and clear of all Liens and Severstal's obligations under the Loan rank at least *pari passu* with all its other unsecured and unsubordinated Indebtedness;

**9.1.8** the audited financial statements of the Group as at and for the years ended 31 December 2005, 2006 and 2007:

(i) were prepared in accordance with IFRS, as consistently applied;

(ii) unless not required by IFRS, as consistently applied, disclose all liabilities (contingent or otherwise) and all unrealised or anticipated losses of the Group; and

(iii) save as disclosed therein, present fairly in all material respects the assets and liabilities of the Group as at that date and the results of operations of the Group during the relevant financial year;

**9.1.9** the interim financial statements of the Group as at and for the three months ended 31 March 2007 and 2008:

(i) were prepared in accordance with IFRS, as consistently applied;

(ii) unless not required by IFRS, as consistently applied, disclose all liabilities (contingent or otherwise) and all unrealised or anticipated losses of the Group; and

(iii) save as disclosed therein, present fairly in all material respects the assets and liabilities of the Group as at that date and the results of operations of the Group during the relevant period;

**9.1.10** save as disclosed in the final prospectus prepared for the listing of the agreed funding (the "**Prospectus**"), since 31 December 2007, neither it nor any of its Material Subsidiaries has made any loans, granted any credit (save in the ordinary course of business) or given any

Guarantee or indemnity (save in the ordinary course of business) to or for the benefit of any person (other than another member of the Group) or otherwise assumed any liability, whether actual or contingent, in respect of any obligation of any person (other than another member of the Group), which loans, credits, guarantees or indemnities are material to the Group;

**9.1.11** there has been no material adverse change since 31 December 2007 in the condition (financial or otherwise), results of business, operations or immediate prospects of Severstal or any of its Material Subsidiaries or on Severstal's ability to perform its obligations under this Agreement;

**9.1.12** the execution, delivery and enforceability of this Agreement is not subject to any tax, duty, fee or other charge, including, but without limitation to, any registration or transfer tax, stamp duty or similar levy, imposed by or within the Russian Federation or any political subdivision or taxing authority thereof or therein;

**9.1.13** neither Severstal nor any Material Subsidiary nor their respective property has any right of immunity from suit, execution, attachment or other legal process on the grounds of sovereignty or otherwise in respect of any action or proceeding relating in any way to this Agreement;

**9.1.14** Severstal and each Material Subsidiary is in compliance with all applicable provisions of law, except where a failure to do so does not and will not have a Material Adverse Effect;

**9.1.15** there are no strikes or other employment disputes against Severstal or any Material Subsidiary which have been started or are pending or, to the knowledge of Severstal, threatened, that could reasonably be expected to have a Material Adverse Effect;

**9.1.16** in any proceedings taken in the Russian Federation in relation to this Agreement, the choice of English law as the governing law of this Agreement and any arbitration award obtained in England in relation thereto will be recognised and enforced in the Russian Federation after compliance with the applicable procedural rules and subject to all other legal requirements in Russia;

**9.1.17** subject to the performance by the relevant parties of the relevant established procedures in connection with the obtaining of an applicable withholding tax exemption for payments hereunder, no withholding in respect of any taxes is required to be made from any payment by Severstal under this Agreement;

**9.1.18** all licences, consents, examinations, clearances, filings, registrations and authorisations which are or may be necessary to enable Severstal or any of its Material Subsidiaries to own their respective assets and carry on their respective businesses are in full force and effect, except for those an absence of which do not and will not have a Material Adverse Effect;

**9.1.19** Severstal and its Material Subsidiaries (i) have, duly complied with, and have operated, used and only permitted the use of all properties and businesses owned, leased, occupied or operated by them in compliance with, all Environmental Laws, unless a failure to do so does not and will not have a Material Adverse Effect, (ii) after due inquiry, are not aware and have no reason to suspect that any property or business now owned, leased, occupied or operated by them is or may be contaminated by, or is adjacent to any property that may be contaminated by, or used in connection with, any Material of Environmental Concern where this has or will have a Material Adverse Effect or that any such property or business was used or operated by any prior owner, lessee, occupant or operator or other third party (with or without permission) in any way that constituted or is now capable of constituting a violation of any provision of an Environmental Law that has or will have a Material Adverse Effect, (iii) have not received any notice of any material violation or alleged material violation of any provision of any Environmental Law for which they may be held responsible and (iv) to the best of Severstal's knowledge, have no obligations with which they are not complying or liabilities, contingent or absolute, relating to the use, possession, collection, storage, processing, treatment, emission, release, discharge, disposal, transfer or transport of Materials of Environmental Concern, or the remediation of any of the foregoing, except in each case where such non-compliance or liability does not and will not have a Material Adverse Effect;

**9.1.20** it is subject to civil and commercial law with respect to its obligations under this Agreement, and its execution of this Agreement constitutes, and its exercise of its rights and performance of its obligations hereunder will constitute, private and commercial acts done and performed for private and commercial purposes; and

**9.1.21** Severstal and each Material Subsidiary has no overdue tax liabilities in excess of U.S.$50,000,000 other than those which have been disclosed in the Prospectus or which Severstal is contesting in good faith and by appropriate proceedings.

**9.2 Lender's Representations and Warranties**

The Lender represents and warrants to Severstal as follows:

**9.2.1** the Lender is duly incorporated and validly existing under the laws of and is resident for Luxembourg taxation purposes in Luxembourg and has full power and capacity to execute this Agreement and the agreed funding agreements and to undertake and perform the obligations expressed to be assumed by it herein and therein and the Lender has taken all necessary action to approve and authorise the same;

**9.2.2** the execution of this Agreement and the agreed funding agreements and the undertaking and performance by the Lender of the obligations expressed to be assumed by it herein and therein will not conflict with, or result in a breach of or default under, the laws of Luxembourg or any agreement or instrument to which it is a party or by which it is bound;

**9.2.3** this Agreement and the agreed funding agreements have been duly executed by and constitute or, as the case may be, will be before the Closing Date duly executed by and will constitute, legal, valid and binding obligations of the Lender subject to applicable bankruptcy, insolvency, moratorium and similar laws affecting creditors' rights generally, and subject, as to enforceability, to general principles of equity; and

**9.2.4** all authorisations, consents and approvals required by the Lender for or in connection with the execution of this Agreement and the agreed funding agreements and the performance by the Lender of the obligations expressed to be undertaken by it herein and therein have been obtained and are in full force and effect.

**10 Covenants**

So long as any amount remains outstanding hereunder:

**10.1 Negative Pledge**

Severstal shall not, and shall not permit any of its Material Subsidiaries to, directly or indirectly, create, Incur, assume or suffer to exist any Liens, other than Permitted Liens, on any of its assets, now owned or hereafter acquired, or any income or profits therefrom, securing any Indebtedness, unless, at the same time or prior thereto, the Loan is secured equally and rateably with such other Indebtedness.

**10.2 Mergers**

(i) Severstal shall not enter into any reorganisation (by way of a merger, accession, division, separation or transformation, or other bases or procedures for reorganisation contemplated or as may be contemplated from time to time by Russian legislation, as these terms are construed by applicable Russian legislation), and (ii) Severstal shall ensure that, without the prior written consent of the Lender, no Material Subsidiary (A) enters into any reorganisation (whether by way of a merger, accession, division, separation or transformation as these terms are construed by applicable Russian legislation), or (B) in the case of a Material Subsidiary incorporated in a jurisdiction other than Russia participates in any type of corporate reconstruction or other analogous event (as determined under the legislation of the relevant jurisdiction) if (in the case of either (i) or (ii) above) any such reorganisation or other type of corporate reconstruction might have a Material Adverse Effect.

**10.3 Disposals**

**10.3.1** Severstal shall not and shall ensure that its Material Subsidiaries do not (in each case disregarding sales of stock in trade on an arm's-length basis in the ordinary course of business and assignments of or other arrangements over the rights or revenues arising from any Steel or Ferrous Metal Contract) sell, lease, transfer or otherwise dispose of, to a person other than a Subsidiary or Severstal, as the case may be, by one or more transactions or series of transactions (whether related or not), the whole or any part of its revenues or its assets which have the aggregate value in excess of U.S.$150,000,000 or the equivalent thereof in any 12 month period, if such sale, lease, transfer or disposal has a Material Adverse Effect.

**10.3.2** Sub-Clause 10.3.1 above shall not apply to assets not comprising the core business of the Group (being the production and sale of steel and ferrous metal and/or steel and ferrous metal products) (the "**Core Business**").

**10.4 Maintenance of Authorisations**

Severstal shall, and shall procure that each of its Material Subsidiaries shall, take all necessary action to obtain and do or cause to be done all things reasonably necessary, in the opinion of Severstal or the relevant Material Subsidiary, to ensure the continuance of its corporate existence, its business and intellectual property relating to its business and Severstal shall take all necessary action to obtain, and do or cause to be done all things reasonably necessary to ensure the continuance of, all consents, licences, approvals and authorisations, and make or cause to be made all registrations, recordings and filings, which may at any time be required to be obtained or made in the Russian Federation for the execution, delivery or performance of this Agreement or for the validity or enforceability thereof, provided that, in any case if Severstal and/or the relevant Material Subsidiary, as the case may be, can remedy any failure to comply with this Clause 10.4 within 90 days of such failure or of the occurrence of such event, then this covenant shall be deemed not to have been breached.

**10.5 Maintenance of Property**

Severstal shall, and shall ensure that its Material Subsidiaries will, cause all property used in the conduct of its or their business to be maintained and kept in good condition, repair and working order and supplied with all necessary equipment and shall cause to be made all necessary repairs, renewals, replacements, betterments and improvements thereof, all as, in the judgment of Severstal or any Material Subsidiary, may be reasonably necessary so that the business carried on in connection therewith may be properly conducted at all times, provided that if Severstal or any such Material Subsidiary can remedy any failure to comply with the above within 90 days or any failure relates to property with a value not exceeding U.S.$50,000,000 (or its foreign currency equivalent), this covenant shall be deemed not to have been breached.

**10.6 Payment of Taxes and Other Claims**

Severstal shall, and shall ensure that its Material Subsidiaries will, pay or discharge or cause to be paid or discharged, before the same shall become overdue and without incurring penalties, (a) all taxes, assessments and governmental charges levied or imposed upon, or upon the income, profits or property of, Severstal and its Material Subsidiaries and (b) all lawful claims for labour, materials and supplies which, if unpaid, might by law become a Lien (other than a Permitted Lien) upon the property of Severstal or any of its Material Subsidiaries; provided, however, that none of Severstal nor any Material Subsidiary shall be required to pay or discharge or cause to be paid or discharged any such tax, assessment, charge or claim (i) whose amount, applicability or validity is being contested in good faith by appropriate proceedings and for which adequate reserves in accordance with Accounting Standards to which the then most recent published audited consolidated financial statements of Severstal comply, as consistently applied or other appropriate provision has been made or (ii) whose amount, together with all such other unpaid or undischarged taxes, assessments, charges and claims, does not in the aggregate exceed U.S.$50,000,000.

**10.7 Withholding Tax Exemption**

Severstal shall give to the Lender all the assistance it reasonably requires to ensure that, prior to the first interest payment and at the beginning of each calendar year, the Lender can provide Severstal with the documents required under Russian laws for the relief of the Lender from Russian withholding tax in respect of payments hereunder.

**10.8 Maintenance of Insurance**

Severstal shall, and shall ensure that each of its Material Subsidiaries will, keep those of their properties which are of an insurable nature insured with insurers of good standing (as determined in the reasonable judgment of Severstal) against loss or damage to the extent that, in the reasonable judgment of Severstal, property of similar character is usually so insured by corporations in the same jurisdictions similarly situated and owning like properties in the same jurisdictions, provided that if Severstal or any such Material Subsidiary can remedy any failure to comply with the above within 90 days or if such potential losses or risks (which may be assessed by reference to the actual risks and losses borne by Severstal or such Material Subsidiary over the preceding 3 years) do not exceed U.S.$50,000,000 (or its foreign currency equivalent), this covenant shall be deemed not to have been breached.

**10.9 Financial Information**

**10.9.1** Severstal shall deliver to the Lender within six months after the end of each of its financial years, copies of its audited consolidated financial statements for such financial year, prepared in accordance with applicable Accounting Standards applied consistently with the corresponding financial statements for the preceding period.

**10.9.2** Severstal shall deliver to the Lender within three months after the end of the first half-year of each of its financial years, copies of its unaudited consolidated financial statements for that half-year, prepared in accordance with applicable Accounting Standards applied consistently with the corresponding financial statements for the preceding period.

**10.9.3** Severstal shall deliver to the Lender, without undue delay, such additional information regarding the financial position or the business of Severstal and its Subsidiaries as the Lender may reasonably request, including a certificate upon request by the Lender as to the amount of the agreed funding purchased but not cancelled by Severstal (or any Subsidiary of Severstal) and retained by it for its own account or the account of any other company.

**10.9.4** Severstal shall from time to time, on the request of the Lender and without undue delay, furnish the Lender with such information about the business and financial condition of Severstal and its Subsidiaries as the Lender may reasonably request for regulatory compliance purposes, provided that any such request from the Lender shall specify the relevant regulation on the basis of which it is made, and provided further that Severstal may furnish the information under this sub-Clause 10.9.4 in the format used to provide information under or in connection with the Severstal Agreements, unless the Lender certifies that a different format is specified by the relevant regulator.

**10.10 Limitation on Indebtedness**

**10.10.1** Severstal will not, and will not permit any Subsidiary to, Incur, directly or indirectly, any Indebtedness; *provided, however*, that Severstal and any Subsidiary will be entitled to Incur Indebtedness if:

(i) after giving effect to such Incurrence and the application of the proceeds thereof, on a pro forma basis, no Default or Event of Default would occur or be continuing; and

(ii) on the date of such Incurrence and after giving effect thereto on a pro forma basis, the Consolidated Leverage Ratio does not exceed 3.5 to 1.

**10.10.2** Notwithstanding the foregoing Clause 10.10.1, Severstal and its Subsidiaries will be entitled to Incur any or all of the following Indebtedness (each, "**Permitted Indebtedness**"):

(i) intercompany and intra-Group indebtedness owed to and held by Severstal or a Subsidiary of Severstal; *provided, however*, that any subsequent disposition, pledge or transfer of such Indebtedness (other than to Severstal or a Subsidiary of Severstal) shall be deemed, in each case, to constitute the Incurrence of such Indebtedness by the obligor thereon;

(ii) the Loan under this Agreement or any supplemental or amended loan under a supplement or amendment to this Agreement made in order to fund a further issuance by the Lender of securities having identical terms and conditions, term, tenor and rate of interest as, and forming a single fungible series with, the agreed funding;

(iii) Indebtedness outstanding on the Closing Date;

(iv) Indebtedness of Severstal or a Subsidiary Incurred and outstanding on or prior to the date on which such Subsidiary became a Subsidiary of Severstal (other than Indebtedness Incurred in connection with, or to provide all or any portion of the funds or credit support utilised to consummate, the transaction or series of related transactions pursuant to which such Subsidiary became a Subsidiary of Severstal); provided, however, that on the date of such acquisition and after giving pro forma effect thereto, Severstal would have been entitled to Incur at least US$1.00 of additional Indebtedness pursuant to Clause 10.10.1 above;

(v) Refinancing Indebtedness Incurred by Severstal or a Subsidiary in respect of Indebtedness Incurred by Severstal or a Subsidiary of Severstal pursuant to Clause 10.10.1 above or pursuant to sub-Clause (iii), (iv) or (v) of this Clause 10.10.2;

(vi) Hedging Obligations of Severstal or any Subsidiary of Severstal; provided that each Interest Rate Agreement is entered into for the purpose of limiting interest rate risk and all such Hedging Obligations are entered into in the ordinary course of business and not for speculative purposes;

(vii) obligations in respect of performance, bid and surety bonds, completion guarantees, letters of credit, *veksels* (Russian rouble-denominated short-term promissory notes) or similar obligations provided by Severstal or any Subsidiary of Severstal in the ordinary course of business, provided that, upon demand being made under such obligations, such obligations are reimbursed or the Indebtedness thereunder repaid within 30 days following such drawing or occurrence;

(viii) Indebtedness arising from the honouring by a bank or other financial institution of a cheque, draft or similar instrument inadvertently drawn against insufficient funds in the ordinary course of business; provided, however, that such Indebtedness is extinguished within five Business Days of its Incurrence;

(ix) Indebtedness arising from agreements of Severstal or a Subsidiary of Severstal providing for indemnification, adjustment of purchase price or similar obligations, in each case, incurred or assumed in connection with the acquisition or disposition of any business, assets or Capital Stock of Severstal or any Subsidiary of Severstal; provided that (A) the maximum aggregate liability in respect of all such Indebtedness shall at no time exceed the net proceeds (including the Fair Market Value of non-cash consideration) actually received by (or held in escrow as a collateral for such Indebtedness for later release to) Severstal and its Subsidiaries in connection with such disposition (without giving effect to any subsequent changes in value) and (B) such Indebtedness is not reflected on the balance sheet of Severstal or any Subsidiary of Severstal (contingent obligations referred to in a footnote to financial statements and not otherwise reflected on the balance sheet shall not be deemed to be reflected on such balance sheet for purposes of this part (B) of this sub-Clause (x));

(x) Purchase Money Indebtedness Incurred to finance the acquisition by Severstal or a Subsidiary of Severstal of assets in the ordinary course of business;

(xi) Refinancing Indebtedness Incurred to Refinance such Indebtedness (i) having an original maturity at issuance of 180 days or less or (ii) otherwise in an aggregate principal amount which, when added together with the amount of Indebtedness Incurred pursuant to this sub-Clause (xi)(ii) and then outstanding, does not exceed US$100,000,000 provided, however, that if an item of Indebtedness initially Incurred pursuant to this sub-Clause (xi) can subsequently be Incurred pursuant to Clause 10.1.1, such Indebtedness shall be deemed to have been Incurred under Clause 10.1.1 and not under this sub-Clause (x);

(xii) Indebtedness in respect of workers' compensation claims or claims arising under similar legislation, or pursuant to self-insurance obligations and not in connection with the borrowing of money or the obtaining of advances or credit;

(xiii) customer deposits and advance payments received from customers in the ordinary course of business; and

(xiv) other Indebtedness of Severstal and its Subsidiaries in an aggregate principal amount which, when taken together with the principal amount of all other Indebtedness Incurred pursuant to this Clause (xiii) and then outstanding, will not exceed U.S.$300,000,000 at any time outstanding provided, however, that if an item of Indebtedness initially Incurred pursuant to this sub-Clause (xiv) can subsequently be Incurred pursuant to Clause 10.1.1, such Indebtedness shall be deemed to have been Incurred under Clause 10.1.1 and not under this sub-Clause (x);

**10.10.3** Notwithstanding the foregoing, Severstal will not Incur any Indebtedness pursuant to Clause 10.10 if the proceeds thereof are used, directly or indirectly, to Refinance any Subordinated Obligations of Severstal unless such Indebtedness shall be subordinated to the Loan to at least the same extent as such Subordinated Obligations.

**10.10.4** For purposes of determining compliance with this covenant:

(i) in the event that an item of Indebtedness (or any portion thereof) meets the criteria of more than one of the types of Indebtedness described in Clauses 10.10.1 or 10.10.2, Severstal, in its sole discretion, will classify such item of Indebtedness (or any portion thereof) at the time of Incurrence and will only be required to include the amount and type of such Indebtedness in one of the above sub-Clauses; and

(ii) Severstal will be entitled to divide and classify an item of Indebtedness in more than one of the types of Indebtedness described in Clauses 10.10.1 or 10.10.2 and may change the classification of an item of Indebtedness (or any portion thereof) to any other type of Indebtedness described in Clauses 10.10.1 or 10.10.2 at any time. The outstanding principal amount of any particular Indebtedness shall be counted only once and any obligations arising under any guarantees, Lien, letter of credit or similar instrument supporting such Indebtedness shall not be double counted.

**10.10.5** For purposes of determining compliance with any U.S. dollar denominated restriction on the Incurrence of Indebtedness where the Indebtedness Incurred is denominated in a different currency, the amount of such Indebtedness will be the U.S. Dollar Equivalent determined on the date of the Incurrence of such Indebtedness; *provided, however*, that if any such Indebtedness denominated in a different currency is subject to a Currency Agreement with respect to U.S. dollars covering all principal, premium, if any, and interest payable on such Indebtedness, the amount of such Indebtedness expressed in U.S. dollars will be as provided in such Currency Agreement. The principal amount of any Refinancing Indebtedness Incurred in the same currency as the Indebtedness being Refinanced will be the U.S. Dollar Equivalent, as appropriate, of the Indebtedness Refinanced, except to the extent that (A) such U.S. Dollar Equivalent was determined based on a Currency Agreement, in which case the principal amount of such Refinancing Indebtedness will be determined in accordance with the preceding sentence, and (B) the principal amount of the Refinancing Indebtedness exceeds the principal amount of the Indebtedness being Refinanced, in which case the U.S. Dollar Equivalent of such excess, as appropriate, will be determined on the date such Refinancing Indebtedness is Incurred. Notwithstanding any other provision of this covenant, the maximum amount that Severstal or a Subsidiary of Severstal may Incur pursuant to this covenant shall not be deemed to be exceeded, with respect to outstanding Indebtedness, due solely as a result of fluctuations in the exchange rates of currencies.

**10.11 Certificates**

Severstal shall deliver to the Lender within 20 days of any written request by the Lender: (i) an Officers' Certificate as to any fact or matter *prima facie* within the knowledge of Severstal, as sufficient evidence thereof and (ii) a like certificate to the effect that any particular dealing or transaction or step or thing is, in the opinion of the Person so certifying, expedient as sufficient evidence that it is expedient, and (iii) written notice in the form of an Officers' Certificate substantially in the form set out in Schedule 1 confirming whether (a) on a pro forma basis the Consolidated Leverage Ratio exceeds 3.5 to 1 and (b) any Default or Event of Default has occurred and, if it has occurred, what action Severstal is taking or proposes to take with respect thereto.

**10.12 Change of business**

Severstal shall procure that no material change is made to the Core Business as conducted as at the date of this Agreement.

**10.13 Ranking of Claims**

Severstal shall ensure that at all times the claims of the Lender against it under this Agreement rank at least *pari passu* with the claims of all its other unsecured creditors save those whose claims are preferred by any bankruptcy, insolvency, liquidation or similar laws of general application.

**11 Events of Default**

**11.1 Events of Default**

If one or more of the following events of default (each, an "**Event of Default**") shall occur, the Lender shall be entitled to the remedies set forth in Clause 11.3:

**11.1.1** Severstal fails to pay any amount payable hereunder as and when such amount becomes payable in the currency and in the manner specified herein, provided such failure to pay continues for more than five Business Days.

**11.1.2** Severstal fails to perform or observe any covenant or agreement contained herein to be performed or observed by it, provided such failure continues for more than 30 Business Days.

**11.1.3** Any representation or warranty of Severstal or any statement deemed to be made by Severstal in this Agreement or any other document, certificate or notice delivered by

Severstal in connection with this Agreement, the agreed funding agreements or the agreed funding proves to have been inaccurate, incomplete or misleading in any material respect in the opinion of the Lender at the time it was made or repeated or deemed to have been made or repeated, provided that any such event under this Clause 11.1.3 remains unremedied for more than 30 Business Days.

**11.1.4** Either:

(i) any Indebtedness of Severstal or any of its Material Subsidiaries is not paid when due (after the expiry of any applicable grace period); or

(ii) any such Indebtedness becomes due and payable prior to its stated maturity otherwise than at the option of Severstal or (as the case may be) the relevant Material Subsidiary or (provided that no event of default, howsoever described, has occurred) any Person entitled to such Indebtedness;

provided that the amount of Indebtedness referred to in sub-paragraph (i) and/or sub-paragraph (ii) above, individually or in the aggregate, exceeds U.S.$50,000,000 (or its equivalent in any other currency or currencies).

**11.1.5** The occurrence of any of the following events: (i) any of Severstal, or any of its Material Subsidiaries seeking or consenting to the introduction of proceedings for its liquidation or the appointment of a liquidation commissioner (*likvidatsionnaya komissiya*) or a similar officer of any of Severstal, or any of its Material Subsidiaries as the case may be; (ii) the presentation or filing of a petition in respect of any of Severstal or its Material Subsidiaries in any court, arbitration court or before any Agency alleging, or for, the bankruptcy, insolvency, dissolution, liquidation (or any analogous proceedings) of any of Severstal or its Material Subsidiaries, unless such petition is demonstrated to the reasonable satisfaction of the Lender to be vexatious or frivolous; (iii) the institution of the supervision (*nablyudeniye*), financial rehabilitation (*finansovoye ozdorovlenie*), external management (*vneshneye upravleniye*), bankruptcy management (*konkursnoye proizvodstvo*) over Severstal or any of its Material Subsidiaries, (iv) the entry by Severstal or any of its Material Subsidiaries into, or the agreeing by Severstal or any of its Material Subsidiaries to enter into, amicable settlement (*mirovoe soglashenie*) with its creditors, as such terms are defined in the Federal Law of Russia No. 127-FZ "On Insolvency (Bankruptcy)" dated 26 October, 2002 (as amended or replaced from time to time); and/or (v) any judicial liquidation in respect of Severstal or any of its Material Subsidiaries.

**11.1.6** Severstal or any of its Material Subsidiaries is unable or admits inability to pay its debts as they fall due, generally suspends making payments on any of its debts or, by reason of actual or anticipated financial difficulties, commences negotiations with one or more of its creditors with a view to rescheduling any of its Indebtedness; the value of the assets of any of Severstal or its Material Subsidiaries is less than its liabilities; and/or a moratorium is declared in respect of any Indebtedness of any of Severstal or its Material Subsidiaries.

**11.1.7** Any expropriation, attachment, sequestration, execution or distress is levied against, or an encumbrancer takes possession of or sells, the whole or any material part of, the property, undertaking, revenues or assets of Severstal or any of its Material Subsidiaries.

**11.1.8** Any governmental or agency authorisation necessary for the performance of any obligation of Severstal under this Agreement fails to be in full force and effect and such failure continues for more than 30 Business Days.

**11.1.9** Any government, Agency or court takes any action that, in the reasonable opinion of the Lender, has a Material Adverse Effect.

**11.1.10** The shareholders of Severstal shall have approved any plan of liquidation or dissolution of Severstal.

**11.1.11** The aggregate amount of unsatisfied judgments, decrees or orders of courts or other appropriate law-enforcement bodies for the payment of money against Severstal and other Material Subsidiaries in the aggregate exceeds U.S.$75,000,000, or the equivalent thereof in any other currency or currencies, which in each case has not within 60 days of the entry thereof been appealed, discharged, waived or the execution thereof stayed.

**11.1.12** At any time it is or becomes unlawful for Severstal to perform or comply with any or all of its obligations under this Agreement or any of such obligations (subject as provided in sub-Clause 9.1.2) are not, or cease to be, legal, valid, binding and enforceable and any such event under this Clause 11.1.12 remains unremedied for more than 30 Business Days.

**11.1.13** the Group ceases to carry on the Core Business that it carried on at the date hereof.

**11.1.14** Severstal repudiates this Agreement or the agreed funding agreements to which it is a party or evidences an intention to repudiate this Agreement or the agreed funding agreements to which it is a party.

**11.1.15** Any event occurs which under the laws of any relevant jurisdiction has an analogous effect to any of the events referred to in any of the foregoing sub-Clauses.

**11.2 Notice of Default**

Severstal shall deliver to the Lender within 30 days after the occurrence thereof, written notice in the form of an Officers' Certificate of any event which is, or with the giving of notice or the lapse of time, or both, would become, an Event of Default, its status and what action Severstal is taking or proposes to take with respect thereto.

**11.3 Default Remedies**

If any Event of Default shall occur and be continuing, the Lender may, by notice to Severstal, (a) declare the obligations of the Lender hereunder to be terminated, whereupon such obligations shall terminate, and (b) declare all amounts payable hereunder by Severstal that would otherwise be due after the date of such termination to be immediately due and payable, whereupon all such amounts shall become immediately due and payable, all without diligence, presentment, demand of payment, protest or notice of any kind, which are expressly waived by Severstal; provided, however, that if any event of any kind referred to in Clause 11.1.5 or 11.1.6 occurs, the obligations of the Lender hereunder shall immediately terminate, and all amounts payable hereunder by Severstal that would otherwise be due after the occurrence of such event shall become immediately due and payable, all without diligence, presentment, demand of payment, protest or notice of any kind, which are expressly waived by Severstal.

**11.4 Right of Set-off**

If any amount payable by Severstal hereunder is not paid as and when due, Severstal authorises the Lender to proceed, to the fullest extent permitted by applicable law, without prior notice, by right of set-off, banker's lien, counterclaim or otherwise, against any assets of Severstal in any currency that may at any time be in the possession of the Lender, at any branch or office, to the full extent of all amounts payable to the Lender hereunder.

**11.5 Rights Not Exclusive**

The rights provided for herein are cumulative and are not exclusive of any other rights, powers, privileges or remedies provided by law.

**12 Indemnity**

**12.1 Indemnification**

Severstal undertakes to the Lender, that if the Lender or any of its Affiliates, each director, officer, employee or agent of the Lender and each Person controlling the Lender within the meaning of the United States securities laws (each an "**indemnified party**") incurs any loss, liability, cost, claim, charge, expense (including without limitation taxes, legal fees, costs and expenses), demand or damage (a "**Loss**") as a result of or in connection with the Loan, this Agreement (or enforcement thereof), and/or the issue, constitution, sale, listing and/or enforcement of the agreed funding and/or the agreed funding being outstanding, Severstal shall pay to the Lender on demand an amount equal to such Loss and all costs, charges and expenses which it or any indemnified party may pay or incur in connection with investigating, disputing or defending any such action or claim as such costs, charges and expenses are incurred unless such Loss was either caused by such indemnified party's negligence or wilful misconduct or arises out of a breach of the representations and warranties of the Lender contained in this Agreement and the agreed funding agreements. The Lender shall not have any duty or obligation whether as fiduciary or trustee for any indemnified party or otherwise, to recover any such payment or to account to any other Person for any amounts paid to it under this Clause.

**12.2 Independent Obligation**

Clause 12.1 constitutes a separate and independent obligation of Severstal from its other obligations under or in connection with this Agreement or any other obligations of Severstal in connection with the issue of the agreed funding by the Lender and shall not affect, or be construed to affect, any other provision of this Agreement or any such other obligations.

**12.3 Evidence of Loss**

A certificate of the Lender setting forth the amount of losses, expenses and liabilities described in Clause 12.1 and specifying in full detail the basis therefor shall be conclusive evidence of the amount of such losses, expenses and liabilities.

**12.4 Currency Indemnity**

Each reference in this Agreement to Dollars is of the essence. To the fullest extent permitted by law, the obligation of Severstal in respect of any amount due in Dollars under this Agreement shall, notwithstanding any payment in any other currency (whether pursuant to a judgment or otherwise), be discharged only to the extent of the amount in Dollars that the party entitled to receive such payment may, acting reasonably in accordance with normal banking procedures, purchase with the sum paid in such other currency (after any premium and costs of exchange) on the Business Day immediately following the day on which such party receives such payment. If the amount in Dollars that may be so purchased for any reason falls short of the amount originally due, Severstal hereby agrees to indemnify the Lender against any such deficiency in Dollars. Any obligation of Severstal not discharged by payment in Dollars shall, to the fullest extent permitted by applicable law, be due as a separate and independent obligation and, until discharged as provided herein, shall continue in full force and effect.

**13 Survival**

The obligations of Severstal pursuant to Clauses 6.2, 6.3, 12 and 14.1 shall survive the execution and delivery of this Agreement, the drawdown of the Facility and the repayment of the Loan, in each case by Severstal.

**14 General**

**14.1 Stamp Duties**

**14.1.1** Severstal shall pay all stamp, registration and documentary taxes or similar charges (if any) imposed by any Person in the Russian Federation or Luxembourg which may be payable or determined to be payable in connection with the execution, delivery, performance, enforcement, or admissibility into evidence of this Agreement and shall indemnify the Lender against any and all costs and expenses which may be incurred or suffered by the Lender with respect to, or resulting from, delay or failure to pay such taxes or similar charges.

**14.1.2** Severstal agrees that if the Lender incurs a liability to pay any stamp, registration and documentary taxes or similar charges (if any) imposed by any Person in the Russian Federation or Luxembourg which may be payable or determined to be payable in connection with the execution, delivery, performance, enforcement, or admissibility into evidence of this Agreement, Severstal shall reimburse the Lender on demand an amount equal to such stamp or other documentary taxes or duties and shall indemnify on demand the Lender against any and all costs and expenses which may be incurred or suffered by the Lender with respect to, or resulting from, delay or failure by Severstal to procure the payment of such taxes or similar charges.

**14.2 Waivers**

No failure to exercise and no delay in exercising, on the part of the Lender or Severstal, any right, power or privilege hereunder and no course of dealing between Severstal and the Lender shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power or privilege preclude any other or further exercise thereof, or the exercise of any other right, power or privilege. The rights and remedies herein provided are cumulative and not exclusive of any rights or remedies provided by applicable law.

**14.3 Prescription**

In the event that any agreed funding becomes void pursuant to the conditions of such agreed funding, the Lender shall forthwith repay to Severstal the principal amount of such agreed funding subject to the Lender having previously received from Severstal a corresponding amount in respect of principal pursuant to this Agreement.

**15 Notices**

All notices, requests, demands, invoices, acts of acceptance or other communications to or upon the respective parties hereto shall be given or made in the English language by fax or or by hand or by courier and shall be deemed to have been duly given or made, in the case of a fax, when the relevant delivery receipt is received by the sender and, in the case of delivery by hand or courier, at the time of delivery, as follows:

**15.1.1** if to Severstal:

2/3 K. Tsetkin Street
127299 Moscow
Russia

Fax: +7 495 150 8800
Attention: Chief Financial Officer

**15.1.2** if to the Lender:

Steel Capital S.A.
2, Boulevard Konrad Adenauer
L-1115 Luxembourg

Fax: +352 421 22 449
Attention: Board of Directors

or to such other address or facsimile number as any party may hereafter specify in writing to the other.

**16 Assignment**

**16.1 General**

This Agreement shall inure to the benefit of and be binding upon the parties, their respective successors and any permitted assignee or transferee of some or all of a party's rights or obligations under this Agreement. Any reference in this Agreement to any party shall be construed accordingly and, in particular, references to the exercise of any rights, benefits and discretions by, or the making of any determinations (including forming an opinion) by, and the delivery of notices or other information to, the Lender, following notification to Severstal of the assignment referred to in Clause 16.3, shall be references to the exercise of such rights, benefits or discretions by or on behalf of, or the making of any determinations (including forming an opinion) by, and the delivery of notices or other information to, the agreed funding source, or any assignee or transferee appointed in connection with the agreed funding source, without regard to the Lender.

**16.2 By Severstal**

Severstal shall not be entitled to assign or transfer, in whole or in part, any of its rights and benefits or obligations hereunder to any other person.

**16.3 By the Lender**

Subject to the provisions of any agreed funding agreement, the Lender may not assign or transfer, in whole or in part, any of its rights and benefits or obligations under this Agreement other than the Reserved Rights except (i) the charge by way of first fixed charge granted by the Lender to or on behalf of the agreed funding source of certain of the Lender's rights and benefits under this Agreement and (ii) the absolute assignment by the Lender to or on behalf of the agreed funding source of certain rights, interests and benefits under this Agreement, in each case, pursuant to the agreed funding agreement.

**17 Law and Jurisdiction**

**17.1 Choice of Law**

This Agreement shall be governed by, and construed in accordance with, the laws of England.

**17.2 Arbitration**

**17.2.1** Subject to Clause 17.3, any dispute arising out of or in connection with this Agreement (including a dispute regarding the existence, validity or termination of this Agreement) (a "**Dispute**") shall be referred to and finally resolved by arbitration under the LCIA Arbitration Rules (the "**Rules**").

**17.2.2** The arbitral tribunal shall consist of three arbitrators. The claimant(s), irrespective of number, shall nominate jointly one arbitrator; the respondent(s), irrespective of number, shall nominate jointly the second arbitrator; and a third arbitrator, who shall serve as Chairman, shall be selected by the two party nominated arbitrators. For the avoidance of doubt, the parties to this agreement agree for the purpose of Article 8.1 of the LCIA Rules, that the claimant(s), irrespective of number, and the respondent(s), irrespective of number, constitute two separate sides for the formation of the arbitral tribunal.

**17.2.3** In the event that the claimant(s) fail to nominate an arbitrator in accordance with the Rules, such arbitrator shall be nominated by the LCIA Court as soon as possible, preferably within 15 days of such failure. In the event that the respondent(s) or both the claimant(s) and the respondent(s) fail to nominate an arbitrator within the time limits specified in the Rules, all three arbitrators shall be nominated and appointed by the LCIA Court as soon as possible, preferably within 15 days of such failure, and such arbitrators shall then designate one amongst them as chairman.

**17.2.4** The seat of arbitration shall be London, England and the language of the arbitration shall be English.

**17.2.5** Where disputes arise under this Agreement and any other agreed funding agreement which, in the reasonable opinion of the first arbitral tribunal to be appointed in any of the disputes, are so closely connected that it is expedient for them to be resolved in the same proceedings, that arbitral tribunal shall have the power to order that the proceedings to resolve that dispute shall be consolidated with those to resolve any of the other disputes (whether or not proceedings to resolve those other disputes have yet been instituted), provided that no date for the hearing on the merits of the dispute in the first arbitration has been fixed. If the first arbitral tribunal so orders, the parties to each dispute which is a subject of its order shall be treated as having consented to that dispute being finally decided:

(i) by the arbitral tribunal that ordered the consolidation unless the LCIA Court decides that any member of such tribunal would not be suitable or impartial; and

(ii) in accordance with the procedure, at the seat and in the language specified in the arbitration agreement in this Agreement or the agreed funding agreement under which the arbitral tribunal that ordered the consolidation was appointed, save as otherwise agreed by all parties to the consolidated proceedings or, in the absence of such agreement, ordered by the arbitral tribunal in the consolidated proceedings.

For the avoidance of doubt, the parties to any other agreed funding agreement are intended by the parties to this Agreement to have the right under the Contracts (Rights of Third Parties) Act 1999 to enforce the terms of this Clause 17.2.5.

**17.2.6** The parties exclude the jurisdiction of the courts under Sections 45 and 69 of the Arbitration Act 1996.

**17.3 Courts**

**17.3.1** Before any arbitrator or arbitral tribunal has been appointed to determine a Dispute, the Lender may by notice in writing to Severstal require that all Disputes or a specific Dispute be heard by a court of law. If such notice is duly given, the Dispute to which such notice refers shall be determined in accordance with Clause 17.3.2.

**17.3.2** (i) With respect to any Dispute heard in a court of law, the courts of England have exclusive jurisdiction to settle such Disputes.

(ii) The parties hereto agree that the courts of England are the most appropriate and convenient courts to settle Disputes and accordingly no party will argue to the contrary.

(iii) This Clause is for the benefit of the Lender only. Nothing contained in this Agreement shall limit the right of the Lender to take Disputes against Severstal in any other court of competent jurisdiction to the extent permitted by any applicable law, nor shall the taking of Disputes in connection with this Agreement in one or more jurisdictions preclude the Lender from the taking of Disputes in any other jurisdiction (whether concurrently or not) or in any other court of competent jurisdiction in connection with this Agreement to the extent permitted by any applicable law.

(iv) Each of Severstal and the Lender irrevocably appoints Freshfields Bruckhaus Deringer LLP at its London office (the "**Agent**"), now of 65 Fleet Street, London, EC4Y 1HS, as its agent to accept service of process in England. If such person is not or ceases to be effectively appointed to accept service of process on behalf of either Severstal or the Lender, the relevant party (the "**First Party**"), shall, on written demand by the other party (the "**Second Party**"), appoint a further person in England to accept service of process on its behalf by written notice to the other party and failing such appointment, within 15 calendar days, the Second Party shall be entitled to appoint such a person by written notice to the First Party. Nothing in this clause shall affect the right of the Second Party to serve process in any other manner permitted by law.

**17.4 Immunity**

To the extent that Severstal or the Lender may now or hereafter be entitled, in any jurisdiction in which any legal action or proceeding may at any time be commenced with respect to this Agreement, to claim for itself or any of its undertaking, properties, assets or revenues present or future any immunity (sovereign or otherwise) from suit, jurisdiction of any court, attachment prior to judgment, attachment in aid of execution of a judgment, execution of a judgment or award or from set-off, banker's lien, counterclaim or any other legal process or remedy with respect to its obligations under this Agreement and/or to the extent that in any such jurisdiction there may be attributed to Severstal or the Lender any such immunity (whether or not claimed), Severstal and the Lender hereby irrevocably agree not to claim, and hereby waive, any such immunity.

**18 Severability**

In case any provision in or obligation under this Agreement shall be invalid, illegal or unenforceable in any jurisdiction, the validity, legality and enforceability of the remaining provisions or obligations, or of such provision or obligation in any other jurisdiction, shall not in any way be affected or impaired thereby.

**19 Contracts (Rights of Third Parties) Act 1999**

A person who is not a party to this Agreement has no right under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Agreement except to the extent expressly provided herein, including in Clauses 6.1 and 17.2.5.

**20 Language**

The language which governs the interpretation of this Agreement is the English language. This Agreement will be signed in the English language and translated into Russian and may be signed in the Russian language. In the event of any discrepancies between the English and Russian versions of this Agreement or any dispute regarding the interpretation of any provision in the English or Russian versions of this Agreement, the English version of this Agreement shall prevail and questions of interpretation shall be addressed solely in the English language.

**21 Amendments**

Except as otherwise provided by its terms, this Agreement may not be varied except by an agreement in writing signed by the parties.

**22 Counterparts**

This Agreement may be executed in any number of counterparts and by different parties hereto in separate counterparts, each of which when so executed shall be deemed to be an original and all of which when so executed shall constitute one and the same binding agreement between the parties.

**In witness whereof**, the parties hereto have caused this Agreement to be executed on the date first written above.

## Schedule 1

## Form of Officers' Certificate

To: Steel Capital S.A.

From: OAO Severstal

Dated:

Dear Sirs

**OAO Severstal — U.S.$1,250,000,000 Loan Agreement dated 25 July 2008 (the "Loan Agreement")**

**1** We refer to the Loan Agreement. This is an Officers' Certificate for the purposes of Clause 10.11 of the Loan Agreement.

**2** We confirm that on the aggregate amount of Consolidated Indebtedness on a pro forma basis was and on the aggregate amount of EBITDA for the period of the two most recent consecutive semi-annual periods for which financial statements have been delivered under Clause 10.9 was . Therefore the Consolidated Leverage Ratio on a pro forma basis [did/did not] exceed 3.5 to 1 and the covenant contained in sub-Clause 10.10 [has/has not] been complied with; and

**3** We confirm that the following Subsidiaries are Material Subsidiaries:

[*specify relevant Subsidiaries*]

**4** We confirm that no Default or Event of Default has occurred(1).

for and on behalf of OAO Severstal

Signed:

| | |
|---|---|
| [principal executive officer/<br>principal accounting officer/<br>principal financial officer] of OAO Severstal | [officer]<br>of<br>OAO Severstal |

(1) If this statement cannot be made, the certificate should identify any Default or Event of Default that is continuing and the steps, if any, being taken to remedy it.

## TERMS AND CONDITIONS OF THE NOTES

*The following is the text of the Terms and Conditions of the Notes, which will be attached to the Notes in definitive form (if any) and (subject to the provisions thereof) will apply to the Global Certificates.*

The US$1,250,000,000 9.75 percent Loan Participation Notes due 29 July 2013 (the "**Notes**" which expression includes any further Notes issued pursuant to Condition 15 and forming a single series therewith) of Steel Capital SA, a company organised and existing as a "société anonyme" under the laws of the Grand Duchy of Luxembourg, having its registered office at 2, Boulevard Konrad Adenauer, L-1115 Luxembourg, registered with the Luxembourg Register of Commerce and Companies under number B116975 (the "**Issuer**") are constituted by, are subject to, and have the benefit of, a trust deed (the "**Trust Deed**", which expression includes such trust deed as from time to time modified in accordance with the provisions therein contained and any deed or other document expressed to be supplemental thereto, as from time to time so modified) dated 29 July 2008 and made between the Issuer and Citibank, N.A., London Branch (the "**Trustee**", which expression shall include any trustee or trustee for the time being of the Trust Deed) as trustee for the Noteholders (as defined below).

The Issuer has authorised the creation, issue and sale of the Notes for the sole purpose of financing a US$1,250,000,000 five-year loan (the "**Loan**") to OAO Severstal (an open joint stock company established under the laws of the Russian Federation) (the "**Borrower**"). The terms of the Loan are recorded in a loan agreement (the "**Loan Agreement**") dated 25 July 2008 between the Issuer and the Borrower.

In each case where amounts of principal, interest and additional amounts (if any) are stated herein or in the Trust Deed to be payable in respect of the Notes, the obligations of the Issuer to make any such payment shall constitute an obligation only to account to the Noteholders on each date upon which such amounts of principal, interest and additional amounts (if any) are due in respect of the Notes, for an amount equivalent to sums of principal, interest and additional amounts (if any) actually received by or for the account of the Issuer pursuant to the Loan Agreement, less any amounts in respect of the Reserved Rights (as defined below). Noteholders must therefore rely solely and exclusively on the covenant to pay under the Loan Agreement and the credit and financial standing of the Borrower. Noteholders shall have no recourse (direct or indirect) to any other asset of the Issuer.

The Issuer has charged by way of first fixed charge in favour of the Trustee certain of its rights and interests as lender under the Loan Agreement as security for its payment obligations in respect of the Notes and under the Trust Deed (the "**Charge**") and has assigned absolutely certain other rights under the Loan Agreement to the Trustee (the "**Assigned Rights**" and, together with the Charge, the "**Security Interests**") in each case excluding the Reserved Rights. "**Reserved Rights**" are the rights excluded from the Charge and the Assigned Rights, being all and any rights, interests and benefits in respect of the obligations of the Borrower under Clauses 3.2, 5.3 (other than the right to receive any amount payable under such Clause), 6.2 (to the extent that the Borrower shall reimburse the Issuer on demand for any amount paid by the Issuer in respect of taxes, penalties or interest), 6.3 (to the extent that the Issuer has received amounts to which the Noteholders are not entitled), 6.4, 6.6, 6.8, 6.9, 8, 10.7 and 10.9.4 of the Loan Agreement.

In certain circumstances, the Trustee can (subject to it being indemnified and/or secured to its satisfaction) be required by Noteholders holding in aggregate at least one quarter of the principal amount of the Notes outstanding or by an Extraordinary Resolution (as defined in the Trust Deed) of the Noteholders to exercise certain of its powers under the Trust Deed (including those arising under the Security Interests).

Payments in respect of the Notes will be made (subject to the receipt of the relevant funds from the Borrower) pursuant to an agency agreement (the "**Agency Agreement**") dated 25 July 2008 and made between the Borrower, the Issuer, Citigroup Global Markets Deutschland AG & Co. KGaA, as the registrar (the "**Registrar**", which expressions shall include any successors), Citibank, N.A., London Branch, as the principal paying agent (the "**Principal Paying Agent**", which expressions shall include any successors), and the transfer agents and paying agents named therein (the "**Transfer Agents**" and "**Paying Agents**" respectively, which expressions shall include any successors) and the Trustee.

Copies of the Trust Deed, the Loan Agreement and the Agency Agreement are available for inspection by Noteholders during normal business hours at the principal office of the Trustee being, at the date hereof, Citigroup Centre, 33 Canada Square, Canary Wharf, London E14 5LB, England and at the Specified Office of the Principal Paying Agent.

Certain provisions of these terms and conditions (the "**Conditions**") are summaries or restatements of, and are subject to, the detailed provisions of the Trust Deed, the Loan Agreement (the form of which is scheduled to and incorporated in the Trust Deed) and the Agency Agreement. Noteholders are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions thereof.

**1. Status**

The sole purpose of the issue of the Notes is to provide the funds for the Issuer to finance the Loan. The Notes constitute the obligation of the Issuer to apply the proceeds from the issue of the Notes solely for financing the Loan and to account to the Noteholders for an amount equivalent to sums of principal, interest and additional amounts (if any) actually received by or for the account of the Issuer pursuant to the Loan Agreement, less any amount in respect of Reserved Rights.

The Trust Deed provides that payments in respect of the Notes equivalent to the sums actually received by or for the account of the Issuer by way of principal, interest or additional amounts (if any) pursuant to the Loan Agreement, less any amount in respect of the Reserved Rights, will be made pro rata among all Noteholders, on the date of, and in the currency of, and subject to the conditions attaching to, the equivalent payment pursuant to the Loan Agreement. The Issuer shall not be liable to make any payment in respect of the Notes other than as expressly provided herein and in the Trust Deed. As provided therein, the Issuer shall be under no obligation to exercise in favour of the Noteholders any rights of set-off or of banker's lien or to combine accounts or counterclaim that may arise out of other transactions between the Issuer and the Borrower.

Noteholders have notice of, and have accepted, these Conditions and the contents of the Trust Deed, the Agency Agreement and the Loan Agreement. It is hereby expressly provided that, and Noteholders are deemed to have accepted that:

(a) neither the Issuer nor the Trustee makes any representation or warranty in respect of, or shall at any time have any responsibility for, or, save as otherwise expressly provided in the Trust Deed, the Loan Agreement (in the case of the Issuer) or in paragraph (f) below, liability or obligation in respect of the performance and observance by the Borrower of its obligations under the Loan Agreement or the recoverability of any sum of principal or interest (or any additional amounts) due or to become due from the Borrower under the Loan Agreement;

(b) neither the Issuer nor the Trustee shall at any time have any responsibility for, or obligation or liability in respect of, the condition (financial or otherwise), creditworthiness, affairs, status, nature or prospects of the Borrower;

(c) neither the Issuer nor the Trustee shall at any time be liable for any representation or warranty or any act, default or omission of the Borrower under or in respect of the Loan Agreement;

(d) neither the Issuer nor the Trustee shall at any time have any responsibility for, or liability or obligation in respect of, the performance and observance by the Principal Paying Agent, the Paying Agents, the Registrar or the Transfer Agents of their respective obligations under the Agency Agreement;

(e) the financial servicing and performance of the terms of the Notes depend solely and exclusively upon performance by the Borrower of its obligations under the Loan Agreement and its covenants, credit and financial standing. The Borrower has represented and warranted to the Issuer in the Loan Agreement that the Loan Agreement constitutes a legal, valid and binding obligation of the Borrower; and

(f) the Issuer and the Trustee shall be entitled to rely on self-certification of the Borrower (and, where applicable, certification by third parties) as a means of monitoring whether the Borrower is complying with its obligations under the Loan Agreement and shall not otherwise be responsible for investigating any aspect of the Borrower's performance in relation thereto and, subject as further provided in the Trust Deed, neither the Issuer as lender under the Loan Agreement nor the Trustee will be liable for any failure to make the usual or any investigations which might be made by a lender or a security holder (as applicable) in relation to the property which is the subject of the Trust Deed and held by way of security for the Notes, and shall not be bound to enquire into or be liable for any defect or failure in the right or title of the Issuer to the property which is subject to the Security Interests whether such defect or failure was known to the Trustee or might have been discovered upon examination or enquiry or whether capable of remedy or not, nor will it have any liability for the enforceability of the security created by the Security Interests whether as a result of any failure, omission or defect in registering or filing or otherwise protecting or perfecting such security; the Trustee has no responsibility for the value of such security.

Under the Trust Deed, the obligations of the Issuer in respect of the Notes rank *pari passu* and rateably without any preference among themselves.

In the event that the payments under the Loan Agreement are made by the Borrower to, or to the order of, the Trustee or (subject to the provisions of the Trust Deed) the Principal Paying Agent, they will *pro tanto* satisfy the obligations of the Issuer in respect of the Notes.

Save as otherwise expressly provided herein and in the Trust Deed, no proprietary or other direct interest in the Issuer's right under or in respect of the Loan Agreement or the Loan exists for the benefit of the Noteholders. Subject to the terms of the Trust Deed, no Noteholder will have any entitlement to enforce the Loan Agreement or direct recourse to the Borrower except through action by the Trustee pursuant to the Charge and the assignment of the Assigned Rights granted to the Trustee in the Trust Deed. Neither the Issuer nor, following the enforcement of the Security Interests created in the Trust Deed, the Trustee shall be required to take proceedings to enforce payment under the Loan Agreement unless it has been indemnified and/or secured by the Noteholders to its satisfaction.

### 2. Form And Denomination

The Notes are issued in registered form in the denomination of US$100,000 and integral multiples of US$1,000 in excess thereof (each an "**Authorised Holding**").

### 3. Register, Title And Transfers

#### (a) Register

The Registrar will maintain outside the United Kingdom a register (the "**Register**") in respect of the Notes in accordance with the provisions of the Agency Agreement. The Registrar will provide to the Issuer a copy of the Register as soon as possible after each change to the register. In these Conditions the "holder" of a Note means the person in whose name such Note is for the time being registered in the Register (or, in the case of a joint holding, the first named thereof) and "**Noteholder**" shall be construed accordingly. A certificate (each a "**Certificate**") will be issued to each Noteholder in respect of its registered holding. Each Certificate will be serially numbered with an identifying number which will be recorded in the Register.

#### (b) Title

The holder of each Note shall (except as otherwise required by law) be treated as the absolute owner of such Note for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any other interest therein, any writing on the Certificate relating thereto (other than the endorsed form of transfer) or any notice of any previous loss or theft of such Certificate) and no person shall be liable for so treating such holder.

#### (c) Transfers

Subject to paragraphs (f) and (g) below, a Note may be transferred upon surrender of the relevant Certificate, with the endorsed form of transfer duly completed, at the Specified Office of the Registrar or any Transfer Agent, together with such evidence as the Registrar or the Transfer Agent may reasonably require to prove the title of the transferor and the authority of the individuals who have executed the form of transfer provided, however, that a Note may not be transferred unless the principal amount of Notes transferred and (where not all of the Notes held by a holder are being transferred) the principal amount of the balance of Notes not transferred are Authorised Holdings. Where not all the Notes represented by the surrendered Certificate are the subject of the transfer, a new Certificate in respect of the balance of the Notes will be issued to the transferor.

#### (d) Registration And Delivery Of Certificates

Within five business days of the surrender of a Certificate in accordance with paragraph (c) above, the Registrar will register the transfer in question and deliver a new Certificate of a like principal amount to the Notes transferred to each relevant holder at its specified office or (at the request and risk of such relevant holder) by uninsured first class mail (airmail if overseas) to the address specified for the purpose by such relevant holder. In this paragraph, "**business day**" means a day on which commercial banks are open for business (including dealings in foreign currencies) in the city where the Registrar or the relevant Transfer Agent has its specified office.

**(e) No Charge**

The transfer of a Note will be effected without charge by or on behalf of the Issuer, the Registrar or the relevant Transfer Agent but against such indemnity as the Registrar or (as the case may be) the Transfer Agent may require in respect of any tax or other duty of whatsoever nature which may be levied or imposed in connection with such transfer.

**(f) Closed Periods**

The Noteholders may not require transfers to be registered during the period of 15 days ending on the due date for any payment of principal or interest in respect of the Notes.

**(g) Regulations Concerning Transfers And Registration**

All transfers of Notes and entries on the Register are subject to the detailed regulations concerning the transfer of Notes scheduled to the Agency Agreement. The regulations may be changed by the Issuer with the prior written approval of the Trustee and the Registrar. A copy of the current regulations will be mailed (free of charge) by the Registrar to any Noteholder who requests in writing a copy of such regulations. Any transfer of an interest in the Regulation S Certificates (as defined in the Trust Deed) prior to the expiration of the "distribution compliance period" (as such term is defined in Rule 902 of Regulation S under the Securities Act) shall only be to a person whom the transferor reasonably believes (i) to be a non-US person in an offshore transaction in accordance with Rule 903 or Rule 904 of Regulation S under the Securities Act or (ii) to be a person who takes delivery in the form of an interest in the Rule 144A Certificates (as defined in the Trust Deed) (if applicable).

**4. Restrictive Covenants**

As provided in the Trust Deed, so long as any of the Notes remains outstanding (as defined in the Trust Deed), the Issuer will not, without the prior written consent of the Trustee, agree to any amendments to or any modification or waiver of, or authorise any breach or proposed breach of, the terms of the Loan Agreement and will act at all times in accordance with any instructions of the Trustee from time to time with respect to the Loan Agreement, except as otherwise expressly provided in the Trust Deed or the Loan Agreement. Any such amendment, modification, waiver or authorisation made with the consent of the Trustee shall be binding on the Noteholders and, unless the Trustee agrees otherwise, any such amendment or modification shall be notified by the Issuer to the Noteholders in accordance with Condition 14.

Save as provided above, so long as any Note remains outstanding, the Issuer, without the prior written consent of the Trustee shall not, *inter alia,* (i) incur any other indebtedness for borrowed moneys, other than issuing further Notes (which may be consolidated and form a single series with the Notes of any series) and/or creating or incurring further obligations relating to such Notes or issuing other series of limited recourse notes or bonds for the sole purpose of financing loans to the Borrower and/or creating or incurring further obligations relating to such other notes or bonds, (ii) engage in any business other than issuing Notes or such other notes or bonds from time to time in each case for the sole purpose of making available to the Borrower a loan, enter into related agreements and transactions and perform any act incidental to or necessary in connection with the foregoing, (iii) declare any dividends, (iv) have any subsidiaries or employees, (v) purchase, own, lease or otherwise acquire any real property (including office premises or like facilities), (vi) (to the extent the same is within the control of the Issuer) consolidate or merge with any other person or convey or transfer its properties or assets substantially as an entity to any person (otherwise than as contemplated in these conditions and the Trust Deed), (vii) (to the extent the same is within the control of the Issuer) issue or allot any shares (other than such shares as are in issue at the date of the Trust Deed) or (viii) make any distribution to its shareholders, give any guarantee or assume any other liability, or, (ix) subject to the laws of Luxembourg, petition for any winding-up or bankruptcy. For the avoidance of doubt, this paragraph shall not prohibit the Issuer from acquiring the rights and assuming the obligations of Citigroup Global Markets Deutschland AG & Co. KGaA ("**Citi**") under, or in connection with, the US$375,000,000 loan agreement between Citi as the lender and the Borrower as the borrower dated 14 April 2004 and the US$325,000,000 loan agreement between Citi as the lender and the Borrower as the borrower dated 19 February 2004.

**5. Interest**

On each Interest Payment Date the Issuer shall account to the Noteholders for an amount equivalent to amounts of interest actually received by or for the account of the Issuer pursuant to the Loan Agreement, which interest under the Loan is equal to 9.75 percent per annum (as set out in Clause 4 of the Loan Agreement).

If interest is required to be calculated for any other period, it will be calculated on the basis of a year of 360 days consisting of 12 months of 30 days each and, in the case of an incomplete month, the actual number of days elapsed.

In this Condition 5, "**Interest Payment Date**" means 29 January and 29 July of each year.

**6. Redemption**

**(a) Scheduled Redemption**

Unless previously prepaid or repaid, the Borrower will be required to repay the Loan on 29 July 2013 and, subject to such repayment, as set forth in the Loan Agreement, all the Notes then remaining outstanding will on 29 July 2013 be redeemed or repaid by the Issuer at 100 percent of the principal amount thereof.

**(b) Early Redemption**

If the Loan should become repayable (and be repaid) pursuant to the Loan Agreement prior to 29 July 2013, as set forth in the Loan Agreement, all Notes then remaining outstanding will thereupon become due and redeemable or repayable at par together with accrued interest and (subject to the Loan being repaid together with accrued interest) shall be redeemed or repaid and the Issuer will endeavour to give not less than 8 days' notice thereof to the Trustee and the Noteholders in accordance with Condition 14. Under the Loan Agreement:

(i) the Borrower may prepay the Loan in whole (but not in part) in the circumstances set out in Clause 5.2 of the Loan Agreement; and

(ii) the Issuer may require the Borrower to prepay the Loan in whole (but not in part) in the circumstances set out in Clause 5.3 of the Loan Agreement.

**(c) Cancellation**

The Loan Agreement provides that the Borrower may, among other things, from time to time deliver to the Issuer Notes, having an aggregate principal value of at least US$1,000,000, together with a request for the Issuer to present such Notes to the Registrar for cancellation, whereupon the Issuer shall, pursuant to the Agency Agreement, request the Registrar to cancel such Notes. Upon any such cancellation by or on behalf of the Registrar, the principal amount of the Loan corresponding to the principal amount of such Notes surrendered for cancellation shall be extinguished as of the date of such cancellation and no further payment shall be made or required to be made by the Issuer in respect of such Notes.

**(d) Right To Compel Sale**

The Issuer may compel any beneficial owner of Rule 144A Certificates (as defined in the Trust Deed) to sell its interest in such Notes, or may sell such interest on behalf of such holder, if such holder is not a qualified institutional buyer (as defined in Rule 144A under the Securities Act) and a qualified purchaser (as defined in Section 2(a)(51) of the US Investment Company Act of 1940) at a price equal to the lowest of (x) the purchase price therefor paid by the beneficial owner, (y) 100 percent of the principal amount thereof or (z) the fair market value thereof.

## 7. Payments

### (a) Principal

Payments of principal shall be made by US dollar cheque drawn on, or, upon application by a holder of a Note to the Specified Office of the Principal Paying Agent not later than the fifteenth day before the due date for any such payment, by transfer to a US dollar account maintained by the payee with, a bank in New York City upon surrender (or, in the case of part payment only, endorsement) of the relevant Certificates at the Specified Office of any Paying Agent.

### (b) Interest

Payments of interest shall be made by US dollar cheque drawn on, or upon application by a holder of a Note to the Specified Office of the Principal Paying Agent not later than the fifteenth day before the due date for any such payment, by transfer to a US dollar account maintained by the payee with, a bank in New York City and (in the case of interest payable on redemption) upon surrender (or, in the case of part payment only, endorsement) of the relevant Certificates at the Specified Office of any Paying Agent.

### (c) Payments Subject To Fiscal Laws

All payments in respect of the Notes are subject in all cases to any applicable fiscal or other laws and regulations in the place of payment, but without prejudice to the provisions of Condition 8, no commissions or expenses shall be charged to the Noteholders in respect of such payments.

### (d) Payments On Business Days

If the due date for payments of interest or principal is not a business day, the holder of a Note shall not be entitled to payment of the amount due until the next following business day and shall not be entitled to any further interest or other payment in respect of any such delay. In this paragraph, "**business day**" means a day on which (a) the London Interbank Market is open for dealings between banks generally, and (b) if on that day a payment is to be made hereunder, commercial banks generally are open for business in Luxembourg, New York City, Moscow and in the city where the Specified Office of the Principal Paying Agent is located.

### (e) Record Date

Each payment in respect of a Note will be made to the person shown as the holder in the Register at the opening of business (in the place of the Registrar's Specified Office) on the fifteenth day before the due date for such payment (the "**Record Date**"). Where payment in respect of a Note is to be made by cheque, the cheque will be mailed at the expense of the Issuer to the address shown as the address of the holder in the Register at the opening of business on the relevant Record Date.

### (f) Accrued Interest

In addition, if the due date for redemption or repayment of a Note is not an Interest Payment Date, interest accrued from the preceding Interest Payment Date or, as the case may be, from the date of issuance of the Notes, shall be payable only as and when actually received by or for the account of the Issuer pursuant to the Loan Agreement.

### (g) Payments By Borrower

Save as directed by the Trustee at any time after the security created in the Trust Deed becomes enforceable, the Issuer will require the Borrower to make all payments of principal, interest and any additional amounts to be made pursuant to the Loan Agreement to the Principal Paying Agent for the account of the Issuer. Pursuant to the Charge, the Issuer will charge by way of first fixed charge all its rights, title and interest in and to all sums of money then or in the future deposited in an account in the name of the Issuer with the Principal Paying Agent and the debts represented thereby to the Trustee for the benefit of the Noteholders.

**8. Taxation**

All payments in respect of the Notes by or on behalf of the Issuer shall be made free and clear of, and without deduction or withholding for or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by or on behalf of Luxembourg or any political subdivision or any authority thereof or therein having the power to tax, unless the deduction or withholding of such taxes or duties is required by law.

In such event, the Issuer shall make such additional payments as shall result in the receipt by the Noteholders of such amount as would have been received by them if no such withholding or deduction had been required. However, the Issuer shall only make such additional payments to the extent and at such time as it shall receive equivalent sums from the Borrower under the Loan Agreement. To the extent that the Issuer does not receive any such equivalent sum, the Issuer shall account to the relevant Noteholder for an additional amount equivalent to a pro rata proportion of such additional amount (if any) as is actually received by, or for the account of, the Issuer pursuant to the provisions of the Loan Agreement on the date of, in the currency of, and subject to any conditions attaching to the payment of such additional amount to the Issuer provided that no such additional amount will be payable:

(a) to a Noteholder who (i) is able to avoid such deduction or withholding by satisfying any statutory requirements or by making a declaration of non-residence or other claim for exemption to the relevant tax authority; or (ii) is liable for such taxes or duties by reason of his having some connection with Luxembourg other than the mere holding of such Notes or the receipt of payments in respect thereof;

(b) in respect of a Certificate presented for payment of principal more than 30 days after the Relevant Date except to the extent that such additional payment would have been payable if such Certificate had been presented for payment on such thirtieth day;

(c) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; or

(d) in respect of a Note held by or on behalf of a Noteholder who would have been able to avoid such withholding or deduction by arranging to receive the relevant payment through another Paying Agent in a Member State of the European Union.

As used herein, "**Relevant Date**" means (i) the date on which the equivalent payment under the Loan Agreement first becomes due but (ii) if the full amount payable by the Borrower has not been received by, or for the account of, the Issuer pursuant to the Loan Agreement on or prior to such date, means the date on which such full amount shall have been so received and notice to that effect shall have been duly given to the Noteholders by or on behalf of the Issuer.

Any reference herein or in the Trust Deed to payments in respect of the Notes shall be deemed also to refer to any additional amounts which may be payable in accordance with the Trust Deed and this Condition 8 or any undertaking given in addition thereto or in substitution therefor pursuant to the Trust Deed.

**9. Enforcement**

The Trust Deed provides that only the Trustee may pursue the remedies under the general law, the Trust Deed or the Notes to enforce the rights of the Noteholders and no Noteholder will be entitled to pursue such remedies unless the Trustee (having become bound to do so in accordance with the terms of the Trust Deed) fails or neglects to do so within a reasonable period and such failure or neglect is continuing.

The Trust Deed also provides that, in the case of an Event of Default (as defined in the Loan Agreement), or of a Relevant Event (as defined in the Trust Deed), the Trustee may, and shall, if requested to do so by Noteholders owning at least one quarter in aggregate principal amount of the Notes outstanding, or if directed to do so by an Extraordinary Resolution and, in either case, subject to it being secured and/or indemnified to its satisfaction, declare all amounts payable under the Loan Agreement by the Borrower to be immediately due and payable (in the case of an Event of Default), or enforce the security created in the Trust Deed in favour of the Trustee (in the case of a Relevant Event). Upon repayment of the Loan following an Event of Default and a declaration as provided herein, the Notes will be redeemed or repaid and thereupon shall cease to be outstanding.

**10. Meetings Of Noteholders; Modification; Waiver; Substitution Of The Issuer**

**(a) Meetings Of Noteholders**

The Trust Deed contains provisions for convening meetings of Noteholders to consider any matter affecting their interests, including any modification of, or any arrangement in respect of, the Notes or the Trust Deed. Noteholders will vote pro rata according to the principal amount of their Notes. The Trust Deed provides that special quorum provisions apply for meetings of Noteholders convened for the purpose of amending certain terms concerning, *inter alia*, the amount payable on, and the currency of payment in respect of, the Notes and the amounts payable and currency of payment under the Loan Agreement. Any resolution duly passed at a meeting of Noteholders will be binding on all the Noteholders, whether present or not.

**(b) Modification And Waiver**

The Trustee may agree, without the consent of the Noteholders, to any modification of the Notes and the Trust Deed or, following the creation of the Security Interests, the Loan Agreement which in the opinion of the Trustee is of a formal, minor or technical nature, is made to correct a manifest error or is not materially prejudicial to the interests of the Noteholders. The Trustee may also waive or authorise or agree to the waiving or authorising of any breach or proposed breach by the Issuer of the Conditions, or the Trust Deed or, following the creation of the Security Interests, by the Borrower of the terms of the Loan Agreement, or determine that any event which would or might otherwise give rise to a right of acceleration under the Loan Agreement shall not be treated as such, if in the sole opinion of the Trustee, to do so would not be materially prejudicial to the interests of the Noteholders (as a class). Any such modification, waiver or authorisation shall be binding on the Noteholders and, unless the Trustee agrees otherwise, shall be promptly notified to the Noteholders in accordance with Condition 14.

**(c) Substitution**

The Trust Deed contains provisions to the effect that the Issuer may, having obtained the consent of the Borrower and the Trustee (which latter consent may be given without the consent of the Noteholders) and subject to having complied with certain requirements as set out therein including the substitute obligor's rights under the Loan Agreement being charged and assigned, respectively, to the Trustee as security for the payment obligations of the substitute obligor under the Trust Deed and the Notes, substitute any entity in place of the Issuer as creditor under the Loan Agreement, as issuer and principal obligor in respect of the Notes and as obligor under the Trust Deed. Not later than 14 days after compliance with the aforementioned requirements, notice thereof shall be given by the Issuer to the Noteholders in accordance with Condition 14 or the Issuer shall use its best endeavours to ensure that the substitute obligor does so.

**(d) Exercise Of Powers**

In connection with the exercise of any of its powers, trusts, authorities or discretions, the Trustee shall have regard to the interests of the Noteholders as a class and, in particular, shall not have regard to the consequences of such exercise for individual Noteholders resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory. No Noteholder is entitled to claim from the Issuer or the Trustee any indemnification or payment in respect of any tax consequence of any such exercise upon individual Noteholders.

**11. Prescription**

Notes will become void unless presented for payment within ten years (in the case of principal) or five years (in the case of interest) from the due date for payment in respect thereof.

## 12. Trustee And Agents

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility in certain circumstances, including provisions relieving it from taking proceedings to enforce payment unless indemnified and/or secured to its satisfaction, and to be paid its costs and expenses in priority to the claims of Noteholders. In addition, the Trustee is entitled to enter into business transactions with the Issuer and the Borrower and any entity relating to the Issuer and the Borrower without accounting for any profit.

The Trustee's responsibilities are solely those of trustee for the Noteholders on the terms of the Trust Deed. Accordingly, the Trustee makes no representations and assumes no responsibility for the validity or enforceability of the Loan Agreement or the security created in respect thereof or for the performance by the Issuer of its obligations under or in respect of the Notes and the Trust Deed or by the Borrower in respect of the Loan Agreement.

In acting under the Agency Agreement and in connection with the Notes, the Agents act solely as agents of the Issuer and (to the extent provided therein) the Trustee and do not assume any obligations towards or relationship of agency or trust for or with any of the Noteholders.

The initial Agents and their initial Specified Offices are listed below. The Issuer reserves the right (with the prior written approval of the Trustee) at any time to vary or terminate the appointment of any Agent and to appoint a successor principal paying agent or registrar and additional or successor paying agents and transfer agents; provided, however, that the Issuer shall at all times maintain (a) a principal paying agent and a registrar, (b) a paying agent and transfer agent having specified offices in at least two major European cities approved by the Trustee and (c) a paying agent in a member state of the European Union that will not be obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced to conform to, such Directive.

Notice of any change in any of the Agents or in their Specified Offices shall promptly be given to the Noteholders in accordance with Condition 14.

## 13. Replacement Of Certificates

If a Certificate shall become mutilated, defaced, lost, stolen or destroyed it may, subject to all applicable laws and regulations and requirements of the Stock Exchange, be replaced at the Specified Office of the Registrar and any Transfer Agent on payment of such costs, expenses, taxes and duties as may be incurred in connection therewith and on such terms as to evidence, security and indemnity and otherwise as may reasonably be required by or on behalf of the Issuer or the Trustee. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

## 14. Notices

All notices regarding the Notes will be deemed to be validly given if published on the website of the relevant Stock Exchange. It is expected that such publication will be made on the website of the London Stock Exchange. The Issuer shall also ensure that notices are duly published in a manner which complies with the rules of any stock exchange or other relevant authority on which the Notes are for the time being listed or by which they have been admitted to listing. Any such notice will be deemed to have been given on the date of the first publication.

## 15. Further Issues

The Issuer may from time to time, without the consent of the Noteholders, create and issue further Notes having the same terms and conditions as the Notes in all respects (or in all respects except for the first payment of interest) so as to form a single series with the Notes. Such further Notes shall be issued under a deed supplemental to the Trust Deed. The Trust Deed contains provisions for convening a single meeting of Noteholders and the holders of Notes of other series in certain circumstances where the Trustee so decides.

**16. Contracts (Rights Of Third Parties) Act 1999**

No person shall have any right to enforce any term or condition of the Notes under the Contracts (Rights of Third Parties) Act 1999. The provisions of articles 86 to 94-8 of the Luxembourg law of 10 August 1915, as amended, on commercial companies are excluded.

**17. Governing Law**

The Notes and the Trust Deed are governed by and shall be construed in accordance with, English law. The Issuer has submitted in the Trust Deed to the jurisdiction of the courts of England and has appointed an agent for the service of process in England.

## BOOK ENTRY, DELIVERY AND FORM

### THE GLOBAL CERTIFICATES

The Regulation S Notes will be evidenced on issue by the Regulation S Global Certificate registered in the name of a nominee for, and deposited with a common depository on behalf of, Euroclear and Clearstream, Luxembourg. Beneficial interests in the Regulation S Global Certificate may be held only through Euroclear or Clearstream, Luxembourg at any time. See "— Book-entry Procedures for the Global Certificates". By acquisition of a beneficial interest in the Regulation S Global Certificate, the purchaser thereof will be deemed to represent, among other things, that it is not a US person, that is is located outside the United States and that, if it determines to transfer such beneficial interest prior to the expiration of the "distribution compliance period" (as such term is defined in Rule 902 of Regulation S), it will transfer such interest only (a) to a non-US person in an offshore transaction in accordance with Rule 903 or Rule 904 of Regulation S or (b) in accordance with Rule 144A to a person that it and any person acting on its behalf reasonably believe is a QIB that is also a QP purchasing for its own account or the account of a QIB that is also a QP, in each case in accordance with any applicable securities laws of any state of the United States. See "Selling and Transfer Restrictions".

The Rule 144A Notes will be evidenced on issue by the Rule 144A Global Certificate deposited with a custodian for, and registered in the name of a nominee of, DTC. Beneficial interests in the Rule 144A Global Certificate may only be held through DTC at any time. See "— Book-entry Procedures for the Global Certificates". By acquisition of a beneficial interest in the Rule 144A Global Certificate, the purchaser thereof will be deemed to represent, among other things, that it is a QIB that is also a QP and that, if in the future it determines to transfer such beneficial interest, it will transfer such interest in accordance with the procedures and restrictions contained in the Trust Deed. See "Selling and Transfer Restrictions".

Beneficial interests in Global Certificates will be subject to certain restrictions on transfer set forth therein and in the Trust Deed and the Global Certificates will bear the applicable legends regarding the restrictions set forth under "Selling and Transfer Restrictions". A beneficial interest in the Regulation S Global Certificate may be transferred to a person who takes delivery in the form of an interest in the Rule 144A Global Certificate only in denominations greater than or equal to the minimum denominations applicable to interests in the Rule 144A Global Certificate and only upon receipt by the Registrar of a written certification (in the form provided in an Agency Agreement relating to the Notes (the "**Agency Agreement**")) to the effect that the transferor reasonably believes that the transferee is a QIB that is also a QP and that such transaction is in accordance with any applicable securities laws of any state of the United States or any other jurisdiction. Beneficial interests in the Rule 144A Global Certificate may be transferred to a person who takes delivery in the form of an interest in the Regulation S Global Certificate only upon receipt by the Registrar of a written certification (in the form provided in the Agency Agreement) from the transferor to the effect that the transfer is being made in an offshore transaction in accordance with Regulation S.

Any beneficial interest in the Regulation S Global Certificate that is transferred to a person who takes delivery in the form of an interest in the Rule 144A Global Certificate will, upon transfer, cease to be an interest in the Regulation S Global Certificate and become an interest in the Rule 144A Global Certificate, and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to beneficial interests in the Rule 144A Global Certificate for as long as it remains such an interest. Any beneficial interest in the Rule 144A Global Certificate that is transferred to a person who takes delivery in the form of an interest in the Regulation S Global Certificate will, upon transfer, cease to be an interest in the Rule 144A Global Certificate and become an interest in the Regulation S Global Certificate and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to beneficial interests in the Regulation S Global Certificate for so long as it remains such an interest. No service charge will be made for any registration of transfer or exchange of Notes, but the Registrar may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection therewith.

Except in the limited circumstances described below, owners of beneficial interests in Global Certificates will not be entitled to receive physical delivery of Definitive Certificates. The Notes are not issuable in bearer form.

In addition, each Global Certificate will contain a provision which modifies the Terms and Conditions of the Notes as they apply to the Notes evidenced by the Global Certificate. The following is a summary of this provision:

### NOTICES

Notwithstanding Condition 14, so long as the Global Certificate is held by or on behalf of DTC, Euroclear, Clearstream, Luxembourg or any other clearing system (an "**Alternative Clearing System**"), notices to Noteholders represented by the Global Certificate may be given by delivery of the relevant notice to DTC, Euroclear, Clearstream, Luxembourg or (as the case may be) such Alternative Clearing System.

### EXCHANGE FOR DEFINITIVE CERTIFICATES

#### Exchange

Subject to receipt by the Issuer of the funds necessary to cover the cost therefor from the Company, each Global Certificate will be exchangeable, free of charge to the holder, on or after its Exchange Date (as defined below), in whole but not in part, for Notes in definitive form if: (i) a Global Certificate is held by or on behalf of (A) DTC, and DTC notifies the Issuer that it is no longer willing or able to discharge properly its responsibilities as depository with respect to the Global Certificate or ceases to be a "clearing agency" registered under the Exchange Act or if at any time it is no longer eligible to act as such, and the Issuer is unable to locate a qualified successor within 90 days of receiving notice or becoming aware of such ineligibility on the part of DTC or (B) Euroclear or Clearstream, Luxembourg, as the case may be, and Euroclear or Clearstream, Luxembourg, as the case may be, is closed for business for a continuous period of 14 days (other than by reason of holidays, statutory or otherwise) or announces an intention to permanently cease business or does in fact do so, by the holder giving notice to the Registrar or any Transfer Agent and the Issuer or (ii) the Issuer would suffer a material disadvantage in respect of the Notes as a result of a change in the laws or regulations (taxation or otherwise) of any jurisdiction referred to in Condition 8 which would not be suffered were the Notes in definitive form and a note to such effect signed by two Members of the Management Board of the Issuer is delivered to the Trustee, by the Issuer giving notice to the Registrar or any Transfer Agent and the Noteholders of its intention to exchange the relevant Global Certificate for Definitive Certificates on or after the Exchange Date (as defined below) specified in the notice or (iii) the Trustee has instituted or has been directed to institute any judicial proceeding in a court to enforce the rights of the Noteholders under the Notes and the Trustee has been advised by counsel that in connection with such proceeding it is necessary or appropriate for the Trustee to obtain possession of the Notes, by the Trustee giving notice to the Registrar or any Transfer Agent and the Noteholders.

The Registrar will not register the transfer of, or exchange of interests in, a Global Certificate for Definitive Certificates for a period of 15 calendar days ending on the date for any payment of principal or interest in respect of the Notes.

If only one of the Global Certificates (the "**Exchanged Global Certificate**") becomes exchangeable for Definitive Certificates in accordance with the above paragraphs, transfers of Notes may not take place between, on the one hand, persons holding Definitive Certificates issued in exchange for beneficial interests in the Exchanged Global Certificate and, on the other hand, persons wishing to purchase beneficial interests in the other Global Certificate.

"Exchange Date" means a day falling not later than 90 days after that on which the notice requiring exchange is given and on which banks are open for business in the city in which the specified office of the Registrar and any Transfer Agent is located.

#### Delivery

In such circumstances, the relevant Global Certificate shall be exchanged in full for Definitive Certificates and the Issuer will, at the cost of the Issuer (and against such indemnity as the Registrar or any relevant Transfer Agent may require in respect of any tax or other duty of whatever nature which may be levied or imposed in connection with such exchange), cause sufficient Definitive Certificates to be executed and delivered to the Registrar for completion, authentication and dispatch to the relevant Noteholders. A person having an interest in a Global Certificate must provide the Registrar with (a) a written order containing instructions and such other information as the Issuer and the Registrar may require to complete, execute and deliver such Notes and (b) in the case of the Rule 144A Global Certificate only, a fully completed, signed certification substantially to the effect that the exchanging holder is not transferring its interest at the time of such exchange or, in the case of simultaneous sale pursuant to Rule 144A, a certification that the transfer is being made in compliance with the provisions of Rule 144A to a QIB that is also a QP. Definitive Certificates issued in exchange for a beneficial interest in the Rule 144A Global Certificate shall bear the legend applicable to transfer pursuant to Rule 144A, as set forth under "Selling and Transfer Restrictions".

### LEGENDS

The holder of a Definitive Certificate may transfer the Notes evidenced thereby in whole or in part in the applicable minimum denomination by surrendering it at the specified office of the Registrar or any Transfer Agent, together with the completed form of transfer thereon. Upon the transfer, exchange or replacement of a Rule 144A Definitive Certificate bearing the legend referred to under "Selling and Transfer Restrictions", or upon specific request for removal of the legend on a Rule 144A Definitive Certificate, the Issuer will deliver only Rule 144A Definitive Certificates that bear such legend, or will refuse to remove such legend, as the case may be, unless there is delivered to the Issuer and the Registrar such satisfactory evidence, which may include an opinion of counsel, as may reasonably be required by the Issuer that neither the legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act and the Investment Company Act.

### BOOK-ENTRY PROCEDURES FOR THE GLOBAL CERTIFICATES

#### Euroclear, Clearstream, Luxembourg and DTC

Custodial and depository links have been established between Euroclear, Clearstream, Luxembourg and DTC to facilitate the initial issue of the Notes and cross-market transfers of the Notes associated with secondary market trading. See "— Book-entry Ownership — Settlement and Transfer of Notes".

#### Euroclear and Clearstream, Luxembourg

Euroclear and Clearstream, Luxembourg each hold securities for their customers and facilitate the clearance and settlement of securities transactions through electronic book-entry transfer between their respective accountholders. Indirect access to Euroclear and Clearstream, Luxembourg is available to other institutions which clear through or maintain a custodial relationship with an accountholder of either system. Euroclear and Clearstream, Luxembourg provide various services including safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Euroclear and Clearstream, Luxembourg also deal with domestic securities markets in several countries through established depository and custodial relationships. Euroclear and Clearstream, Luxembourg have established an electronic bridge between their two systems across which their respective customers may settle trades with each other. Their customers are worldwide financial institutions including underwriters, securities brokers and dealers, banks, trust companies and clearing corporations. Investors may hold their interests in such Global Certificates directly through Euroclear or Clearstream, Luxembourg if they are accountholders ("**Direct Participants**") or indirectly ("**Indirect Participants**" and together with Direct Participants, "**Participants**") through organisations which are accountholders therein.

#### DTC

DTC has advised the Issuer as follows: DTC is a limited-purpose trust company organised under the laws of the State of New York, a "banking organisation" under the laws of the State of New York, a member of the US Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code and a "clearing agency" registered pursuant to the provisions of Section 17A of the Exchange Act. DTC was created to hold securities for its participants ("**DTC Participants**") and facilitate the clearance and settlement of securities transactions between DTC Participants through electronic computerised book-entry changes in accounts of its DTC Participants, thereby eliminating the need for physical movement of certificates. DTC Participants include securities brokers and dealers, banks, trust companies, clearing corporations and certain other organisations. Indirect access to DTC is available to others, such as banks, securities brokers, dealers and trust companies, that clear through or maintain a custodial relationship with a DTC Participant, either directly or indirectly.

Investors may hold their interests in the Rule 144A Global Certificate directly through DTC if they are DTC Participants in the DTC system, or indirectly through organisations which are DTC Participants in such system.

DTC has advised the Issuer that it will take any action permitted to be taken by a holder of Notes only at the direction of one or more DTC Participants and only in respect of such portion of the aggregate principal amount of the relevant Rule 144A Global Certificates as to which such DTC Participant or DTC Participants has or have given such direction. However, in the circumstances described under "Exchange for Definitive Notes", DTC will surrender the relevant Rule 144A Global Certificates for exchange for individual Rule 144A Definitive Certificates (which will bear the legend applicable to transfers pursuant to Rule 144A).

## BOOK-ENTRY OWNERSHIP

### Euroclear and Clearstream, Luxembourg

The Regulation S Global Certificate will have an ISIN and a Common Code and will be registered in the name of a nominee for, and deposited with a common depository on behalf of, Euroclear and Clearstream, Luxembourg.

The address of Euroclear is 1 Boulevard du Roi Albert 11, B-1210 Brussels, Belgium, and the address of Clearstream, Luxembourg is 42 Avenue J.F. Kennedy, L-1855, Luxembourg.

### DTC

The Rule 144A Global Certificate will have a CUSIP number and will be deposited with a custodian (the "**Custodian**") for, and registered in the name of a nominee of, DTC. The Custodian and DTC will electronically record the principal amount of the Notes held within the DTC system. The address of DTC is 55 Water Street, New York, New York 10041, United States of America.

### Relationship of Participants with Clearing Systems

Each of the persons shown in the records of Euroclear, Clearstream, Luxembourg or DTC as the holder of a Note evidenced by a Global Certificate must look solely to Euroclear, Clearstream, Luxembourg or DTC (as the case may be) for his share of each payment made by the Issuer to the holder of such Global Certificate and in relation to all other rights arising under the Global Certificate, subject to and in accordance with the respective rules and procedures of Euroclear, Clearstream, Luxembourg or DTC (as the case may be). The Issuer expects that, upon receipt of any payment in respect of Notes evidenced by a Global Certificate, the common depository by whom such Note is held, or nominee in whose name it is registered, will immediately credit the relevant participants' or accountholders' accounts in the relevant clearing system with payments in amounts proportionate to their respective beneficial interests in the principal amount of the relevant Global Certificate as shown on the records of the relevant clearing system or its nominee. The Issuer also expects that payments by Direct Participants or DTC Participants, as the case may be, in any clearing system to owners of beneficial interests in any Global Certificate held through such Direct Participants or DTC Participants, as the case may be, in any clearing system will be governed by standing instructions and customary practices. Save as aforesaid, such persons shall have no claim directly against the Issuer in respect of payments due on the Notes for so long as the Notes are evidenced by such Global Certificate and the obligations of the Issuer will be discharged by payment to the registered holder, as the case may be, of such Global Certificate in respect of each amount so paid. None of the Issuer, the Trustee or any Agent will have any responsibility or liability for any aspect of the records relating to or payments made on account of ownership interests in any Global Certificate or for maintaining, supervising or reviewing any records relating to such ownership interests.

### Settlement and Transfer of Notes

Subject to the rules and procedures of each applicable clearing system, purchases of Notes held within a clearing system must be made by or through Direct Participants or DTC Participants, as the case may be, which will receive a credit for such Notes on the clearing system's records. The ownership interest of each actual purchaser of each such Note (the "**Beneficial Owner**") will in turn be recorded on the Direct Participants' or DTC Participants', as the case may be, records. Beneficial Owners will not receive written confirmation from any clearing system of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct Participant or DTC Participants, as the case may be, through which such Beneficial Owner entered into the transaction. Transfers of ownership interests in Notes held within the clearing system will be affected by entries made on the books of Direct Participants or DTC Participants, as the case may be, acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in such Notes, unless and until interests in any Global Certificate held within a clearing system are exchanged for Definitive Certificates.

No clearing system has knowledge of the actual Beneficial Owners of the Notes held within such clearing system and their records will reflect only the identity of the Direct Participants or DTC Participants, as the case may be, to whose accounts such Notes are credited, which may or may not be the Beneficial Owners. The Direct Participants or DTC Participants, as the case may be, will remain responsible for keeping account of their holdings on behalf of their customers. Conveyance of notices and other communications by the clearing systems to Direct Participants or DTC Participants, as the case may be; by Direct Participants to Indirect Participants, and by Direct Participants, Indirect Participants or DTC Participants, as the case may be, to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

The laws of some jurisdictions may require that certain persons take physical delivery in definitive form of securities. Consequently, the ability to transfer interests in a Global Certificate to such persons may be limited. Because DTC can only act on behalf of DTC Participants, the ability of a person having an interest in the Rule 144A Global Certificate to pledge such interest to persons or entities that do not participate in DTC, or otherwise take actions in respect of such interest, may be affected by the lack of a physical certificate in respect of such interest.

**Trading between Euroclear and/or Clearstream, Luxembourg Participants**

Secondary market sales of book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg to purchasers of book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg will be conducted in accordance with the normal rules and operating procedures of Euroclear and Clearstream, Luxembourg and will be settled using the procedures applicable to conventional Eurobonds.

**Trading between DTC Participants**

Secondary market sales of book-entry interests in the Notes between DTC Participants will occur in the ordinary way in accordance with DTC rules and will be settled using the procedures applicable to US corporate debt obligations in DTC's Same-Day Funds Settlement ("**SDFS**") system in same-day funds, if payment is effected in US dollars, or free of payment, if payment is not effected in US dollars. Where payment is not effected in US dollars, separate payment arrangements outside DTC are required to be made between DTC Participants.

**Trading between DTC Seller and Euroclear/Clearstream, Luxembourg Purchaser**

When book-entry interests in Notes are to be transferred from the account of a DTC Participant holding a beneficial interest in the Rule 144A Global Certificate to the account of a Euroclear or Clearstream, Luxembourg accountholder wishing to purchase a beneficial interest in the Regulation S Global Certificate (subject to the certification procedures provided in the Agency Agreement), the DTC Participant will deliver instructions for delivery to the relevant Euroclear or Clearstream, Luxembourg accountholder to DTC by 12:00 pm, New York time, on the settlement date. Separate payment arrangements are required to be made between the DTC Participant and the relevant Euroclear or Clearstream, Luxembourg Participant. On the settlement date, the custodian of the Rule 144A Global Certificate will instruct the Registrar to (i) decrease the amount of Notes registered in the name of Cede & Co. and evidenced by the Rule 144A Global Certificate of the relevant class and (ii) increase the amount of Notes registered in the name of the nominee of the common depository for Euroclear and Clearstream, Luxembourg and evidenced by the Regulation S Global Certificate. Book-entry interests will be delivered free of payment to Euroclear or Clearstream, Luxembourg, as the case may be, for credit to the relevant accountholder on the first business day following the settlement date.

**Trading between Euroclear/Clearstream, Luxembourg Seller and DTC purchaser**

When book-entry interests in the Notes are to be transferred from the account of a Euroclear or Clearstream, Luxembourg accountholder to the account of a DTC Participant wishing to purchase a beneficial interest in the Rule 144A Global Certificate (subject to the certification procedures provided in the Agency Agreement), the Euroclear or Clearstream, Luxembourg Participant must send to Euroclear or Clearstream, Luxembourg delivery free of payment instructions by 7:45 pm, Brussels or Luxembourg time, one business day prior to the settlement date. Euroclear or Clearstream, Luxembourg, as the case may be, will in turn transmit appropriate instructions to the common depository for Euroclear and Clearstream, Luxembourg and the Registrar to arrange delivery to the DTC Participant on the settlement date. Separate payment arrangements are required to be made between the DTC Participant and the relevant Euroclear or Clearstream, Luxembourg accountholder, as the case may be. On the settlement date, the common depositary for Euroclear and Clearstream, Luxembourg will (a) transmit appropriate instructions to the custodian of the Rule 144A Global Certificate who will in turn deliver such book-entry interests in the Notes free of payment to the relevant account of the DTC Participant and (b) instruct the Registrar to (i) decrease the amount of Notes registered in the name of the nominee of the common depository for Euroclear and Clearstream, Luxembourg and evidenced by the Regulation S Global Certificate; and (ii) increase the amount of Notes registered in the name of Cede & Co. and evidenced by the Rule 144A Global Certificate.

Although Euroclear, Clearstream, Luxembourg and DTC have agreed to the foregoing procedures in order to facilitate transfers of beneficial interest in Global Certificates among participants and accountholders of Euroclear, Clearstream, Luxembourg and DTC, they are under no obligation to perform or continue to perform such procedure, and such procedures may be discontinued at any time. None of the Issuer, the Trustee or any Agent will have the responsibility for the performance by Euroclear, Clearstream, Luxembourg or DTC or their respective Direct Participants, Indirect Participants or DTC Participants, as the case may be, of their respective obligations under the rules and procedures governing their operations.

**Pre-issue Trades Settlement**

It is expected that delivery of Notes will be made against payment therefor on the Closing Date, which is expected to be on or around the sixth business day following the date of pricing (such settlement being referred to as "**T+6**"). Under Rule 15c6-l under the Exchange Act, trades in the United States secondary market generally are required to settle in three business days (T+3), unless the parties to any such trade expressly agree otherwise. Accordingly, purchasers who wish to trade Notes in the United States on the date of pricing or the next two succeeding business days will be required, by virtue of the fact the Notes will initially settle in T+6, to specify an alternate settlement cycle at the time of any such trade to prevent a failed settlement. Settlement procedures in other countries may vary and purchasers of Notes may be affected by such local settlement practices. Purchasers of Notes who wish to trade the Notes on the date of pricing or the next two succeeding business days should consult their own adviser.

# TAXATION

The following summary of certain Russian, Luxembourg, United Kingdom and United States tax consequences of ownership of Notes is based upon laws, regulations, decrees, rulings, income tax conventions (treaties), administrative practice and judicial decisions in effect at the date of this Prospectus. Legislative, judicial or administrative changes or interpretations may, however, be forthcoming that could alter or modify the statements and conclusions set forth herein. Any such changes or interpretations may be retroactive and could affect the tax consequences to holders of the Notes. This summary does not purport to be a legal opinion or to address all tax aspects that may be relevant to a holder of Notes. Each prospective holder is urged to consult its own tax adviser as to the particular tax consequences to such holder of the ownership and disposition of Notes, including the applicability and effect of any other tax laws or tax treaties, and of pending or proposed changes in applicable tax laws as at the date of this Prospectus, and of any actual changes in applicable tax laws after such date.

## RUSSIAN FEDERATION

### General

The following is a general summary of certain Russian tax considerations relevant to the purchase, ownership and disposition of the Notes as well as the taxation of interest on the Loan. The summary is based on the laws of Russia in effect at the date of this Prospectus, which are subject to change (possibly with retroactive effect). The summary does not seek to address the applicability of, or procedures in relation to, taxes levied by regions, municipalities or other non-federal authorities of Russia. Similarly, the summary does not seek to address the availability of double tax treaty relief in respect of the Notes, and it should be noted that there may be practical difficulties, including satisfying certain documentation requirements, involved in claiming such double tax treaty relief. Prospective investors should consult their own advisors regarding the tax consequences of investing in the Notes. No representation with respect to the Russian tax consequences for any particular holder is made hereby.

Many aspects of Russian tax law are subject to significant uncertainty. Furthermore, the substantive provisions of Russian tax law applicable to financial instruments may be subject to more rapid and unpredictable change and inconsistency than in jurisdictions with more developed capital markets and tax systems.

For the purposes of this summary, a "**Non-Resident Noteholder**" means:

- an individual Noteholder ("**Non-Resident Noteholder — Individual**") who does not satisfy the criteria for being a Russian tax resident. This means an individual not actually present in Russia for an aggregate period of 183 days or more (excluding days of arrival into Russia, but including days of departure from Russia) in any period comprised of 12 consecutive months. Presence in Russia is not considered interrupted if an individual departs for short periods (less than six months) for medical treatment or education; or
- a legal entity or an organisation in each case not organised under Russian law, which holds and disposes of the Notes otherwise than through a permanent establishment in Russia ("**Non-Resident Noteholder — Legal Entity**").

For the purposes of this summary, a "**Russian Resident Noteholder**" means:

- an individual Noteholder who is present in Russia for an aggregate period of 183 days or more (excluding days of arrival into Russia, but including days of departure from Russia) in any period comprised of 12 consecutive months. Presence in Russia is not considered interrupted if an individual departs for short periods (less than six months) for medical treatment or education;
- a Russian legal entity that holds and disposes of the Notes; or
- a legal entity or an organisation, in each case organised under a foreign law, that holds and disposes of the Notes, where the disposal is attributable to its permanent establishment in Russia.

For the purposes of this summary, the definitions of "Russian Resident Noteholder" and "Non-Resident Noteholder" in respect of individuals are taken at face value based on the wording of the tax law as currently written. In practice, however, the application of the above formal residency definition may differ based on the position of the tax authorities. The law is currently worded in a way that implies the potential for a split-year residency for individuals. However the tax authorities have expressed the view that an individual should be either resident or non-resident in Russia for the full calendar year and consequently even where the travel pattern dictates a differing residency status for a part of the tax year, the application of the residency tax rate may in practice be disallowed. This situation may be altered by amendments to other articles of the Tax Code of the Russian Federation (the "**Tax Code**") dealing with the taxation of individuals.

Russia's rights with regard to taxation rules may be affected by an applicable double tax treaty. The Russian tax treatment of interest payments made by the Company to the Issuer or to the Trustee under the Loan Agreement may affect the holders of the Notes. See "— Taxation of Interest on the Loan" below.

**Taxation of the Notes**

***Non-Resident Noteholders***

A Non-Resident Noteholder should not be subject to any Russian taxes in respect of payments of interest and repayments of principal on the Notes received from the Issuer. A Non-Resident Noteholder also generally should not be subject to any Russian taxes in respect of any gain or other income realised on redemption, sale or other disposition of the Notes outside Russia, provided that the proceeds of such disposition are not received from a source within Russia. In the event that proceeds from a disposition of the Notes are received from a source within Russia, a Non-Resident Noteholder — Legal Entity should not be subject to Russian tax on any gain on sale or other disposition of the Notes, although there is some residual uncertainty regarding the treatment of the portion of the proceeds, if any, from disposition of the Notes that is attributable to accrued interest on the Notes. Subject to reduction or elimination under the provisions of an applicable double tax treaty that are related to interest income, proceeds attributable to accrued interest may be taxed at a rate of 20 percent, even if the disposal results in a capital loss.

Subject to any available tax treaty relief, the receipt of proceeds by a Non-Resident Noteholder — Individual from a source within Russia in respect of the gain from a disposition of the Notes is likely to be treated as Russian-source income for personal income tax purposes and, as such, will be subject to Russian personal income tax at a rate of 30 percent on the gross proceeds received less any available documented cost deduction (including the original purchase value). In certain circumstances, if the disposal proceeds are paid by a licensed broker or an asset manager that is a Russian legal entity or organisation, or any other person located in Russia, including a foreign company with a permanent establishment or any registered presence in Russia or by an individual entrepreneur located in Russia, who carries out operations under an agency agreement, a commission agreement or other similar agreement for the benefit of the Non-Resident Noteholder — Individual, the applicable personal income tax at the rate of 30 percent should be withheld at source. The amount of tax withheld would be calculated after taking into account deductions for the purchase value and related expenses to the extent such deductions and expenses can be determined by the entity making the payment of income. When a sale is made to other legal entities or individuals, generally no withholding of tax needs to be made and the Non-Resident Noteholder — Individual would be liable to file a tax return, report his or her income realized and apply for any available cost deductions based on the provision of supporting documentation. The applicable tax would then have to be paid by the individual on the basis of the tax return. There is also a risk that any gain may be affected by changes in the exchange rate between the currency of acquisition of the Notes, the currency of disposition and the Rouble.

There is some uncertainty regarding the treatment of the element of the proceeds, if any, from a disposition of the Notes that is attributable to accrued interest on the Notes. Subject to reduction or elimination of tax under the provisions of an applicable tax treaty that are related to interest income, proceeds attributable to accrued interest may be taxed at a rate of 30 percent, even if the disposal results in a capital loss.

***Tax Treaty Relief***

The Russian Federation has concluded double tax treaties with a number of countries and honours some double tax treaties concluded by the Union of Soviet Socialist Republics. These tax treaties may contain provisions that reduce or eliminate Russian tax due with respect to income received from a source within Russia by a Non-Resident Noteholder on a disposition of Notes. To obtain the benefit of such tax treaty provisions, the Noteholder must comply with the certification, information and reporting requirements in force in Russia.

Currently a Non-Resident Noteholder — Legal Entity would need to provide the payer of income with a certificate of tax residence issued by the competent tax authority of the relevant treaty country. This certificate should be apostilled or legalised and a notarised Russian translation of the certificate would be required. There can be no assurance that advance treaty relief will be available, whilst obtaining a refund of the tax withheld can be difficult and extremely time-consuming.

A Non-Resident Noteholder — Individual must provide to the tax authorities a tax residency certificate and appropriate documentary evidence of income received and the tax payment made outside Russia on income with respect to which treaty benefits are claimed. Individuals in practice would not be able to obtain advance treaty relief on receipt of proceeds from a source within Russia, whilst obtaining a refund of the taxes withheld can be extremely difficult, if not impossible. The tax authorities may also, in practice, ask for further documentation in order to ensure the eligibility of a Non-Resident Noteholder — Individual for relief under the treaty.

Non-Resident Noteholders should consult their own tax advisors regarding possible tax treaty relief and procedures for obtaining such relief with respect to any Russian taxes imposed in respect of proceeds received on a disposition of Notes.

***Resident Noteholders***

A Russian Resident Noteholder will be subject to all applicable Russian taxes in respect of gains from a disposal of the Notes and interest received on the Notes.

**Taxation of Interest on the Loan**

In general, payments of interest on borrowed funds by a Russian entity to a non-resident legal entity are subject to Russian withholding tax at a rate of 20 percent, absent reduction or elimination pursuant to the terms of an applicable double tax treaty. Based on professional advice it has received, the Company believes that payments of interest to the Issuer on the Loan should not be subject to withholding tax under the terms of the Convention between the Grand Duchy of Luxembourg and the Russian Federation for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and Capital signed on 28 June 1993. However, there can be no assurance that advance relief will be available.

For treaty relief from Russian withholding tax, preliminary approval from the Russian tax authorities is neither required nor possible. Moreover, the Russian tax authorities may subsequently scrutinise the Issuer's eligibility for treaty relief during tax audits. If interest under the Loan becomes payable to the Trustee pursuant to the Trust Deed, any benefit of the double tax treaty between Russia and Luxembourg will cease and payments of interest should be subject to Russian withholding tax at the rate of 20 percent, or such other rate as may be in force at the time of payment. It is not expected that the Trustee will, or will be able to, claim a withholding tax exemption under any double tax treaty under such circumstances. In such cases, Noteholders may seek reduction or a refund of withholding tax under applicable double taxation treaties entered into between their countries of residence and Russia, where such treaties exist and to the extent they are applicable. There is no assurance that treaty relief will be available.

If payments under the Loan are subject to any withholding of Russian tax (as a result of which the Issuer would reduce payments under the Notes in the amount of such withholding), the Company is obliged (subject to certain conditions) to increase payments as may be necessary so that the net payments received by the Noteholders will be equal to the amounts they would have received in the absence of such withholding. It should be noted, however, that the tax gross-up provisions may not be enforceable under Russian law. In the event that the Company fails to make increased payments, such failure would constitute an Event of Default pursuant to the Loan Agreement. If the Company is obliged to increase payments, it may (without premium or penalty), subject to certain conditions, prepay the Loan in full. In such case, all outstanding Notes would be redeemable at par together with accrued and unpaid interest and additional amounts, if any, to the date of redemption.

No value added tax should be payable in Russia in respect of interest and principal payments under the Loan.

**GRAND DUCHY OF LUXEMBOURG**

The following is a general discussion of certain Luxembourg tax consequences of the acquisition, ownership and disposal of Notes by purchasers resident or non-resident in Luxembourg. The discussion is based on laws currently in force and as applied in practice on the date of this Prospectus, all of which are subject to change, possibly with retroactive effect. The information provided below does not purport to be a complete or exhaustive summary of the tax laws and practice currently applicable in Luxembourg. Prospective investors should therefore consult their own tax advisors regarding the tax consequences of investing in the Notes in their own particular circumstances.

**Luxembourg Tax Residency of the Noteholders**

A Noteholder will not become resident, or be deemed to be resident, in Luxembourg by reason only of the holding of the Notes, or the execution, performance, delivery and/or enforcement of the Notes.

**Withholding Tax**

Save for the application of the European Directive on the Taxation of Savings Income (2003/48/EC) (the "**Savings Directive**") (see "— European Union"), under Luxembourg tax law currently in effect, no withholding tax applies on payments of interest (including accrued but unpaid interest) to non-resident Noteholders to the extent that the interest rate of the Notes is at arm's length and is not profit participating.

Under the Luxembourg laws dated 21 June 2005 and effective from 1 July 2005 implementing the Savings Directive and several agreements concluded between Luxembourg and certain dependent territories of the European Union, certain interest payments made by Luxembourg-based paying agents to individual Noteholders and certain residual entities could be subject to withholding tax (see below).

As from 1 January 2006, interest payments made by a Luxembourg based paying agent (defined in the same way as in the Savings Directive) to Luxembourg resident individuals and certain residual entities (unless such entity has opted for the exchange of information regime) are subject to a 10 percent withholding tax. This 10 percent Luxembourg withholding tax represents the final tax liability on interest received by Luxembourg resident individuals receiving the payment in the framework of their private estate, Luxembourg resident individuals receiving the interest payments as business income must include the interest income in their taxable basis. The 10 percent withholding tax levied will then be credited against their final income tax liability.

**Taxation of the Noteholders**

A Noteholder who derives income from a Note or who realises a gain on the disposal or redemption of a Note will not be subject to Luxembourg taxation on income or capital gains unless:

- the Noteholder is, or is deemed to be, resident in Luxembourg for the purpose of the relevant provisions; or
- such income or gain is attributable to an enterprise or part thereof which is carried on by a non-resident through a permanent establishment or a permanent representative in Luxembourg;

Luxembourg resident individual Noteholders are however not subject to taxation on capital gain upon disposal of a Note, unless such a disposal precedes the acquisition of the Note or the Note is disposed of within the 6 months of its date of acquisition.

**Net Wealth Tax**

Luxembourg net wealth tax will not be levied on a Noteholder, unless (i) such holder is a fully taxable Luxembourg resident company or (ii) such Notes are attributable to an enterprise or part thereof which is carried on by a non-resident company in Luxembourg through a permanent establishment or a permanent representative.

**Other Taxes and Duties**

There is no Luxembourg registration tax, stamp duty or any other similar tax or duty payable in Luxembourg by Noteholders as a consequence of the issue of the Notes, nor will any of these taxes be payable as a consequence of a subsequent transfer, repurchase or redemption of the Notes. Proceedings in a Luxembourg court or the presentation of documents relating to the Notes, other than the Notes themselves, to an "autorité constituée" may require registration of the documents, in which case the documents will be subject to registration duties depending on the nature of the documents. In particular, a loan agreement not represented by the Notes will be subject to an ad valorem registration duty of 0.24 percent of the amounts mentioned therein.

There is no Luxembourg value added tax payable in respect of payments in consideration for the issue of the Notes or in respect of the payment of interest or principal under the Notes or the transfer of the Notes. Luxembourg value added tax may, however, be payable in respect of fees charged for certain services rendered to the Issuer, if for Luxembourg value added tax purposes such services are rendered or are deemed to be rendered in Luxembourg and an exemption from Luxembourg value added tax does not apply with respect to such services.

No Luxembourg gift, estate or inheritance tax is levied on the transfer of the Notes upon death of a Noteholder in cases where the deceased was not a resident of Luxembourg for inheritance tax purposes.

## UNITED KINGDOM

The following is a general description of certain UK withholding tax, stamp duty and stamp duty reserve tax considerations relating to the Notes and is not intended to be exhaustive. It is based on current UK tax law and HM Revenue & Customs ("**HMRC**") published practice and does not discuss any other UK tax considerations relating to the Notes, including but not limited to their acquisition, holding or disposal. Prospective noteholders should consult their own tax advisors as to the consequences, both under the tax law of the country of which they are resident for tax purposes and (if different) the tax law of the UK, of acquiring, holding and disposing of the Notes and receiving payments of interest, principal and/or other amounts under the Notes.

**Withholding tax**

Payments of interest on the Notes will be made without withholding or deduction for or on account of UK income tax, provided that such interest does not have a UK source. It is currently expected that the circumstances will be such that interest on the Notes should not have a UK source.

If payments of interest on the Notes do have a UK source, payments may still be made without withholding or deduction for or on account of UK income tax provided that the Notes constitute "quoted Eurobonds" within the meaning of section 987 of the Income Tax Act 2007 (the "**Income Tax Act**"). The Notes will constitute quoted Eurobonds within the meaning of this section so long as they are and continue to be listed on a "recognised stock exchange" within the meaning of section 1005 of the Income Tax Act. In the case of Notes to be traded on the London Stock Exchange, which is a recognised stock exchange, this condition will be satisfied if the Notes are admitted to listing on the Official List and to trading on the London Stock Exchange.

**Stamp duty and Stamp Duty Reserve Tax**

No UK stamp duty or stamp duty reserve tax will be payable on the issue or, providing any instrument of transfer is executed and retained outside of the UK, a transfer of the Notes.

**Provision of Information**

Persons in the UK by or through whom interest is paid to, or by or through whom interest is received on behalf of, another person who is an individual may, in certain circumstances, be required to provide information to HMRC regarding the payment and the individual concerned (including as to the identity of the individual). These provisions will apply whether the individual is resident in the UK or elsewhere. In certain circumstances, the information may be exchanged with tax authorities in other jurisdictions.

The provisions referred to above may also apply, in certain circumstances, to payments made on redemption of Notes where the amount payable on redemption is greater than the amount payable on the issue of the Notes. However, in relation to amounts payable on the redemption of such Notes, HMRC published practice indicates that HMRC will not exercise its power to obtain information where such amounts are paid or received on or before 6 April 2009.

## United States Federal Income Tax

The following discussion is a summary based on present law of certain US federal income tax considerations relevant to the purchase, ownership and disposition of the Notes. This discussion addresses only US Holders who purchase Notes in the original offering at the original offering price, hold the Notes as capital assets and use the US dollar as their functional currency. This discussion is not a complete description of all US tax considerations relating to the Notes. It does not address the tax treatment of prospective purchasers that will hold the Notes in connection with a permanent establishment. It also does not address the tax treatment of prospective purchasers subject to special rules, such as banks, dealers, traders that elect to mark to market, insurance companies, investors liable for the alternative minimum tax, US expatriates, tax-exempt entities or persons holding the Notes as part of a hedge, straddle, conversion or other integrated financial transaction. It also does not address prospective purchasers of further Notes, which may be issued at a discount or premium.

No authority directly addresses the US federal income tax characterisation of securities like the Notes and the Issuer has not and will not seek a ruling from the US Internal Revenue Service ("**IRS**") as to their characterisation for such purposes. To the extent relevant for US federal income tax purposes, the Issuer intends to treat the Notes as indebtedness for such purposes and this discussion assumes that treatment is correct. No assurance can be given that the IRS will not assert, or a court would not sustain, a position regarding the characterisation of the Notes that is contrary to this discussion. Alternative characterisations include treatment of the Notes as beneficial ownership of the Loan or as equity in the Issuer, which is a passive foreign investment company ("**PFIC**"). Prospective investors should seek advice from their own tax advisors as to the consequences to them of alternative characterisations of the Notes for US federal income tax purposes.

**THE FOLLOWING STATEMENTS ABOUT US FEDERAL TAX ISSUES ARE MADE TO SUPPORT MARKETING OF THE NOTES. NO TAXPAYER CAN RELY ON THEM TO AVOID TAX PENALTIES. EACH PROSPECTIVE PURCHASER SHOULD SEEK ADVICE FROM AN INDEPENDENT TAX ADVISOR ABOUT THE TAX CONSEQUENCES UNDER ITS OWN PARTICULAR CIRCUMSTANCES OF INVESTING IN NOTES UNDER THE LAWS OF LUXEMBOURG, THE RUSSIAN FEDERATION, THE UNITED STATES AND ITS CONSTITUENT JURISDICTIONS AND ANY OTHER JURISDICTION WHERE THE PURCHASER MAY BE SUBJECT TO TAXATION.**

For purposes of this discussion, a "**US Holder**" is a beneficial owner that is, for purposes of US federal income taxation, (i) an individual citizen or resident of the United States, (ii) a corporation, partnership or other business entity created or organised under the laws of the United States or its political subdivisions, (iii) a trust subject to the control of a US person and the primary supervision of a US court, or (iv) an estate the income of which is subject to US federal income taxation regardless of its source.

If a partnership acquires or holds the Notes, the tax treatment of a partner generally will depend upon the status of the partner and the activities of the partnership. A partner of a partnership that acquires or holds the Notes should consult its own tax advisors.

### Interest

Stated interest paid on the Notes, including any additional payments, will be included in the gross income of a US Holder in accordance with the holder's regular method of tax accounting. The interest and any original issue discount ("**OID**") accrued on the Notes will generally be ordinary income from sources outside the United States.

A US Holder of a Note issued with OID must accrue the OID into income on a constant yield to maturity basis whether or not it receives cash payments. Generally, a Note will have OID to the extent that its stated redemption price at maturity exceeds its issue price. However, a Note generally will not have OID if the stated redemption exceeds its issue price by less than ¼ of 1 percent of the Note's stated redemption price at maturity multiplied by the number of complete years to maturity ("**de minimis OID**"). The issue price of a Note is the initial offering price at which a substantial amount of the Notes are sold (excluding sales to brokers or similar persons). The stated redemption price at maturity of a Note is the total of all payments due on the Note other than payments of qualified stated interest. In general, qualified stated interest is interest that is unconditionally payable at least annually at a single fixed rate, provided reasonable legal remedies exist to compel timely payment or the terms of which make non-payment remote.

A US Holder may elect to recognise all yield on a Note (including de minimis OID) using a constant yield method. The constant yield election generally will apply only to the Note with respect to which it is made, and it may not be revoked without the consent of the IRS.

It is possible that interest on the Notes will not be treated as qualified stated interest. In such circumstances, all interest (and any discount) on the Notes would be treated as OID and a US Holder would be required to include the OID in income on a constant yield to maturity basis whether or not it receives a cash payment on any payment date. Assuming the Notes are issued at par and stated interest is paid on time, US Holders generally would recognise income for each interest accrual period equal to the amount paid during that period.

It is unclear whether a US Holder of Notes eligible for benefits under the income tax treaty between the Russian Federation and the United States may claim an exemption from Russian withholding tax, if any, imposed on the Notes. A US Holder also may not be able to claim a deduction or a foreign tax credit for Russian withholding tax, if any, imposed on the Notes. Each US Holder should consult its own tax advisor about its eligibility for exemption from, and its ability to credit or deduct, Russian withholding tax, if any, imposed on the Notes.

**Disposition**

A US Holder will recognise gain or loss on the sale, redemption or other disposition of a Note in an amount equal to the difference between the US dollar value of the amount realised (less any accrued but unpaid interest, which will be taxable as interest income to the extent not previously included in income) and the US Holder's adjusted tax basis in the Note. A US Holder's adjusted tax basis in a Note generally will be the amount the US Holder paid for the Note increased by OID included in the US Holder's income with respect to the Note and reduced by payments other than qualified stated interest.

Gain or loss on disposition of a Note generally will be US source capital gain or loss. A US Holder will have long-term capital gain or loss if it has held the Note for more than one year. The long-term capital gains of non-corporate US Holders may be taxed at lower rates. Deductions for capital losses are subject to limitations.

**Information Reporting and Backup Withholding**

Payments of principal and interest on and proceeds from the sale, redemption or other disposition of a Note by a US paying agent or other US intermediary may be reported to the IRS unless the holder (i) is a corporation, (ii) provides a properly executed IRS Form W-8BEN or (iii) otherwise establishes a basis for exemption. Backup withholding tax may apply to amounts subject to reporting if the holder fails to provide an accurate taxpayer identification number, otherwise fails to certify its exempt status or fails to report all interest and dividends required to be shown on its US federal income tax returns. A holder can claim a credit against its US federal income tax liability for the amount of any backup withholding tax and a refund of any excess. Holders should consult their tax advisers as to their qualification for exemption from backup withholding and the procedure for obtaining an exemption.

THE ABOVE DISCUSSION IS A GENERAL SUMMARY. IT DOES NOT COVER ALL TAX MATTERS THAT MAY BE OF IMPORTANCE TO A PARTICULAR INVESTOR. EACH PROSPECTIVE INVESTOR IS STRONGLY URGED TO CONSULT ITS OWN TAX ADVISOR ABOUT THE TAX CONSEQUENCES TO IT OF AN INVESTMENT IN THE NOTES.

**EUROPEAN UNION**

Under the European Council Directive 2003/48/EC on the taxation of savings income, each Member State is required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a paying agent within its jurisdiction to or for an individual beneficial owner who is resident in that other Member State. However, for a transitional period, Austria, Belgium and Luxembourg will (unless during such period they elect otherwise) instead apply a withholding system in relation to such payments. Under such a withholding system, tax will be deducted at rates rising over time from 15 percent (as at July 2005) to 20 percent (as at 1 July 2008) and finally to 35 percent (as at 1 July 2011), unless the recipient of the interest payment elects instead for an exchange of information procedure or presents a certificate from the relevant tax authority establishing exemption therefrom. The end of the transitional period depends on the conclusion of certain other agreements relating to information exchange with certain other countries.

A number of non-EU countries, and certain dependent or associated territories of certain Member States, have agreed to adopt similar measures (either provision of information or transitional withholding) in relation to payments made by a person within their respective jurisdictions to an individual beneficial owner who is resident in a Member State. In addition, the Member States have entered into reciprocal provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to an individual beneficial owner who is resident in one of those territories. The attention of the Noteholders is drawn to Condition 8(c) of the Terms and Conditions of the Notes.

Noteholders and potential investors are advised to consult their professional advisors concerning possible taxation or other consequences of purchasing, holding, selling or otherwise disposing of the Notes under the laws of their country of incorporation, establishment, citizenship, residence or domicile. The above statements on taxation are based on the laws and practices in force at the date of this Prospectus. As is the case with any investment, there can be no guarantee that the tax position or proposed tax position at the time of an investment will endure indefinitely.

## ERISA

ERISA imposes fiduciary standards and certain other requirements on employee benefit plans subject thereto (collectively, "**ERISA Plans**"), including collective investment funds, separate accounts, and other entities or accounts whose underlying assets are treated as assets of such plans pursuant to the US Department of Labor "plan assets" regulation, 29 CFR Section 2510.3-101 (the "**Plan Assets Regulation**") and on those persons who are fiduciaries with respect to ERISA Plans.

Section 406 of ERISA and Section 4975 of the Internal Revenue Code (the "**Code**") prohibit certain transactions involving the assets of an ERISA Plan (as well as those plans that are not subject to ERISA but which are subject to Section 4975 of the Code (together with ERISA Plans, "**Plans**")) and certain persons (referred to as **"Parties in Interest**" or "**Disqualified Persons**") having certain relationships to such Plans, unless a statutory or administrative exemption applies to the transaction. In particular, an extension of credit between a Plan and a "party in interest" or "disqualified person" may constitute a prohibited transaction. It is possible that the Notes, even if regarded as equity for purposes of the Plan Assets Regulations (as discussed below) would nevertheless be regarded as debt for purposes of the prohibited transaction rules of ERISA and Section 4975 of the Code. A party in interest or disqualified person who engages in a prohibited transaction may be subject to excise taxes or other liabilities under ERISA and the Code.

Government plans, church plans and non-US plans, while not subject to the fiduciary responsibility provisions of ERISA or the provisions of Section 4975 of the Code, may nevertheless be subject to Federal, state, local or non-US laws that are similar to the foregoing provisions of ERISA or the Code (any such law, a "**Similar Law**").

The Issuer or the Trustee, directly or through affiliates, may be considered a party in interest or disqualified person with respect to many Plans. Prohibited transactions within the meaning of Section 406 of ERISA or Section 4975 of the Code may arise if the Notes are acquired by a Plan with respect to which the Issuer or the Trustee or any of their respective affiliates is a party in interest or a disqualified person, unless the Notes are acquired pursuant to and in accordance with an applicable exemption. Certain exemptions from the prohibited transaction provisions of Section 406 of ERISA and Section 4975 of the Code may apply depending in part on the type of Plan fiduciary making the decision to acquire a Note and the circumstances under which that decision is made. However, Notes may not be acquired by any Plans as discussed below.

Under a "look-through rule" set forth in the Plan Assets Regulation, if a Plan invests in an "equity interest" of an entity and no other exception applies, the Plan's assets include both the equity interest and an undivided interest in each of the entity's underlying assets. This rule will only apply where equity participation in an entity by benefit plan investors is "significant". Equity participation by benefit plan investors is significant if 25 percent or more of the value of any class of equity interest in the entity is held by benefit plan investors. An equity interest does not include debt (as determined by applicable local law) which does not have substantial equity features. The term "benefit plan investor" as defined in Section 3(42) of ERISA, includes (a) an employee benefit plan (as defined in Section 3(3) of ERISA) subject to Title I of ERISA, (b) a plan to which Section 4975(e)(1) of the Code applies or (c) an entity whose underlying assets include "plan assets" by reason of any such plan's investment in the entity. Where the value of an interest in an entity relates solely to identified property of the entity, that property is treated as the sole property of a separate entity.

Because the Notes do not represent an interest in any property of the Issuer other than the relevant Loan, they may be regarded for ERISA purposes as equity interests in a separate entity whose sole asset is the relevant Loan. Further, the Issuer will not be able to monitor the Noteholders' possible status as benefit plan investors. Accordingly, the Notes should not be acquired by any benefit plan investor.

BY ITS PURCHASE AND HOLDING OF A NOTE OR ANY INTEREST THEREIN, THE PURCHASER AND/OR HOLDER THEREOF AND EACH TRANSFEREE WILL BE DEEMED TO HAVE REPRESENTED AND WARRANTED AT THE TIME OF ITS PURCHASE AND THROUGHOUT THE PERIOD THAT IT HOLDS SUCH NOTE OR INTEREST THEREIN, THAT (1) IT IS NOT A BENEFIT PLAN INVESTOR (AS DEFINED IN SECTION 3(42) OF ERISA) OR A GOVERNMENT PLAN, A CHURCH PLAN OR A NON-US PLAN THAT IS SUBJECT TO ANY SIMILAR LAW,) AND (2) IT WILL NOT SELL OR OTHERWISE TRANSFER ANY SUCH NOTE OR INTEREST TO ANY PERSON WITHOUT FIRST OBTAINING THESE SAME FOREGOING REPRESENTATIONS AND WARRANTIES FROM THAT PERSON.

## SELLING AND TRANSFER RESTRICTIONS

### RULE 144A NOTES

Each purchaser of Rule 144A Notes, by accepting delivery of this Prospectus and the Notes, will be deemed to have represented, agreed and acknowledged that:

(1) It is (a) a QIB that is also a QP, (b) not a broker-dealer which owns and invests on a discretionary basis less than US$25 million in securities of unaffiliated issuers, (c) not a participant-directed employee plan, such as a 401 (k) plan, (d) acquiring such Notes for its own account, or for the account of one or more QIBs each of which is also a QP, (e) not formed for the purpose of investing in the Notes or the Issuer, and (f) aware, and each beneficial owner of such Notes has been advised, that the sale of such Notes to it is being made in reliance on Rule 144A.

(2) It will (a) along with each account for which it is purchasing, hold and transfer beneficial interests in the Rule 144A Notes in a principal amount that is not less than US$100,000 and (b) provide notice of these transfer restrictions to any subsequent transferees. In addition, it understands that the Issuer may receive a list of participants holding positions in its securities from one or more book-entry depositories.

(3) It understands that the Rule 144A Notes have not been and will not be registered under the Securities Act and may not be offered, sold, pledged or otherwise transferred except (a) in accordance with Rule 144A to a person that it and any person acting on its behalf reasonably believe is a QIB that is also a QP purchasing for its own account or for the account of one or more QIBs that are also QPs each of which is purchasing not less than US$100,000 principal amount of Notes or (b) outside the United States in accordance with Rule 903 or Rule 904 of Regulation S under the Securities Act, and in each case in accordance with any applicable securities laws of any State of the United States.

(4) It understands that the Issuer has the power under the Trust Deed to compel any beneficial owner of Rule 144A Notes that is not a QIB and a QP to sell its interest in the Rule 144A Notes, or may sell such interest on behalf of, or purchase such interest from, such owner at the price described in the legend below. The Issuer has the right to refuse to honour the transfer of an interest in the Rule 144A Notes to a US person who is not a QIB and a QP.

(5) It understands that the Rule 144A Notes, unless otherwise agreed between the Issuer and the Trustee in accordance with applicable law, will bear a legend to the following effect:

THIS NOTE AND THE LOAN IN RESPECT HEREOF HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE US SECURITIES ACT OF 1933, AS AMENDED (THE "**SECURITIES ACT**") OR WITH ANY SECURITIES REGULATORY AUTHORITY OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES AND MAY NOT BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED EXCEPT (1) IN ACCORDANCE WITH RULE 144A UNDER THE SECURITIES ACT ("**RULE 144A**") TO A PERSON THAT THE HOLDER AND ANY PERSON ACTING ON ITS BEHALF REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER WITHIN THE MEANING OF RULE 144A (A "**QIB**") THAT IS A QUALIFIED PURCHASER (A "**QP**") WITHIN THE MEANING OF SECTION 2(a)(51) OF THE US INVESTMENT COMPANY ACT OF 1940 (THE "**INVESTMENT COMPANY ACT**") PURCHASING FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF A QIB THAT IS ALSO A QP WHOM THE HOLDER HAS INFORMED, IN EACH CASE, THAT SUCH OFFER, SALE, PLEDGE OR OTHER TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A, AND IN AN AMOUNT NOT LESS THAN US$100,000 PRINCIPAL AMOUNT OF NOTES OR (2) OUTSIDE THE UNITED STATES IN ACCORDANCE WITH RULE 903 OR RULE 904 OF REGULATION S UNDER THE SECURITIES ACT ("**REGULATION S**"), AND IN EACH CASE IN ACCORDANCE WITH ANY APPLICABLE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES, AND THE HOLDER WILL, AND EACH SUBSEQUENT HOLDER IS REQUIRED TO, NOTIFY ANY PURCHASER FROM IT OF THE NOTES IN RESPECT HEREOF OF THE RESALE RESTRICTIONS REFERRED TO ABOVE. TRANSFER IN VIOLATION OF THE FOREGOING WILL BE OF NO FORCE OR EFFECT, WILL BE VOID AB INITIO AND WILL NOT OPERATE TO TRANSFER ANY RIGHTS TO THE TRANSFEREE, NOTWITHSTANDING ANY INSTRUCTIONS TO THE CONTRARY TO THE ISSUER OF THIS NOTE, THE TRUSTEE OR ANY INTERMEDIARY. NO REPRESENTATION CAN BE

MADE AS TO THE AVAILABILITY OF ANY EXEMPTION UNDER THE SECURITIES ACT FOR RESALES OF THIS NOTE.

EACH BENEFICIAL OWNER HEREOF REPRESENTS THAT (1) IT IS A QIB THAT IS ALSO A QP; (2) IT IS NOT A BROKER-DEALER WHICH OWNS AND INVESTS ON A DISCRETIONARY BASIS LESS THAN US$25,000,000 IN SECURITIES OF UNAFFILIATED ISSUERS; (3) IT IS NOT A PARTICIPANT-DIRECTED EMPLOYEE PLAN, SUCH AS A 401 (k) PLAN; (4) IT IS HOLDING THIS NOTE FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF ANOTHER QIB THAT IS ALSO A QP; (5) IT WAS NOT FORMED FOR THE PURPOSE OF INVESTING IN THE ISSUER OR THIS NOTE; (6) IT, AND EACH ACCOUNT FOR WHICH IT HOLDS NOTES, WILL HOLD AND TRANSFER AT LEAST US$100,000 IN PRINCIPAL AMOUNT OF NOTES; (7) IT UNDERSTANDS THAT THE ISSUER MAY RECEIVE A LIST OF PARTICIPANTS HOLDING POSITIONS IN ITS SECURITIES FROM ONE OR MORE BOOK-ENTRY DEPOSITORIES AND (8) IT WILL PROVIDE NOTICE OF THE FOREGOING TRANSFER RESTRICTIONS TO ITS SUBSEQUENT TRANSFEREES. THE BENEFICIAL OWNER HEREOF HEREBY ACKNOWLEDGES THAT, IF AT ANY TIME WHILE IT HOLDS AN INTEREST IN THIS NOTE IT IS A PERSON WHO IS NOT A QIB THAT IS ALSO A QP, THE ISSUER MAY (A) COMPEL IT TO SELL ITS INTEREST IN THIS NOTE TO A PERSON (I) WHO IS ALSO A QIB THAT IS ALSO A QP AND WHO IS OTHERWISE QUALIFIED TO PURCHASE THIS NOTE IN A TRANSACTION EXEMPT FROM REGISTRATION UNDER THE SECURITIES ACT OR (II) OUTSIDE THE UNITED STATES IN ACCORDANCE WITH RULE 903 OR 904 OF REGULATION S OR (B) COMPEL THE BENEFICIAL OWNER TO SELL ITS INTEREST IN THIS NOTE TO THE ISSUER OR AN AFFILIATE OF THE ISSUER OR TRANSFER ITS INTEREST IN THIS NOTE TO A PERSON DESIGNATED BY OR ACCEPTABLE TO THE ISSUER AT A PRICE EQUAL TO THE LEAST OF (X) THE PURCHASE PRICE THEREFOR PAID BY THE BENEFICIAL OWNER, (Y) 100 PERCENT OF THE PRINCIPAL AMOUNT THEREOF OR (Z) THE FAIR MARKET VALUE THEREOF. THE ISSUER HAS THE RIGHT TO REFUSE TO HONOUR A TRANSFER OF AN INTEREST IN THIS NOTE TO A PERSON WHO IS NOT A QIB AND A QP. THE ISSUER HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE INVESTMENT COMPANY ACT.

EACH BENEFICIAL OWNER HEREOF OR OF ANY INTEREST HEREIN REPRESENTS AND WARRANTS THAT FOR SO LONG AS IT HOLDS THIS NOTE OR ANY INTEREST HEREIN (1) IT IS NOT (A) A BENEFIT PLAN INVESTOR (AS DEFINED IN SECTION 3(42) OF THE UNITED STATES EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974, AS AMENDED ("**ERISA**")) OR (B) A GOVERNMENTAL, CHURCH OR NON-U.S. PLAN THAT IS SUBJECT TO ANY FEDERAL, STATE, LOCAL OR NON-U.S. LAW THAT IS SUBSTANTIALLY SIMILAR TO THE PROVISIONS OF SECTION 406 OF ERISA OR SECTION 4975 OF THE CODE OR ANY ENTITY WHOSE ASSETS ARE TREATED AS ASSETS OF ANY SUCH PLAN, AND (2) IT WILL NOT SELL OR OTHERWISE TRANSFER ANY SUCH NOTE OR INTEREST TO ANY PERSON WITHOUT FIRST OBTAINING THESE SAME FOREGOING REPRESENTATIONS AND WARRANTIES "BENEFIT PLAN INVESTORS" INCLUDE (1) ANY EMPLOYEE BENEFIT PLAN (AS DEFINED IN SECTION 3(3) OF ERISA), THAT IS SUBJECT TO PART 4 OF TITLE I OF ERISA, (2) ANY PLAN DESCRIBED IN SECTION 4975(e)(1) OF THE UNITED STATES INTERNAL REVENUE CODE OF 1986, AS AMENDED (THE "**CODE**"), INCLUDING, WITHOUT LIMITATION, INDIVIDUAL RETIREMENT ACCOUNTS AND KEOGH PLANS, AND (3) ANY ENTITY WHOSE UNDERLYING ASSETS INCLUDE PLAN ASSETS BY REASON OF A PLAN'S INVESTMENT IN THE ENTITY PURSUANT TO THE PLAN ASSET REGULATION ISSUED BY THE UNITED STATES DEPARTMENT OF LABOR, 29 C.F.R. SECTION 2510.3-101, AS MODIFIED BY SECTION 3(42) OF ERISA (INCLUDING, FOR THIS PURPOSE, THE GENERAL ACCOUNT OF AN INSURANCE COMPANY, ANY OF THE UNDERLYING ASSETS OF WHICH CONSTITUTE "PLAN ASSETS" UNDER SECTION 401(C) OF ERISA, OR A WHOLLY-OWNED SUBSIDIARY THEREOF).

THE ISSUER MAY COMPEL EACH BENEFICIAL OWNER HEREOF TO CERTIFY PERIODICALLY THAT SUCH OWNER IS A QIB AND A QP.

(6) It understands and acknowledges that its purchase and holding of such Notes constitutes a representation and agreement by it that, by its purchase and holding of such Notes or any interest therein, the purchaser and/or holder thereof and each transferee will be deemed to have represented and warranted at the time of its purchase and throughout the period that it holds such Note or any interest therein, that (1) it is not (i) a Benefit Plan Investor (as defined in Section 3(42) of the United States Employee Retirement Income Security Act of 1974, as amended ("ERISA")) or (ii) a governmental, church or non-U.S. plan that is subject to any federal, state, local or non-U.S. law that is substantially similar to the provisions of Section 406 of ERISA or Section 4975 of the Code or any entity whose assets are treated as assets of any such plan, and (2) it will not sell or otherwise transfer any such note or interest to any person without first obtaining these same foregoing representations and warranties. "Benefit Plan Investors" include (1) any employee benefit plan (as defined in Section 3(3) of ERISA), that is subject to Part 4 of Title I of ERISA, (2) any plan described in Section 4975(e)(1) of the United States Internal Revenue Code of 1986, as amended (the "Code"), including, without limitation, individual retirement accounts and Keogh plans, and (3) any entity whose underlying assets include plan assets by reason of a plan's investment in the entity pursuant to the Plan Asset Regulation issued by the United States Department of Labor, 29 C.F.R. Section 2510.3-101, as modified by Section 3(42) of ERISA (including, for this purpose, the general account of an insurance company, any of the underlying assets of which constitute "plan assets" under section 401(c) of ERISA, or a wholly-owned subsidiary thereof). It acknowledges that the Issuer, the Company, the Registrar, the Managers and their respective affiliates, and others will rely upon the truth and accuracy of the above acknowledgements, representations and agreements and agrees that, if any of the acknowledgements, representations or agreements deemed to have been made by it by its purchase of Rule 144A Notes is no longer accurate, it shall promptly notify the Issuer, the Company and the Managers. If it is acquiring any Notes as a fiduciary or agent for one or more investor accounts who are QIBs that are also QPs, it represents that it has sole investment discretion with respect to each such account, and that it has full power to make the above acknowledgements, representations and agreements on behalf of each such account.

(7) It understands that the Rule 144A Notes will be evidenced by the Rule 144A Global Certificate. Before any interest in the Rule 144A Global Certificate may be offered, sold, pledged or otherwise transferred to a person who takes delivery in the form of an interest in the Regulation S Global Certificate, it will be required to provide a Transfer Agent with a written certification (in the form provided in the Agency Agreement) as to compliance with applicable securities laws.

Prospective purchasers are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A.

**Regulation S Notes**

Each purchaser of Regulation S Notes by accepting delivery of this Prospectus and the Regulation S Notes, will be deemed to have represented, agreed and acknowledged that:

(1) It is, or at the time Regulation S Notes are purchased will be, the beneficial owner of such Regulation S Notes and (a) it is not a US person and it is located outside the United States (within the meaning of Regulation S) and (b) it is not an affiliate of the Issuer, the Company or a person acting on behalf of such an affiliate.

(2) It understands that the Regulation S Notes have not been and will not be registered under the Securities Act and that, prior to the expiration of the "distribution compliance period" (as such term is defined in Rule 902 of Regulation S), it will not offer, sell, pledge or otherwise transfer such Notes except (a) in accordance with Rule 144A to a person that it and any person acting on its behalf reasonably believes is a QIB that is also a QP purchasing for its own account or for the account of a QIB that is also a QP or (b) to a non-US person in an offshore transaction in accordance with Rule 903 or Rule 904 of Regulation S, in each case in accordance with any applicable securities laws of any state of the United States.

(3) It understands that the Regulation S Notes will be evidenced by the Regulation S Global Certificate. Before any interest in the Regulation S Global Certificate may be offered, sold, pledged or otherwise transferred to a person who takes delivery in the form of an interest in the Rule 144A Global

Certificate, it will be required to provide a Transfer Agent with a written certification (in the form provided in the Agency Agreement) as to compliance with applicable securities laws.

(4) It understands and acknowledges that its purchase and holding of such Notes constitutes a representation and agreement by it that, by its purchase and holding of such Notes or any interest therein, the purchaser and/or holder thereof and each transferee will be deemed to have represented and warranted at the time of its purchase and throughout the period that it holds such Note or any interest therein, that (1) it is not (i) a Benefit Plan Investor (as defined in Section 3(42) of the United States Employee Retirement Income Security Act of 1974, as amended ("ERISA")) or (ii) a governmental, church or non-U.S. plan that is subject to any federal, state, local or non-U.S. law that is substantially similar to the provisions of Section 406 of ERISA or Section 4975 of the Code or any entity whose assets are treated as assets of any such plan, and (2) it will not sell or otherwise transfer any such note or interest to any person without first obtaining these same foregoing representations and warranties. "Benefit Plan Investors" include (1) any employee benefit plan (as defined in Section 3(3) of ERISA), that is subject to Part 4 of Title I of ERISA, (2) any plan described in Section 4975(e)(1) of the United States Internal Revenue Code of 1986, as amended (the "Code"), including, without limitation, individual retirement accounts and Keogh plans, and (3) any entity whose underlying assets include plan assets by reason of a plan's investment in the entity pursuant to the Plan Asset Regulation issued by the United States Department of Labor, 29 C.F.R. Section 2510.3-101, as modified by Section 3(42) of ERISA (including, for this purpose, the general account of an insurance company, any of the underlying assets of which constitute "plan assets" under section 401(c) of ERISA, or a wholly-owned subsidiary thereof). It acknowledges that the Issuer, the Company, the Registrar, the Managers and their affiliates and others will rely upon the truth and accuracy of the above acknowledgements, representations and agreements and agrees that, if any of the acknowledgements, representations or agreements deemed to have been made by it by its purchase of Notes is no longer accurate, it shall promptly notify the Issuer, the Company and the Managers. If it is acquiring any Notes as a fiduciary or agent for one or more investor accounts, it represents that it has sole investment discretion with respect to each of those accounts and that it has full power to make the above acknowledgements, representations and agreements on behalf of each account.

## SUBSCRIPTION AND SALE

ABN AMRO Bank N.V., BNP Paribas and Citigroup Global Markets Limited (the "**Joint Bookrunners**") and The Royal Bank of Scotland plc (together with the Joint Bookrunners, the "**Managers**") have, in a subscription agreement dated 25 July 2008 (the "**Subscription Agreement**") and made between the Issuer, the Company and the Managers upon the terms and subject to the conditions contained therein, severally agreed to subscribe and pay for the Notes at their issue price of 100 percent of their principal amount. The Managers are entitled to commissions and reimbursement of expenses pursuant to the Subscription Agreement and a fees and expenses side agreement between, inter alios, the Issuer and the Managers. The Managers are entitled in certain circumstances to be released and discharged from their obligations under the Subscription Agreement prior to the closing of the issue of the Notes.

### United States

The Notes and the Loan have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the benefit of, US persons except in certain transactions exempt from, or not subject to, the registration requirements of the Securities Act. Each Manager has agreed that, except as permitted by the Subscription Agreement, it will not offer, sell or deliver the Notes (i) as part of their distribution at any time or (ii) otherwise until 40 days after the later of the commencement of the offering of the Notes and the closing date of the offering of the Notes, within the United States or to, or for the account or benefit of, US persons, and that it will have sent to each distributor, dealer or person receiving a selling concession, fee or other remuneration to which it sells the Notes (other than a sale pursuant to Rule 144A) during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, US persons. Terms used in this paragraph have the meanings given to them by Regulation S.

Notes offered and sold outside the United States to non-US persons may be sold in reliance on Regulation S. The Subscription Agreement provides that the Managers may directly or through their respective US broker-dealer affiliates arrange for the offer and resale of Notes in the United States only to persons whom they reasonably believe are QIBs and QPs who can represent that (a) they are QPs who are QIBs within the meaning of Rule 144A; (b) they are not broker-dealers who own and invest on a discretionary basis less than US$25 million in securities of unaffiliated issuers; (c) they are not participant-directed employee plans, such as a 401(k) plan; (d) they are acting for their own account, or the account of one or more QIBs each of which is a QP; (e) they are not formed for the purpose of investing in the Issuer or the Notes; (f) each account for which they are purchasing will hold and transfer at least US$100,000 in principal amount of Notes at any time; (g) they understand that the Issuer may receive a list of participants holding positions in its securities from one or more book-entry depositories; and (h) they will provide notice of the transfer restrictions set forth in this Prospectus to any subsequent transferees.

In addition, until 40 days after the commencement of the offering of the Notes, an offer or sale of Notes within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with Rule 144A.

The Issuer and the Managers reserve the right to reject any offer to purchase the Notes, in whole or in part, for any reason. This Prospectus does not constitute an offer to any person in whole or in part, for any reason. This Prospectus does not constitute an offer to any person in the United States or to any US person other than any QIB who is also a QP and to whom an offer has been made directly by one of the Managers or its US broker-affiliate. Distribution of this Prospectus by any non-US person outside the United States or by any QIB who is a QP within the United States to any US person or any person within the United States other than any QIB who is a QP, and those persons, if any, retained to advise such person outside the United States or QIB who is a QP with respect thereto, is unauthorised and any disclosure without the prior written consent of the Issuer of any of its contents to any such US person or any person within the United States other than any QIB who is a QP and those persons, if any, retained to advise such non-US person outside the United States or QIB who is a QP, is prohibited.

### United Kingdom

Each Manager has represented and agreed that:

1 it has only communicated or caused to be communicated, and will only communicate or cause to be communicated, any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the "**FSMA**")) received by it in connection with the issue or sale of any Notes in circumstances in which section 21(1) of the FSMA does not apply to the Issuer; and

2 it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

### Russian Federation

Each Manager has acknowledged that no Russian prospectus has been registered or is intended to be registered with respect to the Notes and the Notes have not been and are not intended to be registered in the Russian Federation, and, consequently, each Manager has represented and agreed that it has not offered or sold or otherwise transferred, and will not offer or sell or otherwise transfer, as part of its initial distribution or at any time thereafter, any Notes to or for the benefit of any persons (including legal entities) resident, incorporated, established or having their usual residence in the Russian Federation, or to any person located within the territory of the Russian Federation unless and to the extent otherwise permitted under Russian law; it being understood and agreed that the Managers or their affiliates may distribute this Prospectus to persons in the Russian Federation in a manner that does not constitute an "advertisement" (as defined in Russian law) of Notes and may sell the Notes to Russian persons in a manner that does not constitute "placement" or "public circulation" of the Notes in the Russian Federation (as defined in Russian law).

## LEGAL MATTERS

Certain legal matters in connection with the issue of the Notes will be passed upon for the Company with respect to the laws of the Russian Federation and the United States by Freshfields Bruckhaus Deringer LLP and with respect to the laws of Luxembourg by Arendt & Medernach. Certain legal matters in connection with the issue of the Notes will be passed upon for the Managers with respect to the laws of the United Kingdom and the United States by Linklaters LLP and with respect to the laws of the Russian Federation by Linklaters CIS.

## INDEPENDENT AUDITORS

The Annual Financial Statements included in this Prospectus, have been audited by KPMG Limited, 18 Krasnopresnenskaya Naberezhnaya Block C Moscow 123317 as stated in its report appearing herein. The Interim Financial Statements included in this Prospectus, have been reviewed by KPMG Limited in accordance with International Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity," as stated in its report appearing herein.

## ADDITIONAL INFORMATION

1. The Notes have been accepted for clearance through Euroclear, Clearstream, Luxembourg and DTC. The Common Code and ISIN numbers for the Regulation S Notes are 037618985 and XS0376189857, respectively. The ISIN and CUSIP Numbers for the Rule 144A Notes are US858057AA1 and 858057AA0, respectively.

2. The securitised assets backing the issue of the Notes have characteristics that demonstrate capacity to produce funds to service any payments due and payable on the Notes.

3. The Company and the Issuer has obtained all necessary consents, approval, authorisations or other orders for the issue of the Notes and the other documents to be entered into by the Company and the Issuer in connection with the issue of the Notes in Luxembourg.

4. The issue of the Notes and their offer, sale and listing was approved by the Company's Board of Directors on 23 June 2008.

5. It is expected that listing of the Notes on the Official List and admission of the Notes to trading on the Market will be granted on or before 29 July 2008, subject only to the issue of the Notes. Prior to official listing and admission to trading, however, the London Stock Exchange will permit dealings in accordance with its rules. Transactions will normally be effected for settlements in US dollars and for delivery on the third business day after the day of the transaction. The Company expects that the total expenses related to the listing and admission of the Notes to trading will be approximately US$14,090.

6. There has been no significant change in the financial or trading position of the Company since 31 March 2008, such date being the date of the latest financial statements of the Company.

7. There has been no material adverse change in the prospects of the Company since 31 December 2007, such date being the date of the latest audited financial statements of the Company.

8. Copies in English of the following documents may be inspected at the offices of the Principal Paying and Transfer Agent during usual business hours on any weekday (Saturday, Sunday and public holidays excepted) for so long as any Notes are outstanding:

   (a) the articles of incorporation of the Issuer and of the Company;

   (b) the consolidated financial statements for the year ended 31 December 2007;

   (c) the consolidated condensed interim financial statements for the three months ended 31 March 2008; and

   (d) the Trust Deed to constitute the Notes.

9. The Company prepares annual and interim consolidated financial statements in accordance with IFRS.

10. Save for the fees payable to the Managers, the Trustee and the Agents, and as disclosed in paragraph 13 below, so far as the Company is aware no person, natural or legal, involved in the issue of the Notes has an interest that is material to the issue of the Notes.

11. Neither the Issuer nor the Company intends to provide any post-issuance transaction information regarding the Notes or the performance by the Company of its obligations under the Loan Agreement.

12. With effect from 30 June 2008, the Issuer was substituted in place of Citigroup Global Markets Deutschland AG & Co. KGaA ("**Citigroup Germany**") as the issuer of US$325 million 8.625 percent loan participation notes due 2009 and US$375 million 9.25 percent loan participation notes due 2014, issued by, but without recourse to, Citigroup Germany in February 2004 and April 2004, respectively, for the sole purpose of financing certain loans to the Company.

13. Mr. Ronald Freeman, a member of the Company's Board of Directors, is expected to purchase, at face value, US$1 million of the Notes.

## GLOSSARY

**Alloys**
Various metals or element compositions, of which at least one is a metal, which are added to the liquid steel to achieve certain required properties of the finished steel. Alloys containing iron are referred to as ferroalloys.

**Annealing**
The heat treatment process by which steel products are reheated to a suitable temperature in order to remove stresses resulting from previous processing and to soften them and/or improve their machinability and cold-forming properties.

**Bars**
Long steel products that are rolled from billets blooms or ingots. Merchant bar and reinforcing bar, or rebar, are two common categories of bars, where merchants include rounds, flats, angles, squares and channels that are used by fabricators to manufacture a wide variety of products such as furniture, stair railings and farm equipment. Rebar is used to strengthen concrete structures.

**Basic oxygen furnace**
A pear-shaped furnace, lined with refractory bricks, which refines hot metal from the blast furnace and scrap into steel. Scrap is charged into the furnace vessel, followed by the hot metal from the blast furnace. In top blown BOF, a lance is lowered from above, through which blows a high-pressure stream of oxygen to cause chemical reactions that separate impurities into fumes or slag.

**Beneficiation**
Treatment of the lump ore aimed at achieving higher levels of concentration of the key composition element, such as Fe for the iron ores. Includes crushing, grinding, and often froth-flotation to remove waste rock from ore.

**Billet**
A semi-finished steel product with a square or round cross section. Billet can be either rolled from an ingot/bloom or continuously cast. It is further hot rolled into finished long products. Semi-finished steel products with larger or rectangular cross sections are usually called blooms.

**Blast furnace**
A furnace used in the integrated metallurgical process in which iron ore in the form of sinter and/or pellets is melted down under a hot air blast flow (enriched with oxygen), using carbon in the form of coke, natural gas, pulverized coal or fuel oil as heating and reducing agents. Resulting product is called hot metal (when liquid) or pig iron (when cast).

**Blooms**
See "Billet".

**Coated steel**
Steel coated with a layer of the protective metal (such as zinc, aluminium etc) to prevent corrosion of the base material. An additional layer of organic coating (paint, plastic) can be applied on top of the metal coating. Zinc-coated steel is often referred to as "galvanised steel".

**Cogging**
An intermediate rolling process when a hot ingot is reduced to a bloom or slab in a cogging mill.

**Coils**
Steel strip/sheet in the coiled form.

**Coke**
Product of the coal pyrolisys in coke ovens which is further used as a reducing agent in the blast furnace.

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| **Coke breeze** | Small diameter coke that forms as a result of coke destruction through shipping and handling and is not suitable for use in the blast furnace. Screened off and redirected for other applications. |
| **Coking coal** | Raw material for producing coke, which is further used in the blast furnace iron making. |
| **Cold-rolled sheet** | Sheet steel that has been run through a cold-rolling mill. |
| **Cold-rolling mill** | Equipment that reduces hot rolled strip to specified thickness (gauge) without prior reheating. |
| **Continuous casting** | The process by which semi-finished steel products such as billets, blooms and slabs are manufactured. The liquid steel is poured at a steady rate from a ladle into a bottomless mould. As the molten steel enters the water-cooled mould, it starts to cool into a solid that can then be cut into required lengths. |
| **Cooling-tower** | A structure which cools heated refining process water by circulating the water through a series of louvers and baffles through which cool air is forced by large fans. |
| **Cowper** | A modern furnace to pre-heat the blast air to high temperatures in order to avoid cooling (and thus having to re-heat) the mix, and use fairly complex systems to extract the heat from the hot carbon dioxide when it escapes from the top of the furnace, further improving efficiency. |
| **Debottlenecking** | When the output of a multi-step process is limited by the capacity of one unit or activity, that unit or activity is a bottleneck. Debottlenecking in a step or measure to resolve a bottleneck situation. |
| **Dolomite** | A sedimentary rock composed largely of calcium magnesium carbonate used as flux in the steelmaking. |
| **Draglines** | Large scale mining equipment for removing overburden and inter-zone rock intervals. The rock is removed along a long strip by dragging a bucket capable of holding up to 90 cubic metres until the top of the coal is exposed. Waste rock is deposited behind the active mining area on land under which the coal has already been removed. This waste rock is then smoothed and land surface reclamation to restore the surface to its pre-mining condition is undertaken. |
| **Electric arc furnace (“EAF”)** | A furnace that melts and scrap substitutes and occasionally hot metal into steel. In this process, the proportion of scrap used can be increased to 100 percent of the metallic charge. Once the furnace is charged and covered, graphite electrodes are lowered through holes in the roof. The electric arc between the electrodes and the metallic charge surface creates intense heat that melts the charge. Alloying elements surface can be added at the tapping stage. |
| **Ferrous** | Metals that consist primarily of iron. |

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| **Flat products** | A product of the rolling process with a large width to thickness ratio. The major flat steel product categories are (i) thin flat products (up to 4mm in thickness); (ii) thick flat products (between 4 millimetres and 50 millimetres in thickness); and (iii) plates (over 50 millimetres in thickness). Flat products are used in the automotive and white-goods industries, for production of large welded pipes, shipbuilding, construction, major works and boilers. They include hot- and cold-rolled sheet, plates and coils. |
| **Galvanised steel** | See "Coated Steel". |
| **Galvannealed** | Steel that is zinc-iron alloy-coated by the hot-dip process followed by heating the steel to induce diffusion alloying between the molten zinc coating and the steel. |
| **High Strength Low Alloy steel ("HSLA")** | A type of steel that provides many benefits over regular steel. It is much tougher and stronger than ordinary carbon-based steel. It is used in cars, trucks, cranes, bridges and other structures that must be able to handle a lot of strain. |
| **Hot-rolled steel** | Product of a hot-rolling process. |
| **Hot-rolling** | A process whereby semi finished steel products (such slab, billet, bloom), preheated to a high temperature, is rolled to required geometrical dimensions and mechanical properties. |
| **Ingot** | An intermediate steel product made by pouring liquid steel into moulds of certain dimensions. The ingots are first reduced to the semi-finished products such as blooms or slabs by the cogging mill and then further fed to the hot-rolling mills. Ingot casting is now largely replaced by continuous casting, unless specifically called for by the quality requirements. |
| **Integrated metallurgical process** | Steel making process under which steel is produced from the on site generated hot metal, as opposed to the scrap-based steel making. Same site will usually also include coking and/or sintering facilities, generating the raw materials for the blast furnace operations, as well as rolling and other downstream. |
| **Ladle furnace** | A furnace used for refining hot metal between the steel making furnaces and casting. |
| **Lance (Oxygen)** | A pipe used to convey oxygen onto a bath of molten metal. A steel tube, consumed during cutting, through which cutting oxygen passes, for the cutting or boring of holes. |
| **Long products** | Long products are used in all industrial sectors, particularly in the construction and engineering industries. They include all types of bars, wire rod and a wide range of cold-formed profiles like closed profile, S-shape profile, E-shape profile, trough-shape profile, angle profile and others. They also include pipes with circular, oblong and semi-oblong, square and rectangular cross sections of a wide range of sizes. |
| **Long-wall mining** | A mining technique in which large blocks of coal are removed in a single pass. This technique uses two tunnels which are about 1,500 metres long and 250 metres apart and are joined together at the end by a third tunnel. The third tunnel marks the spot where longwall mining starts. |

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| **Metallurgical lime** | Quick lime. Slag-former and lining protector used in metallurgical processes. |
| **Metalware** | Small industrial, household and similar articles made from wire and wire rod. |
| **Middlings** | The mixture of water, clay, sand and bitumen that remains between the bitumen froth at the surface and the sand at the bottom of a primary separation vessel. |
| **Open-hearth furnace** | A broad, shallow hearth to refine hot metal and scrap into steel (also known as a "Martin furnace"). Process heat is provided by the fuel burners situated over the surface of the molten metal and the refining usually takes 7-9 hours. |
| **Open-pit methods** | Open-pit mining refers to a method of extracting rock or minerals from the earth by their removal from an open pit or borrow. The term is used to differentiate this form of mining from extractive methods that require tunnelling into the earth. |
| **Pellets** | Little balls of condensed iron ore concentrate fines and fluxing materials which are hardened by heat for further use by blast furnaces for reduction into hot metal. |
| **Pickling** | The process in which the surface of the steel is cleaned with acid to remove scale, rust and dirt, such process being preparation for further processing, such as cold-rolling, galvanising or polishing. |
| **Polymer-coated steel products** | A variety of products produced either by film coating or direct extrusion of a multi-layer polymer coating. |
| **Refining** | A process stage between steel melting and casting, during which the undesired residuals are removed and the alloys are added (see also "Ladle furnace"). |
| **Reinforcing bar or Rebar** | A commodity grade steel used to strengthen concrete in highway and building construction. |
| **Scrap** | Iron containing material (mainly industrial or household waste) that is re-melted and recast into new steel. The scrap is used as a component of the metallic charge of the steel making furnaces, such as BOF and EAF, together with hot metal, pig iron etc. |
| **Semi-finished products** | Steel products such as billet, blooms and slabs. These products can be made by direct continuous casting of the liquid steel or by rolling of the cast ingots through a clogging mill. |
| **Sinter** | Porous chunks of the agglomerated iron ore concentrate and limestone flux that are used by blast furnaces for reduction into hot metal. |
| **Slab** | A semi-finished steel product obtained by continuous casting of the liquid steel or by rolling cast ingots through the clogging mill. The slab has a rectangular cross section and is used as feed stock for the flat rolled products. |
| **Slag** | A non-metallic by-product of both iron and steel making processes. |
| **Slitting** | Cutting a steel sheet into narrower strips. |

| | |
|---|---|
| **Strip** | Flat steel products used for production of pipes. Strips with widths of less than 600 millimetres are used for large pipes with a spiral welded seam and smaller pipes with a straight-line welded seam. Large-diameter pipes (of up to 1,420 millimetres diameter) with a straight-line welded seam require strips up to 4,600 millimetres wide and 30 millimetres thick. |
| **Tandem mill** | A rolling mill (such as cold-rolling mill) that consists of more than one stand and operates under constant material flow. |
| **Tempering** | Heat treatment of steel aimed at achieving the desired properties (such as ductility etc) |
| **Vacuum degasser** | An advanced steel refining facility that removes oxygen, hydrogen and nitrogen under low pressures (in a vacuum) to produce ultra-low-carbon and low gas residuals steel for demanding electrical and automotive applications. Normally performed in the ladle, the removal of dissolved gases results in cleaner, higher-quality, more pure steel. |

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# OAO Severstal and subsidiaries

Consolidated condensed interim financial statements
for the three months ended March 31, 2008

**OAO Severstal and subsidiaries**

**Consolidated condensed interim financial statements for the three months ended March 31, 2008**

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**Independent Auditors' Report**

Board of Directors

OAO Severstal

**Report on Review of the Interim Financial Information**

*Introduction*

We have reviewed the accompanying consolidated condensed interim balance sheet of OAO Severstal (the "Company") and its subsidiaries (the "Group") as at 31 March 2008, and the related consolidated condensed interim statements of income, changes in equity and cash flows for the three-month period then ended (the "consolidated interim financial information"). Management is responsible for the preparation and presentation of this consolidated interim financial information in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting*. Our responsibility is to express a conclusion on this consolidated interim financial information based on our review.

*Scope of Review*

We conducted our review in accordance with International Standard on Review Engagements 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

*Conclusion*

Based on our review, nothing has come to our attention that causes us to believe that the consolidated interim financial information as at 31 March 2008 and for the three-month period then ended is not prepared, in all material respects, in accordance with International Financial Reporting Standard IAS 34 *Interim Financial Reporting*.

KPMG Limited.

KPMG Limited

15 May 2008

**OAO Severstal and subsidiaries**

**Consolidated condensed interim income statement**
**Three months ended March 31, 2008**
***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

| | Note | Three months ended March 31, 2008 (unaudited) | Three months ended March 31, 2007 (restated, unaudited) |
|---|---|---|---|
| **Sales** | | | |
| Sales — external | | 4,144,363 | 3,526,021 |
| Sales — to related parties | 5 | 164,630 | 166,502 |
| | 3 | 4,308,993 | 3,692,523 |
| Cost of sales | | (3,165,953) | (2,531,468) |
| **Gross profit** | | 1,143,040 | 1,161,055 |
| General and administrative expenses | | (230,850) | (169,410) |
| Distribution expenses | | (275,665) | (233,529) |
| Indirect taxes and contributions | | (45,503) | (35,147) |
| Share of associates' (loss)/profit | | (542) | 2,413 |
| Net (loss)/income from securities operations | | (8,064) | 1,503 |
| Loss on disposal of property, plant and equipment | | (14,495) | (9,230) |
| Net other operating income/(expenses) | 9 | 197,185 | (1,037) |
| **Profit from operations** | | 765,106 | 716,618 |
| Impairment of property, plant and equipment | | (1,855) | (950) |
| Negative goodwill, net | | 2,166 | 633 |
| Net other non-operating expenses | | (32,629) | (17,969) |
| **Profit before financing and taxation** | | 732,788 | 698,332 |
| Interest income | | 28,944 | 36,765 |
| Interest expense | | (90,875) | (68,363) |
| Foreign exchange difference | | 13,887 | (180) |
| **Profit before income tax** | | 684,744 | 666,554 |
| Income tax expense | | (232,770) | (190,279) |
| **Profit from continuing operations** | | 451,974 | 476,275 |
| Profit from discontinued operations | | — | 4,935 |
| **Profit for the period** | | 451,974 | 481,210 |
| Attributable to: | | | |
| shareholders of OAO Severstal | | 438,706 | 458,091 |
| minority interest | | 13,268 | 23,119 |
| Weighted average number of shares outstanding during the period (millions of shares) | | 1,007.7 | 1,007.7 |
| Basic and diluted earnings per share (US dollars) | | 0.44 | 0.45 |

These consolidated condensed interim financial statements were approved by the Board of Directors on May 15, 2008.

The accompanying notes form an integral part of these consolidated condensed interim financial statements.

**OAO Severstal and subsidiaries**

**Consolidated condensed interim balance sheet**
**March 31, 2008**
***(Amounts expressed in thousands of US dollars)***

| | Note | March 31, 2008 (unaudited) | December 31, 2007 (unaudited) |
|---|---|---|---|
| **Assets** | | | |
| **Current assets:** | | | |
| Cash and cash equivalents | | 2,406,295 | 1,619,872 |
| Short-term bank deposits | | 321,472 | 665,977 |
| Short-term financial investments | | 206,127 | 207,632 |
| Trade accounts receivable | | 2,003,879 | 1,719,441 |
| Amounts receivable from related parties | 4 | 99,692 | 78,304 |
| Inventories | | 2,837,856 | 2,609,751 |
| VAT recoverable | | 302,511 | 283,746 |
| Income tax recoverable | | 98,629 | 75,993 |
| Assets held for sale | | 451,662 | 461,197 |
| Other current assets | | 402,584 | 325,961 |
| **Total current assets** | | 9,130,707 | 8,047,874 |
| **Non-current assets:** | | | |
| Long-term financial investments | | 144,216 | 136,496 |
| Investment in associates and joint ventures | | 199,131 | 203,122 |
| Property, plant and equipment | | 8,705,285 | 8,216,615 |
| Intangible assets | | 624,712 | 611,881 |
| Restricted cash | | 14,468 | 13,810 |
| Deferred tax assets | | 61,146 | 52,324 |
| Other non-current assets | | 43,124 | 38,949 |
| **Total non-current assets** | | 9,792,082 | 9,273,197 |
| **Total assets** | | 18,922,789 | 17,321,071 |
| **Liabilities and shareholders' equity** | | | |
| **Current liabilities:** | | | |
| Trade accounts payable | | 1,325,472 | 1,207,185 |
| Amounts payable to related parties | 4 | 72,130 | 58,915 |
| Short-term debt finance | | 1,257,587 | 972,701 |
| Income taxes payable | | 96,978 | 41,382 |
| Other taxes and social security payable | | 297,927 | 200,424 |
| Dividends payable | | 6,078 | 107,485 |
| Liabilities related to assets held for sale | | 103,993 | 91,750 |
| Other current liabilities | | 708,277 | 610,784 |
| **Total current liabilities** | | 3,868,442 | 3,290,626 |
| **Non-current liabilities:** | | | |
| Long- term debt finance | | 2,852,956 | 2,813,011 |
| Deferred tax liabilities | | 436,332 | 399,424 |
| Retirement benefit liability | | 437,514 | 387,398 |
| Other non-current liabilities | | 394,986 | 324,468 |
| **Total non-current liabilities** | | 4,121,788 | 3,924,301 |
| **Equity:** | | | |
| Share capital | | 3,311,288 | 3,311,288 |
| Additional capital | | 1,165,530 | 1,165,530 |
| Foreign exchange differences | | 1,562,220 | 1,145,379 |
| Retained earnings | | 4,404,914 | 4,004,459 |
| Hedging reserve | | (21,698) | — |
| **Total equity attributable to shareholders of parent** | | 10,422,254 | 9,626,656 |
| **Minority interest** | | 510,305 | 479,488 |
| **Total equity** | | 10,932,559 | 10,106,144 |
| **Total equity and liabilities** | | 18,922,789 | 17,321,071 |

The accompanying notes form an integral part of these consolidated condensed interim financial statements.

**OAO Severstal and subsidiaries**

**Consolidated condensed interim statement of cash flows**
**Three months ended March 31, 2008**
***(Amounts expressed in thousands of US dollars)***

| | Three months ended March 31, | |
|---|---|---|
| | **2008 (unaudited)** | **2007 (restated, unaudited)** |
| **Operating activities:** | | |
| Profit before financing and taxation | 732,788 | 698,332 |
| Adjustments to reconcile profit to cash generated from operations: | | |
| Depreciation and amortization | 255,912 | 178,154 |
| Impairment of property, plant and equipment | 1,855 | 950 |
| Provision for inventories, receivables and other provisions | 6,828 | (6,610) |
| Negative goodwill, net | (2,166) | (633) |
| Loss on disposal of property, plant and equipment | 14,495 | 9,230 |
| Loss on disposal of subsidiaries | 3,621 | — |
| Loss/(gain) on remeasurement and disposal of financial investments | 8,064 | (1,503) |
| Share of associates' results less dividends from associates | 542 | (2,413) |
| Changes in operating assets and liabilities: | | |
| Trade accounts receivable | (203,727) | (230,178) |
| Amounts receivable from related parties | (16,531) | 14,812 |
| VAT recoverable | (5,928) | 77,834 |
| Inventories | (88,446) | 105,201 |
| Trade accounts payable | 76,159 | 73,742 |
| Bank customer accounts | — | 11,284 |
| Amounts payable to related parties | 10,105 | (57,502) |
| Other taxes and social security payables | 72,665 | 7,005 |
| Other non-current liabilities | 65,381 | 9,160 |
| Assets held for sale | 35,001 | — |
| Net other changes in operating assets and liabilities | (20,679) | 25,774 |
| **Cash generated from operations** | 945,939 | 912,639 |
| Interest paid (excluding banking operations) | (58,006) | (63,424) |
| Income tax paid | (192,592) | (179,708) |
| **Net cash from operating activities** | 695,341 | 669,507 |
| **Investing activities:** | | |
| Additions to property, plant and equipment | (414,320) | (341,772) |
| Additions to intangible assets | (7,048) | (1,266) |
| Net decrease/(increase) in short-term bank deposits | 358,152 | (549,507) |
| Additions to financial investments and associates | (176,016) | (137,249) |
| Acquisition of minority interests and entities under common control | (44,042) | — |
| Net cash outflow on acquisitions of subsidiaries | — | (45,309) |
| Proceeds from disposal of property, plant and equipment | 1,269 | 6,205 |
| Proceeds from disposal of financial investments | 178,931 | 81,459 |
| Interest received (excluding banking operations) | 29,924 | 28,193 |
| **Cash from investing activities** | (73,150) | (959,246) |
| **Financing activities:** | | |
| Proceeds from debt finance | 840,588 | 328,970 |
| Repayment of debt finance | (662,399) | (269,360) |
| Repayments under lease obligations | (1,553) | — |
| Dividends paid | (103,683) | (17,303) |
| **Cash from financing activities** | 72,953 | 42,307 |
| Effect of exchange rates on cash and cash equivalents | 91,279 | 14,658 |
| **Net increase/(decrease) in cash and cash equivalents** | 786,423 | (232,774) |
| **Cash and cash equivalents at beginning of the period** | 1,619,872 | 1,733,414 |
| **Cash and cash equivalents at end of the period** | 2,406,295 | 1,500,640 |

The accompanying notes form an integral part of these consolidated condensed interim financial statements.

**OAO Severstal and subsidiaries**

**Consolidated condensed interim statement of changes in equity**
**Three months ended March 31, 2008**
***(Amounts expressed in thousands of US dollars)***

| | Attributable to the shareholders of OAO Severstal | | | | | | Minority interest | Total |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Additional capital | Foreign exchange differences | Retained earnings | Hedging reserve | Total | | |
| Balances at December 31, 2006 as previously reported | 3,311,288 | 1,165,530 | 535,591 | 2,983,954 | — | 7,996,363 | 557,645 | 8,554,008 |
| Acquisition of entities under common control (unaudited) | — | — | — | (15,257) | — | (15,257) | 14,986 | (271) |
| Balances at December 31, 2006 (unaudited) | 3,311,288 | 1,165,530 | 535,591 | 2,968,697 | — | 7,981,106 | 572,631 | 8,553,737 |
| Profit for the period (restated, unaudited) | — | — | — | 458,091 | — | 458,091 | 23,119 | 481,210 |
| Foreign exchange differences (restated, unaudited) | — | — | 153,727 | — | — | 153,727 | 3,023 | 156,750 |
| Total recognized income and expenses (restated, unaudited) | | | | | — | 611,818 | 26,142 | 637,960 |
| Dividends (unaudited) | — | — | — | — | — | — | (1,321) | (1,321) |
| Effect of acquisitions and disposals (restated, unaudited) | — | — | — | (25,119) | — | (25,119) | (9,489) | (34,608) |
| Balances at March 31, 2007 (restated, unaudited) | 3,311,288 | 1,165,530 | 689,318 | 3,401,669 | — | 8,567,805 | 587,963 | 9,155,768 |
| Balances at December 31, 2007 as previously reported | 3,311,288 | 1,165,530 | 1,176,321 | 4,082,834 | — | 9,735,973 | 474,706 | 10,210,679 |
| Acquisition of entities under common control (unaudited) | — | — | (30,942) | (78,375) | — | (109,317) | 4,782 | (104,535) |
| Balances at December 31, 2007 (unaudited) | 3,311,288 | 1,165,530 | 1,145,379 | 4,004,459 | — | 9,626,656 | 479,488 | 10,106,144 |
| Profit for the period (unaudited) | — | — | — | 438,706 | — | 438,706 | 13,268 | 451,974 |
| Fair value adjustments of hedges (unaudited) | — | — | — | — | (28,974) | (28,974) | (6,627) | (35,601) |
| Deferred tax on fair value adjustments (unaudited) | — | — | — | — | 7,276 | 7,276 | 1,839 | 9,115 |
| Foreign exchange differences (unaudited) | — | — | 416,841 | — | — | 416,841 | 31,196 | 448,037 |
| Total recognized income and expenses (unaudited) | | | | | | 833,849 | 39,676 | 873,525 |
| Dividends (unaudited) | — | — | — | — | | — | (820) | (820) |
| Effect of acquisitions and disposals (unaudited) | — | — | — | (38,251) | — | (38,251) | (8,039) | (46,290) |
| Balances at March 31, 2008 (unaudited) | 3,311,288 | 1,165,530 | 1,562,220 | 4,404,914 | (21,698) | 10,422,254 | 510,305 | 10,932,559 |

The accompanying notes form an integral part of these consolidated condensed interim financial statements.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

## 1. Accounting policies

These consolidated condensed interim financial statements for OAO Severstal and subsidiaries (the "Group") have been prepared in accordance with International Financial Reporting Standards ("IFRS"), IAS 34 "Interim Financial Reporting", as issued by the International Accounting Standards Board.

In 2007, management decided to change the accounting policy for property, plant and equipment from the revaluation model to the cost model. In accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors", the change in accounting policy was applied retrospectively and comparatives figures for the three months ended March 31, 2007 were restated. The aggregate effect of the change is disclosed in the consolidated financial statements for the year ended December 31, 2007.

The accounting policies and methods of computation applied by the Group in these consolidated condensed interim financial statements are the same as those applied by the Group in its consolidated financial statements for the year ended December 31, 2007.

## 2. Seasonality

There are no material seasonal effects in the business activities of the Group.

## 3. Sales

Sales by product were as follows:

| | Three months ended March 31, | |
|---|---|---|
| | 2008 (unaudited) | 2007 (unaudited) |
| Hot-rolled strip and plate | 968,081 | 950,152 |
| Long products | 924,460 | 773,978 |
| Cold-rolled sheet | 385,488 | 311,269 |
| Galvanized and other metallic coated sheet | 375,553 | 333,685 |
| Semi-finished products | 298,526 | 281,294 |
| Metalware products | 281,115 | 218,623 |
| Shipping and handling costs billed to customers | 192,088 | 156,177 |
| Large diameter pipes | 160,023 | 63,058 |
| Pellets and iron ore | 125,627 | 68,070 |
| Others tubes and pipes, formed shapes | 102,284 | 88,508 |
| Rails, wheels and axles | 71,116 | 100,734 |
| Color coated sheet | 68,137 | 67,144 |
| Scrap | 59,174 | 32,145 |
| Coal and coking coal concentrate | 50,391 | 79,741 |
| Gold | 44,633 | — |
| Others | 202,297 | 167,945 |
| | 4,308,993 | 3,692,523 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

Sales by delivery destination were as follows:

| | Three months ended March 31, 2008 (unaudited) | Three months ended March 31, 2007 (unaudited) |
|---|---|---|
| Russian Federation | 1,820,827 | 1,427,003 |
| Europe | 1,482,661 | 1,388,076 |
| North America | 620,478 | 535,714 |
| The Middle East | 136,201 | 117,796 |
| South-East Asia | 132,646 | 56,110 |
| Central and South America | 24,646 | 57,791 |
| China and Central Asia | 82,559 | 87,455 |
| Africa | 8,975 | 22,578 |
| | 4,308,993 | 3,692,523 |

## 4. Related party balances

| | March 31, 2008 (unaudited) | December 31, 2007 |
|---|---|---|
| **Joint ventures' balances** | | |
| Trade accounts payable | 15,103 | 16,353 |
| **Other related party balances** | | |
| Cash and cash equivalents at related party bank | 331,755 | 239,909 |
| Deposits with related party bank | 19,450 | 18,985 |
| Amounts receivable from other related parties: | | |
| Trade accounts receivable | 63,438 | 43,770 |
| Advances paid | 3,842 | 6,546 |
| Other receivables | 32,412 | 27,988 |
| | 99,692 | 78,304 |
| Short-term financial investments include the following balances with other related parties: | | |
| Loans | 13,607 | 22,205 |
| Promissory notes | 7,361 | 7,457 |
| | 20,968 | 29,662 |
| Long-term financial investments include the following balances with other related parties: | | |
| Loans | 39,224 | 37,147 |
| Held-to-maturity securities and deposits | 65,729 | 62,759 |
| | 104,953 | 99,906 |
| Amounts payable to other related parties: | | |
| Trade accounts payable | 50,502 | 36,886 |
| Advances received | 3,278 | 3,843 |
| Other accounts payable | 3,247 | 1,833 |
| | 57,027 | 42,562 |
| Debt financing includes the following balances with other related parties: | | |
| Short-term debt financing | 39,958 | 36,866 |
| Long-term debt financing | 1,437 | 1,536 |
| | 41,395 | 38,402 |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

## 5. Related party transactions

| | Three months ended March 31, 2008 (unaudited) | Three months ended March 31, 2007 (unaudited) |
|---|---|---|
| Sales to and income received from other related parties: | | |
| Sales | 164,630 | 166,502 |
| Interest income | 3,342 | 8,669 |
| | 167,972 | 175,171 |
| Purchases from related parties: | | |
| Purchases from associates: | | |
| Non-capital expenditures | 329 | 472 |
| Purchases from joint ventures: | | |
| Non-capital expenditures | 47,413 | 50,309 |
| Purchases from other related parties: | | |
| Non-capital expenditures | 81,470 | 195,265 |
| Capital expenditures | 214 | 5,028 |
| | 129,426 | 251,074 |

## 6. Contingent liabilities and commitments

As of March 31, 2008, the Group had capital commitments of US$ 965.5 million (December 31, 2007: US$ 540.2 million).

## 7. Acquisitions and disposals

*Acquisitions of subsidiaries from Majority Shareholder*

In January 2008, the Group completed the acquisition of a 100% stake in Baracom Limited for a total consideration of US$ 84.4 million. Baracom Limited owns 79.9% of the voting stock of the holding structure which controls 74.2% of SeverCorr. SeverCorr is mini-mill which produces high quality steel for motor-car, construction, pipe and engineering industries.

These consolidated financial statements take account of such acquisition as if it had occurred at the beginning of the earliest comparative period presented.

*Acquisitions of subsidiaries from third parties*

In January 2008, the Group acquired a 91.57% stake in OAO StalMag for a total consideration of US$ 17.6 million. OAO Stalmag is a ferroniobium producer which production will be used by the Group's entities.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

A summary of fair valued assets and liabilities acquired is presented below:

| | |
|---|---|
| Short-term investments | 6,374 |
| Trade and other accounts receivable | 482 |
| Inventories | 2,282 |
| Other current assets | 3,236 |
| Property, plant and equipment | 11,619 |
| Deferred tax assets | 223 |
| Other current liabilities | (2,630) |
| Net identifiable assets acquired | 21,586 |
| Minority interest | (1,820) |
| Share of net identifiable assets acquired | 19,766 |
| Consideration paid in financial assets | (17,600) |
| Negative goodwill | 2,166 |

The acquiree's profit since the acquisition date included in the Group's profit for the period, as well as the revenue and profit of the acquired entity from the beginning of the period to the date of final acquisition are insignificant to the Group's revenue and profit for the period.

***Acquisitions of minority interest***

In January 2008, the Group completed the acquisition of a 100% stake in Celtic Resources Holdings Plc by acquiring the remaining 13.7% stake in the company for a total consideration of US$ 44 million. Celtic Resources Holdings Plc is a gold producer which has three operating gold mines in Kazakhstan. Management has not yet completed the estimation of fair values of the acquired assets and liabilities and, accordingly, does not currently possess all necessary information to disclose the effect of this acquisition on the Group's financial position or results of operations. Final purchase price allocation is expected to be completed before December 31, 2008.

## 8. Segmental information — Income statement

| | Three months ended March 31, | |
|---|---|---|
| | **2008 (unaudited)** | **2007 (unaudited)** |
| **Sales** | | |
| Mining segment | 697,761 | 491,803 |
| Russian Steel segment | 2,086,368 | 1,891,946 |
| Lucchini segment | 1,056,822 | 977,569 |
| North America | 591,308 | 455,457 |
| IPM | 160,023 | 63,058 |
| Metalware segment | 272,251 | 224,101 |
| Intersegmental transactions | (555,540) | (411,411) |
| Total | 4,308,993 | 3,692,523 |
| **Profit before financing and taxation:** | | |
| Mining segment | 140,935 | 90,135 |
| Russian Steel segment | 318,572 | 499,825 |
| Lucchini segment | 99,514 | 98,161 |
| North America | 111,280 | 24,181 |
| IPM | 34,737 | 4,060 |
| Metalware segment | 26,389 | 5,816 |
| Intersegmental transactions | 1,361 | (23,846) |
| Total | 732,788 | 698,332 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

### 9. Net other operating income/(expenses)

In January 2008, an explosion occurred on one of Severstal North America's ("SNA") furnaces, blast furnace "B". Following the accident, SNA has ceased blast furnace "B" operation. SNA is insured against property damage and business interruption with a combined gross coverage of US$ 500 million, subject to customary deductibles. The business interruption covers fixed costs and loss of profits. Management has estimated net recoverable fixed costs in the period from the accident until March 31, 2008 at US$ 21 million which amount has been recognized as other operating income. No amount has been recognized for the loss of profits in these financial statements.

In February 2008, a long term electricity supply contract between SNA and Dearborn Industrial Generation ("DIG") has been terminated with a lump sum payment from DIG to compensate SNA for the differential between the contract price and the price SNA will have to pay another electricity supplier for the duration of the original contract. This penalty amounted to US$ 177 million.

### 10. Completion of ZAO Neva-Metal and ZAO Neva-Metal-Trans purchase price allocation

In March 2008, management has completed the purchase price allocation of ZAO Neva-Metal and ZAO Neva-Metal-Trans acquired in May 2007. The effect of the final purchase price allocation on these consolidated financial statements is the following:

| | Increase/(decrease) compared to the provisional purchase price allocation at December 31, 2007 US$, million |
|---|---|
| Goodwill | (47) |
| Property, plant and equipment | 15 |
| Intangible assets | 47 |
| Deferred tax liabilities | 15 |

### 11. Subsequent events

In April 2008, the Group acquired an additional 9.4% stake in SeverCorr from the former management and a 34.6% stake in OAO Dneprometiz from third parties for a total consideration of US$ 40 million.

In April 2008, the Group sold its 97.9%, 99.46% and 100% participation in OAO Mine Berezovskaya, OAO Mine Pervomaiskaya and ZAO Zhernovskaya-3 respectively to ArcelorMittal for a total consideration of US$ 652 million.

In May 2008, the Group acquired a 100% stake in Sparrows Point LLC for a total consideration of US$ 810 million. Sparrows Point LLC is an integrated steel plant on the East Coast of USA with its own deep water port and rail connection to the main East Coast rail networks. Management has not yet completed the estimation of fair values of the acquired assets and liabilities and, accordingly, does not currently possess all necessary information to disclose the effect of this acquisition on the Group's financial position or results of operations. Final purchase price allocation is expected to be completed before December 31, 2008.

# OAO Severstal and subsidiaries

Consolidated financial statements
for the year ended December 31, 2007

**OAO Severstal and subsidiaries**

**Consolidated financial statements**
**for the year ended December 31, 2007**

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**Independent Auditors' Report**

Board of Directors

OAO Severstal

**Report on the Consolidated Financial Statements**

We have audited the accompanying consolidated financial statements of OAO Severstal (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated balance sheet as at 31 December 2007, 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. We have also previously audited the corresponding figures for 2006 and 2005 before the adjustments described in Note 3 c and our report thereon dated 30 March 2007 expressed an unqualified opinion on those statements.

**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 financial statements that are free from material misstatements, 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 relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

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

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2007, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

**Emphasis of Matter**

Without qualifying our opinion, we draw attention to the fact that during the year the Group changed its accounting policy for property, plant and equipment. The reason for and the effects of the change are described in Note 3 c to these consolidated financial statements. We have also audited the adjustments described in Note 3 c that were applied to restate the 2006 and 2005 financial statements. In our opinion, such adjustments are appropriate and have been properly applied.

KPMG Limited.

KPMG Limited

14 March 2008

**OAO Severstal and subsidiaries**

**Consolidated income statement**
**Year ended December 31, 2007**
***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

| | | Year ended December 31, | | |
|---|---|---|---|---|
| | Note | 2007 | 2006 (restated) | 2005 (restated) |
| **Sales** | | | | |
| Sales — external | | 14,543,043 | 11,723,318 | 9,786,057 |
| Sales — to related parties | 15 | 701,868 | 725,714 | 665,589 |
| | 4 | 15,244,911 | 12,449,032 | 10,451,646 |
| Cost of sales | | (10,541,571) | (8,601,227) | (6,831,138) |
| **Gross profit** | | 4,703,340 | 3,847,805 | 3,620,508 |
| General and administrative expenses | | (691,210) | (654,987) | (524,662) |
| Distribution expenses | | (909,510) | (697,308) | (657,684) |
| Indirect taxes and contributions | | (153,614) | (142,109) | (95,343) |
| Share of associates' loss | | (89,397) | (1,193) | (4,190) |
| Net income from securities operations | 6 | 25,564 | 28,263 | 24,443 |
| Loss on disposal of property, plant and equipment | | (35,280) | (39,292) | (36,780) |
| Net other operating expenses | | (7,520) | (27,109) | (20,344) |
| **Profit from operations** | | 2,842,373 | 2,314,070 | 2,305,948 |
| Impairment of property, plant and equipment | 19 | (29,109) | (57,736) | (111,384) |
| Net gain on restructuring of tax liabilities | 26 | — | 14,669 | 174,178 |
| Negative goodwill, net | | 12,223 | 4,213 | 7,630 |
| Net other non-operating expenses | 7 | (58,576) | (53,536) | (52,753) |
| **Profit before financing and taxation** | | 2,766,911 | 2,221,680 | 2,323,619 |
| Interest income | 8 | 172,937 | 102,402 | 65,134 |
| Interest expense | 8 | (288,293) | (244,977) | (203,057) |
| Foreign exchange difference | | 2,900 | 33,324 | (60,231) |
| **Profit before income tax** | | 2,654,455 | 2,112,429 | 2,125,465 |
| Income tax expense | 9 | (681,269) | (635,298) | (500,907) |
| **Profit from continuing operations** | | 1,973,186 | 1,477,131 | 1,624,558 |
| Profit from discountinued operations | 29 | 433 | 32,849 | 602 |
| **Profit for the year** | | 1,973,619 | 1,509,980 | 1,625,160 |
| Attributable to: | | | | |
| shareholders of OAO Severstal | | 1,936,423 | 1,454,198 | 1,561,182 |
| minority interest | | 37,196 | 55,782 | 63,978 |
| Weighted average number of shares outstanding during the period (millions of shares) | | 1,007.7 | 928.4 | 912.2 |
| Basic and diluted earnings per share (US dollars) | | 1.92 | 1.57 | 1.71 |

These consolidated financial statements were approved by the Board of Directors on March 14, 2008.

The accompanying notes form an integral part of these consolidated financial statements.

**OAO Severstal and subsidiaries**

**Consolidated balance sheet**
**December 31, 2007**
***(Amounts expressed in thousands of US dollars)***

| | Note | December 31, 2007 | December 31, 2006 (restated) | December 31, 2005 (restated) |
|---|---|---|---|---|
| **Assets** | | | | |
| **Current assets:** | | | | |
| Cash and cash equivalents | 10 | 1,546,881 | 1,701,022 | 1,327,887 |
| Short-term bank deposits | 11 | 665,977 | 1,147,270 | 674,512 |
| Short-term financial investments | 12 | 267,633 | 321,842 | 267,851 |
| Trade accounts receivable | 13 | 1,674,618 | 1,324,585 | 1,174,193 |
| Amounts receivable from related parties | 14 | 162,719 | 127,703 | 173,808 |
| Inventories | 16 | 2,537,470 | 2,222,372 | 1,725,528 |
| VAT recoverable | | 283,745 | 339,392 | 442,297 |
| Income tax recoverable | | 75,993 | 35,904 | 28,671 |
| Assets held for sale | 29 | 461,196 | — | — |
| Other current assets | 17 | 321,362 | 259,208 | 181,685 |
| **Total current assets** | | 7,997,594 | 7,479,298 | 5,996,432 |
| **Non-current assets:** | | | | |
| Long-term financial investments | 21 | 152,866 | 199,940 | 89,541 |
| Investment in associates and joint ventures | 20 | 589,092 | 354,906 | 210,652 |
| Property, plant and equipment | 19 | 7,292,811 | 6,470,385 | 5,319,568 |
| Intangible assets | 18 | 611,261 | 61,666 | 56,523 |
| Assets held for sale | 29 | — | 113,516 | 66,117 |
| Deferred tax assets | 9 | 52,324 | 30,150 | 35,076 |
| Amounts receivable from related parties | 14 | — | — | 35,095 |
| Other non-current assets | | 21,474 | 3,844 | 3,105 |
| **Total non-current assets** | | 8,719,828 | 7,234,407 | 5,815,677 |
| **Total assets** | | 16,717,422 | 14,713,705 | 11,812,109 |
| **Liabilities and shareholders' equity** | | | | |
| **Current liabilities:** | | | | |
| Trade accounts payable | | 1,090,884 | 1,038,901 | 866,629 |
| Bank customer accounts | 22 | — | 31,143 | 98,867 |
| Amounts payable to related parties | 14 | 58,915 | 175,740 | 491,957 |
| Short-term debt finance | 23 | 972,079 | 957,564 | 996,125 |
| Income taxes payable | | 41,381 | 44,348 | 86,001 |
| Other taxes and social security payable | | 200,424 | 199,963 | 257,678 |
| Dividends payable | | 107,485 | 23,243 | 12,275 |
| Liabilities related to assets held for sale | 29 | 91,750 | — | — |
| Other current liabilities | 24 | 600,580 | 506,848 | 379,218 |
| **Total current liabilities** | | 3,163,498 | 2,977,750 | 3,188,750 |
| **Non-current liabilities:** | | | | |
| Long-term debt finance | 23 | 2,354,823 | 2,048,035 | 1,931,694 |
| Deferred tax liabilities | 9 | 374,636 | 403,076 | 356,739 |
| Retirement benefit liability | 25 | 387,398 | 442,954 | 338,486 |
| Liabilities related to assets held for sale | 29 | — | 1,792 | 172 |
| Other non-current liabilities | 26 | 226,388 | 286,090 | 281,075 |
| **Total non-current liabilities** | | 3,343,245 | 3,181,947 | 2,908,166 |
| **Equity:** | | | | |
| Share capital | 27 | 3,311,288 | 3,311,288 | 3,311,254 |
| Additional capital | | 1,165,530 | 1,165,530 | 60,367 |
| Foreign exchange differences | | 1,176,321 | 535,591 | 34,368 |
| Retained earnings | | 4,082,834 | 2,983,954 | 1,818,475 |
| **Total equity attributable to shareholders of parent** | | 9,735,973 | 7,996,363 | 5,224,464 |
| **Minority interest** | | 474,706 | 557,645 | 490,729 |
| **Total equity** | | 10,210,679 | 8,554,008 | 5,715,193 |
| **Total equity and liabilities** | | 16,717,422 | 14,713,705 | 11,812,109 |

The accompanying notes form an integral part of these consolidated financial statements.

**OAO Severstal and subsidiaries**

**Consolidated statement of cash flows**
**Year ended December 31, 2007**
***(Amounts expressed in thousands of US dollars)***

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 (restated) | 2005 (restated) |
| **Operating activities:** | | | |
| Profit before financing and taxation | 2,766,911 | 2,221,680 | 2,323,619 |
| Adjustments to reconcile profit to cash generated from operations: | | | |
| Depreciation and amortization (Notes 18 and 19) | 802,695 | 603,740 | 496,597 |
| Impairment of property, plant and equipment | 29,109 | 57,736 | 111,384 |
| Provision for inventories, receivables and other provisions | 52,542 | (11,641) | 27,629 |
| Negative goodwill, net | (12,223) | (4,213) | (7,630) |
| Loss on disposal of property, plant and equipment | 35,280 | 39,292 | 36,780 |
| Net gain on restructuring of tax liabilities (Note 26) | — | (14,669) | (174,178) |
| (Gain)/loss on disposal of subsidiaries and associates | (31,507) | (846) | 9,759 |
| Gain on remeasurement and disposal of financial investments | (25,564) | (28,263) | (24,443) |
| Share of associates' results less dividends from associates | 89,397 | 1,193 | 17,413 |
| Changes in operating assets and liabilities: | | | |
| Trade accounts receivable | (334,967) | (16,474) | 10,585 |
| Amounts receivable from related parties | 25,083 | 92,387 | 43,006 |
| VAT recoverable | 96,603 | 140,315 | (222,739) |
| Inventories | (189,848) | (291,466) | (73,542) |
| Trade accounts payable | 58,704 | 57,562 | 16,323 |
| Bank customer accounts | 36,500 | (74,511) | (28,322) |
| Amounts payable to related parties | 80,316 | (101,337) | 53,386 |
| Other taxes and social security payables | (63,729) | (111,604) | 16,797 |
| Other non-current liabilities | (107,185) | 10,396 | 13,114 |
| Assets held for sale | (1,856) | — | (14,512) |
| Net other changes in operating assets and liabilities | 42,490 | 52,044 | 60,245 |
| **Cash generated from operations** | 3,348,751 | 2,621,321 | 2,691,271 |
| Interest paid (excluding banking operations) | (230,791) | (215,081) | (199,177) |
| Income tax paid | (802,871) | (676,582) | (557,303) |
| **Net cash from operating activities** | 2,315,089 | 1,729,658 | 1,934,791 |
| **Investing activities:** | | | |
| Additions to property, plant and equipment | (1,561,911) | (1,243,831) | (1,204,415) |
| Additions to intangible assets | (27,194) | (8,808) | (32,322) |
| Net decrease/(increase) in short-term bank deposits | 580,706 | (431,142) | (133,526) |
| Additions to financial investments and associates | (1,303,537) | (1,203,824) | (817,558) |
| Acquisition of minority interests and entities under common control | (232,447) | (294,249) | 108,466 |
| Net cash outflow on acquisitions of subsidiaries | (644,094) | (57,625) | (4,223) |
| Net cash inflow on disposals of subsidiaries | 235,978 | 1,588 | 13,701 |
| Proceeds from disposal of property, plant and equipment | 32,926 | 14,023 | 10,893 |
| Proceeds from disposal of assets held for sale | — | — | 10,313 |
| Proceeds from disposal of financial investments | 787,037 | 949,480 | 816,671 |
| Interest received (excluding banking operations) | 150,569 | 105,251 | 53,911 |
| **Cash from investing activities** | (1,981,967) | (2,169,137) | (1,178,089) |
| **Financing activities:** | | | |
| Proceeds from debt finance | 2,794,285 | 1,379,209 | 1,156,982 |
| Proceeds from share issue | — | 1,105,197 | — |
| Repayment of debt finance | (2,623,463) | (1,495,440) | (1,357,997) |
| Repayments under lease obligations | (3,915) | — | — |
| Dividends paid | (736,156) | (269,286) | (277,605) |
| Minority capital contributions | — | 6,685 | 37,734 |
| Net other cash flows from financing activities | — | — | (7,742) |
| **Cash from financing activities** | (569,249) | 726,365 | (448,628) |
| Effect of exchange rates on cash and cash equivalents | 81,986 | 86,249 | (70,551) |
| **Net increase/(decrease) in cash and cash equivalents** | (154,141) | 373,135 | 237,523 |
| **Cash and cash equivalents at beginning of the period** | 1,701,022 | 1,327,887 | 1,090,364 |
| **Cash and cash equivalents at end of the period** | 1,546,881 | 1,701,022 | 1,327,887 |

The accompanying notes form an integral part of these consolidated financial statements.

**OAO Severstal and subsidiaries**

**Consolidated statement of changes in equity**
**Year ended December 31, 2007**
***(Amounts expressed in thousands of US dollars)***

| | Attributable to the shareholders of OAO Severstal | | | | | | Minority interest | Total |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Additional capital | Revaluation reserve | Foreign exchange differences | Retained earnings | Total | | |
| Balances at December 31, 2004 as previously reported | 3,311,248 | 60,367 | 631,996 | 191,770 | (75,938) | 4,119,443 | 122,250 | 4,241,693 |
| Acquisition of entities under common control | — | — | — | 538 | (3,385) | (2,847) | 1,409 | (1,438) |
| Change in accounting policy (Note 3c) | — | — | (631,996) | — | 631,996 | — | — | — |
| Balances at December 31, 2004 as restated | 3,311,248 | 60,367 | — | 192,308 | 552,673 | 4,116,596 | 123,659 | 4,240,255 |
| Profit for the year (restated) | — | — | — | — | 1,561,182 | 1,561,182 | 63,978 | 1,625,160 |
| Foreign exchange differences | — | — | — | (151,293) | — | (151,293) | (35,065) | (186,358) |
| Total recognized income and expenses | | | | | | 1,409,889 | 28,913 | 1,438,802 |
| Dividends | — | — | — | — | (271,996) | (271,996) | (3,181) | (275,177) |
| Effect of acquisitions and disposals | 6 | — | — | (6,647) | (23,384) | (30,025) | 341,338 | 311,313 |
| Balances at December 31, 2005 (restated) | 3,311,254 | 60,367 | — | 34,368 | 1,818,475 | 5,224,464 | 490,729 | 5,715,193 |
| Profit for the year (restated) | — | — | — | — | 1,454,198 | 1,454,198 | 55,782 | 1,509,980 |
| Foreign exchange differences | — | — | — | 501,223 | — | 501,223 | 49,210 | 550,433 |
| Total recognized income and expenses | | | | | | 1,955,421 | 104,992 | 2,060,413 |
| Dividends | — | — | — | — | (278,798) | (278,798) | — | (278,798) |
| Share issues | 34 | 1,105,163 | — | — | — | 1,105,197 | — | 1,105,197 |
| Effect of acquisitions and disposals | — | — | — | — | (9,921) | (9,921) | (38,076) | (47,997) |
| Balances at December 31, 2006 (restated) | 3,311,288 | 1,165,530 | — | 535,591 | 2,983,954 | 7,996,363 | 557,645 | 8,554,008 |
| Profit for the year | — | — | — | — | 1,936,423 | 1,936,423 | 37,196 | 1,973,619 |
| Foreign exchange differences | — | — | — | 640,730 | — | 640,730 | 56,583 | 697,313 |
| Total recognized income and expenses | | | | | | 2,577,153 | 93,779 | 2,670,932 |
| Dividends | — | — | — | — | (801,462) | (801,462) | (11,982) | (813,444) |
| Effect of acquisitions and disposals | — | — | — | — | (36,081) | (36,081) | (164,736) | (200,817) |
| Balances at December 31, 2007 | 3,311,288 | 1,165,530 | — | 1,176,321 | 4,082,834 | 9,735,973 | 474,706 | 10,210,679 |

The accompanying notes form an integral part of these consolidated financial statements.

## 1. Operations

These consolidated financial statements of OAO Severstal and subsidiaries comprise the parent company, OAO Severstal ("Severstal" or the "Parent Company") and its subsidiaries (collectively the "Group") as listed in note 28.

Severstal began operations on August 24, 1955 and completed the development of an integrated iron and steel mill in Cherepovets during February 1959 when the first steel was rolled. On September 24, 1993, as part of the Russian privatization program, Severstal was registered as a Joint Stock Company ("OAO") and privatized. Through participating in Severstal's privatization auctions and other purchases, Alexey Mordashov (the "Majority Shareholder") has purchased shares in Severstal such that as at the balance sheet date he controlled, directly or indirectly, 82.37% (December 31, 2006 and 2005: 82.37% and 82.75%, respectively) of Severstal's share capital.

Severstal's GDRs have been quoted on the London Stock Exchange since November 2006. Severstal's shares are quoted on the Russian Trading System and on the Moscow Interbank Currency Exchange ("MICEX"). Severstal's registered office is located at Ul Mira 30, Cherepovets, Russia.

The Group comprises the following segments:

- *Mining segment* — this segment comprises gold mining in one location in Kazakhstan and the following operations in Russia: coking coal production in two locations, one location where iron ore is produced, one location where pellets are produced, gold mining in two locations and also coal refining facilities and other auxiliary businesses.
- *Russian Steel* — this segment operates a full cycle integrated iron and steel mill, has supporting companies for the sale of products in the Russian and international markets and also includes service companies.
- *Lucchini* — this segment produces special and high quality steels and quality and specialty long products. Production sites are located in Western Europe, primarily in Italy and France. This segment also includes its distribution network companies, which are located primarily in Western Europe.
- *Severstal North America* — this segment operates a full cycle integrated iron and steel mill in USA and has joint control and non-controlling equity interests in US based steel galvanizing, steel slitting and coking coal production entities.
- *Izhora Pipe Mill (hereinafter — "IPM", previously referred to as "ITZ")* — this segment operates a large pipe mill in Russia, which was reported together with Russian Steel segment prior to 2007.
- *Metalware segment* — this segment comprises three plants in Russia, two plants in Ukraine and one plant in the United Kingdom containing wire drawing equipment that takes long products (mainly wire) from the Russian Steel and Lucchini segments and external suppliers and turns them into products with a higher value added for the Russian and international markets.
- *Financing segment* — this segment operated a retail bank until November 2007 when the bank was disposed off. This transaction was accounted for as a discontinued operation. The transaction is further discussed in Note 29 to these consolidated financial statements.

A segmental analysis of the consolidated balance sheet and income statement is given in note 31.

***Acquisitions of controlling stakes from the Group's Majority Shareholder***

In July 2007, the Group acquired from the Group's Majority Shareholder a 100% stake in each of the companies OOO Petrovtormet and OOO Severstalskrap-Komi, and a 75.01% and a 75.1% stake in OAO Arhangelskii vtormet and in OAO Murmanskvtormet, respectively.

These transactions are further discussed in note 28 to these consolidated financial statements.

***Economic environment***

A large part of the Group is based in the Russian Federation and is consequently exposed to the economic and political effects of the policies adopted by the Russian government. These conditions and future policy changes could affect the operations of the Group and the realization and settlement of its assets and liabilities.

International sales of rolled steel from the Group's Russian operations have been the subject of several anti-dumping investigations. The Group has taken steps to address the concerns of such investigations and participates actively in their resolution. A brief description of protective measures effective at Severstal's key export markets is given below:

- Exports of hot-rolled coils and thin sheets from Russia to the USA are restricted by the minimum prices and quantities issued quarterly by the US Department of Commerce and quotas.
- Exports of hot-rolled plates from Russia to the USA are restricted by the minimum prices established based on the producer's actual cost and profit on the domestic market. Severstal is the first Russian company, for which since September 2005 the hot-rolled plates market is open.
- The Canadian market of hot-rolled plate was restricted by minimum prices in 2007. However from January 9, 2008 this restriction was cancelled.
- The European Union ("EU") market is protected by quotas. During the last few years quotas have been raised consistently after adjusting for the effects of EU enlargements, equaling 2.272 mln. tons in 2007. Severstal traditionally gets approximately 35% of the total Russian quota and strives to utilize it fully because the EU market is a key market for Severstal.
- The Chinese market is open to the Russian exporters. No antidumping or safeguard measures are in force.

## 2. Presentation of the consolidated financial statements

***Statement of compliance***

These consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board.

***Basis of measurement***

The consolidated financial statements are prepared under the historic cost convention except that investments designated at fair value through profit and loss and investments available-for-sale are stated at fair value.

The Group's statutory financial records are maintained in accordance with the legislative requirements of the countries in which the individual entities are located, which differ in certain respects from IFRS. The accounting policies applied in the preparation of these consolidated financial statements are set out in note 3.

***Going concern basis***

These consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business.

***Critical accounting judgments and estimates***

Preparation of the consolidated financial statements in accordance with IFRS requires the Group's management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of financial statements, and the reported amounts of revenues and expenses during the reporting period. The determination of estimates requires judgments which are based on historical experience, current and expected economic conditions, and other available information. Actual results could differ from those estimates.

The most significant areas requiring the use of management estimates and assumptions relate to:

- useful economic lives of property, plant and equipment;
- impairment of assets;
- allowances for doubtful debts, obsolete and slow-moving raw materials and spare parts;
- decommissioning liabilities;
- retirement benefit liabilities;
- deferred income tax assets; and
- contingencies.

**Useful economic lives of property, plant and equipment**

The Group assesses the remaining useful lives of items of property, plant and equipment at least at each financial year-end and, 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 on depreciation expense for the period.

**Impairment of assets**

The Group reviews the carrying amount of its tangible and intangible assets to determine whether there is any indication that those assets are impaired. In making the assessments for impairment, assets that do not generate independent cash flows are allocated to an appropriate cash-generating unit. Management necessarily applies its judgment in allocating assets that do not generate independent cash flows to appropriate cash-generating units, and also in estimating the timing and value of underlying cash flows within the value in use calculation. Subsequent changes to the cash generating unit allocation or to the timing of cash flows could impact the carrying value of the respective assets.

**Allowances for doubtful accounts**

The Group makes allowances for doubtful receivables 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 current overall economic conditions, the ageing of accounts receivable balances, historical write-off experience, customer creditworthiness and changes in payment terms. Changes in the economy, industry or specific customer conditions may require adjustments to the allowance for doubtful accounts recorded in the consolidated financial statements.

**Provision for obsolete inventory**

The Group makes a provision for obsolete and slow-moving raw materials and spare parts. In addition, certain finished goods of the Group are carried at net realizable value. Estimates of net realizable value of finished goods are based on the most reliable evidence available at the time the estimates are made. These estimates take into consideration fluctuations of price or cost directly relating to events occurring subsequent to the balance sheet date to the extent that such events confirm conditions existing at the end of the period.

**Decommissioning Liability**

The Group reviews its decommissioning liability, representing site restoration provisions, at each balance sheet date and adjusts it to reflect the current best estimate in accordance with IFRIC 1 "Changes in Existing Decommissioning, Restoration and Similar Liabilities". The amount recognized as a provision is the best estimate of the expenditures required to settle the present obligation at the balance sheet date based on the requirements of the current legislation of the country where the respective operating assets are located. The risks and uncertainties that inevitably surround many events and circumstances are taken into account in reaching the best estimate of a provision. Considerable judgment is required in forecasting future site restoration costs. Future events that may affect the amount required to settle an obligation are reflected in the amount of a provision when there is sufficient objective evidence that they will occur.

**Retirement Benefit Liability**

The Group uses an actuarial valuation method for measurement of the present value of post-employment benefit obligations and related current service cost. This involves the use of demographic assumptions about the future characteristics of the current and former employees who are eligible for benefits (mortality, both during and after employment, rates of employee turnover, disability and early retirement, etc.) as well as financial assumptions (discount rate, future salary and benefit levels, expected rate of return on plan assets, etc.).

**Deferred Income Tax Assets**

Deferred tax assets are reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. The estimation of that probability includes judgments based on the expected performance. Various factors are considered to assess the probability of the future utilization of deferred tax assets, including past operating results, operational plans, expiration of tax losses carried forward, and tax planning strategies. If actual results differ from that estimates or if these estimates must be adjusted in future periods, the financial position, results of operations and cash flows may be negatively affected. In the event that the assessment of future utilization of deferred tax assets must be reduced, this reduction will be recognized in the income statement.

**Contingencies**

By their nature, contingencies will only be resolved when one or more future events occur or fail to occur. The assessment of such contingencies inherently involves the exercise of significant judgment and estimates of the outcome of future events.

***Functional and presentation currency***

The presentation currency of these consolidated financial statements is the US dollar.

The functional currency is determined separately for each of the Group's entities. For all Russian entities, the majority of costs and revenues are denominated in Russian roubles, and accordingly, their functional currency is the Russian rouble. The functional currency of the Group's entities located in North America is the US dollar. The functional currency of the majority of the Group's entities located in Western Europe is the Euro.

The translation into the presentation currency is made as follows:

- all assets and liabilities, both monetary and non-monetary, are translated at the closing exchange rates at the dates of each balance sheet presented;
- all income and expenses in each income statement are translated at the average exchange rates for the periods presented; and
- all resulting exchange differences are recognized as a separate component in equity.

Any conversion of amounts into US dollars should not be construed as a representation that such amounts have been, could be, or will be in the future, convertible into US dollars at the exchange rates used, or at any other exchange rate.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

***Adoption of new and revised IFRS***

As of January 1, 2007, the Group has adopted IFRS 7 "Financial Instruments: Disclosures" which is effective for annual reporting periods beginning on or after 1 January 2007, and the consequential amendments to IAS 1 "Presentation of Financial Statements".

The impact of the adoption of IFRS 7 and the changes to IAS 1 has been to expand the disclosures provided in these financial statements regarding the Group's financial instruments (see note 33) and management of capital (see note 27).

Four Interpretations issued by the International Financial Reporting Interpretations Committee are effective for the current period. These are: IFRIC 7 "Applying the Restatement Approach under IAS 29, Financial Reporting in Hyperinflationary Economies"; IFRIC 8 "Scope of IFRS 2"; IFRIC 9 "Reassessment of Embedded Derivatives"; and IFRIC 10 "Interim Financial Reporting and Impairment". The adoption of these Interpretations did not affect the Group's financial statements.

***New accounting pronouncements***

At the date of authorization of these financial statements, the following Interpretations were in issue but not yet effective:

- IAS 1 (Revised) "Presentation of Financial Statements";
- IAS 23 (Revised) "Borrowing Costs";
- IAS 27 (Revised) "Consolidated and Separate Financial Statements";
- IFRS 2 "Share-based payments";
- IFRS 3 (Revised) "Business Combinations";
- IFRS 8 "Operating Segments";
- IFRIC 11 "IFRS 2: Group and Treasury Share Transactions";
- IFRIC 12 "Service Concession Arrangements";
- IFRIC 13 "Customer Loyalty Programmes"; and
- IFRIC 14 "IAS 19 — The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction".

The impact of adoption of these standards and interpretations in the preparation of consolidated financial statement in future periods is currently being assessed by management. No material effect on the Group's financial statements is anticipated.

***Reclassifications***

In order to conform with the current year presentation the following reclassifications to the prior years were made:

| | 2006 Increase/ (decrease) | 2005 Increase/ (decrease) |
|---|---|---|
| Cost of sales | (22,192) | (17,562) |
| General and administrative expenses | 4,812 | 5,294 |
| Distribution expenses | 44,987 | 34,230 |
| Indirect taxes and contributions | (27,184) | (21,962) |
| Net other operating expenses | (423) | — |

## 3. Summary of the principal accounting policies

The following significant accounting policies have been consistently applied in the preparation of these consolidated financial statements.

### a. Basis of consolidation

***Subsidiaries***

Subsidiaries are those enterprises controlled, directly or indirectly, by the Parent Company. The financial statements of subsidiaries are included in these consolidated financial statements from the date that control effectively commences until the date that control effectively ceases. The minority interest represents the minorities' proportion of the net identifiable assets of the subsidiaries, including the minorities' share of fair value adjustments on acquisitions.

Intra-group balances and transactions, and any unrealized gains arising from intra-group transactions, are eliminated in preparing these consolidated financial statements.

***Investments in associates***

Associates are those enterprises in which the Group has significant influence, but does not have control over the financial and operating policies. These consolidated financial statements include the Group's share of the total recognized gains and losses of associates accounted for on an equity accounting basis, from the date that significant influence effectively commences until the date that significant influence effectively ceases. When the Group's share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

Where a group entity transacts with an associate of the Group, profits and losses are eliminated to the extent of the Group's interest in the relevant associate.

***Interests in joint ventures***

A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity that is subject to joint control that is when the strategic financial and operating policy decisions relating to the activities of the joint venture require the unanimous consent of the parties sharing control.

Where a Group entity undertakes its activities under joint venture arrangements directly, the Group's share of jointly controlled assets and any liabilities incurred jointly with other venturers are recognized in the financial statements of the relevant entity and classified according to their nature. Liabilities and expenses incurred directly in respect of interests in jointly controlled assets are accounted for on an accrual basis. Income from the sale or use of the Group's share of the output of jointly controlled assets, and its share of joint venture expenses, are recognized when it is probable that the economic benefits associated with the transactions will flow to/from the Group and their amount can be measured reliably.

Joint venture arrangements that involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly controlled entities. The Group reports its interests in jointly controlled entities using the equity method.

Where the Group transacts with its jointly controlled entities, profits and losses are eliminated to the extent of the Group's interest in the joint venture.

***Accounting for business combinations of entities under common control***

IFRS provides no guidance on accounting for business combinations of entities under common control. Management adopted the accounting policy for such transactions based on the relevant guidance of accounting principles generally accepted in the United States ("US GAAP"). Management believes that this approach and the accounting policy disclosed below are in compliance with IFRS.

Acquisitions of controlling interests in companies that were previously under the control of the same controlling shareholder as the Group have been accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date on which control was obtained by the common controlling shareholder. The assets and liabilities acquired have been recognized at their book values. The components of equity of the acquired companies have been added to the same components within Group equity except that any share capital of the acquired companies has been recorded as part of additional paid in capital. Cash consideration for such acquisitions has been recognized as a liability to or a reduction of receivables from related parties, with a corresponding reduction in equity, from the date the acquired company is included in these consolidated financial statements until the cash consideration is paid. Parent Company shares issued in consideration for the acquired companies are recognized from the moment the acquired companies are included in these financial statements.

Acquisitions by the Majority Shareholder of additional interests in the acquired companies, after control over those companies has been obtained by the Majority Shareholder, are treated as if those additional interests were acquired by the Group. No goodwill is recognized on these transactions. The difference between the share of net assets acquired and the cost of investment is recognized directly in equity.

#### *Goodwill*

Goodwill arising on the acquisition of a subsidiary, associate or a jointly controlled entity represents the excess of the cost of acquisition over the Group's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities of the subsidiary, associate or jointly controlled entity recognized at the date of acquisition. Goodwill is initially recognized as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill in respect of subsidiaries is disclosed as an intangible asset and goodwill relating to associates and jointly controlled entities is included within the carrying value of the investments in these entities.

Where an investment in subsidiary, associate or jointly control entity is made, any excess of the Group's share in the fair value acquiree's of the identifiable assets, liabilities and contingent liabilities over the cost of acquisition is recognized in the income statement immediately.

### b. Foreign currency

#### *Foreign currency transactions*

Transactions in foreign currencies are translated to the functional currency of each entity at the foreign exchange rate ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the functional currency of each entity at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies are translated to the functional currency of the entity at the foreign exchange rate ruling at the date of the transaction. Foreign exchange gains and losses arising on translation are recognized in the income statement.

### c. Property, plant and equipment

#### *Change in accounting policy for property, plant and equipment*

In 2007, management decided to change the accounting policy for property, plant and equipment from the revaluation model to the cost model. Management believes that the change to the cost model provides reliable financial information which is more relevant for the users of the financial statements primarily due to the fact that Severstal's competitors use the cost model to account for property, plant and equipment. Accordingly, the change enhances comparability with competitors.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

In accordance with IAS 8 "Accounting Policies, Changes in Accounting Estimates and Errors" the change in accounting policy has been applied retrospectively and comparative figures have been restated. The effect of the change on the comparative figures is:

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Decrease in inventory | (19,582) | — |
| Decrease in property, plant and equipment | (4,081,303) | (3,528,892) |
| Decrease in deferred tax liabilities | 978,712 | 849,255 |
| Decrease in equity attributable to shareholders of parent | 3,052,185 | 2,641,627 |
| Decrease in minority interest | 69,988 | 38,010 |

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Decrease in cost of sales | 340,457 | — |
| Decrease in loss on disposal of property, plant and equipment | 31,777 | — |
| Decrease/(increase) in impairment of property, plant and equipment | 29 | (176,543) |
| (Increase)/decrease in income tax expense | (93,918) | 42,370 |
| Increase/(decrease) in profit for the year | 278,345 | (134,173) |
| Increase/(decrease) in basic and diluted earnings per share (US Dollars) | 0.30 | (0.15) |

There were no changes in profit for the year or total equity relating to periods before 2005.

The Group did not obtain the fair values of its property, plant and equipment as of December 31, 2007. Accordingly, it was not practicable to determine the effects on the current and future years of the change in accounting policy.

***New accounting policy for property, plant and equipment***

Property, plant and equipment are carried at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset and, for qualifying assets, borrowing costs capitalized in accordance with the Group's accounting policy. In the case of assets constructed by the Group, related works and direct project overheads are included in cost. Repair and maintenance expenses are charged to the income statement as incurred. Gains or losses on disposals of property, plant and equipment are recognized in the income statement.

Depreciation is provided so as to write off property, plant and equipment over its expected useful life. Depreciation is calculated using the straight line basis, except for depreciation on vehicles and certain metal-rolling equipment, which is calculated on the basis of mileage and units of production, respectively. The estimated useful lives of assets are reviewed regularly and revised when necessary.

The principal periods over which assets are depreciated are as follows:

| | |
|---|---|
| Buildings and constructions | 20–50 years |
| Plant and machinery | 10–20 years |
| Other productive assets | 5–20 years |
| Community and infrastructure assets | 5–50 years |

**d. Lease**

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

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

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to the income statement as part of interest expense.

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

**e. Intangible assets (excluding goodwill)**

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

**f. Asset impairment**

The carrying amount of goodwill is tested for impairment annually. The carrying amounts of the Group's other assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognized whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount.

***Calculation of recoverable amount***

The recoverable amount of the Group's held-to-maturity investments and loans and receivables, is calculated as the present value of expected future cash flows, discounted at the effective interest rate inherent in the asset. For other assets the recoverable amount is the greater of the net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

***Reversals of impairment***

An impairment loss in respect of a held-to-maturity investment, loan or receivable is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognized. An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognized.

**g. Inventories**

Inventories are stated at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The cost of inventories is based on the weighted average principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads. Provisions are recorded against slow moving and obsolete inventories.

**h. Financial assets**

Financial assets include cash and cash equivalents, investments, and loans and receivables.

Cash and cash equivalents comprise cash balances, cash deposits and highly liquid investments with original maturities of three months or less, that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

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

***Efective interest method***

The effective interest method is a method of calculating the carrying value of a financial asset held at amortized cost and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees on points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

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

***Financial assets at FVTPL***

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

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking.

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

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial asset forms part of a group of financial instruments, which are managed and performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis.

Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any dividend or interest earned on the financial asset.

***Held-to-maturity investments***

Bills of exchange and debentures with fixed or determinable payments and fixed maturity dates that the Group has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are recorded at amortised cost using the effective interest method less any impairment.

***AFS financial assets***

Available for sale financial assets are those non-derivative financial assets that are not classified as financial assets at FVTPL or held-to-maturity and are stated at fair value. Gains and losses arising from changes in fair value are recognised directly in equity with the exception of impairment losses, which are recognised directly in the income statement. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the equity is included in the income statement for the period.

Dividends on AFS equity instruments are recognised in the income statement when the Group's right to receive the dividends is established.

***Loans and receivables***

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

***Derecognition of financial assets***

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

**i. Financial liabilities**

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

***Financial liabilities at FVTPL***

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

A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking.

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

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial instruments, which are managed and performance is evaluated on a fair value basis, in accordance with the Group's documented risk management or investment strategy, and information about the grouping is provided internally on that basis.

Financial liabilities at FVTPL are stated at fair value, with any resultant gain or loss recognized in profit or loss. The net gain or loss recognized in profit or loss incorporates any interest paid on the financial liability.

***Other financial liabilities***

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs. Borrowing costs on loans specifically for the purchase or construction of a qualifying asset are capitalized as part of the cost of the asset they are financing.

Other financial liabilities are subsequently measured at amortized cost using the effective interest method, with interest expense recognized in the income statement.

*Derecognition offinancial liabilities*

The Group derecognizes financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

## j. Dividends payable

Dividends are recognized as a liability in the period in which they are authorized by the shareholders.

## k. Indirect taxes and contributions

Indirect taxes and contributions are taxes and mandatory contributions paid to the government, or government controlled agencies, that are calculated on a variety of bases, but exclude taxes calculated on profits, value added taxes calculated on revenues and purchases and social security costs calculated on wages and salaries. Social security costs are included in cost of sales, distribution expenses and selling, general and administrative expenses in accordance with the nature of related wages and salaries expenses.

## l. Income tax

Income tax on the profit for the year comprises current and deferred tax. Income tax is recognized in the income statement except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax expense is calculated by each entity on the pretax income determined in accordance with the tax law of the country, in which the entity is incorporated, using tax rates enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is calculated using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting and taxation purposes. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. Deferred tax assets are recognized only to the extent that it is probable that future taxable profits will be available against which these assets can be utilized. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred tax is not recognized in respect of the following:

- investments in subsidiaries where the Group is able to control the timing of the reversal of the temporary differences and it is probable that the temporary difference will not reverse in the foreseeable future;
- if it arises from the initial recognition of an asset or liability that affect neither accounting nor taxable profit;
- initial recognition of goodwill.

## m. Provisions

*Retirement benefit liability*

The Group pays retirement and post-employment medical benefits to former employees. The calculation of the Group's net obligation in respect of defined retirement benefit plans is performed annually by management using the projected unit credit method. In accordance with this method, the Group's net obligation is calculated separately for each defined benefit plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to its present value and the fair value of any plan assets is deducted. The discount rate used is the yield at the balance sheet date on high quality corporate bonds for UK, USA, France and Italy and on government bonds for Russia that have maturity dates approximating the terms of the Group's obligations.

Any actuarial gain or loss arising from the calculation of the retirement benefit obligation is fully recognized in the current year's income statement.

***Decommissioning liability***

The Group has environmental liabilities related to restoration of soil and other related works, which are due upon the closures of certain of its production sites. The Group generally estimates provisions related to environmental issues on a case-by-case basis, taking into account applicable legal requirements. A best estimate, based on available information, is calculated, provided that the available information indicates that the loss is probable. Decommissioning liabilities are estimated using existing technology, at current prices, and discounted using a real discount rate.

***Other provisions***

Other provisions are recognized in the balance sheet when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

**n. Revenue recognition**

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

***Sale of goods***

Revenue from the sale of goods is recognized in the income statement when the significant risks and rewards of ownership have been transferred to the buyer; the Group retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold; the amount of revenue can be measured reliably; it is probable that the economic benefits associated with the transaction will flow to the entity; and the costs incurred or to be incurred in respect of the transaction can be measured reliably.

***Rendering of services***

Revenue from a contract to provide services is recognized by reference to the stage of completion of the contract.

**o. Interest income**

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

**p. Interest expense**

Interest expense is recognized in the income statement as it accrues, taking into account the effective yield on the liability.

All interest costs incurred in connection with borrowings, which are not directly attributable to the acquisition, construction or production of qualifying assets, are expensed as incurred.

**q. Net income from securities operations**

Net income from securities operations comprises dividend income (except for dividends from equity associates), realized and unrealized gains on financial assets at fair value through profit or loss, realized gains and impairment losses on available for sale and held to maturity investments.

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

### r. Earnings per share

Earnings per share is calculated by dividing the net profit by the weighted average number of shares outstanding during the year, assuming that shares issued in consideration for the companies acquired from the Majority Shareholder were issued from the moment these companies are included in these consolidated financial statements.

### s. Discontinued operations

Discontinued operations are disclosed when a component of the Group either has been disposed of during the reporting period, or is classified as held for sale or other type of disposal at the balance sheet date. This condition is regarded as met only when the disposal is highly probable within one year from the date of classification.

The comparative income statement is presented as if the operation had been discontinued from the beginning of the comparative period.

Assets and liabilities of a disposal group are presented in the balance sheet separately from other assets and liabilities. Comparative information related to discontinued operations is not amended in the balance sheet.

## 4. Sales

Sales by product were as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Hot-rolled strip and plate | 3,681,592 | 3,435,545 | 3,443,571 |
| Long products | 3,097,933 | 2,301,550 | 1,436,830 |
| Galvanized and other metallic coated sheet | 1,307,317 | 1,105,521 | 1,051,370 |
| Cold-rolled sheet | 1,258,641 | 1,328,063 | 1,540,951 |
| Semi-finished products | 1,101,902 | 939,351 | 879,627 |
| Metalware products | 1,002,180 | 833,877 | 574,458 |
| Shipping and handling costs billed to customers | 644,000 | 537,411 | 174,156 |
| Large diameter pipes | 530,726 | — | — |
| Others tubes and pipes, formed shapes | 391,708 | 320,413 | 210,590 |
| Rails, wheels and axles | 321,751 | 375,270 | 149,121 |
| Pellets and iron ore | 304,825 | 242,697 | 337,516 |
| Scrap | 301,482 | 26,513 | 19,500 |
| Color coated sheet | 281,071 | 148,458 | — |
| Coal and coking coal concentrate | 264,753 | 249,280 | 143,140 |
| Others | 755,030 | 605,083 | 490,816 |
| | 15,244,911 | 12,449,032 | 10,451,646 |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

Sales by delivery destination were as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Russian Federation | 6,744,113 | 4,912,642 | 3,785,133 |
| Europe | 5,308,680 | 4,390,786 | 2,751,196 |
| North America | 1,889,280 | 2,406,090 | 2,198,248 |
| The Middle East | 450,360 | 215,056 | 353,286 |
| China and Central Asia | 353,550 | 138,016 | 569,898 |
| South-East Asia | 291,052 | 143,553 | 408,228 |
| Central and South America | 151,281 | 156,685 | 237,087 |
| Africa | 56,595 | 86,204 | 148,570 |
| | 15,244,911 | 12,449,032 | 10,451,646 |

## 5. Staff costs

Employment costs were as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Wages and salaries | (1,505,630) | (1,262,613) | (964,528) |
| Social security costs | (414,462) | (301,407) | (247,524) |
| Retirement benefit costs (Note 25) | (7,719) | (2,385) | (3,806) |
| | (1,927,811) | (1,566,405) | (1,215,858) |
| Actuarial gains/(losses) recognized (Note 25) | 37,056 | (67,658) | (62,380) |
| Staff costs | (1,890,755) | (1,634,063) | (1,278,238) |

For the year ended December 31, 2007, key management's remuneration totalled US$ 57.2 million (2006: US$ 44.5 million; 2005: US$ 39.0 million). As a part of the above amounts US$ 40.1 million and US$ 35.7 million were paid to the Group's related party, ZAO Severstal Group that employed executive officers of Severstal and seconded them to Severstal during the years ended December 31, 2006 and 2005 respectively.

## 6. Net income from securities operations

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Held-for-trading securities: | | | |
| Profit on disposal | — | 153 | 133 |
| Restatement to fair value | 3,864 | 401 | 1,160 |
| Held-to-maturity securities and loans: | | | |
| Restatement to fair value (discounting) | 3,577 | 13,909 | 4,209 |
| Available-for-sale securities: | | | |
| Profit on disposal | 11,849 | 6,376 | 28,405 |
| Reversal of impairment/(impairment) | 4,012 | 7,183 | (13,076) |
| Dividends received | 2,262 | 241 | 3,612 |
| | 25,564 | 28,263 | 24,443 |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

## 7. Net other non-operating expenses

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Social expenditure | (42,468) | (33,857) | (28,408) |
| Charitable donations | (41,276) | (17,060) | (13,283) |
| Depreciation of community and infrastructure assets | (6,339) | (3,465) | (1,303) |
| Gain/(loss) on disposal of subsidiaries and associates | 31,507 | 846 | (9,759) |
| | (58,576) | (53,536) | (52,753) |

## 8. Financing

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Interest income: | | | |
| Third parties | 148,752 | 70,835 | 52,150 |
| Related parties | 24,185 | 31,567 | 12,984 |
| | 172,937 | 102,402 | 65,134 |
| Interest expense: | | | |
| Third parties | (277,622) | (236,950) | (195,517) |
| Related parties | (1,663) | (3,158) | (2,963) |
| Amortization of transaction costs | (9,008) | (4,869) | (4,577) |
| | (288,293) | (244,977) | (203,057) |

## 9. Taxation

The following is an analysis of the income tax expense:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Current tax charge | (783,070) | (608,760) | (586,708) |
| Corrections to prior year's current tax charge | 15,416 | (13,152) | (7,176) |
| Deferred tax benefit/(expense) | 86,385 | (13,386) | 92,977 |
| Income tax expense | (681,269) | (635,298) | (500,907) |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

The following table is a reconciliation of the reported net income tax expense and the amount calculated by applying the Russian statutory tax rate of 24% to reported profit before income tax.

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Profit before income tax | 2,654,455 | 2,112,429 | 2,125,465 |
| Tax charge at Russian statutory rate — 24% | (637,069) | (506,983) | (510,112) |
| Profits taxed at different rates | (35,784) | (36,247) | 12,786 |
| Corrections to prior year's current tax charge | 15,416 | (13,152) | (7,176) |
| Net gain on tax restructuring | — | 3,521 | 41,803 |
| Non-tax deductible expenses, net | (37,843) | (76,920) | (55,171) |
| Tax-loss carry forwards expired | (18,494) | (17,462) | (67,629) |
| Changes in non-recognized deferred tax assets | 32,505 | 32,375 | 73,839 |
| Reassessment of deferred tax liabilities | — | (20,430) | 10,753 |
| Income tax expense | (681,269) | (635,298) | (500,907) |

Income tax charge for the year ended December 31, 2007 includes tax expense of US$ 1.3 million (2006: US$ 2.7 million, 2005: US$ 2.4 million) related to profits from discontinued operations (see note 29) and tax expense of US$ 9.0 million related to gains on disposals of discontinued operations (2006: nil, 2005: nil).

The composition of, and movements in, the net deferred tax liability based on the temporary differences arising between the fiscal and reporting balance sheets of the consolidated companies, is given below:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Deferred tax assets: | | | |
| Tax-loss carry forwards | 33,382 | 48,610 | 67,123 |
| Property, plant and equipment | 21,565 | 18,205 | 24,477 |
| Provisions | 25,689 | 15,707 | 11,320 |
| Financial investments | — | 2,770 | 14,530 |
| Other | 6,198 | 10,108 | 30,750 |
| Less: non-recognized deferred tax assets | (34,510) | (65,250) | (113,124) |
| Deferred tax assets | 52,324 | 30,150 | 35,076 |
| Deferred tax liabilities: | | | |
| Property, plant and equipment | (435,436) | (456,466) | (390,914) |
| Provisions | 82,524 | 65,859 | 52,153 |
| Tax-loss carry forwards | 15,991 | — | — |
| Other | (37,715) | (12,469) | (17,978) |
| Deferred tax liabilities | (374,636) | (403,076) | (356,739) |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

The movement in the net deferred tax liability is as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Opening balance | (372,926) | (321,663) | (339,616) |
| Recognized in income statement | 86,385 | (13,386) | 92,977 |
| Business combinations | 3,461 | (10,421) | (95,447) |
| Business de-combinations | 8,491 | — | 913 |
| Reclassified to assets held for sale | (24,913) | — | — |
| Foreign exchange difference | (22,810) | (27,456) | 19,510 |
| Closing balance | (322,312) | (372,926) | (321,663) |

As at December 31, 2007 the Group had not recognized cumulative tax-loss carry forwards of US$ 104.7 million that expire as follows: in 2008: US$ 44.4 million; and US$ 60.3 million have no expiry date.

Temporary differences, related to investments in subsidiaries where the Group is able to control the timing of the reversal and it is probable that the temporary difference will not reverse in the foreseeable future, amounted to US$ 1,905.7 million at December 31, 2007 (December 31, 2006: US$ 1,088.5 million; December 31, 2005, US$ 733.9 million respectively).

## 10. Cash and cash equivalents

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Petty cash | 607 | 254 | 429 |
| Cash at bank | 1,181,536 | 427,944 | 389,807 |
| Escrow accounts | 82 | 6,994 | 18,918 |
| Short-term deposits with maturity of less than 3 months | 364,656 | 893,829 | 687,166 |
| Investments in quoted monetary instruments | — | 62,327 | 88,320 |
| Cash balances of consolidated bank: | | | |
| Cash | — | 1,171 | 823 |
| Nostro accounts at the Central Bank of Russia | — | 110,036 | 39,781 |
| Nostro accounts at other banks | — | 6,637 | 16,997 |
| Placements with banks | — | 191,830 | 85,646 |
| | 1,546,881 | 1,701,022 | 1,327,887 |

As described in note 28 to these consolidated financial statements, as at December 31, 2006 and December 31, 2005 the Group had a subsidiary OAO Metallurgical commercial bank ("Metcombank"). Nostro accounts of Metcombank at the Central Bank of Russia and at other banks and interbank loans given by Metcombank with an original maturity of three months or less were included in cash and equivalents as at December 31, 2006 and 2005 respectively.

## 11. Short-term bank deposits

Short-term bank deposits totaled US$ 666.0 million at December 31, 2007 (December 31, 2006: US$ 1,147.3 million, December 31, 2005: US$ 674.5 million) and comprised of deposits with an original maturity of more than three months but remaining period to maturity of less than one year. The majority of such deposits have an original maturity of less than 6 months, and such deposits are used by the Group to earn investment income, while preserving a high liquidity position. Substantially all such deposits can be withdrawn, in case of necessity, prior to the maturity date with no loss in principal but reduced interest income.

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

## 12. Short-term financial investments

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| **Held-for-trading securities:** | | | |
| Promissory notes and bonds of third parties | 26,834 | 128,375 | 72,429 |
| Promissory notes of related parties | 7,457 | 5,198 | 4,772 |
| Quoted equity securities | 56,003 | 19,143 | 1,079 |
| Other securities | 56,270 | — | — |
| **Loans:** | | | |
| Loans to related parties | 82,205 | 75,699 | 81,133 |
| Loans to third parties | 38,046 | 11,912 | 24,408 |
| Loans to bank customers: | | | |
| Third parties | — | 54,991 | 71,232 |
| Related parties | — | 29,166 | 15,739 |
| Loan loss provisions | — | (2,758) | (3,008) |
| **Available-for-sale securities** | 818 | 116 | 67 |
| | 267,633 | 321,842 | 267,851 |

Loans given to related parties were provided at interest rates ranging from nil to 15% per annum, and were given to finance working capital and investments.

## 13. Trade accounts receivable

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Customers | 1,701,268 | 1,351,529 | 1,217,836 |
| Allowance for doubtful accounts | (26,650) | (26,944) | (43,643) |
| | 1,674,618 | 1,324,585 | 1,174,193 |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

## 14. Related party balances

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| **Joint ventures' balances** | | | |
| Trade accounts payable | 16,353 | 12,675 | 5,929 |
| **Other related party balances** | | | |
| Cash and cash equivalents at related party banks | 239,909 | 542 | 33,046 |
| Deposits with related party banks | 18,985 | — | — |
| Amounts receivable from other related parties: | | | |
| Trade accounts receivable | 43,770 | 80,296 | 172,164 |
| Advances paid | 90,961 | 34,299 | 18,158 |
| Other receivables | 27,988 | 13,108 | 18,581 |
| Short-term loans | 82,205 | 75,699 | 81,133 |
| Short-term promissory notes | 7,457 | 5,198 | 4,772 |
| Short-term loans to bank customers | — | 29,166 | 15,739 |
| Long-term loans | 37,147 | 76,528 | 43,003 |
| Long-term loans to bank customers | — | 7,078 | — |
| Held-to-maturity securities and deposits | 79,129 | 56,237 | 1,988 |
| | 368,657 | 377,609 | 355,538 |
| Amounts payable to other related parties: | | | |
| Trade accounts payable | 36,886 | 73,528 | 114,448 |
| Advances received | 3,843 | 732 | 2,026 |
| Payable for Lucchini acquisition | — | — | 216,483 |
| Other accounts payable | 1,833 | 14,182 | 119,430 |
| Bank demand deposits | — | 58,719 | 16,302 |
| Bank term deposits | — | 15,904 | 17,339 |
| | 42,562 | 163,065 | 486,028 |
| Debt financing includes the following balances with other related parties: | | | |
| Short-term debt financing | 36,866 | 4,893 | 27,059 |
| Long-term debt financing | 1,536 | 7,500 | 74 |
| | 38,402 | 12,393 | 27,133 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

## 15. Related party transactions

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Sales and income received from other related parties: | | | |
| Sales | 701,868 | 725,714 | 665,589 |
| Interest income | 24,185 | 31,567 | 12,984 |
| | 726,053 | 757,281 | 678,573 |
| Purchases from related parties: | | | |
| Purchases from associates: | | | |
| Non-capital expenditures | 1,810 | 1,878 | 7,956 |
| Purchases from joint ventures: | | | |
| Non-capital expenditures | 218,912 | 139,752 | 77,464 |
| Purchases from other related parties: | | | |
| Non-capital expenditures | 666,137 | 1,012,740 | 647,643 |
| Capital expenditures | 8,572 | 130,769 | 57,413 |
| | 674,709 | 1,143,509 | 705,056 |

## 16. Inventories

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Raw materials and supplies | 1,346,320 | 1,239,119 | 899,758 |
| Work-in-progress | 459,051 | 389,660 | 319,992 |
| Finished goods | 732,099 | 593,593 | 505,778 |
| | 2,537,470 | 2,222,372 | 1,725,528 |

Of the above amounts US$ 162.2 million (December 31, 2006: US$ 146.9 million, December 31, 2005: US$ 193.6 million) are stated at net realizable value.

During the year ended December 31, 2007, the Group recognized a US$ 24.9 million release and a US$ 25.5 million accrual of inventory obsolescence provision (December 31, 2006: US$ 32.2 million and US$ 8.2 million respectively; December 31, 2005: US$ 20.8 million and US$ 1.0 million respectively).

## 17. Other current assets

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Advances paid and prepayments | 232,998 | 185,767 | 144,892 |
| Other taxes and social security prepaid | 16,359 | 19,578 | 12,809 |
| Reserves at Central Bank of Russia | — | 12,325 | 4,938 |
| Other assets | 72,005 | 41,538 | 19,046 |
| | 321,362 | 259,208 | 181,685 |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

**18. Intangible assets**

| | Goodwill | Mineral licences | Software | Other intangible assets | Total |
|---|---|---|---|---|---|
| **Cost:** | | | | | |
| December 31, 2004 | 1,439 | — | 4,871 | 4,975 | 11,285 |
| Additions | — | 29,732 | 2,590 | — | 32,322 |
| Business combinations | — | — | 22,407 | 2,036 | 24,443 |
| Disposal | — | — | (271) | — | (271) |
| Foreign exchange difference | (1) | (512) | (1,599) | (684) | (2,796) |
| December 31, 2005 | 1,438 | 29,220 | 27,998 | 6,327 | 64,983 |
| Additions | — | 4,717 | 1,473 | 2,618 | 8,808 |
| Disposals | — | — | — | (337) | (337) |
| Foreign exchange difference | 2 | 2,948 | 3,033 | 689 | 6,672 |
| December 31, 2006 | 1,440 | 36,885 | 32,504 | 9,297 | 80,126 |
| Additions | — | 11,884 | 12,546 | 5,625 | 30,055 |
| Business combinations | 505,501 | 164 | — | 58,140 | 563,805 |
| Disposals | — | — | (6,161) | (966) | (7,127) |
| Reclassified to assets held for sale | — | (34,254) | — | — | (34,254) |
| Business de-combinations | — | — | (6,224) | (4,728) | (10,952) |
| Foreign exchange difference | 4,336 | 2,729 | 2,701 | 3,157 | 12,923 |
| December 31, 2007 | 511,277 | 17,408 | 35,366 | 70,525 | 634,576 |
| **Amortization and impairment:** | | | | | |
| December 31, 2004 | 21 | — | — | 3,975 | 3,996 |
| Amortization expense | — | — | 4,979 | — | 4,979 |
| Disposals | — | — | (264) | — | (264) |
| Foreign exchange difference | (1) | — | (157) | (93) | (251) |
| December 31, 2005 | 20 | — | 4,558 | 3,882 | 8,460 |
| Amortization expense | — | 1,708 | 5,045 | 2,240 | 8,993 |
| Disposals | — | — | — | (249) | (249) |
| Foreign exchange difference | 2 | 55 | 823 | 376 | 1,256 |
| December 31, 2006 | 22 | 1,763 | 10,426 | 6,249 | 18,460 |
| Amortization expense | — | 2,070 | 3,229 | 3,308 | 8,607 |
| Disposals | — | — | (6,161) | (396) | (6,557) |
| Reclassified to assets held for sale | — | (3,602) | — | — | (3,602) |
| Business combinations | — | 29 | — | 12,338 | 12,367 |
| Business de-combinations | — | — | (3,924) | (3,923) | (7,847) |
| Foreign exchange difference | 2 | 214 | 844 | 827 | 1,887 |
| December 31, 2007 | 24 | 474 | 4,414 | 18,403 | 23,315 |
| **Net book values:** | | | | | |
| December 31, 2005 | 1,418 | 29,220 | 23,440 | 2,445 | 56,523 |
| December 31, 2006 | 1,418 | 35,122 | 22,078 | 3,048 | 61,666 |
| December 31, 2007 | 511,253 | 16,934 | 30,952 | 52,122 | 611,261 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

## 19. Property, plant and equipment

The movements in property, plant and equipment are as follows:

| | Land and buildings | Plant and machinery | Other productive assets | Community and infrastructure assets | Construction-in-progress | Total assets |
|---|---|---|---|---|---|---|
| **Cost:** | | | | | | |
| December 31, 2004 | 1,041,866 | 2,725,924 | 186,909 | 40,743 | 753,664 | 4,749,106 |
| Reclassifications | (6,288) | 6,908 | 215 | (835) | — | — |
| Additions: | | | | | | |
| External | — | — | — | — | 1,216,875 | 1,216,875 |
| Interest capitalised | — | — | — | — | 13,128 | 13,128 |
| Business combinations | 417,874 | 1,067,527 | 3,051 | — | 50,337 | 1,538,789 |
| Disposals | (5,087) | (66,679) | (10,294) | (1,243) | (12,972) | (96,275) |
| Business de-combinations | (5,542) | (5,720) | (24) | — | (258) | (11,544) |
| Transfer to other assets | — | — | — | — | (12,060) | (12,060) |
| Transfers | 109,826 | 595,373 | 59,452 | 22,622 | (787,273) | — |
| Foreign exchange difference | (73,628) | (195,505) | (8,031) | (1,759) | (33,840) | (312,763) |
| December 31, 2005 | 1,479,021 | 4,127,828 | 231,278 | 59,528 | 1,187,601 | 7,085,256 |
| Reclassifications | (3,170) | 6,769 | (4,676) | 1,077 | — | — |
| Additions: | | | | | | |
| External | — | — | — | — | 1,243,514 | 1,243,514 |
| Interest capitalised | — | — | — | — | 10,129 | 10,129 |
| Business combinations | 81,452 | 11,203 | 917 | 687 | 1,728 | 95,987 |
| Disposals | (8,789) | (199,593) | (20,782) | (765) | (22,244) | (252,173) |
| Business de-combinations | — | — | — | (394) | — | (394) |
| Transfer to other assets | — | — | — | — | (11,907) | (11,907) |
| Transfers | 401,347 | 1,259,628 | 35,821 | 15,809 | (1,712,605) | — |
| Foreign exchange difference | 164,215 | 415,750 | 22,769 | 6,063 | 90,446 | 699,243 |
| December 31, 2006 | 2,114,076 | 5,621,585 | 265,327 | 82,005 | 786,662 | 8,869,655 |
| Reclassifications | 9,978 | (26,117) | 6,669 | 9,470 | — | — |
| Additions: | | | | | | |
| External | — | — | — | — | 1,594,681 | 1,594,681 |
| Interest capitalised | — | — | — | — | 4,101 | 4,101 |
| Business combinations | 77,829 | 108,055 | 2,501 | 631 | 9,563 | 198,579 |
| Disposals | (11,318) | (187,234) | (11,885) | (14,613) | (6,256) | (231,306) |
| Business de-combinations | (53,885) | (154,917) | (4,262) | (2,277) | (4,981) | (220,322) |
| Reclassified to assets held for sale | (182,171) | (166,972) | (13,863) | (152) | (56,508) | (419,666) |
| Transfer to other assets | — | (7,793) | — | — | (23,729) | (31,522) |
| Transfers | 183,703 | 1,126,899 | 74,378 | 26,683 | (1,411,663) | — |
| Foreign exchange difference | 167,214 | 452,205 | 24,806 | 7,583 | 60,669 | 712,477 |
| December 31, 2007 | 2,305,426 | 6,765,711 | 343,671 | 109,330 | 952,539 | 10,476,677 |

**Notes to the consolidated financial statements**
**for the year ended December 31, 2007**
***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

| | Land and buildings | Plant and machinery | Other productive assets | Community and infrastructure assets | Construction-in-progress | Total assets |
|---|---|---|---|---|---|---|
| **Depreciation and impairment:** | | | | | | |
| December 31, 2004 | 180,364 | 887,179 | 62,523 | 21,592 | 113,889 | 1,265,547 |
| Reclassifications | (3,187) | 5,315 | (834) | (1,294) | — | — |
| Depreciation expense | 72,601 | 385,036 | 32,678 | 1,303 | — | 491,618 |
| Disposals | (1,591) | (37,181) | (5,680) | (1,188) | (2,962) | (48,602) |
| Business de-combinations | (625) | (2,011) | (10) | — | — | (2,646) |
| Transfers | 402 | 6,080 | 659 | 17,071 | (24,212) | — |
| Impairment of assets | 8,662 | 80,367 | 2,489 | 5,046 | 14,820 | 111,384 |
| Foreign exchange difference | (7,660) | (36,387) | (2,757) | (1,133) | (3,676) | (51,613) |
| December 31, 2005 | 248,966 | 1,288,398 | 89,068 | 41,397 | 97,859 | 1,765,688 |
| Reclassifications | (3,640) | 5,515 | (1,678) | (197) | — | — |
| Depreciation expense | 112,891 | 448,901 | 29,490 | 3,465 | — | 594,747 |
| Business combinations | 1,634 | 91 | 277 | 3 | — | 2,005 |
| Disposals | (3,718) | (169,249) | (14,274) | (561) | (11,056) | (198,858) |
| Business de-combinations | — | — | — | (374) | — | (374) |
| Transfers | 7,952 | 2,165 | 3 | 5,003 | (15,123) | — |
| Impairment of assets | 10,454 | 33,169 | 1,824 | 2,605 | 9,684 | 57,736 |
| Foreign exchange difference | 27,274 | 131,173 | 8,846 | 4,189 | 6,844 | 178,326 |
| December 31, 2006 | 401,813 | 1,740,163 | 113,556 | 55,530 | 88,208 | 2,399,270 |
| Reclassifications | 1,583 | (4,650) | 565 | 2,502 | — | — |
| Depreciation expense | 139,192 | 614,696 | 33,861 | 6,339 | — | 794,088 |
| Business combinations | 23,541 | 26,970 | 1,051 | 17 | — | 51,579 |
| Disposals | (2,714) | (148,664) | (9,227) | (1,309) | (1,186) | (163,100) |
| Business de-combinations | (6,806) | (51,376) | (1,312) | (1,869) | (69) | (61,432) |
| Reclassified to assets held for sale | (22,223) | (63,321) | (5,190) | (17) | (6,043) | (96,794) |
| Transfers | 3,215 | 304 | 58 | 4,956 | (8,533) | — |
| Impairment of assets | 2,112 | 15,226 | (36) | 2,441 | 9,366 | 29,109 |
| Foreign exchange difference | 40,491 | 167,022 | 11,027 | 4,751 | 7,855 | 231,146 |
| December 31, 2007 | 580,204 | 2,296,370 | 144,353 | 73,341 | 89,598 | 3,183,866 |
| **Net book values:** | | | | | | |
| December 31, 2005 | 1,230,055 | 2,839,430 | 142,210 | 18,131 | 1,089,742 | 5,319,568 |
| December 31, 2006 | 1,712,263 | 3,881,422 | 151,771 | 26,475 | 698,454 | 6,470,385 |
| December 31, 2007 | 1,725,222 | 4,469,341 | 199,318 | 35,989 | 862,941 | 7,292,811 |

Other productive assets include transmission equipment, transportation equipment and tools.

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

## 20. Investment in associates and joint ventures

The Group's investment in associated and joint ventures companies is described in the tables below. Group structure and certain additional information on investments in associated and joint ventures companies, including ownership percentages, is given in note 28.

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| **Associates** | | | |
| Severstal US Holdings LLC | 386,105 | 132,076 | 59,415 |
| Air Liquide Severstal | 7,537 | 7,026 | 3,214 |
| TA Cord | — | 844 | 2,108 |
| Others | 1,276 | 2,811 | 2,927 |
| **Joint ventures** | | | |
| Double Eagle Steel Coating Company | 22,936 | 28,859 | 26,409 |
| Spartan Steel Coating LLC | 53,978 | 63,818 | 56,374 |
| Mountain State Carbon LLC | 117,260 | 119,472 | 60,205 |
| | 589,092 | 354,906 | 210,652 |

The following is summarized financial information in respect of associates and joint ventures:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Assets | 1,797,458 | 1,269,330 | 515,409 |
| Liabilities | 965,270 | 615,767 | 85,206 |
| Equity | 832,188 | 653,563 | 430,203 |

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Revenues | 440,272 | 373,765 | 178,655 |
| Net income/(loss) | (105,326) | 3,262 | (2,964) |

Severstal US Holdings LLC, was created by Severstal and its related parties as a holding company for the SeverCorr project — construction of a mini mill in the United States of America. By December 31, 2007, Severstal have contributed to the project US$ 461.6 million and provided a US dollar denominated loan to SeverCorr LLC in the amount of US$ 60.0 million. The loan is repayable in 2008 and bears interest at 15% per annum. By December 31, 2007, related parties of Severstal have contributed to the project US$ 81.8 million. Having completed those contributions, Severstal and its related parties have fully fulfilled their financing obligations for this project.

By December 31, 2006, the Group, through its subsidiary Severstal North America Inc, had contributed US$ 120.0 million to the Mountain State Carbon LLC, a joint venture with Wheeling-Pittsburgh Steel Corporation ("Wheeling-Pittsburgh"). Wheeling-Pittsburgh had contributed to the joint venture all of its coking assets in Follansbee, USA, valued at US$ 86.9 million, and US$ 3.1 million in cash. This cash and US$ 30.0 million of additional contributions from Wheeling-Pittsburgh over the next three years to 2009 will be used to rehabilitate all of the coke batteries of the joint venture and provide the Group's US integrated steel operations a reliable and competitive supply of metallurgical coke. Each partner has a 50% share in Mountain State Carbon LLC from April 2006.

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

## 21. Long-term financial investments

| | December 31, 2007 | 2006 | 2005 |
|---|---|---|---|
| **Loans:** | | | |
| Loans to related parties | 37,147 | 76,528 | 43,003 |
| Loans to third parties | 10,305 | 30,556 | 31,936 |
| Loans to bank customers: | | | |
| Related parties | — | 7,078 | — |
| Third parties | — | 19,226 | — |
| **Available-for-sale securities** | 26,285 | 10,315 | 12,614 |
| **Held-to-maturity securities and deposits** | 79,129 | 56,237 | 1,988 |
| | 152,866 | 199,940 | 89,541 |

## 22. Bank customer accounts

| | December 31, 2007 | 2006 | 2005 |
|---|---|---|---|
| Demand deposits | — | 22,103 | 30,502 |
| Term deposits | — | 9,040 | 68,365 |
| | — | 31,143 | 98,867 |

## 23. Debt finance

| | December 31, 2007 | 2006 | 2005 |
|---|---|---|---|
| Citibank CLN — Eurobonds 2009 | 325,000 | 325,000 | 325,000 |
| Citibank CLN — Eurobonds 2014 | 375,000 | 375,000 | 375,000 |
| Other issued bonds | — | 113,934 | 327,446 |
| Bank financing | 2,357,588 | 1,901,046 | 1,628,709 |
| Factoring of receivables | 201,909 | 224,049 | 191,732 |
| Other financing | 51,046 | 29,679 | 60,674 |
| Accrued interest | 40,355 | 54,748 | 39,720 |
| Unamortized balance of transaction costs | (23,996) | (17,857) | (20,462) |
| | 3,326,902 | 3,005,599 | 2,927,819 |
| Total debt is denominated in the following currencies: | | | |
| US Dollars | 1,501,465 | 1,210,753 | 1,287,620 |
| Roubles | 391,196 | 345,728 | 338,894 |
| Euro | 1,432,490 | 1,449,118 | 1,301,305 |
| Other currencies | 1,751 | — | — |
| | 3,326,902 | 3,005,599 | 2,927,819 |
| Total debt is contractually repayable after the balance sheet date as follows: | | | |
| Less than one year | 972,079 | 957,564 | 996,125 |
| Between one and five years | 1,659,450 | 1,488,594 | 1,496,325 |
| After more than five years | 695,373 | 559,441 | 435,369 |
| | 3,326,902 | 3,005,599 | 2,927,819 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

Debt finance rose from banks and unused long term credit lines are secured by charges over:

- US$ 210.4 million (December 31, 2006: US$ 221.3 million; December 31, 2005: US$ 129.4 million) net book value of plant and equipment;
- US$ 515.7 million (December 31, 2006: US$ 1,015.6 million; December 31, 2005: US$ 1,296.2 million) of current assets and revenues from export contracts; and
- US$ 243.4 million (December 31, 2006: US$ 365.9 million; December 31, 2005: US$ 97.1 million) of financial assets.

A part of the Group's debt financing is subject to certain covenants. The Group complied with all debt covenants, including equity ratios, during the years ended December 31, 2007, 2006 and 2005.

At the balance sheet date the Group had US$ 983.7 million (December 31, 2006: US$ 422.1 million; December 31, 2005: US$ 319.9 million) of unused long term credit lines available to it.

## 24. Other current liabilities

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Amounts payable to employees | 246,448 | 186,431 | 149,757 |
| Advances received | 214,405 | 230,696 | 156,494 |
| Provisions (Note 26) | 43,974 | 12,011 | 17,736 |
| Accrued expenses | 24,123 | 41,396 | 19,525 |
| Lease liabilities | 9,926 | 2,579 | 1,964 |
| Other liabilities | 61,704 | 33,735 | 33,742 |
| | 600,580 | 506,848 | 379,218 |

## 25. Retirement benefit liability

The Group provides for its employees the following retirement benefits, which are actuarially calculated as defined benefit obligation: lump sums payable to employees on retirement, monthly pensions, jubilee benefits, invalidity and death lump sums, burial expenses compensations and other benefits.

The following assumptions have been used to calculate the retirement benefit liability:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Discount rates: | | | |
| Russia | 6.47% | 6.46% | 6.85% |
| USA | 5.25% | 5.75% | 5.50% |
| UK | 3.10% | 4.90% | n/a |
| Italy and France | 5.10% to 5.45% | 4.60% | 4.0% to 5.0% |
| Future rates of benefit increase: | | | |
| Russia | 5.8% to 6.2% | 6.20% | 6.20% |
| USA | 0.00% | 0.00% | 0.00% |
| UK | 3.40% | 2.80% | n/a |
| Italy and France | 2.0% to 3.0% | 3.00% | 3.0% to 3.5% |

Rates shown for USA are the post-retirement healthcare trend rates. Due to a new labor contract at Severstal North America the following healthcare trend rates apply to the hourly plan:

2007: 9%
2008: 9%
2009: 8%
2010: 0%

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

Hourly plan liability that is incurred to these rates is US$ 35.2 million.

Present value of the defined benefit obligation with the deduction of fair value of the plan assets is recognized as retirement benefit liability at the balance sheet.

| | December 31, | | | | |
|---|---|---|---|---|---|
| | 2007 | 2006 | 2005 | 2004 | 2003 |
| Present value of the defined benefit obligation | 495,713 | 549,009 | 387,657 | 208,325 | 61,152 |
| Fair value of the plan assets | (108,315) | (106,055) | (49,171) | (50,302) | (29,127) |
| Retirement benefit liability | 387,398 | 442,954 | 338,486 | 158,023 | 32,025 |

The components of the retirement benefit liabilities are as follows:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Retirees | 172,244 | 140,658 | 103,915 |
| Other participants: | | | |
| Vested | 126,890 | 203,334 | 133,443 |
| Non-vested | 196,579 | 205,017 | 150,299 |
| Total | 495,713 | 549,009 | 387,657 |

The movements in the defined benefit obligation are as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Opening balance | 549,009 | 387,657 | 208,325 |
| Business combinations/(de-combinations) | (33,612) | 39,328 | 149,110 |
| Reclassified to assets held for sale | (9,260) | — | — |
| Benefits paid | (55,238) | (33,547) | (36,241) |
| Interest cost | 27,589 | 24,962 | 19,144 |
| Service cost | 18,640 | 18,767 | 12,890 |
| Actuarial (gain)/loss | (37,497) | 68,573 | 56,139 |
| Foreign exchange loss/(gain) | 36,082 | 43,269 | (21,710) |
| Closing balance | 495,713 | 549,009 | 387,657 |

The movements in the plan assets are as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Opening balance | 106,055 | 49,171 | 50,302 |
| Business combinations/(de-combinations) | (10,122) | 28,566 | — |
| Contributions made during the year | 11,534 | 13,424 | 16,641 |
| Benefits paid | (14,852) | (12,356) | (18,787) |
| Return on assets | 10,921 | 16,382 | 9,084 |
| Actuarial gain/(loss) | (441) | 915 | (6,241) |
| Foreign exchange gain/(loss) | 5,220 | 9,953 | (1,828) |
| Closing balance | 108,315 | 106,055 | 49,171 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

Defined benefit obligation analysis is as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Wholly unfunded | 258,926 | 284,485 | 238,098 |
| Partly funded | 236,787 | 264,524 | 149,559 |
| Total | 495,713 | 549,009 | 387,657 |

Plan assets analysis is as follows:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Equity instruments | 44,448 | 44,450 | 20,625 |
| Government bonds | 28,548 | 28,850 | 20,009 |
| Corporate bonds | 14,964 | 14,178 | — |
| Deposits | 3,037 | 1,980 | 3,132 |
| Cash | 1,170 | 1,417 | 511 |
| Other investments | 16,148 | 15,180 | 4,894 |
| Total | 108,315 | 106,055 | 49,171 |

The Group's best estimate of contributions expected to be paid to the plan during the year 2008 is US$ 8.5 million. Expected rate of return on plan assets was 17.0% for Russia and 4.95% for United Kingdom during 2007. Actual rate of return on plan assets was 16.1% for Russia and 4.95% for United Kingdom during 2007.

The retirement benefit expenses recognized in the income statement are contained in the caption: "General and administrative expenses", except for the interest cost, which is recognized in the caption "Interest expense".

## 26. Other non-current liabilities

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Decommissioning liability | 108,762 | 128,209 | 102,885 |
| Restructured tax liabilities | 24,978 | 67,731 | 97,368 |
| Provisions | 66,859 | 67,139 | 50,610 |
| Lease liabilities | 14,610 | 13,742 | 9,498 |
| Other | 11,179 | 9,269 | 20,714 |
| | 226,388 | 286,090 | 281,075 |

***Decommissioning liability***

The Group has environmental liabilities related to restoration of soil and other related works, which are due upon the closures of its coal mines. These liabilities have been estimated using existing technology, at current prices, and discounted using a real discount rate of 2%. A substantial part of the decommissioning costs is expected to be incurred between 2020 and 2040.

***Restructured tax liabilities***

OAO Vorkutaugol and OAO Mine Vorgashorskaya had significant amounts of taxes in arrears, when they were acquired by the Group's Majority Shareholder in June 2003.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

In November 2005, these subsidiaries signed restructuring agreements with the tax authorities. In accordance with these agreements, the principal amounts of taxes, and fines thereon and 15% of tax interest are payable by instalments over four years. If those payments are made on schedule, the remaining 85% of tax interest liability at the date of restructuring will be forgiven. The Group's management is confident that all payments will be in accordance with the agreed schedules, and accordingly recognized a US$ 200.9 million gain on tax restructuring in the income statement for the year ended December 31, 2005. This gain is comprised of US$ 186.8 million of tax interest, which will be forgiven, and has been derecognized from liabilities, and US$ 14.1 million of discounting of the remaining liabilities using the interest rate of 9.86%. During 2005, tax authorities accrued an additional US$ 26.7 million of tax interest on tax liabilities being restructured. These amounts were recognized as an expense in the income statement for the year ended December 31, 2005. During 2006, the Group was able to include part of this tax interest into restructuring, recognizing a gain of US$ 14.7 million in the income statement for the year ended December 31, 2006. Restructured tax liabilities are subject to interest rate of 5% per annum, which is included in the caption "Interest expense" since the moment of restructuring.

Accordingly, net gain on restructuring of tax liabilities is shown in the income statement as following:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Tax interest accrued prior to restructuring | — | — | (26,675) |
| Gain on restructuring of tax liabilities | — | 14,669 | 200,853 |
| Net gain on restructuring of tax liabilities | — | 14,669 | 174,178 |

Current portion of restructured tax liabilities is included in the caption "Other taxes and social security payable". The total amount of the restructured taxes is presented in the table below:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Payable within one year | 20,960 | 43,553 | 26,059 |
| Payable after one year | 24,978 | 67,731 | 97,368 |
| | 45,938 | 111,284 | 123,427 |

***Provisions***

The current portion of provisions is included in the caption "Other current liabilities". The total amount of the provisions is presented in the table below:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Social security claims | 30,259 | 28,689 | 23,020 |
| Other employee related | 16,075 | 13,578 | 12,984 |
| Legal claims | 27,423 | 21,917 | 17,004 |
| Restructuring | 8,284 | 5,569 | — |
| Environmental claim | 24,416 | 6,052 | 9,657 |
| Other | 4,376 | 3,345 | 5,681 |
| | 110,833 | 79,150 | 68,346 |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Payable within one year | 43,974 | 12,011 | 17,736 |
| Payable after one year | 66,859 | 67,139 | 50,610 |
| | 110,833 | 79,150 | 68,346 |

These provisions represent management's best estimate of the potential losses arising in these cases. The actual outcome of those cases is currently uncertain, and might differ from the recorded provisions.

## 27. Share capital

The Parent Company's share capital consists of ordinary shares with a nominal value of RUR 0.01 each. Authorized share capital of Severstal at December 31, 2005 comprised 551,854,800 shares and was fully issued and paid on that date. At December 31, 2007 and 2006, Severstal had 1,007,701,355 issued and fully paid shares.

The nominal amount of initial share capital was converted into US dollars using exchange rates during the Soviet period, when the Government contributed the original capital funds to the enterprise. These capital funds were converted into ordinary shares on September 24, 1993 and sold by the Government at privatization auctions.

Consequently, the total value of issued share capital presented in these consolidated financial statements comprises:

| | Number of shares, thsd. | US$'000 |
|---|---|---|
| Share capital at December 31, 2005 | 917,268 | 3,311,254 |
| Share capital at December 31, 2006 | 1,007,701 | 3,311,288 |
| Share capital at December 31, 2007 | 1,007,701 | 3,311,288 |

All shares carry equal voting and distribution rights.

### *Capital management*

The Group's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. This policy includes compliance with certain externally imposed minimum capital requirements. The Group's management constantly monitors profitability and leverage ratios and compliance with the minimum capital requirements. The Group uses the return on assets ratio which is defined as profit from operations divided by total assets (averaged over the measurement period) and the leverage ratio calculated as net debt, comprising of long-term and short-term indebtedness less cash, cash equivalents and short-term bank deposits, divided by shareholder's equity. The level of dividends is also monitored by the Board of Directors of the Group.

There were no changes in the Group's approach to capital management during the year.

### *Dividends*

The maximum dividend payable is restricted to the total accumulated retained earnings of the Parent Company determined according to Russian law. As at the balance sheet date, reserves available for distribution, were US$ 5,894.9 million (December 31, 2006: US$ 4,667.6 million; December 31, 2005: US$ 3,308.6 million).

On June 15, 2007 the Meeting of Shareholders approved annual dividend of 5.0 rubles (US$ 0.2 at June 15, 2007 exchange rate) per share and per GDR in respect of 2006.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

On June 29, 2007 the Meeting of Shareholders approved a dividend of 2.6 rubles (US$ 0.1 at June 29, 2007 exchange rate) per share and per GDR for the first quarter of 2007 with the record date of May 18, 2007.

On September 28, 2007 the Meeting of Shareholders approved a dividend of 10.0 rubles (US$ 0.4 at September 28, 2007 exchange rate) per share and per GDR for the first half of 2007.

On December 20, 2007 the Meeting of Shareholders approved a dividend of 2.5 rubles (US$ 0.1 at December 20, 2007 exchange rate) per share and per GDR in respect of the third quarter of 2007.

## 28. Subsidiaries, associates and joint ventures

The following is a list of the Group's significant subsidiaries, associates and joint ventures and the effective ownership holdings therein:

| | December 31, | | | | |
|---|---|---|---|---|---|
| **Company** | **2007** | **2006** | **2005** | **Location** | **Activity** |
| **Russian Steel segment:** | | | | | |
| *Subsidiaries*: | | | | | |
| ZAO Severgal | 100.0% | 75.0% | 75.0% | Russia | Hot dip galvanizing |
| ZAO Severstal SMZ-Kolpino | 100.0% | n/a | n/a | Russia | Steel constructions |
| ZAO Severstal TPZ-Sheksna | 100.0% | n/a | n/a | Russia | Steel constructions |
| ZAO Severstal Steel Solutions | 100.0% | n/a | n/a | Russia | Steel constructions |
| OOO SSM-Tyazhmash | 100.0% | 100.0% | 100.0% | Russia | Repairs & construction |
| OAO Domnaremont | 82.7% | 82.1% | 56.4% | Russia | Repairs & construction |
| ZAO Firma Stoik | 100.0% | 100.0% | 100.0% | Russia | Repairs & construction |
| OAO Metallurgremont | 79.8% | 79.8% | 79.3% | Russia | Repairs & construction |
| OOO Energoremont | 100.0% | 100.0% | 100.0% | Russia | Repairs & construction |
| OOO Electroremont | 93.3% | 93.3% | 93.3% | Russia | Repairs & construction |
| Victory Industries, Inc | 100.0% | 100.0% | n/a | USA | Repairs & construction |
| OOO Uralmash MO | n/a | 100.0% | 100.0% | Russia | Engineering |
| OOO AviaCompany Severstal | 100.0% | 100.0% | 100.0% | Russia | Air transport |
| Severstal Export GmbH | 100.0% | 100.0% | 100.0% | Switzerland* | Steel sales |
| AS Severstallat | 50.5% | 50.5% | 50.5% | Latvia* | Steel sales |
| Latvijas Metals | 50.5% | 50.5% | 50.5% | Latvia* | Steel sales |
| ZAO SeverStalBel | 80.6% | n/a | n/a | Belarus* | Steel sales |
| Severstal-Ukraine LLC. | 51.0% | n/a | n/a | Ukraine* | Steel sales |
| Armaturu Servisa Centrs SIA | 25.2% | 25.2% | 25.2% | Latvia* | Steel service center |
| ZAO Neva-Metall Trans | 100.0% | n/a | n/a | Russia | Shipping operations |
| ZAO Neva-Metall | 100.0% | n/a | n/a | Russia | Shipping operations |
| Upcroft Limited | 100.0% | 100.0% | 100.0% | Cyprus* | Holding company*** |
| Varndell Limited | 100.0% | 100.0% | 100.0% | Cyprus* | Holding company*** |
| *Associates:* | | | | | |
| Severstal US Holdings LLC** | 85.0% | 63.3% | 60.0% | USA* | Holding company |
| **Severstal North America segment:** | | | | | |
| *Subsidiaries:* | | | | | |
| Severstal North America Inc | 100.0% | 100.0% | 93.0% | USA | Iron & steel mill |
| *Associates:* | | | | | |
| Delaco Processing LLC | 49.0% | 49.0% | 45.6% | USA | Steel slitting |
| *Joint ventures:* | | | | | |
| Spartan Steel Coating LLC | 48.0% | 48.0% | 44.6% | USA | Hot dip galvanizing |
| Double Eagle Steel Coating Company | 50.0% | 50.0% | 46.5% | USA | Electro-galvanizing |
| Mountain State Carbon LLC | 50.0% | 50.0% | 31.0% | USA | Coking coal |

(*) Russian Steel segment contains Russian production entities, foreign trading companies, which are selling products primarily produced in Russia, and other foreign companies, which either provide services to Russian production entities or are managed from Russia.

(**) 20.1% of ordinary shares at December 31, 2007 (December 31, 2006: 20.2%; December 31, 2005: 19.9%).

(***) Upcroft is holding 29.0% of Lucchini SpA and Varndell is holding 50.8% of Lucchini SpA.

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

| Company | December 31, 2007 | 2006 | 2005 | Location | Activity |
|---|---|---|---|---|---|
| **Lucchini segment:** | | | | | |
| *Subsidiaries:* | | | | | |
| Lucchini SpA | 79.8% | 70.8% | 70.8% | France | Holding company |
| Ascometal SAS | 79.8% | 70.8% | 70.8% | France | Steel manufacturing |
| Ascometal GmbH | 79.8% | 70.8% | 70.8% | Germany | Sales |
| Ascoforge Safe SAS | n/a | 70.8% | 70.8% | France | Forgings |
| Bari Fonderie Meridionali SpA | 79.8% | 70.8% | 70.8% | Italy | Forgings |
| Bi-Mec Srl | 79.8% | 70.8% | 70.8% | Italy | Maintenance |
| GSI Lucchini SpA | 55.3% | 49.1% | 49.1% | Italy | Steel spheres |
| Nitruvid SAS | n/a | 70.8% | 70.8% | France | Steel finishing |
| Lucchini Asia Pacific Pte Ltd | 79.8% | 70.8% | 70.8% | Singapore | Sales |
| Lucchini Holland BV | 79.8% | 70.8% | 70.8% | Netherlands | Investment holding |
| Lucchini HPS GmbH | n/a | 23.5% | 46.0% | Germany | Sales |
| Lucchini Iberia SI | 79.8% | 70.8% | 70.8% | Spain | Sales |
| Lucchini Poland Spzoo | n/a | 70.8% | 70.8% | Poland | Machining |
| Lucchini Servizi Srl | 79.8% | 70.8% | 70.8% | Italy | Dormant |
| Lucchini Sidermeccanica SpA | n/a | 70.8% | 70.8% | Italy | Casting and machining |
| Lucchini Siderprodukte AG | 51.9% | 46.0% | 46.0% | Switzerland | Sales |
| Lucchini Sweden AB | n/a | 70.8% | 70.8% | Sweden | Machining |
| Lucchini UK Ltd | n/a | 70.8% | 70.8% | UK | Machining |
| Luchini USA Inc | 79.8% | 70.8% | 70.8% | USA | Sales |
| Servola SpA | 79.8% | 70.8% | 70.8% | Italy | Asset holding |
| Sideris Steel SAS | 79.8% | 70.8% | 70.8% | France | Investment holding |
| Simmofos Sarl | 79.8% | 70.8% | 70.8% | France | Asset holding |
| Sipro HPS AG | n/a | n/a | 46.0% | Switzerland | Sales |
| Vertek Srl | 79.8% | 70.8% | 70.8% | Italy | Steel finishing |
| Siderco SpA | 79.8% | n/a | n/a | Italy | Slag processor |
| *Associates:* | | | | | |
| ESPRA SAS | 27.9% | 24.8% | 24.8% | France | Steel scrap |
| Logistica Servola Srl | 39.9% | 35.4% | 35.4% | Italy | Dormant |
| Setrans Srl | n/a | 21.2% | 21.2% | Italy | Logistics and storage |
| Tecnologie Ambientali Pulite Srl | 19.9% | 17.6% | 17.6% | Italy | Enviromental services |
| GICA SA | 19.9% | n/a | n/a | Switzerland | Carbon dioxide trading |
| *Companies classified as held for sale:* | | | | | |
| Relco Spzoo | 79.8% | 70.8% | 70.8% | Poland | Land holding |
| Coimpex Spzoo | 31.9% | 28.3% | 28.3% | Poland | Land holding |
| **Metalware segment:** | | | | | |
| *Subsidiaries:* | | | | | |
| OAO Severstal-Metiz | 97.0% | 97.0% | 100.0% | Russia | Steel machining |
| OAO Dneprometiz | 58.2% | 58.2% | nil% | Ukraine | Steel machining |
| Carrington Wire Ltd | 97.0% | 97.0% | nil% | UK | Steel machining |
| OAO Cherepovets Steel Rolling Mill | n/a | n/a | 88.8% | Russia | Steel machining |
| OAO Orlovsky Steel Rolling Mill | n/a | n/a | 87.2% | Russia | Steel machining |
| OOO Volgometiz | n/a | 100.0% | 100.0% | Russia | Steel machining |
| OOO Policher | n/a | 87.3% | 80.0% | Russia | Polymer coatings |
| OOO UniFence | 97.0% | n/a | n/a | Russia | Steel machining |
| OOO ChSPZ MKR (UniSpring) | 97.0% | 48.5% | 44.4% | Russia | Mattress springs |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

| Company | December 31, 2007 | 2006 | 2005 | Location | Activity |
|---|---|---|---|---|---|
| **Mining segment:** | | | | | |
| *Subsidiaries:* | | | | | |
| OAO Karelsky Okatysh | 94.8% | 90.8% | 90.8% | Russia | Iron ore pellets |
| OAO Olkon | 92.7% | 91.8% | 91.6% | Russia | Iron ore concentrate |
| OAO Vorkutaugol | 93.1% | 89.2% | 88.1% | Russia | Coking coal concentrate |
| OAO Mine Vorgashorskaya | 75.0% | 73.6% | 70.2% | Russia | Coking coal concentrate |
| OAO Mine Pervomaiskaya | 99.4% | 99.1% | 99.1% | Russia | Coking coal concentrate |
| OAO Mine Berezovskaya | 97.5% | 96.3% | 96.0% | Russia | Coking coal concentrate |
| OAO SShEMK | 75.6% | 75.6% | 75.6% | Russia | Engineering |
| OAO Severokuzbasskoe PTU | 87.3% | 87.3% | 87.3% | Russia | Transportation |
| OAO Anzhero-Sudzhenskoe PTU | 94.4% | 94.4% | 94.4% | Russia | Transportation |
| ZAO Vtorchermet | 84.8% | n/a | n/a | Russia | Processing scrap |
| ZAO Rospromresursy | 100.0% | n/a | n/a | Russia | Processing scrap |
| OAO Murmanskvtormet | 75.1% | n/a | n/a | Russia | Processing scrap |
| OAO Arhangelskii vtormet | 75.0% | n/a | n/a | Russia | Processing scrap |
| OOO Nerengri-Metallik | 100.0% | n/a | n/a | Russia | Gold mining |
| ZAO Rudnik Aprelkovo | 100.0% | n/a | n/a | Russia | Gold mining |
| Celtic Resources Holdings Plc | 86.3% | n/a | n/a | Ireland | Gold mining |
| OOO SPB-Giproshakht | 100.0% | n/a | n/a | Russia | Engineering |
| OAO Pechorugol | n/a | 99.3% | 99.3% | Russia | Holding company |
| OOO Olkon-Invest | n/a | 100.0% | 100.0% | Russia | Holding company |
| OOO Terra | n/a | 100.0% | 100.0% | Russia | Holding company |
| OOO Holding Gornaya Company | 100.0% | 100.0% | 100.0% | Russia | Holding company |
| ZAO Impulse-Consult | n/a | 100.0% | 100.0% | Russia | Holding company |
| OOO Investment Company Kuzbassugol | n/a | 100.0% | 100.0% | Russia | Holding company |
| **Financing segment:** | | | | | |
| *Subsidiaries:* | | | | | |
| OAO Metallurgical Commercial Bank | n/a | 72.9% | 72.6% | Russia | Banking |
| **IPM segment:** | | | | | |
| *Subsidiaries:* | | | | | |
| ZAO Izhora Pipe Mill | 100.0% | 100.0% | 100.0% | Russia | Wide pipes |

In addition, at the balance sheet date, a further 34 (December 31, 2006: 26; December 31, 2005: 26) subsidiaries and associates, which are not material to the Group, either individually or in aggregate, have been included in these consolidated financial statements.

Information on carrying amounts, acquisitions and disposals of associated companies is disclosed in Note 20 of these consolidated financial statements.

During 2007, Severstal completed acquisitions of controlling stakes in a number of companies previously controlled by Severstal's Majority Shareholder. These consolidated financial statements take account of such acquisitions as if they had occurred at the beginning of the earliest comparative period presented or, if later, at the date on which control was obtained by the common controlling shareholder. These acquisition transactions are described in the following paragraphs.

***Acquisitions of Mining companies from Majority Shareholder during 2007***

In July 2007, the Group acquired a 100% stake in OOO Petrovtormet and OOO Severstalskrap-Komi, for a total consideration of US$ 0.02 million and US$ 0.2 million, respectively, and a 75.01% and a 75.1% stake in OAO Arhangelskii vtormet and in OAO Murmanskvtormet, for a total consideration of US$ 2.2 million and US$ 2.9 million, respectively. OAO Arhangelskii vtormet, OAO Murmanskvtormet, OOO Petrovtormet and OOO Severstalskrap-Komi were acquired from the controlling shareholder and comparatives were restated in accordance with the Group's accounting policy.

The acquirees' profit since the acquisition dates included in the Group's profit for the period, as well as the revenue and profit of the acquired entities from the beginning of the period to the dates of acquisition, individually and in the aggregate, are insignificant to the Group's revenue and profit for the period.

***Acquisitions of subsidiaries from third and related parties during 2007***

In January 2007, the Group completed the acquisition of 84.8% of the share capital of ZAO Vtorchermet and its wholly-owned subsidiaries and certain related companies for a total consideration of US$ 45.4 million. ZAO Vtorchermet is a scrap processing and wholesale company, and the majority of its operations is located in Saint Petersburg. The acquisition was conducted to secure a reliable source of scrap for the Russian steel mill in case of future changes in the Russian scrap market.

In March 2007, the Group purchased 100% of the share capital of Siderco SpA from the Lucchini family for €1.35 million (US$ 1.78 million at the transaction date exchange rate). Management determined that the fair value of the net identifiable assets and liabilities acquired was substantially the same as the book value.

In May 2007, the Group completed the acquisition of 100% of a stevedore company, ZAO Neva-Metall, for US$ 98.7 million and 100% of the shipping agency ZAO Neva-Metall Trans for US$ 1.3 million from a related party. The majority of their operations are located in Saint Petersburg. The acquisition was conducted to secure a self-supporting export logistic chain. Management has not yet completed the estimation of fair values of the acquired assets and liabilities and, accordingly, does not currently possess all necessary information to disclose the effect of this acquisition on the Group's financial position or results of operations. Final purchase price allocation is expected to be completed during the first quarter of the year 2008.

In July 2007, the Group acquired a 100% stake in each of the companies OOO Georesurs, OOO Severstal-Vtormet, and OOO SPB-Giproshakht for a total consideration of US$ 2.1 million, US$ 24.9 million, and US$ 6.3 million, respectively.

In October 2007, the Group acquired a 100% stake in OOO Nerengri-Metallik and a 100% stake in ZAO Mine Aprelkovo for a total consideration of US$ 105 million and US$ 153 million, respectively. OOO Nerengri-Metallik mines gold from the Tabornoye deposit in the Sakha-Yakutiya Republic, ZAO Mine Aprelkovo mines from the Pogromnoye gold deposit in the Chita Region. Both deposits are operated as open-pit mines with gold extracted utilizing heap leaching technology. Management has not yet completed the estimation of fair values of the acquired assets and liabilities and, accordingly, does not currently possess all necessary information to disclose the effect of this acquisition on the Group's financial position or results of operations. Final purchase price allocation is expected to be completed within one year starting from the date of acquisition.

The acquirees' profit since the acquisition dates included in the Group's profit for the period, as well as the revenue and profit of the acquired entities from the beginning of the period to the dates of acquisition, individually and in the aggregate, are insignificant to the Group's revenue and profit for the period.

During August–December 2007, the Group acquired an 86.3% stake in Celtic Resources Holdings Plc. for a total consideration of US$ 264.6 million. Management has not yet completed the estimation of fair values of the acquired assets and liabilities and, accordingly, does not currently possess all necessary information to disclose the effect of this acquisition on the Group's financial position or results of operations. Final purchase price allocation is expected to be completed within one year starting from the date of acquisition.

The acquirees' profit since the acquisition dates included in the Group's profit for the period, is insignificant to the Group's profit for the period. The acquirees' revenue and profit from the beginning of the period to the dates of acquisition comprised US$ 62 million and US$ 7 million respectively.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

A summary of assets and liabilities acquired from third and related parties but excluding acquisitions from the Majority Shareholder during 2007, 2006 and 2005 is presented below:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Cash and cash equivalents | 25,665 | 5,875 | 657 |
| Trade accounts receivable | 14,462 | 26,463 | 1,311 |
| Inventories | 46,902 | 18,841 | 4,906 |
| Deferred tax assets | 3,461 | — | — |
| Other current assets | 88,106 | 7,601 | 792 |
| Property, plant and equipment | 147,000 | 93,982 | 4,036 |
| Intangible assets | 45,937 | — | — |
| Assets held for sale | 14,644 | — | 16,365 |
| Trade accounts payable | (14,007) | (33,557) | (199) |
| Other taxes and social security payable | (8,641) | (70) | (144) |
| Deferred tax liabilities | — | (10,421) | — |
| Retirement benefit liability | — | (10,762) | — |
| Debt finance | (63,223) | (8,623) | (841) |
| Other liabilities | (64,156) | (6,387) | (151) |
| Net identifiable assets and liabilities acquired | 236,150 | 82,942 | 26,732 |
| Minority interest | (25,329) | (17,792) | — |
| Severstal's share of net identifiable assets and liabilities acquired | 210,821 | 65,150 | 26,732 |
| Consideration paid: | | | |
| Consideration in cash | (669,759) | (63,500) | (4,880) |
| Consideration in financial assets | (33,321) | — | (17,022) |
| Positive goodwill on acquisition of subsidiaries | (505,501) | — | — |
| Negative goodwill on acquisition of subsidiaries | 12,223 | 1,650 | 4,830 |
| Negative goodwill on minority buy-out | — | 2,563 | 2,800 |
| Net change in cash and cash equivalents | (644,094) | (57,625) | (4,223) |

***Acquisitions of minority interest***

In March 2007, the Group acquired a 2.01%, a 0.04%, and a 0.05% stake in OAO Karelsky Okatysh, OAO Olkon, and in OAO Vorkutaugol for a total consideration of US$ 35.4 million, US$ 0.1 million, and US$ 0.4 million, respectively.

In May 2007, the Group acquired an additional 9% stake in Lucchini SpA from a Lucchini family company for a total consideration of €85.2 million (US$ 114.8 million at the transaction date exchange rate). After the acquisition, the Group's share in the capital of Lucchini SpA is 79.8%.

In May 2007, the Group acquired a 25.01% stake in ZAO Severgal for a total consideration of US$ 20 million. After the acquisition, the Group's share in the capital of ZAO Severgal is 100%.

In June 2007, the Group acquired a 1.94%, a 0.62%, a 3.56%, a 1.23%, and a 1.02% stake in OAO Karelsky Okatysh, OAO Olkon, OAO Vorkutaugol, OAO Mine Vorgashorskaya, and in OAO Mine Berezovskaya for a total consideration of US$ 23.5 million, US$ 1.9 million, US$ 29.3 million, US$ 0.6 million, and US$ 0.7 million, respectively.

***Disposals of subsidiaries during 2007***

In June 2007, the Group sold its 100% (effective ownership was 79.8%) of Lucchini Sidermeccanica SpA and its wholly owned subsidiaries (Lucchini UK Ltd, Lucchini Sweden AB and Lucchini Poland Spzoo) to members of the founding Lucchini family for a total consideration of €127.8 million (US$ 172.5 million at the transaction date exchange rate). To support this transaction an independent fairness opinion of the transaction was obtained from a properly qualified Italian bank.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

In July 2007, the Group sold 100% (effective ownership was 79.8%) of Nitruvid SAS to an independent third party for a total consideration of €6.5 million (US$ 8.9 million at the transaction date exchange rate).

In October 2007, the Group sold its 100% (effective ownership was 79.8%) participation in Ascoforge Safe SAS to an independent third party for a total consideration of one Euro (US$ 1.3 at the transaction date exchange rate).

In November 2007, the Group sold its 73.1% of OAO Metallurgical Commercial Bank to a company controlled by Severstal's Majority Shareholder for a total consideration of US$ 43.0 million.

In December 2007, the Group sold 100% of OOO URALMASH-Metallurgicheskoe Oborudovanie to an independent third party for a total consideration of US$ 14.9 million.

As part of the realization of the disposal plan identified in 2003, in August, 2005 the Group sold interest in Huta LW Spzoo and its subsidiaries to Arcelor. The proceeds comprised an immediate cash payment and a deferred consideration of €61.42 million (US$ 72.95 million at December 31, 2005 exchange rate) that was received by the Group in August, 2007.

A summary of assets and liabilities disposed during 2007, 2006 and 2005 is presented below:

| | 2007 | 2006 | 2005 |
|---|---|---|---|
| Cash and cash equivalents | (235,220) | — | — |
| Trade accounts receivable | (151,658) | — | — |
| Inventories | (108,238) | (476) | — |
| Financial investments | (237,408) | — | — |
| Other assets | (30,537) | (531) | — |
| Property, plant and equipment | (158,890) | (20) | (8,898) |
| Intangible assets | (3,105) | — | — |
| Deferred tax assets | (759) | — | — |
| Assets held for sale | — | — | (217,908) |
| Trade accounts payable | 205,171 | — | — |
| Bank customer accounts | 345,753 | — | — |
| Income tax payable | 9,375 | — | — |
| Other taxes and social security payable | 13,369 | 57 | — |
| Deferred tax liabilities | 9,250 | — | 913 |
| Retirement benefit liability | 23,490 | — | — |
| Debt finance | 66,108 | — | — |
| Liabilities held for sale | — | — | 138,809 |
| Other liabilities | 30,743 | 74 | 3,190 |
| Net identifiable assets | (222,556) | (896) | (83,894) |
| Minority interest | 16,315 | 154 | 8,928 |
| Sub-total | (206,241) | (742) | (74,966) |
| Consideration in cash | 239,308 | 1,588 | 13,701 |
| Deferred consideration | — | — | 72,952 |
| Adjustment to fair value of deferred consideration | — | — | (21,446) |
| Selling costs | (1,560) | — | — |
| Net gain/(loss) on disposal | 31,507 | 846 | (9,759) |
| Deferred consideration received | 83,842 | — | — |
| Group's cash and cash equivalents in Metcombank | 149,608 | — | — |
| Net change in cash and cash equivalents | 235,978 | 1,588 | 13,701 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

## 29. Discontinued operations and assets held for sale

The Group's discontinued operations consist of OAO Metallurgical Commercial Bank (presented the Group's Financing segment) which was disposed of in November 2007, and Lucchini companies which are classified as held for sale as at December 31, 2007, December 31, 2006 and December 31, 2005. The post-tax loss on the disposal of OAO Metallurgical Commercial Bank amounted to US$ 10.2 million.

The results of discontinued operations and net cash flows were as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | **2007** | **2006** | **2005** |
| Revenue | 831 | 8,675 | 74,506 |
| Expenses | (2,914) | (3,365) | (81,537) |
| Other income/expenses | 3,821 | 30,212 | 10,011 |
| **Profit before income tax** | 1,738 | 35,522 | 2,980 |
| Income tax expense | (1,305) | (2,673) | (2,378) |
| **Profit for the year** | 433 | 32,849 | 602 |
| Net cash (used in)/generated from operating activities | (64,446) | 148,650 | (112,737) |
| Net cash (used in)/generated from financing activities | — | 17,779 | (974) |

The Group's assets held for sale balances are mostly represented by Kuzbass coal mines, a group of subsidiaries, which the Group intends to dispose of in first half of 2008, and Lucchini and Metalware segment's companies.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

The major classes of assets and liabilities of the disposal group measured at the lower of carrying amount and fair value less costs to sell at December 31, 2007, 2006 and 2005 were as follows:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| **Current assets:** | | | |
| Cash and cash equivalents | 6,199 | 5,986 | 89 |
| Short-term financial investments | 18,550 | — | — |
| Trade accounts receivable | 2,365 | 100 | 80 |
| Amounts receivable from related parties | 2,732 | — | — |
| Inventories | 9,182 | — | — |
| VAT recoverable | 1,808 | — | — |
| Income tax recoverable | 422 | 3 | 4 |
| Other current assets | 5,160 | — | — |
| **Total current assets** | 46,418 | 6,089 | 173 |
| **Non-current assets:** | | | |
| Long-term financial investments | 2,540 | 514 | — |
| Investment in associates | 1 | 1,395 | — |
| Property, plant and equipment | 332,632 | 19,375 | 14,438 |
| Intangible assets | 30,710 | 50 | — |
| Deferred tax assets | 24,913 | 11 | — |
| Other non-current assets | 23,982 | 86,082 | 51,506 |
| **Total non-current assets** | 414,778 | 107,427 | 65,944 |
| **Total assets** | 461,196 | 113,516 | 66,117 |
| **Current liabilities:** | | | |
| Trade accounts payable | 7,938 | — | — |
| Other taxes and social security payable | 3,862 | — | — |
| Other current liabilities | 6,980 | — | — |
| **Total current liabilities** | 18,780 | — | — |
| **Non-current liabilities:** | | | |
| Retirement benefit liability | 9,260 | — | — |
| Other non-current liabilities | 63,710 | 1,792 | 172 |
| **Total non-current liabilities** | 72,970 | 1,792 | 172 |
| **Total liabilities** | 91,750 | 1,792 | 172 |

## 30. Subsequent events

In January 2008, an explosion occurred on one of Severstal North America's ("SNA") furnaces, blast furnace "B". As a result of the accident SNA has stopped production at this facility. SNA is carrying out an internal investigation and estimation of losses. Blast furnace "B" is the smaller of SNA's two furnaces and is used to produce pig iron for subsequent conversion into steel. "B" furnace's daily production was 1,800 tons. SNA's primary blast furnace "C", a newly rebuilt facility, was not affected by the accident. At the date of these consolidated financial statements it is not possible to quantify any potential loss.

In January 2008, a fire occurred at blast furnace No. 5 of Severstal's steel plant in Cherepovets. A preliminary investigation showed that the fire might had been the result of dispersal and subsequent ignition of the furnace's roofing material caused by opening of the third Cowper stove in the upper part of the furnace. On February 2, 2008 blast furnace No. 5 resumed operations and restored its normal production capacity. At the date of these consolidated financial statements it is not possible to quantify any potential loss.

In January 2008, the Group acquired assets of a Polish steel-pipe producer Technologia Buczek, which was declared bankrupt, for the total consideration of PLN 54.1 million (US$ 21.8 million at the transaction date exchange rate). As a part of the above assets Severstal purchased a 100% stake in the freight company SAMKOL and a 50.72% stake in the tube manufacturing company Buczek Automotive. These assets were bought by the Group's Latvian unit, Severstallatt, which plans to develop production and distribution of steel products in Poland.

In January 2008, the supplier of electricity with whom SNA had a long-term purchase contract decided to terminate the contract and pay a lump sum penalty to compensate SNA for the differential between the contract price and the price of electricity SNA will have to pay another supplier for the duration of the original contract. This penalty payment amounted to US$ 177 million which was paid in February 2008.

In January 2008, the Group acquired a 100% stake in Baracom Limited from its Majority Shareholder for US$ 84.4 million. Baracom owns 79.9% of the voting stock of the holding structure, which controls 74.2% of SeverCorr. Accordingly, starting from January 2008 SeverCorr will be included in the Group's consolidated financial statements.

In January 2008, the Group acquired the remaining 13.7% stake in Celtic Resources Holdings Plc for US$ 44 million.

The acquirees' profit since the acquisition dates is insignificant to the Group's profit for the period.

In March 2008, the Board of Directors recommended the final dividend for 2007 of RUR 4.00 (US$ 0.17) per share and GDR.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

## 31. Segment information

Segmental information statements for the year ended December 31, 2007:

| | Mining segment | Russian Steel segment | Lucchini segment | Severstal North America | IPM | Metalware segment | Financing segment | Inter segment transactions | Consolidated |
|---|---|---|---|---|---|---|---|---|---|
| **Sales** | | | | | | | | | |
| Sales — external | 1,029,407 | 6,690,697 | 3,624,913 | 1,691,818 | 550,715 | 955,493 | — | — | 14,543,043 |
| Sales — to related parties | 1,167,458 | 1,278,328 | 131,595 | 53 | — | 56,216 | — | (1,931,782) | 701,868 |
| | 2,196,865 | 7,969,025 | 3,756,508 | 1,691,871 | 550,715 | 1,011,709 | — | (1,931,782) | 15,244,911 |
| **Cost of sales** | (1,497,487) | (4,837,325) | (3,194,377) | (1,664,065) | (379,824) | (871,799) | — | 1,903,306 | (10,541,571) |
| **Gross profit** | 699,378 | 3,131,700 | 562,131 | 27,806 | 170,891 | 139,910 | — | (28,476) | 4,703,340 |
| General and administrative expenses | (149,755) | (279,485) | (188,016) | (30,626) | (9,509) | (37,030) | — | 3,211 | (691,210) |
| Distribution expenses | (180,788) | (542,904) | (117,998) | — | (29,075) | (44,341) | — | 5,596 | (909,510) |
| Indirect taxes and contributions | (64,964) | (46,763) | (32,188) | — | (4,440) | (5,259) | — | — | (153,614) |
| Share of associates' (losses)/profits | — | (95,637) | (548) | 5,338 | — | 1,450 | — | — | (89,379) |
| Net income from securities operations | 33 | 21,164 | 10,827 | — | — | 22 | — | (6,482) | 25,564 |
| (Loss)/gain on disposal of property, plant and equipment | (12,219) | (31,799) | (508) | (3,485) | (53) | 12,283 | — | 501 | (35,280) |
| Net other operating (expenses)/income | (9,912) | 8,815 | (17,343) | 2,556 | (692) | 8,857 | — | 199 | (7,520) |
| **Profit from operations** | 281,773 | 2,165,091 | 216,357 | 1,589 | 127,122 | 75,892 | — | (25,451) | 2,842,373 |
| Impairment of property, plant and equipment | (3,058) | (5,451) | (15,895) | — | — | (4,705) | — | — | (29,109) |
| Negative goodwill, net | 11,599 | — | 507 | — | — | 117 | — | — | 12,223 |
| Net other non-operating (expenses)/income | (20,608) | (39,178) | 24,374 | — | (18) | (2,828) | — | (20,318) | (58,576) |
| **Profit before financing and taxation** | 269,706 | 2,120,462 | 225,343 | 1,589 | 127,104 | 68,476 | — | (45,769) | 2,766,911 |
| Interest income | 10,996 | 182,619 | 21,978 | 855 | 45 | 823 | — | (44,379) | 172,937 |
| Interest expense | (70,339) | (124,870) | (72,793) | (12,418) | (27,601) | (7,649) | — | 27,377 | (288,293) |
| Foreign exchange difference | (3,447) | 10,544 | (535) | — | (2,850) | (1,096) | — | 284 | 2,900 |
| **Profit before income tax** | 206,916 | 2,188,755 | 173,993 | (9,974) | 96,698 | 60,554 | — | (62,487) | 2,654,455 |
| Income tax (expense)/benefit | (45,684) | (540,509) | (64,808) | 9,247 | (20,080) | (22,312) | — | 2,877 | (681,269) |
| **Profit from continuing operations** | 161,232 | 1,648,246 | 109,185 | (727) | 76,618 | 38,242 | — | (59,610) | 1,973,186 |
| Profit/(loss) from discontinued operations | — | — | (15,660) | — | — | — | 16,093 | — | 433 |
| **Profit for the year** | 161,232 | 1,648,246 | 93,525 | (727) | 76,618 | 38,242 | 16,093 | (59,610) | 1,973,619 |
| Additional information: | | | | | | | | | |
| depreciation expense | 203,409 | 332,536 | 196,569 | 14,492 | 23,370 | 23,712 | — | — | 794,088 |
| capital expenditures | 394,047 | 494,780 | 199,267 | 483,342 | 23,335 | 29,965 | — | — | 1,624,736 |
| intersegment sales (incl. in sales to related parties) | 1,142,654 | 647,880 | 131,595 | — | — | 9,653 | — | (1,931,782) | — |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

Segmental information statements for the year ended December 31, 2006:

| | Mining segment | Russian Steel segment | Lucchini segment | Severstal North America | IPM | Metalware segment | Financing segment | Inter segment transactions | Consolidated |
|---|---|---|---|---|---|---|---|---|---|
| **Sales** | | | | | | | | | |
| Sales — external | 539,886 | 5,352,801 | 3,182,119 | 1,868,426 | — | 780,086 | — | — | 11,723,318 |
| Sales — to related parties | 951,105 | 964,694 | 175,347 | — | — | 58,837 | — | (1,424,269) | 725,714 |
| | 1,490,991 | 6,317,495 | 3,357,466 | 1,868,426 | — | 838,923 | — | (1,424,269) | 12,449,032 |
| **Cost of sales** | (965,799) | (3,804,762) | (2,807,210) | (1,711,899) | (24) | (736,568) | — | 1,425,035 | (8,601,227) |
| **Gross profit** | 525,192 | 2,512,733 | 550,256 | 156,527 | (24) | 102,355 | — | 766 | 3,847,805 |
| General and administrative expenses | (137,299) | (264,884) | (191,282) | (27,561) | (2,879) | (31,082) | — | — | (654,987) |
| Distribution expenses | (96,165) | (456,340) | (101,243) | — | — | (43,560) | — | — | (697,308) |
| Indirect taxes and contributions | (48,369) | (52,742) | (37,190) | — | (826) | (2,982) | — | — | (142,109 |
| Share of associates' (losses)/profits | — | (2,644) | 202 | 2,971 | — | (1,722) | — | — | (1,193) |
| Net income/(loss) from securities operations | 7,087 | 20,605 | 3,713 | — | (80) | 314 | — | (3,376) | 28,263 |
| (Loss)/gain on disposal of property, plant and equipment | (11,642) | (24,147) | (3,412) | 469 | (407) | (153) | — | — | (39,292) |
| Net other operating (expenses)/income | (1,079) | (12,518) | (13,141) | 1,827 | 2,440 | 5 | — | (4,643) | (27,109) |
| **Profit from operations** | 237,725 | 1,720,063 | 207,903 | 134,233 | (1,776) | 23,175 | — | (7,253) | 2,314,070 |
| Impairment of property, plant and equipment | (16,372) | (8,222) | (9,778) | — | — | (23,364) | — | — | (57,736) |
| Net gain on restructuring of tax liabilities | 14,669 | — | — | — | — | — | — | — | 14,669 |
| Negative goodwill/(goodwill impairment), net | 224 | (187) | — | — | — | 1,650 | — | 2,526 | 4,213 |
| Net other non-operating expenses | (11,408) | (40,867) | — | — | — | (1,261) | — | — | (53,536) |
| **Profit before financing and taxation** | 224,838 | 1,670,787 | 198,125 | 134,233 | (1,776) | 200 | — | (4,727) | 2,221,680 |
| Interest income | 11,090 | 99,440 | 11,589 | 4,485 | 67 | 898 | — | (25,167) | 102,402 |
| Interest expense | (48,706) | (137,554) | (58,778) | (13,747) | — | (7,306) | — | 21,114 | (244,977) |
| Foreign exchange difference | (3,197) | 37,553 | 1,638 | — | (1,445) | (1,225) | — | — | 33,324 |
| **Profit before income tax** | 184,025 | 1,670,226 | 152,574 | 124,971 | (3,154) | (7,433) | — | (8,780) | 2,112,429 |
| Income tax (expense)/benefit | (82,101) | (459,753) | (53,790) | (41,355) | 87 | 1,440 | — | 174 | (635,298) |
| **Profit from continuing operations** | 101,924 | 1,210,473 | 98,784 | 83,616 | (3,067) | (5,993) | — | (8,606) | 1,477,131 |
| Profit from discontinued operations | — | — | 22,212 | — | — | — | 6,565 | 4,072 | 32,849 |
| **Profit for the year** | 101,924 | 1,210,473 | 120,996 | 83,616 | (3,067) | (5,993) | 6,565 | (4,534) | 1,509,980 |
| Additional information: | | | | | | | | | |
| depreciation expense | 190,495 | 252,028 | 117,911 | 8,327 | 724 | 25,262 | — | — | 594,747 |
| capital expenditures | 350,863 | 554,357 | 126,687 | 82,778 | 127,413 | 10,144 | 60 | 20 | 1,252,322 |
| intersegment sales (incl. in sales to related parties) | 853,045 | 392,710 | 169,371 | — | — | 9,143 | — | (1,424,269) | — |

(Amounts expressed in thousands of US dollars, except as otherwise stated)

Segmental income statements for the year ended December 31, 2005:

| | Mining segment | Russian Steel segment | Lucchini segment | Severstal North America | IPM | Metalware segment | Financing segment | Inter segment transactions | Consolidated |
|---|---|---|---|---|---|---|---|---|---|
| **Sales** | | | | | | | | | |
| Sales — external | 420,314 | 5,174,637 | 1,805,903 | 1,822,573 | — | 562,630 | — | — | 9,786,057 |
| Sales — to related parties | 971,229 | 789,677 | 41,630 | — | — | 56,200 | — | (1,193,147) | 665,589 |
| | 1,391,543 | 5,964,314 | 1,847,533 | 1,822,573 | — | 618,830 | — | (1,193,147) | 10,451,646 |
| **Cost of sales** | (745,429) | (3,405,374) | (1,569,239) | (1,716,332) | (2,251) | (556,963) | — | 1,164,450 | (6,831,138) |
| **Gross profit** | 646,114 | 2,558,940 | 278,294 | 106,241 | (2,251) | 61,867 | — | (28,697) | 3,620,508 |
| General and administrative expenses | (105,158) | (225,159) | (125,434) | (29,539) | (2,490) | (36,882) | — | — | (524,662) |
| Distribution expenses | (55,935) | (509,943) | (63,958) | — | — | (27,848) | — | — | (657,684) |
| Indirect taxes and contributions | (41,968) | (26,380) | (23,492) | — | (59) | (3,444) | — | — | (95,343) |
| Share of associates' (losses)/ profits | — | (4,969) | 77 | 2,749 | — | (2,047) | — | — | (4,190) |
| Net income/(loss) from securities operations | 3,728 | 20,841 | 1,761 | 505 | (4) | 470 | — | (2,858) | 24,443 |
| (Loss)/gain on disposal of property, plant and equipment | (3,931) | (29,668) | (1,169) | (184) | 57 | (1,885) | — | — | (36,780) |
| Net other operating (expenses)/income | (4,966) | (3,868) | (12,868) | 1,981 | 462 | (273) | — | (812) | (20,344) |
| **Profit from operations** | 437,884 | 1,779,794 | 53,211 | 81,753 | (4,285) | (10,042) | — | (32,367) | 2,305,948 |
| Impairment of property, plant and equipment, net | (10,624) | (91,139) | (8,552) | — | (155) | (914) | — | — | (111,384) |
| Net gain on restructuring of tax liabilities | 174,178 | — | — | — | — | — | — | — | 174,178 |
| Negative goodwill, net | — | 4,830 | — | — | — | — | — | 2,800 | 7,630 |
| Net other non-operating expenses | (8,378) | (30,428) | — | — | (16) | (4,142) | — | (9,789) | (52,753) |
| **Profit before financing and taxation** | 593,060 | 1,663,057 | 44,659 | 81,753 | (4,456) | (15,098) | — | (39,356) | 2,323,619 |
| Interest income | 2,848 | 62,959 | 6,524 | 718 | 127 | 1,601 | — | (9,643) | 65,134 |
| Interest expense | (25,146) | (127,274) | (41,787) | (13,242) | (5) | (1,514) | — | 5,911 | (203,057) |
| Foreign exchange difference | (1,385) | (64,457) | 7,404 | — | (881) | 111 | — | (1,023) | (60,231) |
| **Profit before income tax** | 569,377 | 1,534,285 | 16,800 | 69,229 | (5,215) | (14,900) | — | (44,111) | 2,125,465 |
| Income tax (expense)/ benefit | (117,377) | (372,111) | 9,166 | (27,088) | 306 | (2,819) | — | 9,016 | (500,907) |
| **Profit from continuing operations** | 452,000 | 1,162,174 | 25,966 | 42,141 | (4,909) | (17,719) | — | (35,095) | 1,624,558 |
| Profit/(loss) from discontinued operations | — | — | (10,784) | — | — | — | 6,842 | 4,544 | 602 |
| **Profit for the year** | 452,000 | 1,162,174 | 15,182 | 42,141 | (4,909) | (17,719) | 6,842 | (30,551) | 1,625,160 |
| Additional information: | | | | | | | | | |
| depreciation expense | 156,048 | 233,939 | 74,659 | 7,159 | 263 | 19,550 | — | — | 491,618 |
| capital expenditures | 349,788 | 705,131 | 62,946 | 13,059 | 100,541 | 37,248 | 33 | (19,549) | 1,249,197 |
| intersegment sales (incl. in sales to related parties) | 805,523 | 338,440 | 35,961 | — | — | 13,223 | — | (1,193,147) | — |

(Amounts expressed in thousands of US dollars, except as otherwise stated)

Segmental balance sheets as at December 31, 2007:

| | Mining segment | Russian Steel segment | Lucchini segment | Severstal North America | IPM | Metalware segment | Financing segment | Inter segment balances | Consolidated |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| **Current assets:** | | | | | | | | | |
| Cash and cash equivalents | 143,372 | 846,727 | 507,714 | — | 2,195 | 46,873 | — | — | 1,546,881 |
| Short-term bank deposits | — | 665,977 | — | — | — | — | — | — | 665,977 |
| Short-term financial investments | 25,385 | 878,286 | 23,127 | — | — | 435 | — | (659,600) | 267,633 |
| Trade accounts receivable | 76,727 | 339,708 | 813,534 | 108,102 | 280,862 | 55,685 | — | — | 1,674,618 |
| Amounts receivable from related parties | 50,350 | 214,889 | 2,836 | 2,831 | 101 | 2,671 | — | (110,959) | 162,719 |
| Inventories | 157,397 | 1,162,096 | 694,939 | 457,735 | 51,477 | 102,821 | — | (88,995) | 2,537,470 |
| VAT recoverable | 65,097 | 150,191 | 32,384 | — | 5,565 | 30,508 | — | — | 283,745 |
| Income tax recoverable | 16,292 | 34,447 | 12,245 | 12,504 | — | 505 | — | — | 75,993 |
| Assets held for sale | 436,541 | 448 | 17,718 | — | — | 6,489 | — | — | 461,196 |
| Other current assets | 82,645 | 148,375 | 35,169 | 18,793 | 17,389 | 18,991 | — | — | 321,362 |
| **Total current assets** | 1,053,806 | 4,441,144 | 2,139,666 | 599,965 | 357,589 | 264,978 | — | (859,554) | 7,997,594 |
| **Non-current assets:** | | | | | | | | | |
| Long-term financial investments | 7,344 | 1,938,219 | 21,656 | — | — | 738 | — | (1,815,091) | 152,866 |
| Investment in associates and joint ventures | — | 393,635 | 1,278 | 194,179 | — | — | — | — | 589,092 |
| Property, plant and equipment | 1,347,398 | 3,360,437 | 1,495,614 | 611,378 | 307,577 | 178,562 | — | (8,155) | 7,292,811 |
| Intangible assets | 480,108 | 104,463 | 19,045 | 5,865 | 272 | 1,508 | — | — | 611,261 |
| Assets held for sale | — | — | — | — | — | — | — | — | — |
| Deferred tax assets | 11,611 | 2,770 | 37,943 | — | — | — | — | — | 52,324 |
| Amounts receivable from related parties | — | — | — | — | — | — | — | — | — |
| Other non-current assets | 1,008 | 4,225 | 2,948 | 100 | 5 | 13,188 | — | — | 21,474 |
| **Total non-current assets** | 1,847,469 | 5,803,749 | 1,578,484 | 811,522 | 307,854 | 193,996 | — | (1,823,246) | 8,719,828 |
| **Total assets** | 2,901,275 | 10,244,893 | 3,718,150 | 1,411,487 | 665,443 | 458,974 | — | (2,682,800) | 16,717,422 |
| **Liabilities and shareholders' equity** | | | | | | | | | |
| **Current liabilities:** | | | | | | | | | |
| Trade accounts payable | 57,082 | 204,713 | 610,982 | 185,830 | 7,250 | 25,027 | — | — | 1,090,884 |
| Bank customer accounts | — | — | — | — | — | — | — | — | — |
| Amounts payable to related parties | 4,219 | 90,263 | 5,766 | 18,395 | 31,884 | 14,302 | — | (105,914) | 58,915 |
| Short-term debt finance | 709,051 | 327,157 | 328,391 | 15,671 | 70,455 | 34,198 | — | (512,844) | 972,079 |
| Income taxes payable | 8,790 | 9,437 | 15,065 | — | 2,301 | 5,788 | — | — | 41,381 |
| Other taxes and social security payable | 61,915 | 41,733 | 87,071 | 1,662 | 3,333 | 4,710 | — | — | 200,424 |
| Dividends payable | — | 107,485 | — | — | — | — | — | — | 107,485 |
| Liabilities related to assets held for sale | 91,599 | — | 151 | — | — | — | — | — | 91,750 |
| Other current liabilities | 87,446 | 323,674 | 130,020 | 20,175 | 3,000 | 35,636 | — | 629 | 600,580 |
| **Total current liabilities** | 1,020,102 | 1,104,462 | 1,177,446 | 241,733 | 118,223 | 119,661 | — | (618,129) | 3,163,498 |
| **Non-current liabilities:** | | | | | | | | | |
| Long-term debt finance | 391,878 | 945,176 | 650,105 | 308,937 | 414,344 | 6,213 | — | (361,830) | 2,354,823 |
| Deferred tax liabilities | 53,849 | 189,251 | 85,194 | 60,843 | 158 | 4,386 | — | (19,045) | 374,636 |
| Retirement benefit liability | 71,821 | 118,701 | 138,504 | 48,601 | — | 9,771 | — | — | 387,398 |
| Liabilities related to assets held for sale | — | — | — | — | — | — | — | — | — |
| Other non-current liabilities | 140,135 | 1,674 | 79,471 | 5,108 | — | — | — | — | 226,388 |
| **Total non-current liabilities** | 657,683 | 1,254,802 | 953,274 | 423,489 | 414,502 | 20,370 | — | (380,875) | 3,343,245 |
| **Equity** | 1,223,490 | 7,885,629 | 1,587,430 | 746,265 | 132,718 | 318,943 | — | (1,683,796) | 10,210,679 |
| **Total equity and liabilities** | 2,901,275 | 10,244,893 | 3,718,150 | 1,411,487 | 665,443 | 458,974 | — | (2,682,800) | 16,717,422 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

Segmental balance sheets as at December 31, 2006:

| | Mining segment | Russian Steel segment | Lucchini segment | Severstal North America | IPM | Metalware segment | Financing segment | Inter segment balances | Consolidated |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| **Current assets:** | | | | | | | | | |
| Cash and cash equivalents | 87,930 | 1,231,164 | 225,854 | — | 11,799 | 9,584 | 309,674 | (174,983) | 1,701,022 |
| Short-term bank deposits | 7 | 1,292,345 | — | — | 1,019 | 41,092 | — | (187,193) | 1,147,270 |
| Short-term financial investments | 77,839 | 260,631 | 6,587 | — | 3,798 | 1,598 | 191,358 | (219,969) | 321,842 |
| Trade accounts receivable | 37,294 | 252,193 | 843,737 | 128,768 | 16 | 62,577 | — | — | 1,324,585 |
| Amounts receivable from related parties | 62,117 | 133,764 | 9,601 | 1,184 | 4 | 7,009 | — | (85,976) | 127,703 |
| Inventories | 125,019 | 895,066 | 695,041 | 427,502 | 45,732 | 102,320 | — | (68,308) | 2,222,372 |
| VAT recoverable | 46,458 | 187,872 | 49,476 | — | 25,150 | 30,436 | — | — | 339,392 |
| Income tax recoverable | 1,835 | 9,010 | 8,404 | 16,361 | — | 294 | — | — | 35,904 |
| Other current assets | 51,505 | 126,811 | 29,320 | 17,070 | 5,273 | 16,091 | 13,138 | — | 259,208 |
| **Total current assets** | 490,004 | 4,388,856 | 1,868,020 | 590,885 | 92,791 | 271,001 | 514,170 | (736,429) | 7,479,298 |
| **Non-current assets:** | | | | | | | | | |
| Long-term financial investments | 2,682 | 1,471,353 | 31,934 | — | — | 42,183 | 25,705 | (1,373,917) | 199,940 |
| Investment in associates and joint ventures | — | 139,231 | 2,656 | 212,154 | — | 865 | — | — | 354,906 |
| Property, plant and equipment | 1,289,236 | 3,048,161 | 1,519,357 | 149,721 | 292,420 | 177,808 | 475 | (6,793) | 6,470,385 |
| Intangible assets | 35,747 | 7,086 | 17,408 | — | — | 1,418 | 7 | — | 61,666 |
| Assets held for sale | — | — | 113,516 | — | — | — | — | — | 113,516 |
| Deferred tax assets | 224 | — | 29,926 | — | — | — | — | — | 30,150 |
| Amounts receivable from related parties | — | — | — | — | — | — | — | — | — |
| Other non-current assets | 1,185 | — | 2,659 | — | — | — | — | — | 3,844 |
| **Total non-current assets** | 1,329,074 | 4,665,831 | 1,717,456 | 361,875 | 292,420 | 222,274 | 26,187 | (1,380,710) | 7,234,407 |
| **Total assets** | 1,819,078 | 9,054,687 | 3,585,476 | 952,760 | 385,211 | 493,275 | 540,357 | (2,117,139) | 14,713,705 |
| **Liabilities and shareholders' equity** | | | | | | | | | |
| **Current liabilities:** | | | | | | | | | |
| Trade accounts payable | 61,275 | 209,341 | 620,668 | 116,681 | 7,113 | 23,823 | — | — | 1,038,901 |
| Bank customer accounts | — | — | — | — | — | — | 396,176 | (365,033) | 31,143 |
| Amounts payable to related parties | 19,217 | 72,894 | 36,651 | 17,303 | 15,937 | 21,460 | 74,623 | (82,345) | 175,740 |
| Short-term debt finance | 103,122 | 441,665 | 414,480 | 10,024 | 1,737 | 18,999 | 17,755 | (50,218) | 957,564 |
| Income taxes payable | 6,532 | 28,880 | 8,921 | — | — | 15 | — | — | 44,348 |
| Other taxes and social security payable | 70,016 | 38,035 | 85,952 | 2,357 | 471 | 3,127 | 5 | — | 199,963 |
| Dividends payable | — | 23,243 | — | — | — | — | — | — | 23,243 |
| Other current liabilities | 54,526 | 244,409 | 108,472 | 21,672 | 42,263 | 35,320 | 186 | — | 506,848 |
| **Total current liabilities** | 314,688 | 1,058,467 | 1,275,144 | 168,037 | 67,521 | 102,744 | 488,745 | (497,596) | 2,977,750 |
| **Non-current liabilities:** | | | | | | | | | |
| Long-term debt finance | 242,470 | 1,041,131 | 605,827 | 138,404 | 267,099 | 55,423 | 23 | (302,342) | 2,048,035 |
| Deferred tax liabilities | 59,792 | 188,886 | 89,662 | 74,805 | — | 7,308 | 1,152 | (18,529) | 403,076 |
| Retirement benefit liability | 73,056 | 133,854 | 167,855 | 43,574 | — | 24,615 | — | — | 442,954 |
| Liabilities related to assets held for sale | — | — | 1,792 | — | — | — | — | — | 1,792 |
| Other non-current liabilities | 199,693 | 218 | 81,872 | 4,307 | — | — | — | — | 286,090 |
| **Total non-current liabilities** | 575,011 | 1,364,089 | 947,008 | 261,090 | 267,099 | 87,346 | 1,175 | (320,871) | 3,181,947 |
| **Equity** | 929,379 | 6,632,131 | 1,363,324 | 523,633 | 50,591 | 303,185 | 50,437 | (1,298,672) | 8,554,008 |
| **Total equity and liabilities** | 1,819,078 | 9,054,687 | 3,585,476 | 952,760 | 385,211 | 493,275 | 540,357 | (2,117,139) | 14,713,705 |

*(Amounts expressed in thousands of US dollars, except as otherwise stated)*

Segmental balance sheets as at December 31, 2005:

| | Mining segment | Russian Steel segment | Lucchini segment | Severstal North America | IPM | Metalware segment | Financing segment | Inter segment balances | Consolidated |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| **Current assets:** | | | | | | | | | |
| Cash and cash equivalents | 67,773 | 779,419 | 384,624 | — | 5,257 | 3,921 | 143,246 | (56,353) | 1,327,887 |
| Short-term bank deposits | 1,071 | 718,705 | — | — | — | 18,274 | — | (63,538) | 674,512 |
| Short-term financial investments | 25,922 | 262,996 | 7,935 | — | 76 | 15,619 | 143,999 | (188,696) | 267,851 |
| Trade accounts receivable | 29,772 | 274,020 | 676,208 | 166,541 | — | 27,652 | — | — | 1,174,193 |
| Amounts receivable from related parties | 129,562 | 205,092 | 15,035 | 970 | — | 9,411 | — | (186,262) | 173,808 |
| Inventories | 105,672 | 578,093 | 633,068 | 401,146 | 983 | 59,457 | — | (52,891) | 1,725,528 |
| VAT recoverable | 40,698 | 296,206 | 50,540 | — | 21,056 | 33,797 | — | — | 442,297 |
| Income tax recoverable | 15,903 | 757 | 11,097 | — | — | 914 | — | — | 28,671 |
| Other current assets | 24,113 | 85,268 | 22,824 | 22,964 | 13,289 | 8,041 | 5,186 | — | 181,685 |
| **Total current assets** | 440,486 | 3,200,556 | 1,801,331 | 591,621 | 40,661 | 177,086 | 292,431 | (547,740) | 5,996,432 |
| **Non-current assets:** | | | | | | | | | |
| Long-term financial investments | 3,855 | 1,310,784 | 31,645 | — | — | 7,601 | — | (1,264,344) | 89,541 |
| Investment in associates and joint ventures | — | 63,209 | 2,335 | 142,988 | — | 2,120 | — | — | 210,652 |
| Property, plant and equipment | 1,080,768 | 2,543,161 | 1,376,460 | 75,304 | 131,750 | 111,734 | 391 | — | 5,319,568 |
| Intangible assets | 29,537 | 5,731 | 19,787 | — | — | 1,418 | 50 | — | 56,523 |
| Assets held for sale | — | — | 66,117 | — | — | — | — | — | 66,117 |
| Deferred tax assets | — | — | 35,076 | — | — | — | — | — | 35,076 |
| Amounts receivable from related parties | 22,026 | — | 13,069 | — | — | — | — | — | 35,095 |
| Other non-current assets | 523 | — | 2,582 | — | — | — | — | — | 3,105 |
| **Total non-current assets** | 1,136,709 | 3,922,885 | 1,547,071 | 218,292 | 131,750 | 122,873 | 441 | (1,264,344) | 5,815,677 |
| **Total assets** | 1,577,195 | 7,123,441 | 3,348,402 | 809,913 | 172,411 | 299,959 | 292,872 | (1,812,084) | 11,812,109 |
| **Liabilities and shareholders' equity** | | | | | | | | | |
| **Current liabilities:** | | | | | | | | | |
| Trade accounts payable | 34,916 | 176,328 | 496,110 | 129,040 | 21,650 | 7,354 | — | 1,231 | 866,629 |
| Bank customer accounts | — | — | — | — | — | — | 218,673 | (119,806) | 98,867 |
| Amounts payable to related parties | 143,820 | 390,240 | 21,504 | 14,149 | 8 | 10,610 | 33,725 | (122,099) | 491,957 |
| Short-term debt finance | 87,024 | 243,765 | 646,803 | 143,818 | 943 | 20,560 | — | (146,788) | 996,125 |
| Income taxes payable | 938 | 30,075 | 40,701 | 14,183 | — | 104 | — | — | 86,001 |
| Other taxes and social security payable | 110,296 | 23,014 | 106,584 | 1,681 | 40 | 16,063 | — | — | 257,678 |
| Dividends payable | — | 12,275 | — | — | — | — | — | — | 12,275 |
| Other current liabilities | 50,621 | 163,148 | 132,371 | 22,169 | 222 | 10,587 | 100 | — | 379,218 |
| **Total current liabilities** | 427,615 | 1,038,845 | 1,444,073 | 325,040 | 22,863 | 65,278 | 252,498 | (387,462) | 3,188,750 |
| **Non-current liabilities:** | | | | | | | | | |
| Long-term debt finance | 60,442 | 1,369,878 | 490,391 | — | 100,289 | 4,483 | — | (93,789) | 1,931,694 |
| Deferred tax liabilities | 56,822 | 155,177 | 91,107 | 59,598 | 82 | 8,462 | 466 | (14,975) | 356,739 |
| Retirement benefit liability | 64,181 | 79,034 | 135,029 | 38,888 | — | 21,354 | — | — | 338,486 |
| Liabilities related to assets held for sale | — | — | 172 | — | — | — | — | — | 172 |
| Other non-current liabilities | 201,489 | 75 | 73,059 | 6,452 | — | — | — | — | 281,075 |
| **Total non-current liabilities** | 382,934 | 1,604,164 | 789,758 | 104,938 | 100,371 | 34,299 | 466 | (108,764) | 2,908,166 |
| **Equity** | 766,646 | 4,480,432 | 1,114,571 | 379,935 | 49,177 | 200,382 | 39,908 | (1,315,858) | 5,715,193 |
| **Total equity and liabilities** | 1,577,195 | 7,123,441 | 3,348,402 | 809,913 | 172,411 | 299,959 | 292,872 | (1,812,084) | 11,812,109 |

## 32. Commitments and contingencies

### a. For litigation, tax and other liabilities

The taxation system and regulatory environment of the Russian Federation are relatively new and characterized by numerous taxes and frequently changing legislation, which is often unclear, contradictory and subject to varying interpretations between the differing regulatory authorities and jurisdictions, who are empowered to impose significant fines, penalties and interest charges. Events during the recent years suggest that the regulatory authorities within the Russian Federation are adopting a more assertive stance regarding the interpretation and enforcement of legislation. This situation creates substantial tax and regulatory risks. Management believes that it has complied in all material respects with all relevant legislation.

At the balance sheet date, the Russian tax authorities had made claims for taxes, fines and penalties in the amount of approximately US$ 32 million, mostly related to mineral extraction tax and water usage tax by certain of the Group's entities in the Mining segment. Management does not agree with the tax authorities' claims and believes that the Group has complied with existing legislation in all material respects. Management is unable to assess the ultimate outcome of the claims and the outflow of financial sources to settle such claims, if any. Management believes that it has made adequate provisions for other possible tax claims.

On July 26, 2007 Lucchini SpA received notice by the Tuscan regional fiscal authorities for storing waste from the steel making process in the Piombino steel making facilities. In the notice the authorities specified the potential amount of penalties of €52.5 million (US$ 76.9 million at December 31, 2007 exchange rate). Management has cooperated fully with the authorities and presented the mitigating submissions which should substantially reduce the initial amounts indicated by the authorities. Consequently, these financial statements contain provisions for this issue in accordance with management assessments performed.

### b. Long term purchase and sales contracts

In the normal course of business group companies enter into long term purchase contracts for raw materials, and long term sales contracts. These contracts allow for periodic adjustments in prices dependent on prevailing market conditions.

### c. Capital commitments

At the balance sheet date the Group had contractual capital commitments of US$ 411.7 million (December 31, 2006: US$ 291.1 million; December 31, 2005: US$ 435.4 million).

### d. Insurance

The Group has insured its property and equipment to compensate for expenses arising from accidents. In addition, the Group has insurance for business interruption on a basis of reimbursement of certain fixed costs. The Group has also insured third party liability in respect of property or environmental damage. However, the Group does not have a full insurance coverage.

### e. Guarantees

At the balance sheet date the Group had US$ 143.2 million (December 31, 2006: US$ 22.2 million; December 31, 2005: US$ 23.8 million) of guarantees issued.

## 33. Financial instruments

The Group's risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

The Group's Audit Committee oversees how management monitors compliance with the Group's risk management policies and procedures and reviews the adequacy of the risk management framework in relation to the risks faced by the Group.

Exposure to credit, liquidity, interest rate and currency risk arises in the normal course of the Group's business. The Russian Steel, Metalware, IPM and Mining segments of the Group have not used derivative financial instruments to reduce exposure to fluctuations in foreign exchange rates and interest rates. The use of Severstal North America and Lucchini segments of derivatives to hedge their interest rates, commodity inputs and foreign exchange rate exposures were not material to these consolidated financial statements. As at December 31, 2007, 2006 and 2005, the Financing segment had no outstanding derivatives.

Management believes that the fair value of its financial assets and liabilities approximates their carrying amounts except for the following long-term fixed rate borrowings:

| | December 31, 2007 | | |
|---|---|---|---|
| | Market value | Book value | Difference |
| Citibank CLN — Eurobonds 2009 | 330,513 | 325,000 | 5,513 |
| Citibank CLN — Eurobonds 2014 | 398,781 | 375,000 | 23,781 |
| | 729,294 | 700,000 | 29,294 |

| | December 31, 2006 | | |
|---|---|---|---|
| | Market value | Book value | Difference |
| Citibank CLN — Eurobonds 2009 | 337,857 | 325,000 | 12,857 |
| Citibank CLN — Eurobonds 2014 | 407,616 | 375,000 | 32,616 |
| | 745,473 | 700,000 | 45,473 |

| | December 31, 2005 | | |
|---|---|---|---|
| | Market value | Book value | Difference |
| Citibank CLN — Eurobonds 2009 | 336,830 | 325,000 | 11,830 |
| Citibank CLN — Eurobonds 2014 | 407,438 | 375,000 | 32,438 |
| Other bonds | 225,552 | 223,216 | 2,336 |
| | 969,820 | 923,216 | 46,604 |

The above amounts exclude accrued interest.

The market value of the Group's Eurobonds was determined based on London Stock Exchange quotations.

***Credit risk***

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet and guarantees (see note 32e). The Group has developed policies and procedures for the management of credit exposures, including the establishment of credit committees that actively monitors credit risk.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

The maximum exposure to credit risk for trade receivables including trade receivables from related parties at the reporting date was:

| | December 31, 2007 | 2006 | 2005 |
|---|---|---|---|
| Available-for-sale financial assets | 27,103 | 10,431 | 12,681 |
| Held-to-maturity securities and deposits | 745,106 | 1,203,507 | 676,500 |
| Held-for-trading securities | 146,564 | 152,716 | 78,280 |
| Loans and receivables | 2,099,792 | 1,833,516 | 1,697,950 |
| Cash and cash equivalents | 1,546,881 | 1,701,022 | 1,327,887 |
| | 4,565,446 | 4,901,192 | 3,793,298 |

The maximum exposure to credit risk for trade receivables including trade receivables from related parties at the reporting date by geographic region was:

| | December 31, 2007 | 2006 | 2005 |
|---|---|---|---|
| Russian Federation | 502,174 | 249,086 | 318,725 |
| Europe | 981,440 | 921,789 | 742,949 |
| North America | 128,198 | 162,896 | 207,926 |
| The Middle East | 38,397 | 23,241 | 21,498 |
| South-East Asia | 13,214 | 4,293 | 7,049 |
| Central and South America | 1,604 | 6,678 | 4,744 |
| China and Central Asia | 19,018 | 19,084 | 11,800 |
| Africa | 34,343 | 17,814 | 31,666 |
| | 1,718,388 | 1,404,881 | 1,346,357 |

The maximum exposure to credit risk for trade receivables including trade receivables from related parties at the reporting date by type of customer was:

| | December 31, 2007 | 2006 | 2005 |
|---|---|---|---|
| Wholesale customers | 270,298 | 284,553 | 354,950 |
| Retail customers | 88 | 4,463 | 3,312 |
| End-user customers | 1,298,692 | 954,812 | 835,824 |
| Producers | 106,512 | 137,602 | 104,957 |
| Other customers | 42,798 | 23,451 | 47,314 |
| | 1,718,388 | 1,404,881 | 1,346,357 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

***Impairment losses***

The aging of trade receivables including trade receivables from related parties at the reporting date was:

| | December 31, | | | | | |
|---|---|---|---|---|---|---|
| | 2007 | | 2006 | | 2005 | |
| | Gross | Impairment | Gross | Impairment | Gross | Impairment |
| Not past due | 1,065,731 | (2,512) | 891,505 | (2,667) | 842,773 | (698) |
| Past due 0–30 days | 502,650 | (3,061) | 365,751 | (6,957) | 289,436 | (4,213) |
| Past due 31–90 days | 125,033 | (3,245) | 132,621 | (4,736) | 135,059 | (3,664) |
| Past due 91–180 days | 27,335 | (20,348) | 21,745 | (8,053) | 61,979 | (23,652) |
| Past due 180–365 days | 11,947 | (397) | 12,513 | (605) | 12,708 | (2,207) |
| More than one year | 21,575 | (6,320) | 7,690 | (3,926) | 48,045 | (9,209) |
| | 1,754,271 | (35,883) | 1,431,825 | (26,944) | 1,390,000 | (43,643) |

The impairment allowance at December 31, 2007 includes recognized impairment allowance in respect of trade receivables from related parties for the total amount of US$ 9.2 million (2006: nil; 2005: nil).

The movement in allowance for impairment in respect of trade receivables including trade receivables from related parties during the year was as follows:

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| Balance at 1 January | (26,944) | (43,643) | (60,448) |
| Impairment loss recognised | (9,716) | (9,027) | (5,039) |
| Impairment loss reversed | — | 27,268 | 20,840 |
| Impairment loss — other movements | 777 | (1,542) | 1,004 |
| Balance at 31 December | (35,883) | (26,944) | (43,643) |

The allowance account in respect of trade receivables including trade receivables from related parties is used to record impairment losses unless the Group is satisfied that no recovery of the amount owing is possible; at that point the amount is considered irrecoverable and is written off against the financial asset directly.

No impairment allowance was recognized by the Group in respect of other financial assets.

At the balance sheet date there was a significant concentration of credit risk in respect of trade accounts receivable from related parties, originated loans to related parties and deposits in related parties.

***Trade receivables from related parties***

The Group's most significant customer, a related party ZAO TD Severstal-invest, accounts for US$ 30.1 million of trade receivables carrying amount at December 31, 2007 (US$ 55.1 million and US$ 55.3 million at December 31, 2006 and December 31, 2005 respectively).

***Originated short-term loans to related parties***

The Group's most significant related party in 2007, SeverCorr LLC, accounted for US$ 60 million of the short-term loans receivable carrying amount at December 31, 2007.

The Group's most significant related parties in 2006, OOO Impuls-Consult and ZAO TD Severstal-invest, accounted for US$ 46 million and US$ 7.8 million of the short-term loans receivable carrying amount at December 31, 2006 respectively.

The Group's most significant related parties in 2005, OOO Monolit, OAO Promstroybank and ZAO TD Severstal-invest, accounted for US$ 46.5 million, US$ 7.7 million and US$ 6 million of the short-term loans receivable carrying amount at December 31, 2005.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

***Originated long-term loans to related parties***

The Group's most significant related parties in 2007, OAO Metcombank and ZAO TD Severstal-invest, accounted for US$ 13 million and US$ 19.7 million of the long-term loans receivable carrying amount at December 31, 2007 respectively.

The Group's most significant related party in 2006, SeverCorr LLC, accounted for US$ 60 million of the long-term loans receivable carrying amount at December 31, 2006.

The Group's most significant related party in 2005, Baracom Limited, accounted for US$ 38 million of the long-term loans receivable carrying amount at December 31, 2005.

***Long-term deposits in related parties***

The Group's most significant related party in 2007, NPF Stalfond, accounted for US$ 62.4 million of the long-term deposits carrying amount at December 31, 2007 (US$ 50.1 million at December 31, 2006).

***Liquidity risk***

The Group manages liquidity risk with the objective of ensuring that funds will be available at all times to honor all cash flow obligations as they become due by preparing an annual budgets, by continuously monitoring forecast and actual cash flows and matching the maturity profiles of financial assets and liabilities.

The following are the contractual maturities of financial liabilities, excluding estimated interest payments and excluding the impact of netting agreements:

**December 31, 2007**

| | Carrying amount* | Contractual cash flows* | Less than 1 year | 1–2 years | 2–5 years | More than 5 years |
|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | |
| Debt finance | 3,286,547 | (3,286,547) | (936,440) | (683,314) | (971,420) | (695,373) |
| Finance lease liabilities | 24,536 | (24,536) | (9,926) | (8,860) | (4,042) | (1,708) |
| Trade and other payables | 1,837,796 | (1,837,796) | (1,801,639) | (36,157) | — | — |
| | 5,148,879 | (5,148,879) | (2,748,005) | (728,331) | (975,462) | (697,081) |

**December 31, 2006**

| | Carrying amount* | Contractual cash flows* | Less than 1 year | 1–2 years | 2–5 years | More than 5 years |
|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | |
| Debt finance | 2,950,851 | (2,950,851) | (902,816) | (273,713) | (1,214,881) | (559,441) |
| Finance lease liabilities | 16,321 | (16,321) | (2,579) | (3,406) | (8,602) | (1,734) |
| Trade and other payables | 1,790,478 | (1,790,478) | (1,713,478) | (55,207) | (21,793) | — |
| Bank customer accounts | 31,143 | (31,143) | (31,143) | — | — | — |
| | 4,788,793 | (4,788,793) | (2,650,016) | (332,326) | (1,245,276) | (561,175) |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

**December 31, 2005**

| | Carrying amount* | Contractual cash flows* | Less than 1 year | 1–2 years | 2–5 years | More than 5 years |
|---|---|---|---|---|---|---|
| **Non-derivative financial liabilities** | | | | | | |
| Debt finance | 2,888,099 | (2,888,099) | (956,405) | (187,681) | (1,308,644) | (435,369) |
| Finance lease liabilities | 11,462 | (11,462) | (1,964) | (2,923) | (6,575) | — |
| Trade and other payables | 2,026,193 | (2,026,193) | (1,908,111) | (85,227) | (32,855) | — |
| Bank customer accounts | 98,867 | (98,867) | (98,867) | — | — | — |
| | 5,024,621 | (5,024,621) | (2,965,347) | (275,831) | (1,348,074) | (435,369) |

* The above amounts exclude accrued interest.

### *Currency risk*

The Group incurs currency risk when an entity enters into transactions and balances not denominated in its functional currency. The Group has assets and liabilities denominated in several foreign currencies. Foreign currency risk arises when the actual or forecasted assets in a foreign currency are either greater or less than the liabilities in that currency.

The Group's exposure to foreign currency risk was as follows based on notional amounts:

| | December 31, 2007 | | | | | |
|---|---|---|---|---|---|---|
| | Euro | USD | GBP | CHF | CAD | Other |
| Available-for-sale financial assets | — | 530 | — | — | — | — |
| Held-to-maturity securities and deposits | 373,225 | 120,686 | — | — | — | — |
| Held-for-trading securities | — | 210 | — | — | — | — |
| Loans and receivables | 108,018 | 210,627 | 14,265 | 1,326 | 5,192 | 14 |
| Cash and cash equivalents | 185,692 | 348,020 | 115 | 734 | 2,045 | 2,680 |
| Debt finance | (453,993) | (1,318,029) | — | — | — | — |
| Finance lease liabilities | (1,396) | (7,080) | — | — | — | — |
| Trade and other payables | (17,879) | (97,717) | (13,001) | (4,249) | (5,829) | (346) |
| Net exposure | 193,667 | (742,753) | 1,379 | (2,189) | 1,408 | 2,348 |

| | December 31, 2006 | | | | | |
|---|---|---|---|---|---|---|
| | Euro | USD | GBP | CHF | CAD | Other |
| Available-for-sale financial assets | — | 70 | — | — | — | — |
| Held-to-maturity securities and deposits | 351,448 | 198,205 | — | — | — | — |
| Held-for-trading securities | — | — | — | — | — | — |
| Loans and receivables | 61,593 | 151,404 | 37,689 | 1,051 | 14,156 | — |
| Cash and cash equivalents | 158,841 | 432,877 | 983 | 356 | 2,815 | 2,894 |
| Debt finance | (428,811) | (1,200,729) | — | — | — | — |
| Finance lease liabilities | (685) | (3,161) | — | — | — | — |
| Trade and other payables | (28,126) | (124,671) | (17,994) | (2,937) | (1,891) | (943) |
| Net exposure | 114,260 | (546,005) | 20,678 | (1,530) | 15,080 | 1,951 |

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

| | December 31, 2005 | | | | | |
|---|---|---|---|---|---|---|
| | Euro | USD | GBP | CHF | CAD | Other |
| Available-for-sale financial assets | — | 67 | — | — | — | — |
| Held-to-maturity securities and deposits | — | 477,901 | — | — | — | — |
| Held-for-trading securities | — | — | — | — | — | — |
| Loans and receivables | 109,888 | 105,135 | 8,927 | 547 | 8,791 | — |
| Cash and cash equivalents | 181,883 | 356,228 | 429 | 231 | 5,151 | 2,589 |
| Debt finance | (164,111) | (1,279,302) | — | — | — | — |
| Finance lease liabilities | — | — | — | — | — | — |
| Trade and other payables | (223,441) | (91,234) | (1,405) | (56,052) | (1,096) | (311) |
| Net exposure | (95,781) | (431,205) | 7,951 | (55,274) | 12,846 | 2,278 |

***Sensitivity analysis***

A 10 percent strengthening of the following currencies against the functional currency at December 31, 2007 would have increased (decreased) profit or loss and equity by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant and no translation difference into the presentation currency is included. The analysis is performed on the same basis for 2006 and 2005.

| | Year ended December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| **Net profit or loss** | | | |
| Euro | 14,331 | 8,561 | 4,145 |
| USD | (56,012) | (40,785) | (34,021) |
| GBP | (22) | 1,415 | 533 |
| CHF | (166) | (116) | (4,201) |
| CAD | 94 | 1,010 | 861 |
| Other | 178 | 148 | 173 |

A 10 percent weakening of the following currencies against the functional currency at December 31, 2007 would have had the equal but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

***Interest rate risk***

Interest rates on the Group's debt finance are either fixed or variable, at a fixed spread over LIBOR or Euribor for the duration of each contract. Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favorable to the Group over the expected period until maturity.

***(Amounts expressed in thousands of US dollars, except as otherwise stated)***

At the reporting date the interest rate profile of the Group's interest-bearing financial instruments was:

| | December 31, | | |
|---|---|---|---|
| | 2007 | 2006 | 2005 |
| **Fixed rate instruments** | | | |
| Financial assets | 4,130,846 | 4,518,134 | 3,411,984 |
| Financial liabilities | (3,273,207) | (3,337,636) | (3,594,992) |
| | 857,639 | 1,180,498 | (183,008) |
| **Variable rate instruments** | | | |
| Financial assets | 434,600 | 383,058 | 381,314 |
| Financial liabilities | (1,916,027) | (1,505,905) | (1,469,349) |
| | (1,481,427) | (1,122,847) | (1,088,035) |

***Fair value sensitivity analysis for fixed rate instruments***

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit or loss, and the Group does not designate derivatives (interest rate swaps) as hedging instruments under a fair value hedge accounting model. Therefore a change in interest rates at the reporting date would not affect profit or loss.

***Cash flow sensitivity analysis for variable rate instruments***

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2006 and 2005.

| | Net profit or loss | |
|---|---|---|
| | 100 bp increase | 100 bp decrease |
| **December 31, 2007** | | |
| Variable rate instruments | | |
| Financial assets | 2,912 | (2,912) |
| Financial liabilities | (13,459) | 13,459 |
| Cash flow sensitivity (net) | (10,547) | 10,547 |
| **December 31, 2006** | | |
| Variable rate instruments | | |
| Financial assets | 2,745 | (2,745) |
| Financial liabilities | (10,545) | 10,545 |
| Cash flow sensitivity (net) | (7,800) | 7,800 |
| **December 31, 2005** | | |
| Variable rate instruments | | |
| Financial assets | 2,647 | (2,647) |
| Financial liabilities | (10,377) | 10,377 |
| Cash flow sensitivity (net) | (7,730) | 7,730 |

# Steel Capital S.A.

Directors' report and Financial Statements
For the year ended 31 December 2007 and
the eight months period ended 31 December 2006

**Steel Capital S.A.**

**Directors' report and financial statements**

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**STEEL CAPITAL S.A.**

**Directors' and other information**

| | | |
|---|---|---|
| **Directors** | Rolf Caspers | (Appointed on 11 May 2006) |
| | Vincent de Rycke | (Resigned on 23 April 2007) |
| | Tom Verheyden | (Resigned on 23 April 2007) |
| | Anja Lakoudi | (Appointed on 23 April 2007) |
| | Olivier Laurent Chirostphe Jarny | (Appointed on 23 April 2007) |
| **Registered office** | 2 Boulevard Konrad Adenauer<br>L-1115 Luxembourg | |
| **Administrator & Company Secretary** | Deutsche Bank — Luxembourg<br>2 Boulevard Konrad Adenauer<br>L-1115 Luxembourg | |
| **Statutory Auditor** | Fiduciaire Patrick Sganzeria<br>17 rue des jardiniers<br>L-1835 Luxembourg | |
| **Solicitors** | Maitre Paul Bettingen<br>71, rue de Golf<br>1-1638 SENNINGERBERG<br>L-6905 Niederanven | |

**STEEL CAPITAL S.A.**

**Directors' report**

The directors present the financial statements of STEEL CAPITAL S.A. (the "Company") prepared in accordance with International Financial Reporting Standards (IFRS) for the year and eight months period ended 31 December 2007 and 2006, respectively.

**Principal activities and business review**

The Company was incorporated on 11 May 2006, for an unlimited duration, as a public limited liability company (*societe anonyme*).

The Company has as its business purpose the issue of loan participation notes for the purpose of financing loans to Open Joint Stock Company Severstal and to its affiliated companies, the granting of security interests over its assets in relation to the issuance of the loan participation notes and the making of deposits at banks or with other depositaries.

At the date of our report, no notes have been issued.

**Future developments**

The Company will continue its activities. New activities will be undertaken, when the opportunities arise.

**Results and dividends**

The results for 2007 and 2006 are set out on page F-81. No dividends are recommended by the directors. (2006: Nil)

**Principal risks and uncertainties**

The Company is subject to various risks. The risks facing the Company are set out in note 9 to the financial statements.

**Directors, secretary and their interests**

The directors and secretary who held office on 31 December 2007 and 31 December 2006 did not hold any shares in the Company at those dates, or during the year.

**Post balance sheet events**

At the date of our report, no events occurred which should be included in these financial statements.

**Accounting records**

The books of account of the Company are maintained at 2 Boulevard Konrad Adenauer, L-1115 Luxembourg.

On behalf of the board

| | | |
|---|---|---|
| Rolf Caspers<br>**Director** | Anja Lakoudi<br>**Director** | Olivier Jarny<br>**Director** |

**STEEL CAPITAL S.A.**

**Statement of directors' responsibilities in respect of the directors report and financial statements**

The directors are responsible for preparing the directors' report and the financial statements.

In preparing each of the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping proper books of account that disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with IFRS. They are also responsible for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

On behalf of the board

| | | |
|---|---|---|
| Rolf Caspers<br>**Director** | Anja Lakoudi<br>**Director** | Olivier Jarny<br>**Director** |

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**Independent Auditors' Report**

Board of Directors

Steel Capital S.A.

**Report on the Financial Statements**

We have audited the accompanying financial statements of Steel Capital S.A. (the "Company"), which comprise the balance sheets as at 31 December 2007 and 2006, and the profit and loss accounts, statements of changes in equity and cash flow statements for the year and the eight-month period then ended, respectively, 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 financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

*Auditors' Responsibility*

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

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

*Opinion*

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2007 and 2006, and its financial performance and its cash flows for the year and the eight-month period then ended, respectively, in accordance with International Financial Reporting Standards.

ZAO KPMG

ZAO KPMG

18 June 2008

**STEEL CAPITAL S.A.**

**Profit and Loss Account**
**For the year ended 31 December and the**
**eight months period ended 31 December 2006**

| | Notes | Year ended 31-Dec-07 | Period from 11-May-06 to 31-Dec-06 |
|---|---|---|---|
| | | € | € |
| Other income | 2 | 30,671 | 29,885 |
| Other expenses | 3 | (30,671) | (29,885) |
| **Profit on ordinary activities before taxation** | | — | — |
| Tax on profit on ordinary activities | | — | — |
| **Profit for the year/period** | | — | — |

The notes on pages F-87 to F-89 form an integral part of these financial statements.

**STEEL CAPITAL S.A.**

**Balance Sheet**
**As at 31 December 2007 and 2006**

| | Notes | 31-Dec-07 | 31-Dec-06 |
|---|---|---|---|
| | | € | € |
| **Assets** | | | |
| ***Current assets:*** | | | |
| Cash and cash equivalents | 4 | 13.680 | 16.974 |
| Other debtors | 5 | 60.556 | 29.855 |
| | | 74.236 | 46.859 |
| **Total assets** | | 74.236 | 46.859 |
| **Liabilities** | | | |
| ***Creditors - amounts falling due within one year*** | | | |
| Creditors and accruals | 6 | (43.236) | (15.859) |
| | | (43.236) | (15.859) |
| **Total liabilities** | | (43.236) | (15.859) |
| **Total assets less liabilities** | | 31.000 | 31.000 |
| **Capital and reserves** | 7 | | |
| Share capital | | 31.000 | 31.000 |
| Retained earnings | | - | - |
| **Total capital and reserves** | | 31.000 | 31.000 |

On behalf of the board

Rolf Caspers
**Director**

Anja Lakoudi
**Director**

Olivier Jarny
**Director**

The notes on pages F-87 to F-89 form an integral part of these financial statements.

**STEEL CAPITAL S.A.**

**Statement of Changes in Equity**
**For the year ended 31 December 2007 and the eight months period ended 31 December 2006**

| | Share Capital | Retained Earnings | Total |
|---|---|---|---|
| **Changes in Equity for 2006** | | | |
| Issue of share capital | 31,000 | — | 31,000 |
| Profit for the period after tax | — | — | — |
| **Balance at 31 December 2006** | 31,000 | — | 31,000 |
| **Changes in Equity for 2007** | | | |
| Profit for the period after tax | — | — | — |
| **Balance at 31 December 2007** | 31,000 | — | 31,000 |

The notes on pages F-87 to F-89 form an integral part of these financial statements.

**STEEL CAPITAL S.A.**

**Cash flow statement**
**For the year ended 31 December 2007 and the eight months period ended 31 December 2006**

| | Year ended 31-Dec-07 | Period from 11-May-06 to 31-Dec-06 |
|---|---|---|
| | € | € |
| **Cash flows from operating activities** | | |
| Profit for the period | — | — |
| Adjustments for: | | |
| Change in other debtors | (30,671) | (29,885) |
| Change in creditors and accruals | 27,377 | 15,859 |
| **Net cash from operating activities** | (3,294) | (14,026) |
| **Cash flows from financing activities** | | |
| Proceeds from issue of share capital | — | 31,000 |
| **Increase/(decrease) in cash and cash equivalents** | (3,294) | 16,974 |
| Cash and cash equivalents at start of the year | 16,974 | — |
| Cash and cash equivalents at end of the year | 13,680 | 16,974 |

The notes on pages F-87 to F-89 form an integral part of these financial statements.

**Notes to the financial statements**
**For the year ended 31 December 2007 and the eight months period ended 31 December 2006**

## 1. Significant accounting policies

**Basis of preparation**

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board and under the historical cost convention.

The financial statements have been prepared on a going concern basis.

*Adoption of new and revised IFRS*

In 2007, the Company has adopted IFRS 7 Financial Instruments: Disclosures which is effective for annual reporting periods beginning on or after 1 January 2007, and the consequential amendments to IAS 1 Presentation of Financial Statements. The adoption of IFRS 7 and the changes to IAS 1 on these financial statements was not significant.

A number of Interpretations issued by the International Financial Reporting Interpretations Committee were effective for the financial years 2007 and 2006, adoption of which did not affect the Company's financial statements.

At the date of authorisation of these financial statements, a number of Interpretations were in issue but not yet effective. No material effect on the Company's financial statements is anticipated in the future from the adoption of these Standards and Interpretations.

The Company is domiciled at:
2, Boulevard Konrad Adenauer
L-1115 Luxembourg

The controlling and ultimate controlling shareholder of the Company is STICHTING STEEL CAPITAL LUXEMBOURG, a foundation incorporated under the laws of the Netherlands.

*Assets and liabilities*

Unless stated otherwise, assets and liabilities have been stated at their historical cost, expressed in EURO.

*Financial instruments*

Financial instruments comprise other debtors, cash and cash equivalents and other creditors.

*Financial assets*

Cash and cash equivalents comprise cash balances which are subject to insignificant risk of changes in value.

Other debtors are recognised initially at fair value. Subsequent to initial recognition other debtors are measured at amortised cost using the effective interest method, less any impairment losses.

*Financial liabilities*

Other creditors are initially measured at fair value. Subsequent to initial recognition other creditors are measured at amortised cost using the effective interest method, with interest expense recognised in profit and loss accounts.

Management believes that the fair value of the financial assets and liabilities approximate their carrying amounts.

*Foreign currency transaction*

Transactions in foreign currencies are translated to the functional currency of the Company at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. Non monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in Profit or Loss Account.

The Company's functional currency is EURO.

*Operating income and expenses*

All income and expenses are accounted for on an accruals basis.

*Taxation*

Taxation comprises current and deferred tax. Current tax is provided on taxable profits at the current rates applicable to the Company's activities.

Deferred tax is calculated using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting and taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which these assets can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related benefit will be realised.

| | Year ended 31-Dec-07 | Period from 11-May-06 to 31-Dec-06 |
|---|---|---|
| | € | € |
| **2. Other income** | | |
| Other income | 30,671 | 29,885 |
| **3. Other expenses** | | |
| Notary fees | — | 1,674 |
| Administration fees | 14,375 | 9,590 |
| Audit fees | 749 | 831 |
| Accountancy fees | 8,050 | 7,840 |
| Set up fees | — | 9,775 |
| Other costs | 7,497 | 175 |
| | 30,671 | 29,885 |

The Company is administered by Deutsche Bank — Luxembourg and has no employees.

| | 31-Dec-07 | 31-Dec-06 |
|---|---|---|
| | € | € |
| **4. Cash at bank** | | |
| Cash account with Deutsche Bank Luxembourg S.A. | 13,680 | 16,974 |
| **5. Other debtors** | | |
| Arrangement fee receivable | 60,556 | 29,885 |

**Notes to the financial statements (continued)**
**For the year ended 31 December 2007 and the eight months period ended 31 December 2006**

## 6. Creditors and accruals

| | 31-Dec-07 | 31-Dec-06 |
|---|---|---|
| | € | € |
| Administration fees | 21,563 | 7,188 |
| Audit fees | 1,580 | 831 |
| Accountancy fees | 15,891 | 7,840 |
| Other costs | 4,202 | — |
| | 43,236 | 15,859 |

## 7. Capital and Reserves

The subscribed share capital of the Company shall be thirty-one thousand Euro (31,000.- EUR), divided into three hundred and ten (310) shares of one hundred Euro (100.- EUR) each, all of which were issued and fully paid up as at 31 December 2007. All of the issued and paid-up shares are held by Stichting Steel Capital Luxembourg and Stitchting Participate Ditc Amsterdam.

### Legal reserve

In accordance with Luxembourg Company law, the Company is required to transfer a minimum of 5% of its net profit for each financial year to a legal reserve. This requirement ceases to be necessary once the balance on the legal reserve reaches 10% of the issued share capital. The legal reserve is not available for distribution to the shareholders.

## 8. Transactions with Administrator and related parties

During the year, the Company incurred a fee of €26,628 (2006: €27,380) relating to administration services provided by Deutsche Bank — Luxembourg.

## 9. Financial risk management

Management believes that the Company does not have significant exposure to the financial risks.

### (a) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers.

### (b) Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations from its financial liabilities.

The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

### (c) Operational risk exposure

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Company's processes, personnel and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Company's operations.

All administration functions have been outsourced by the Company.

### (d) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and equity prices will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return.

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# Severstal

Consolidated financial statements
for the year ended December 31, 2006

**Severstal**

**Consolidated financial statements**
**for the year ended December 31, 2006**

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**Independent Auditors' Report**

Board of Directors

OAO Severstal

**Report on the Consolidated Financial Statements**

We have audited the accompanying consolidated financial statements of OAO Severstal (the "Company") and its subsidiaries (the "Group"), which comprise the consolidated balance sheets as at 31 December 2006 and 2005, and the consolidated income statements, consolidated statements of changes in equity and consolidated cash flow statements for the years then ended, and a summary of significant accounting policies and other explanatory notes.

We did not audit the consolidated financial statements of Lucchini S.p.A., a 70.8% owned subsidiary since April 2005, for the year ended 31 December 2006 and for the eight-month period ended 31 December 2005, which consolidated financial statements reflect total assets constituting 19.1% and 21.8% as at 31 December 2006 and 2005, respectively, and total revenues constituting 27.0% and 17.7% for the year ended and the eight-month period ended 31 December 2006 and 2005, respectively, of the related consolidated totals. Those consolidated financial statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for Lucchini S.p.A., is based solely on the reports of the other auditors.

*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 financial statements that are free from material misstatements, 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 audits. We conducted our audits in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audits to obtain reasonable assurance whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles 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, and the reports of the other auditors, is sufficient and appropriate to provide a basis for our opinion.

*Opinion*

In our opinion, based on our audits and the reports of the other auditors, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2006 and 2005, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

KPMG Limited.

KPMG Limited

30 March 2007

**Severstal**

**Consolidated income statement**
**Year ended December 31, 2006**
***(Amounts expressed in thousands of US dollars, except shares and earnings per share)***

| | Note | Year ended December 31, 2006 | 2005 |
|---|---|---|---|
| **Sales** | | | |
| Sales — external | | 11,704,354 | 9,774,886 |
| Sales — to related parties | 15 | 718,164 | 656,880 |
| | 4 | 12,422,518 | 10,431,766 |
| Cost of sales | | (8,943,428) | (6,833,056) |
| **Gross profit** | | 3,479,090 | 3,598,710 |
| Selling, general and administrative expenses | | (650,579) | (520,164) |
| Distribution expenses | | (649,122) | (620,505) |
| Indirect taxes and contributions | | (169,451) | (117,434) |
| Share of associates' losses | | (1,193) | (4,190) |
| Net income from bank lending operations | 6 | 9,394 | 9,982 |
| Net income from securities operations | 7 | 32,927 | 27,904 |
| Loss on disposal of property, plant and equipment | | (69,989) | (36,770) |
| Net other operating expenses | | (26,954) | (17,387) |
| **Profit from operations** | | 1,954,123 | 2,320,146 |
| (Impairment)/reversal of impairment of property, plant and equipment | 19 | (57,736) | 65,159 |
| Net gain on restructuring of tax liabilities | 27 | 14,669 | 174,178 |
| Negative goodwill, net | | 4,213 | 7,630 |
| Net other non-operating expenses | 8 | (53,565) | (52,753) |
| **Profit before financing and taxation** | | 1,861,704 | 2,514,360 |
| Net financing expense | 9 | (109,076) | (198,124) |
| **Profit before income tax** | | 1,752,628 | 2,316,236 |
| Income tax expense | 10 | (543,513) | (545,668) |
| **Profit from continuing operations** | | 1,209,115 | 1,770,568 |
| Profit/(loss) from discountinued operations | | 22,212 | (10,784) |
| **Profit for the year** | | 1,231,327 | 1,759,784 |
| Attributable to: | | | |
| shareholders of OAO Severstal | | 1,180,698 | 1,695,807 |
| minority interest | | 50,629 | 63,977 |
| Weighted average number of shares outstanding during the period (millions of shares) | | 928.4 | 912.2 |
| Basic and diluted earnings per share (US dollars) | | 1.27 | 1.86 |

These consolidated financial statements were approved by the Board of Directors on March 30, 2007.

The accompanying notes form an integral part of these consolidated financial statements.

**Severstal**

**Consolidated balance sheet**
**December 31, 2006**
***(Amounts expressed in thousands of US dollars)***

| | Note | December 31, 2006 | December 31, 2005 |
|---|---|---|---|
| **Assets** | | | |
| **Current assets:** | | | |
| Cash and cash equivalents | 11 | 1,700,295 | 1,327,430 |
| Short-term bank deposits | 12 | 1,147,270 | 674,512 |
| Short-term financial investments | 13 | 321,842 | 267,851 |
| Trade accounts receivable | 14 | 1,324,097 | 1,173,673 |
| Amounts receivable from related parties | 15 | 127,513 | 173,522 |
| Inventories | 16 | 2,239,647 | 1,723,732 |
| VAT receivable | | 338,122 | 441,354 |
| Income tax receivable | | 35,856 | 28,571 |
| Other current assets | 17 | 258,404 | 181,108 |
| **Total current assets** | | 7,493,046 | 5,991,753 |
| **Non-current assets:** | | | |
| Intangible assets | 18 | 61,666 | 56,523 |
| Property, plant and equipment | 19 | 10,549,219 | 8,846,003 |
| Investment in associates | 20 | 354,906 | 210,652 |
| Long-term financial investments | 21 | 199,940 | 89,541 |
| Amounts receivable from related parties | 15 | — | 35,095 |
| Assets held for sale | | 113,516 | 66,117 |
| Deferred tax assets | 10 | 29,926 | 35,076 |
| Other non-current assets | | 3,844 | 3,105 |
| **Total non-current assets** | | 11,313,017 | 9,342,112 |
| **Total assets** | | 18,806,063 | 15,333,865 |
| **Liabilities and shareholders' equity** | | | |
| **Current liabilities:** | | | |
| Trade accounts payable | | 1,038,338 | 866,346 |
| Bank customer accounts | 22 | 31,143 | 98,867 |
| Amounts payable to related parties | 23 | 170,423 | 486,727 |
| Short-term debt finance | 24 | 954,048 | 992,612 |
| Income taxes payable | | 44,322 | 86,001 |
| Other taxes and social security payable | | 199,798 | 257,445 |
| Dividends payable | | 23,243 | 12,275 |
| Other current liabilities | 25 | 494,222 | 361,245 |
| **Total current liabilities** | | 2,955,537 | 3,161,518 |
| **Non-current liabilities:** | | | |
| Long-term debt finance | 24 | 2,048,035 | 1,931,694 |
| Deferred tax liabilities | 10 | 1,381,785 | 1,206,080 |
| Retirement benefit liability | 26 | 442,954 | 338,486 |
| Liabilities related to assets held for sale | | 1,792 | 172 |
| Other non-current liabilities | 27 | 298,101 | 298,811 |
| **Total non-current liabilities** | | 4,172,667 | 3,775,243 |
| **Equity:** | | | |
| Share capital | 28 | 3,311,288 | 3,311,254 |
| Additional capital | | 1,165,530 | 60,367 |
| Revaluation reserve | | 3,185,281 | 3,093,608 |
| Foreign exchange differences | | 786,822 | 28,073 |
| Accumulated earnings | | 2,602,345 | 1,376,103 |
| **Total equity attributable to shareholders of parent** | | 11,051,266 | 7,869,405 |
| Minority interest | | 626,593 | 527,699 |
| **Total equity** | | 11,677,859 | 8,397,104 |
| **Total equity and liabilities** | | 18,806,063 | 15,333,865 |

The accompanying notes form an integral part of these consolidated financial statements.

**Severstal**

**Consolidated statement of cash flows**
**Year ended December 31, 2006**
***(Amounts expressed in thousands of US dollars)***

| | Year ended December 31, 2006 | 2005 |
|---|---|---|
| **Operating activities:** | | |
| Profit before financing and taxation | 1,861,704 | 2,514,360 |
| Adjustments to reconcile profit to cash generated from operations: | | |
| Depreciation and amortization (notes 18 and 19) | 963,148 | 496,597 |
| Impairment/(reversal of impairment) of property, plant and equipment | 57,736 | (65,159) |
| Provisions against inventories, receivables and other provisions | (11,641) | 27,629 |
| Negative goodwill, net | (4,213) | (7,630) |
| Loss on disposal of property, plant and equipment | 69,989 | 36,770 |
| Net gain on restructuring of tax liabilities | (14,669) | (174,178) |
| (Gain)/loss on disposal of subsidiaries and associates | (846) | 9,759 |
| Gain on remeasurement and disposal of financial investments | (32,673) | (24,292) |
| Dividends from associates less share of associates' income | 1,193 | 17,413 |
| Changes in operating assets and liabilities: | | |
| Trade accounts receivable | (16,474) | 10,585 |
| Amounts receivable from related parties | 92,387 | 43,006 |
| VAT receivable | 140,315 | (222,739) |
| Inventories | (309,296) | (73,542) |
| Trade accounts payable | 57,562 | 16,323 |
| Bank customer accounts | (74,511) | (28,322) |
| Amounts payable to related parties | (101,337) | 53,386 |
| Other non-current liabilities | 10,396 | 13,114 |
| Other taxes and social security payables | (111,604) | 16,797 |
| Assets held for sale | — | (14,512) |
| Net other changes in operating assets and liabilities | 43,883 | 45,449 |
| **Cash generated from operations** | 2,621,049 | 2,690,814 |
| Interest paid (excluding banking operations) | (215,081) | (199,177) |
| Income tax paid | (676,582) | (557,303) |
| **Net cash provided from operating activities** | 1,729,386 | 1,934,334 |
| **Investing activities:** | | |
| Additions to property, plant and equipment | (1,243,831) | (1,204,415) |
| Additions to intangible assets | (8,808) | (32,322) |
| Net increase in short-term bank deposits | (431,142) | (133,526) |
| Additions to financial investments and associates | (1,203,824) | (817,558) |
| Buy out of minority interests | (70,741) | (115,432) |
| Net cash (outflow)/inflow on acquisitions of subsidiaries | (281,133) | 219,675 |
| Net cash inflow on disposal of subsidiaries | 1,588 | 13,701 |
| Proceeds from disposal of property, plant and equipment | 14,023 | 10,893 |
| Proceeds from disposal of assets held for sale | — | 10,313 |
| Proceeds from disposal of financial investments | 949,480 | 816,671 |
| Interest received (excluding banking operations) | 105,251 | 53,911 |
| **Cash used for investing activities** | (2,169,137) | (1,178,089) |
| **Financing activities:** | | |
| Proceeds from debt finance | 1,379,209 | 1,156,982 |
| Proceeds from share issues | 1,105,197 | — |
| Repayment of debt finance | (1,495,440) | (1,357,997) |
| Parent company dividends paid | (269,286) | (277,605) |
| Minority capital contributions | 6,685 | 37,734 |
| Net other cash flows from financing acitivities | — | (7,742) |
| **Cash provided from/(used for) financing activities** | 726,365 | (448,628) |
| Effect of exchange rates on cash and cash equivalents | 86,251 | (70,551) |
| **Net increase in cash and cash equivalents** | 372,865 | 237,066 |
| **Cash and cash equivalents at beginning of the year** | 1,327,430 | 1,090,364 |
| **Cash and cash equivalents at end of the year** | 1,700,295 | 1,327,430 |

The accompanying notes form an integral part of these consolidated financial statements.

**Severstal**

**Consolidated statement of changes in equity**
**Year ended December 31, 2006**
***(Amounts expressed in thousands of US dollars)***

| | Attributable to the shareholders of OAO Severstal | | | | | | Minority interest | Total |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Additional capital | Revaluation reserve | Foreign exchange differences | Accumulated earnings/ (deficit) | Total | | |
| Balances at December 31, 2004 | 3,311,248 | 60,367 | 631,996 | 191,770 | (75,938) | 4,119,443 | 122,250 | 4,241,693 |
| Profit for the period | — | — | — | — | 1,695,807 | 1,695,807 | 63,977 | 1,759,784 |
| Realization of revaluation reserve: | | | | | | | | |
| Disposals | — | — | (13,383) | — | 13,383 | — | — | — |
| Depreciation | — | — | (105,030) | — | 105,030 | — | — | — |
| Deferred tax on realization | — | — | 28,419 | — | (28,419) | — | — | — |
| Revaluation of property, plant & equipment: | | | | | | | | |
| Revaluation | — | — | 3,358,502 | (6,104) | (50,580) | 3,301,818 | 50,580 | 3,352,398 |
| Deferred tax on revaluation | — | — | (806,896) | 1,465 | 12,200 | (793,231) | (12,200) | (805,431) |
| Foreign exchange differences | — | — | — | (152,411) | — | (152,411) | (35,065) | (187,476) |
| Total recognized income and expenses | | | | | | 4,051,983 | 67,292 | 4,119,275 |
| Dividends | — | — | — | — | (271,996) | (271,996) | (3,181) | (275,177) |
| Effect of acquisitions and disposals | 6 | — | — | (6,647) | (23,384) | (30,025) | 341,338 | 311,313 |
| Balances at December 31, 2005 | 3,311,254 | 60,367 | 3,093,608 | 28,073 | 1,376,103 | 7,869,405 | 527,699 | 8,397,104 |
| Profit for the period | — | — | — | — | 1,180,698 | 1,180,698 | 50,629 | 1,231,327 |
| Realization of revaluation reserve: | | | | | | | | |
| Disposals | — | — | (40,157) | — | 40,157 | — | — | — |
| Depreciation | — | — | (443,492) | — | 443,492 | — | — | — |
| Deferred tax on realization | — | — | 114,812 | — | (114,812) | — | — | — |
| Revaluation of property, plant & equipment: | | | | | | | | |
| Revaluation | — | — | 605,959 | — | (44,966) | 560,993 | 44,966 | 605,959 |
| Deferred tax on revaluation | — | — | (145,449) | — | 10,792 | (134,657) | (10,792) | (145,449) |
| Foreign exchange differences | — | — | — | 758,749 | — | 758,749 | 52,167 | 810,916 |
| Total recognized income and expenses | | | | | | 2,365,783 | 136,970 | 2,502,753 |
| Dividends | — | — | — | — | (278,798) | (278,798) | — | (278,798) |
| Share issues (note 28) | 34 | 1,105,163 | — | — | — | 1,105,197 | — | 1,105,197 |
| Effect of acquisitions and disposals | — | — | — | — | (10,321) | (10,321) | (38,076) | (48,397) |
| Balances at December 31, 2006 | 3,311,288 | 1,165,530 | 3,185,281 | 786,822 | 2,602,345 | 11,051,266 | 626,593 | 11,677,859 |

The accompanying notes form an integral part of these consolidated financial statements.

## 1. Operations

These consolidated financial statements of OAO Severstal comprise the parent company, OAO Severstal ("Severstal" or "the Parent Company") and its subsidiaries (collectively "the Group") as listed in note 29.

Severstal began operations on August 24, 1955 and completed the development of an integrated iron and steel mill in Cherepovets during February 1959 when the first steel was rolled. On September 24, 1993, as part of the Russian privatization program, Severstal was registered as a Joint Stock Company ("OAO") and privatized. Through participating in Severstal's privatization auctions and other purchases, Alexey Mordashov (the "Majority Shareholder") has purchased shares in Severstal such that as at the balance sheet date he controlled, directly or indirectly, 82.37% (December 31, 2005: 82.75%) of Severstal's share capital.

Severstal's GDRs have been quoted on the London Stock Exchange since November 2006. Severstal's shares are quoted on the Russian Trading System and on the Moscow Interbank Currency Exchange ("MICEX"). Severstal's registered office is located at Ul Mira 30, Cherepovets, Russia.

The Group comprises the following segments:

- *Russian Steel* — this segment operates full cycle integrated iron and steel mill and large diameter pipe plant in Russia, has supporting companies for the sale of products in the Russian and international markets and also includes service companies.
- *Severstal North America* — this segment operates full cycle integrated iron and steel mill in the USA and has non-controlling equity interests in the US based steel galvanizing, steel slitting and coking coal production entities.
- *Lucchini* — this segment produces special and high quality steels and quality and specialty long products. Production sites are located in Western Europe, primarily in Italy and France. This segment also includes its distribution network companies, which are located primarily in Western Europe.
- *Metalware segment* — this segment comprises three plants in Russia, two plants in Ukraine and one plant in the United Kingdom containing wire drawing equipment that takes long products (mainly wire) from the Russian Steel and Lucchini segments and external suppliers and turns them into products with a higher value added for the Russian and international markets.
- *Mining segment* —this segment comprises two locations in Russia, where coking coal is produced, one location where iron ore is produced, and one location where pellets are produced. This segment also includes coal refining facilities and other auxiliary businesses.
- *Financing segment* — this segment operates a retail bank.

A segmental analysis of the consolidated balance sheet and income statement is given in note 31.

***Recent acquisitions of controlling stakes from the Group's Majority Shareholder***

During May and June 2006, the Group acquired controlling stakes in entities of the mining segment and in service companies of the Russian Steel segment from the Group's Majority Shareholder. On October 2, 2006, the Group completed the acquisition from the Group's Majority Shareholder of 50.82% in Lucchini SpA, which, together with its subsidiaries, comprises the Lucchini segment of the Group. These transactions are further discussed in notes 28 and 29 to these consolidated financial statements.

***Additional share issues during 2006***

During 2006 the Group made two additional share issues. The first share issue was completed in June 2006 to finance acquisition of controlling stakes in entities of the mining segment from the Group's Majority Shareholder. The second share issue was completed in December 2006 as part of the initial public offering of the Parent Company's GDRs on the London Stock Exchange. Additional information on those share issues is disclosed in notes 28 and 29 to these consolidated financial statements.

***Economic environment***

A large part of the Group is based in the Russian Federation and is consequently exposed to the economic and political effects of the policies adopted by the Russian government. These conditions and future policy changes could affect the operations of the Group and the realization and settlement of its assets and liabilities.

International sales of rolled steel from the Group's Russian operations have been the subject of several anti-dumping investigations. The Group has taken steps to address the concerns of such investigations and participates actively in their resolution. A brief description of protective measures effective at Severstal's key export markets is given below:

- Exports of hot-rolled coils and thin sheets from Russia to the USA are restricted by the minimum prices issued quarterly by the US Department of Commerce and quotas. Severstal is the first Russian company, for which since September 2005 minimum prices for certain types of steel plate were established based on the producer's actual cost and finance data.
- The Canadian market of hot-rolled plate is restricted by minimum prices.
- The European Union ("EU") market is protected by quotas. During the last few years quotas have been raised about 2–2.5% each year after adjusting for the effects of EU enlargements. Severstal traditionally gets approximately 35% of the total Russian quota and strives to utilize it fully because the EU market is a key market for Severstal.
- The Chinese market is open to the Russian exporters. No antidumping or safeguard measures are in force.

## 2. Presentation of the consolidated financial statements

***Statement of compliance***

These consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board, and are prepared under the historic cost convention except that property, plant and equipment; investments designated at fair value through profit and loss; and investments available-for-sale are stated at fair value. The Group's statutory financial records are maintained in accordance with the legislative requirements of the countries in which the individual entities are located, which differ in certain respects from IFRS. The accounting policies applied in the preparation of these consolidated financial statements are set out in note 3.

***Going concern basis***

These consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the normal course of business.

***Use of estimates***

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the amounts reported therein. Due to the inherent uncertainty involved in making such estimates, actual results could differ from those estimates.

In particular, information about 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 carrying amounts of assets and liabilities within the next financial year is described in the following notes:

- Note 26 — Retirement benefit liabilities
- Note 27 — Other non-current liabilities

***Functional and presentation currency***

The presentation currency of these consolidated financial statements is the US dollar.

The functional currency is determined separately for each of the Group's entities. For all Russian entities, the majority of costs and revenues are denominated in Russian roubles, and accordingly, their functional currency is the Russian rouble. The functional currency of the Group's entities located in North America is the US dollar. The functional currency of the majority of the Group's entities located in Western Europe is the Euro.

Any conversion of amounts in roubles into US dollars should not be construed as a representation that such amounts have been, could be, or will be in the future, convertible into US dollars at the exchange rates used, or at any other exchange rate.

***Basis of consolidation***

Subsidiaries are those enterprises controlled, directly or indirectly, by the Parent Company. The financial statements of subsidiaries are included in these consolidated financial statements from the date that control effectively commences until the date that control effectively ceases. The minority interest represents the minorities' proportion of the net identifiable assets of the subsidiaries, including minorities' share of fair value adjustments on acquisitions.

Associates are those enterprises in which the Group has significant influence, but does not have control over the financial and operating policies. These consolidated financial statements include the Group's share of the total recognized gains and losses of associates accounted for on an equity accounting basis, from the date that significant influence effectively commences until the date that significant influence effectively ceases. When the Group's share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

Intra-group balances and transactions, and any unrealized gains arising from intra-group transactions, are eliminated in preparing these consolidated financial statements.

***Accounting for business combinations of entities under common control***

IFRS provides no guidance on accounting for business combinations of entities under common control. Management adopted the accounting policy for such transactions based on the relevant guidance of accounting principles generally accepted in the United States ("US GAAP"). Management believes that this approach and the accounting policy disclosed below are in compliance with IFRS.

Acquisitions of controlling interests in companies that were previously under the control of the same controlling shareholder as the Group have been accounted for as if the acquisition had occurred at the beginning of the earliest comparative period presented or, if later, at the date on which control was obtained by the common controlling shareholder. The assets and liabilities acquired have been recognized at their book values. The components of equity of the acquired companies have been added to the same components within Group equity except that any share capital of the acquired companies has been recorded as part of additional paid in capital. Cash consideration for such acquisitions has been recognized as a liability to or a reduction of receivables from related parties, with a corresponding reduction in equity, from the date the acquired company is included in these consolidated financial statements until the cash consideration is paid. Parent Company shares issued in consideration for the acquired companies are recognized from the moment the acquired companies are included in these financial statements.

Acquisitions by the Majority Shareholder of additional interests in the acquired companies, after control over those companies has been obtained by the Majority Shareholder, are treated as if those additional interests were acquired by the Group. No goodwill is recognized on these transactions. The difference between the share of net assets acquired and the cost of investment is recognized directly in equity.

As part of acquiring the mining assets, during 2006 the Group acquired fixed assets that were leased during 2004 and 2005 by the companies controlled by the Majority Shareholder to the acquired mining companies. These fixed assets are included in these consolidated financial statements from the moment that they were acquired by the companies controlled by the Majority Shareholder. A liability to related parties for purchasing these fixed assets is recorded in these consolidated financial statements from the moment the acquired fixed assets were included in the consolidated financial statements.

## 3. Summary of the principal accounting policies

The following significant accounting policies have been consistently applied in the preparation of these consolidated financial statements.

### a. Cash and cash equivalents

Cash equivalents are all highly liquid temporary cash investments with original maturity dates of three months or less.

### b. Inventories

Inventories are stated at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The cost of inventories is based on the weighted average principle and includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of manufactured inventories and work in progress, cost includes an appropriate share of production overheads. Provisions are recorded against slow moving and obsolete inventories.

### c. Trade and other receivables

Trade and other receivables are stated at their cost less impairment losses.

### d. Foreign currency

***Foreign currency transactions***

Transactions in foreign currencies are translated to the functional currency of each entity at the foreign exchange rate ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated to the functional currency of each entity at the foreign exchange rate ruling at that date. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated to the functional currency of the entity at the foreign exchange rate ruling at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to functional currency of the entity at the foreign exchange rate ruling at the dates the fair values were determined. Foreign exchange gains and losses arising on translation are recognized as a part of net financing expense in the income statement.

***Presentation and consolidation***

For presentation and consolidation purposes all assets and liabilities at the balance sheet date are translated into US dollars at the foreign exchange rate ruling on that date. Revenues and expenses are translated into US dollars using rates approximating the foreign exchange rates ruling on the dates of the transactions. Components of equity are translated into US dollars using rates approximating historic exchange rates ruling on the dates of the transactions. Foreign exchange gains and losses arising on translation into the presentation currency are recognized directly in the statement of changes in equity.

### e. Investments

Investments are recognized (derecognized) when the Group obtains (loses) control over the contractual rights inherent in that asset. Investments are accounted for as follows:

- Investments designated at fair value through profit and loss, including investments held for trading, are stated at fair value, with any resultant gain or loss recognized in the income statement.
- Investments held-to-maturity are stated initially at cost. Subsequent to initial recognition they are stated at amortized cost with any difference between cost and redemption value being recognized in the income statement over the period to maturity on an effective interest basis.
- Loans and receivables are stated initially at cost, subject to impairment test, which is done using discounted cash flow techniques. Subsequent to initial recognition they are stated at amortized cost with any difference between cost and redemption value being recognized in the income statement over the period to maturity on an effective interest basis.
- Other investments are classified as available-for-sale and are stated at fair value. A gain or loss on an available-for-sale financial asset is recognized directly in equity, except for impairment losses and foreign exchange gains and losses, until the financial asset is derecognized, at which time the cumulative gain or loss previously recognized in equity is recognized in the income statement. Interest, which is calculated using the effective interest method, is recognized in the income statement. Dividends on an available-for-sale equity instrument are recognized in the income statement.

The fair value of investments is their quoted bid price at the balance sheet date. If a quoted market price at the balance sheet date is not available, the fair value of the instrument is estimated using prices of transactions close to the balance sheet date or, if such prices are also not available, discounted cash flow techniques. Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the balance sheet date. Investments in equity securities that are not quoted on a stock exchange, and where fair value cannot be reliably measured by discounted cash flow techniques and other means, are stated at cost less impairment losses.

Additions to financial investments and proceeds from disposals of financial investments are shown separately in the cash flow statement, except for cash inflows and outflows on loans to bank customers, which are shown on a net basis and included, depending on the sign of net change, either in additions to financial investments or in proceeds from disposals of financial investments.

### f. Property, plant and equipment

Property, plant and equipment is periodically revalued to be stated at fair market value. In the case of assets constructed by the Group, related works and direct project overheads are included in cost. Repair and maintenance expenses are charged to the income statement as incurred. Gains or losses on disposals of property, plant and equipment are recognized in the income statement.

Depreciation is provided so as to write off property, plant and equipment over its expected useful life. Depreciation is calculated using the straight line basis, except for depreciation on vehicles and certain metal-rolling equipment, which is calculated on the basis of mileage and units of production, respectively. The estimated useful lives of assets are reviewed regularly and revised when necessary.

The principal periods over which assets are depreciated are as follows:

| | |
|---|---|
| Buildings and constructions | 20–50 years |
| Plant and machinery | 10–20 years |
| Other productive assets | 5–20 years |
| Community and infrastructure assets | 5–50 years |

With effect from October 1, 2006 management commissioned an independent appraiser to assess for the purpose of financial reporting the value of its productive property, plant and equipment at Group's iron ore and pellets production entities and at Russian metalware production facilities.

With effect from December 31, 2005 management commissioned an independent appraiser to assess for the purpose of financial reporting the value of its productive property, plant and equipment at key entities of the Russian Steel segment, Severstal North America segment and coal production entities of the Mining segment.

Property, plant and equipment of entities of Lucchini segment was evaluated by an independent appraiser for the purpose of financial reporting on April 30, 2005.

As at the dates of the valuations, accumulated depreciation was offset against cost, and cost was restated to fair market value. Depreciation charge for the subsequent periods is based on estimated remaining useful lives of assets.

A revaluation increase on an item of property, plant and equipment is recognized directly in equity, net of deferred tax, except to the extent that it reverses a previous revaluation decrease recognized in the income statement, in which case it is recognized in the income statement. A revaluation decrease on an item of property, plant and equipment is recognized in the income statement except to the extent that it reverses a previous revaluation increase recognized directly in equity, in which case it is recognized directly in equity.

As the revaluation reserve is realized through depreciation and disposal of the corresponding items of property, plant and equipment the relevant portion of the revaluation reserve, net of deferred tax, is transferred directly into retained earnings.

### g. Goodwill and negative goodwill

***Goodwill***

Goodwill arising on acquisition represents the excess of the cost of the acquisition over the fair value of the net identifiable assets acquired. Goodwill is stated at cost less impairment losses. In respect of associates, the carrying amount of goodwill is included in the carrying amount of the investment in the associate.

***Negative goodwill***

Negative goodwill arising on an acquisition represents the excess of the fair value of the net identifiable assets acquired over the cost of acquisition. All negative goodwill is recognized in the income statement as it arises.

### h. Asset impairment

The carrying amount of goodwill is tested for impairment annually. The carrying amounts of the Group's other assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognized whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses in respect of revalued property, plant and equipment are recognized in the same way as revaluations; other impairment losses are recognised in the income statement.

***Calculation of recoverable amount***

The recoverable amount of the Group's held-to-maturity investments and loans and receivables, is calculated as the present value of expected future cash flows, discounted at the effective interest rate inherent in the asset. For other assets the recoverable amount is the greater of the net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

***Reversals of impairment***

An impairment loss in respect of a held-to-maturity investment, loan or receivable is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognized. An impairment loss in respect of goodwill is not reversed. In respect of other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognized.

### i. Dividends payable

Dividends are recognized as a liability in the period in which they are authorized by the shareholders.

### j. Indirect taxes and contributions

Indirect taxes and contributions are taxes and mandatory contributions paid to the government, or government controlled agencies, that are calculated on a variety of bases, but exclude taxes calculated on profits, value added taxes calculated on revenues and purchases and social security costs calculated on wages and salaries. Social security costs are included in cost of sales, distribution expenses and selling, general and administrative expenses in accordance with the nature of related wages and salaries expenses.

### k. Income tax

Income tax on the profit for the year comprises current and deferred tax. Income tax is recognized in the income statement except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax expense is calculated by each entity on the pretax income determined in accordance with the tax law of a country, in which the entity is incorporated, using tax rates enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is calculated using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting and taxation purposes. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date. Deferred tax assets are recognized only to the extent that it is probable that future taxable profits will be available against which these assets can be utilized. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Deferred tax is not recognized in respect of the following:

- investments in subsidiaries where the Group is able to control the timing of the reversal of the temporary differences and it is probable that the temporary difference will not reverse in the foreseeable future;
- if it arises from the initial recognition of an asset or liability that affect neither accounting nor taxable profit,
- initial recognition of goodwill.

### l. Debt finance

Debt finance is stated at amortized cost, net of any transaction costs incurred, and includes accrued interest at the balance sheet date. The difference between cost and redemption value is recognized in the income statement over the period of the borrowings on an effective interest basis. Borrowing costs on loans specifically for the purchase or construction of a qualifying asset are capitalized as part of the cost of the asset they are financing.

**m. Income recognition**

***Sales***

Revenue from the sale of goods is recognized in the income statement when the significant risks and rewards of ownership have been transferred to the buyer, the amount of revenue can be measured reliably, it is probable that the economic benefits associated with the transaction will flow to the entity, and the costs incurred or to be incurred in respect of the transaction can be measured reliably. Sales include all amounts billed to customers and are stated net of taxes.

***Banking income***

Interest income is recognized in the income statement as it accrues. Fees relating to the ongoing provision of services to customers are recognized as income in proportion to the service provided in the year.

**n. Net financing expense**

Net financing expense comprises interest on debt finance, amortization of transaction costs, amortization of discount on discounted assets and liabilities, interest income and foreign exchange gains and losses.

Interest is recognized in the income statement as it accrues, taking into account the effective yield on the asset or liability.

All interest costs incurred in connection with borrowings, which are not directly attributable to the acquisition, construction or production of qualifying assets, are expensed as incurred as part of net financing expense.

**o. Net income from securities operations**

Net income from securities operations comprises dividend income (except for dividends from equity associates), realized and unrealized gains on financial assets at fair value through profit or loss, realized gains and impairment losses on available for sale and held to maturity investments.

**p. Earnings per share**

Earnings per share is calculated by dividing the net profit by the weighted average number of shares outstanding during the year, assuming that shares issued in consideration for the companies acquired from the Majority Shareholder were issued from the moment these companies are included in these consolidated financial statements.

**q. Provisions**

***Retirement benefits***

The Group pays retirement and post-employment medical benefits to former employees. The calculation of the Group's net obligation in respect of defined retirement benefit plans is performed annually by management using the projected unit credit method. In accordance with this method, the Group's net obligation is calculated separately for each defined benefit plan by estimating the amount of future benefit that employees have earned in return for their service in the current and prior periods; that benefit is discounted to its present value and the fair value of any plan assets is deducted. The discount rate used is the yield at the balance sheet date on government bonds that have maturity dates approximating the terms of the Group's obligations. Any actuarial gain or loss arising from the calculation of the retirement benefit obligation is fully recognized in the current year's income statement.

***Decommissioning liability***

The Group has environmental liabilities related to restoration of soil and other related works, which are due upon the closures of certain of its production sites. The Group generally estimates provisions related to environmental issues on a case-by-case basis, taking into account applicable legal requirements. A best estimate, based on available information, is calculated, provided that the available information indicates that the loss is probable. Decommissioning liabilities are estimated using existing technology, at current prices, and discounted using a real discount rate.

***Other provisions***

Other provisions are recognized in the balance sheet when the Group has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

**r. New Standards and Interpretations adopted**

Certain new Standards, amendments to Standards and Interpretations are effective for periods beginning on or after January 1, 2006 and accordingly they were adopted in preparing these consolidated financial statements. None of these pronouncements had significant impact on the Group's financial position and results of operations.

**s. New Standards and Interpretations not yet adopted**

A number of new Standards, amendments to Standards and Interpretations were not yet effective as at December 31, 2006, and have not been applied in preparing these consolidated financial statements. The Group plans to adopt these pronouncements when they become effective. Of these pronouncements, potentially the following will have an impact on the Group's financial statements.

- IFRS 7 Financial Instruments: Disclosures, which is effective for annual periods beginning on or after 1 January 2007. The Standard will require increased disclosure in respect of the Group's financial instruments.
- Amendment to IAS 1 *Presentation of Financial Statements — Capital Disclosures*, which is effective for annual periods beginning on or after 1 January 2007. The Standard will require increased disclosure in respect of the Parent Company's capital.

***(Tabular amounts expressed in thousands of US dollars)***

## 4. Sales

Sales by product were as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Hot rolled strip | 3,398,255 | 3,279,885 |
| Hot rolled sections and wire rod | 2,265,907 | 1,409,887 |
| Cold rolled sheet | 1,341,195 | 1,468,927 |
| Galvanized and other metallic coated sheet | 1,107,989 | 1,041,711 |
| Rails, wheels and axles | 375,271 | 149,121 |
| Steel castings, forgings and tool steels | 236,955 | 155,047 |
| Cold transformed products | 155,285 | 81,518 |
| Semi finished products | 702,632 | 689,963 |
| Further processed products | 513,314 | 277,905 |
| Wire and wire products | 676,294 | 445,395 |
| Pellets and iron ore | 254,197 | 388,170 |
| Coal and coke | 249,883 | 142,819 |
| Chemical and other by-products | 299,711 | 167,431 |
| Repair services | 18,118 | 21,337 |
| Manufactured equipment | 39,919 | 23,381 |
| Shipping and handling costs billed to customers | 516,958 | 452,066 |
| Other | 270,635 | 237,203 |
| | 12,422,518 | 10,431,766 |

Sales by delivery destination were as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Russian Federation | 4,903,616 | 3,744,332 |
| North America | 2,403,863 | 2,196,762 |
| Europe | 4,389,199 | 2,774,994 |
| China and Central Asia | 109,739 | 566,529 |
| The Middle East | 211,389 | 353,001 |
| South-East Asia | 142,486 | 410,472 |
| Central America | 101,265 | 172,689 |
| Africa | 81,361 | 148,570 |
| South America | 79,600 | 64,417 |
| | 12,422,518 | 10,431,766 |

## 5. Staff costs

Employment costs were as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Wages and salaries | (1,261,759) | (965,984) |
| Social security costs | (301,194) | (247,777) |
| Retirement benefit costs (see note 26) | (2,385) | (3,806) |
| Actuarial losses recognized (see note 26) | (1,565,338) | (1,217,567) |
| Staff costs | (67,658) | (62,380) |
| | (1,632,996) | (1,279,947) |

***(Tabular amounts expressed in thousands of US dollars)***

Key management received the following remuneration during the year, which is included in the above staff costs:

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Wages and salaries | (4,118) | (3,040) |
| Social security costs | (108) | (136) |
| Other benefits | (146) | (114) |
| | (4,400) | (3,262) |

In addition, the Parent Company was charged US$ 40.1 million excluding VAT (2005: US$ 35.7 million) of management fees by ZAO Severstal Group, a related party. A significant portion of those fees was paid to executive officers of Severstal (who were employed by ZAO Severstal Group) as compensation.

## 6. Net income from bank lending operations

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Interest income: | | |
| Placements with other financial institutions | 5,154 | 3,759 |
| Loans to bank customers: | | |
| — external | 7,127 | 5,664 |
| — related parties | 1,889 | 1,304 |
| Interest expense: | | |
| — external | (1,180) | (593) |
| — related parties | (3,122) | (622) |
| Loan loss provisions | (474) | 470 |
| | 9,394 | 9,982 |

## 7. Net income from securities operations

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Held-for-trading securities | | |
| Profit on disposal | 4,471 | 2,167 |
| Restatement to fair value | (129) | 1,458 |
| Held to maturity securities and loans | 13,909 | 4,114 |
| Available-for-sale securities | | |
| Profit on disposal | 7,239 | 29,629 |
| Restatement to fair value | 7,183 | (13,076) |
| Dividends received | 254 | 3,612 |
| | 32,927 | 27,904 |

***(Tabular amounts expressed in thousands of US dollars)***

### 8. Net other non-operating expenses

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Social expenditure | (33,857) | (28,408) |
| Charitable donations | (17,060) | (13,283) |
| Depreciation of community and infrastructure assets | (3,494) | (1,303) |
| Gain/(loss) on disposal of subsidiaries and associates | 846 | (9,759) |
| | (53,565) | (52,753) |

### 9. Net financing expense

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Interest income: | | |
| Third parties | 70,881 | 52,150 |
| Related parties | 31,605 | 12,977 |
| Interest expense: | | |
| Third parties | (236,950) | (195,487) |
| Related parties | (3,061) | (2,961) |
| Amortization of transaction costs | (4,869) | (4,577) |
| Foreign exchange gains/(losses) | 33,318 | (60,226) |
| | (109,076) | (198,124) |

### 10. Taxation

The following is an analysis of the income tax expense:

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Current tax charge | (609,881) | (588,417) |
| Corrections to prior year's current tax charge | (13,762) | (7,756) |
| Deferred tax benefit | 80,130 | 50,505 |
| Income tax expense | (543,513) | (545,668) |

The following is a reconciliation of the reported net income tax expense and the amount calculated by applying the Russian statutory tax rate of 24.0% to reported profit before income tax.

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Profit before income tax | 1,752,628 | 2,316,236 |
| Tax charge at Russian statutory rate — 24% | (420,631) | (555,897) |
| Profits taxed at different rates | (36,247) | 12,786 |
| Corrections to prior year's current tax charge | (13,762) | (7,756) |
| Net gain on tax restructuring | 3,521 | 41,803 |
| Non-tax deductible expenses, net | (70,877) | (53,567) |
| Tax-loss carry forwards expired | (17,462) | (67,629) |
| Changes in non-recognized deferred tax assets | 32,375 | 73,839 |
| Reassessment of deferred tax liabilities | (20,430) | 10,753 |
| Income tax expense | (543,513) | (545,668) |

***(Tabular amounts expressed in thousands of US dollars)***

Income tax charge for the year ended December 31, 2006 includes tax expense of US$ 0.4 million (2005: nil) related to profits/(losses) of discontinued operations and gains/(losses) on disposals of discontinued operations.

The composition of, and movements in, the net deferred tax liability based on the temporary differences arising between the fiscal and reporting balance sheets of the consolidated companies, is given below:

| | December 31, | |
|---|---|---|
| | **2006** | **2005** |
| Deferred tax assets: | | |
| Tax-loss carry forwards | 48,610 | 67,123 |
| Property, plant and equipment | 18,205 | 24,477 |
| Provisions | 15,707 | 11,320 |
| Financial investments | 2,770 | 14,530 |
| Other | 9,884 | 30,750 |
| Less: non-recognized deferred tax assets | (65,250) | (113,124) |
| Net deferred tax assets recognized | 29,926 | 35,076 |
| Deferred tax liabilities: | | |
| Property, plant and equipment | (1,432,740) | (1,240,169) |
| Provisions | 68,511 | 52,153 |
| Other | (17,556) | (18,064) |
| Deferred tax liabilities recognized | (1,381,785) | (1,206,080) |
| Net deferred tax liability | (1,351,859) | (1,171,004) |

The movement in the net deferred tax liability is as follows:

| | Year ended December 31, | |
|---|---|---|
| | **2006** | **2005** |
| Opening balance | (1,171,004) | (339,616) |
| Recognized in income statement | 80,130 | 50,505 |
| Recognized in shareholders' equity | (145,449) | (805,431) |
| Business combinations | (10,421) | (95,447) |
| Business de-combinations | — | 913 |
| Foreign exchange difference | (105,115) | 18,072 |
| Closing balance | (1,351,859) | (1,171,004) |

As at December 31, 2006 the Group had cumulative tax-loss carry forwards of US$ 149.1 million that expire as follows: in 2007: US$ 59.7 million; in 2008: US$ 40.6 million; in 2011: US$ 10.3 million and US$ 38.5 million have no expiry date.

Temporary differences, related to investments in subsidiaries where the Group is able to control the timing of the reversal and it is probable that the temporary difference will not reverse in the foreseeable future, amounted to US$ 1,088.5 million at December 31, 2006 (December 31, 2005: US$ 733.9 million).

*(Tabular amounts expressed in thousands of US dollars)*

## 11. Cash and cash equivalents

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Petty cash | 254 | 429 |
| Cash at bank | 427,217 | 389,350 |
| Escrow accounts | 6,994 | 18,918 |
| Short term deposits with maturity of less than 3 months | 893,829 | 687,166 |
| Investments in quoted monetary instruments | 62,327 | 88,320 |
| Cash balances of consolidated bank: | | |
| Cash | 1,171 | 823 |
| Nostro accounts at the Central Bank of Russia | 110,036 | 39,781 |
| Nostro accounts at other banks | 6,637 | 16,997 |
| Placements with banks | 191,830 | 85,646 |
| | 1,700,295 | 1,327,430 |

As described in note 29 to these consolidated financial statements, the Group has a subsidiary OAO Metallurgical commercial bank ("Metcombank"). Nostro accounts of Metcombank at the Central Bank of Russia and at other banks and interbank loans given by Metkombank with an original maturity of three months or less are included in cash and equivalents.

## 12. Short-term bank deposits

Short-term bank deposits totaled US$ 1,147.3 million at December 31, 2006 (December 31, 2005: US$ 674.5 million) and comprised of deposits with an original maturity of more than three months but remaining period to maturity of less than one year. The majority of such deposits has an original maturity of less than 6 months, and such deposits are used by the Group to earn investment income, while preserving a high liquidity position. Substantially all such deposits can be withdrawn, in case of necessity, prior to the maturity date with no loss in principal but reduced interest income.

## 13. Short-term financial investments

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| **Held-for-trading securities:** | | |
| Promissory notes and bonds of third parties | 128,375 | 72,429 |
| Promissory notes of related parties | 5,198 | 4,772 |
| Quoted equity securities | 19,143 | 1,079 |
| **Loans:** | | |
| Loans to related parties | 75,699 | 81,133 |
| Loans to third parties | 11,912 | 24,408 |
| Loans to bank customers: | | |
| Third parties | 54,991 | 71,232 |
| Related parties | 29,166 | 15,739 |
| Loan loss provisions | (2,758) | (3,008) |
| **Available-for-sale securities** | 116 | 67 |
| | 321,842 | 267,851 |

Loans given to related parties were provided at interest rates ranging from nil to 15% per annum, and were given to finance working capital and investments.

***(Tabular amounts expressed in thousands of US dollars)***

## 14. Trade accounts receivable

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Customers | 1,351,041 | 1,217,316 |
| Allowance for doubtful accounts | (26,944) | (43,643) |
| | 1,324,097 | 1,173,673 |

## 15. Amounts receivable from related parties

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Trade accounts receivable | 80,134 | 171,878 |
| Advances issued | 34,275 | 18,158 |
| Other receivables | 13,104 | 18,581 |
| | 127,513 | 208,617 |
| Maturity analysis: | | |
| within one year | 127,513 | 173,522 |
| after more than one year | — | 35,095 |
| | 127,513 | 208,617 |

Sales and income received from related parties were as follows:

| | Year ended December 31, 2006 | Year ended December 31, 2005 |
|---|---|---|
| Sales | 718,164 | 656,880 |
| Banking income | 1,889 | 1,304 |
| Interest income | 31,605 | 12,977 |
| | 751,658 | 671,161 |

## 16. Inventories

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Raw materials and supplies | 1,238,129 | 899,282 |
| Work-in-progress | 402,281 | 319,927 |
| Finished goods | 599,237 | 504,523 |
| | 2,239,647 | 1,723,732 |

Of the above amounts US$ 146.9 million (December 31, 2005: US$ 193.6 million) are stated at net realizable value, these amounts exclude inventories fully provided against.

During the year ended December 31, 2006, the Group recognized a US$ 22.3 million release of previously accrued inventory provisions. Inventory write-downs were US$ 10.4 million for the year ended December 31, 2005.

(Tabular amounts expressed in thousands of US dollars)

## 17. Other current assets

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Advances paid | 152,567 | 111,978 |
| Prepayments | 32,762 | 32,599 |
| Other taxes and social security prepaid | 19,564 | 12,790 |
| Reserves at Central Bank of Russia | 12,325 | 4,938 |
| Other assets | 41,186 | 18,803 |
| | 258,404 | 181,108 |

## 18. Intangible assets

| | Goodwill | Mineral licences | Other intangible assets | Total |
|---|---|---|---|---|
| **Cost:** | | | | |
| December 31, 2004 | 1,439 | — | 9,846 | 11,285 |
| Additions | — | 29,732 | 2,590 | 32,322 |
| Business combinations | — | — | 24,443 | 24,443 |
| Disposals | — | — | (271) | (271) |
| Foreign exchange difference | (1) | (512) | (2,283) | (2,796) |
| December 31, 2005 | 1,438 | 29,220 | 34,325 | 64,983 |
| Additions | — | 4,717 | 4,091 | 8,808 |
| Disposals | — | — | (337) | (337) |
| Foreign exchange difference | 2 | 2,948 | 3,722 | 6,672 |
| December 31, 2006 | 1,440 | 36,885 | 41,801 | 80,126 |
| **Amortization and impairment:** | | | | |
| December 31, 2004 | 21 | — | 3,975 | 3,996 |
| Amortization expense | — | — | 4,979 | 4,979 |
| Disposals | — | — | (264) | (264) |
| Foreign exchange difference | (1) | — | (250) | (251) |
| December 31, 2005 | 20 | — | 8,440 | 8,460 |
| Amortization expense | — | 1,708 | 7,285 | 8,993 |
| Disposals | — | — | (249) | (249) |
| Foreign exchange difference | 2 | 55 | 1,199 | 1,256 |
| December 31, 2006 | 22 | 1,763 | 16,675 | 18,460 |
| **Net book values:** | | | | |
| December 31, 2005 | 1,418 | 29,220 | 25,885 | 56,523 |
| December 31, 2006 | 1,418 | 35,122 | 25,126 | 61,666 |

(Tabular amounts expressed in thousands of US dollars)

## 19. Property, plant and equipment

The movements in property, plant and equipment are as follows:

| | Land and buildings | Plant and machinery | Other productive assets | Total productive assets | Community and infrastructure assets | Construction -in-progress | Total assets |
|---|---|---|---|---|---|---|---|
| **Valuation or cost:** | | | | | | | |
| December 31, 2004 | 1,040,529 | 2,724,769 | 184,966 | 3,950,264 | 40,743 | 753,606 | 4,744,613 |
| Reclassifications | (6,288) | 6,908 | 215 | 835 | (835) | — | — |
| Adjustment to fair value | 627,210 | 1,537,135 | 62,729 | 2,227,074 | (36,783) | (95,699) | 2,094,592 |
| Additions: | | | | | | | |
| External | — | — | — | — | — | 1,216,875 | 1,216,875 |
| Interest capitalised | — | — | — | — | — | 13,128 | 13,128 |
| Business combinations | 417,874 | 1,067,527 | 3,051 | 1,488,452 | — | 50,337 | 1,538,789 |
| Disposals | (5,087) | (66,679) | (10,295) | (82,061) | (1,243) | (12,972) | (96,276) |
| Business de-combinations | (5,542) | (5,720) | (24) | (11,286) | — | (258) | (11,544) |
| Transfer to inventories | — | — | — | — | — | (12,060) | (12,060) |
| Transfers | 109,826 | 595,373 | 59,452 | 764,651 | 22,622 | (787,273) | — |
| Foreign exchange difference | (73,610) | (195,578) | (8,002) | (277,190) | (1,759) | (33,837) | (312,786) |
| December 31, 2005 | 2,104,912 | 5,663,735 | 292,092 | 8,060,739 | 22,745 | 1,091,847 | 9,175,331 |
| Reclassifications | (6,938) | 6,110 | 777 | (51) | 51 | — | — |
| Adjustment to fair value | 249,868 | 73,319 | 6,601 | 329,788 | (258) | (1,333) | 328,197 |
| Additions: | | | | | | | |
| External | — | — | — | — | — | 1,242,910 | 1,242,910 |
| Interest capitalised | — | — | — | — | — | 10,744 | 10,744 |
| Business combinations | 81,452 | 11,203 | 917 | 93,572 | 687 | 1,114 | 95,373 |
| Disposals | (7,387) | (89,254) | (7,762) | (104,403) | (486) | (8,369) | (113,258) |
| Business de-combinations | — | — | — | — | (394) | — | (394) |
| Transfer to inventories | — | — | — | — | — | (11,818) | (11,818) |
| Transfers | 395,048 | 1,260,655 | 30,982 | 1,686,685 | 14,856 | (1,701,541) | — |
| Foreign exchange difference | 225,927 | 575,281 | 28,824 | 830,032 | 2,565 | 85,483 | 918,080 |
| December 31, 2006 | 3,042,882 | 7,501,049 | 352,431 | 10,896,362 | 39,766 | 709,037 | 11,645,165 |

*(Tabular amounts expressed in thousands of US dollars)*

| | Land and buildings | Plant and machinery | Other productive assets | Total productive assets | Community and infrastructure assets | Construction -in-progress | Total assets |
|---|---|---|---|---|---|---|---|
| **Depreciation and impairment:** | | | | | | | |
| December 31, 2004 | 179,097 | 886,606 | 62,487 | 1,128,190 | 21,592 | 113,889 | 1,263,671 |
| Reclassifications | (3,187) | 5,315 | (834) | 1,294 | (1,294) | — | — |
| Adjustment to fair value | (187,327) | (987,355) | (45,011) | (1,219,693) | (36,700) | (91,876) | (1,348,269) |
| Depreciation expense | 72,601 | 385,036 | 32,678 | 490,315 | 1,303 | — | 491,618 |
| Disposals | (1,591) | (35,168) | (5,680) | (42,439) | (1,189) | (2,962) | (46,590) |
| Business de-combinations | (625) | (2,011) | (10) | (2,646) | — | — | (2,646) |
| Transfers | 402 | 6,080 | 656 | 7,138 | 17,071 | (24,209) | — |
| Impairment of assets | — | 9,385 | — | 9,385 | 4,933 | 11,064 | 25,382 |
| Foreign exchange difference | (7,678) | (38,452) | (2,761) | (48,891) | (1,134) | (3,813) | (53,838) |
| December 31, 2005 | 51,692 | 229,436 | 41,525 | 322,653 | 4,582 | 2,093 | 329,328 |
| Reclassifications | — | 1,863 | (475) | 1,388 | (1,388) | — | — |
| Adjustment to fair value | (39,986) | (150,349) | (47,524) | (237,859) | (1,228) | (411) | (239,498) |
| Depreciation expense | 207,857 | 698,292 | 44,512 | 950,661 | 3,494 | — | 954,155 |
| Disposals | (933) | (25,370) | (2,605) | (28,908) | (337) | (1) | (29,246) |
| Business combinations | 1,634 | 91 | 277 | 2,002 | 3 | — | 2,005 |
| Business de-combinations | — | — | — | — | (374) | — | (374) |
| Transfers | 29 | 45 | — | 74 | 3,906 | (3,980) | — |
| Impairment of assets | 2,733 | 7,085 | 77 | 9,895 | 2,165 | 7,412 | 19,472 |
| Foreign exchange difference | 11,266 | 43,321 | 4,569 | 59,156 | 647 | 301 | 60,104 |
| December 31, 2006 | 234,292 | 804,414 | 40,356 | 1,079,062 | 11,470 | 5,414 | 1,095,946 |
| **Net book values:** | | | | | | | |
| December 31, 2005 | 2,053,220 | 5,434,299 | 250,567 | 7,738,086 | 18,163 | 1,089,754 | 8,846,003 |
| December 31, 2006 | 2,808,590 | 6,696,635 | 312,075 | 9,817,300 | 28,296 | 703,623 | 10,549,219 |
| **Net book values based on cost, less depreciation and impairment:** | | | | | | | |
| December 31, 2005 | 1,337,243 | 2,173,457 | 109,411 | 3,620,111 | 16,999 | 1,093,457 | 4,730,567 |
| December 31, 2006 | 1,837,180 | 3,258,449 | 148,821 | 5,244,450 | 25,413 | 703,623 | 5,973,486 |

Other productive assets include transmission equipment, transportation equipment and tools.

As described in Note 3f, the Group uses the revaluation model of accounting for property, plant and equipment. Management commissions independent appraisers to evaluate the fair value of productive property, plant and equipment. Property, plant and equipment of the key entities of Russian Steel segment, of Severstal North America and of coal production entities of the Mining segment were valued as of December 31, 2005. Property, plant and equipment of iron ore and pellets production entities of the Mining segment and of the Russian production entity of the Metalware segment were valued as of October 1, 2006. Property, plant and equipment of the Lucchini segment were valued as of April 30, 2005. Management considers that the carrying value of property, plant and equipment of all business segments approximate their fair values as of the balance sheet date.

***(Tabular amounts expressed in thousands of US dollars)***

The following amounts were recognized in the income statement and statement of changes in equity as a result of the revaluations during 2006:

| | Buildings and constructions | Plant and machinery | Other productive assets | Total productive assets | Community and infrastructure assets | Construction -in-progress | Total assets |
|---|---|---|---|---|---|---|---|
| **Adjustment to fair market value during 2006:** | | | | | | | |
| Cost | 249,868 | 73,319 | 6,601 | 329,788 | (258) | (1,333) | 328,197 |
| Accumulated depreciation | 39,986 | 150,349 | 47,524 | 237,859 | 1,228 | 411 | 239,498 |
| | 289,854 | 223,668 | 54,125 | 567,647 | 970 | (922) | 567,695 |
| **Adjustment to fair market value:** | | | | | | | |
| Revaluation included in equity: revaluation increase | 298,510 | 250,040 | 54,863 | 603,413 | 1,016 | 1,530 | 605,959 |
| Revaluation included in income statement: impairment | (8,656) | (26,372) | (738) | (35,766) | (46) | (2,452) | (38,264) |
| | 289,854 | 223,668 | 54,125 | 567,647 | 970 | (922) | 567,695 |

The following amounts were recognized in the income statement and statement of changes in equity as a result of the revaluations during 2005:

| | Buildings and constructions | Plant and machinery | Other productive assets | Total productive assets | Community and infrastructure assets | Construction -in-progress | Total assets |
|---|---|---|---|---|---|---|---|
| **Adjustment to fair market value during 2005:** | | | | | | | |
| Cost | 627,210 | 1,537,135 | 62,729 | 2,227,074 | (36,783) | (95,699) | 2,094,592 |
| Accumulated depreciation | 187,327 | 987,433 | 45,011 | 1,219,771 | 36,700 | 91,876 | 1,348,347 |
| | 814,537 | 2,524,568 | 107,740 | 3,446,845 | (83) | (3,823) | 3,442,939 |
| **Adjustment to fair market value:** | | | | | | | |
| Revaluation included in equity: revaluation increase | 679,346 | 2,584,082 | 109,964 | 3,373,392 | — | — | 3,373,392 |
| revaluation decrease | — | (20,993) | (1) | (20,994) | — | — | (20,994) |
| | 679,346 | 2,563,089 | 109,963 | 3,352,398 | — | — | 3,352,398 |
| Revaluation included in income statement: reversal of previous impairment | 143,843 | 11,428 | 278 | 155,549 | — | — | 155,549 |
| impairment | (8,652) | (49,949) | (2,501) | (61,102) | (83) | (3,823) | (65,008) |
| | 135,191 | (38,521) | (2,223) | 94,447 | (83) | (3,823) | 90,541 |
| | 814,537 | 2,524,568 | 107,740 | 3,446,845 | (83) | (3,823) | 3,442,939 |

*(Tabular amounts expressed in thousands of US dollars)***

The following amounts are recognized in the income statement line "(Impairment)/reversal of impairment of property, plant and equipment":

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Revaluation increase | — | 155,549 |
| Revaluation decrease | (38,264) | (65,008) |
| Other impairment of property, plant and equipment | (19,472) | (25,382) |
| (Impairment)/reversal of impairment of property, plant and equipment | (57,736) | 65,159 |

## 20. Investment in associates

The Group's investment in associated companies is described in the tables below. Group structure and certain additional information on investments in associated companies, including ownership percentages, is given in note 29.

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Double Eagle Steel Coating Company | 28,859 | 26,409 |
| Spartan Steel Coating LLC | 63,818 | 56,374 |
| Severstal US Holdings LLC | 132,076 | 59,415 |
| Mountain State Carbon LLC | 119,472 | 60,205 |
| Air Liquide Severstal | 7,026 | 3,214 |
| TA Cord | 844 | 2,108 |
| Others | 2,811 | 2,927 |
| | 354,906 | 210,652 |

The following is summarized financial information, in aggregate, in respect of associates:

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Assets | 1,269,330 | 515,409 |
| Liabilities | 615,767 | 85,206 |
| Equity | 653,563 | 430,203 |

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Revenues | 373,765 | 178,655 |
| Net income/(loss) | 3,262 | (2,964) |

Double Eagle Steel Coating Company and Spartan Steel Coating LLC were associates of the bankrupt Rouge Steel Company, and were acquired on January 30, 2004, when the Group through its subsidiary Severstal North America Inc, acquired the assets and business of Rouge Steel Company.

Severstal US Holdings LLC, was created by Severstal and its related parties as a holding company for the SeverCorr project — construction of a mini mill in the United States of America. SeverCorr's mini mill is expected to produce approximately 1.5 million tons of high-quality flat-rolled steel on an annual basis. Total financing requirements of this project are approximately US$ 880.0 million, and the project will be financed by Severstal, its related parties, third party equity participants and bank financing. By December 31, 2006, Severstal have contributed to the project US$ 140.5 million and provided a US dollar denominated loan to Severcorr LLC in the amount of US$ 60.0 million. The loan is repayable in 2014 and bears interest at 15% per annum. By December 31, 2006, related parties of Severstal have contributed to the project US$ 85.5 million. Having completed those contributions, Severstal and its related parties have fully fulfilled their financing obligations for this project.

***(Tabular amounts expressed in thousands of US dollars)***

By December 31, 2006, the Group, through its subsidiary Severstal North America Inc, has contributed US$ 120.0 million to the Mountain State Carbon LLC, a joint venture with Wheeling-Pittsburgh Steel Corporation (“Wheeling-Pittsburgh”). Wheeling-Pittsburgh has contributed to the joint venture all of its coking assets in Follansbee, USA, valued at US$ 86.9 million, and US$ 3.1 million in cash. This cash and US$ 30.0 million of additional contributions from Wheeling-Pittsburgh over the next three years will be used to rehabilitate all of the coke batteries of the joint venture and provide the Group’s US integrated steel operations a reliable and competitive supply of metallurgical coke. Each partner has a 50% share in Mountain State Carbon LLC from April 2006.

On August 31, 2005, the Group and Air Liquide established a company Air Liquide Severstal for construction of an air liquefaction plant in Cherepovets. The Group is to contribute Euro 7.5 million for 25% ownership plus one share, Air Liquide is to contribute Euro 22.5 million for 75% ownership minus one share. The remaining project financing requirements of Euro 70.0 million will be met through bank loans.

## 21. Long-term financial investments

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| **Loans:** | | |
| Accounts at related party financial institutions | 50,147 | — |
| Loans to related parties | 76,528 | 43,003 |
| Loans to third parties | 30,556 | 31,936 |
| Loans to bank customers: | | |
| Related parties | 7,078 | — |
| Third parties | 19,226 | — |
| **Available-for-sale securities** | 10,315 | 12,614 |
| **Held to maturity securities** | 6,090 | 1,988 |
| | 199,940 | 89,541 |

## 22. Bank customer accounts

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Demand deposits | 22,103 | 30,502 |
| Term deposits | 9,040 | 68,365 |
| | 31,143 | 98,867 |

## 23. Amounts payable to related parties

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Trade accounts payable | 86,203 | 120,359 |
| Advances received | 699 | 2,026 |
| Payable for Lucchini acquisition | — | 216,483 |
| Other accounts payable | 8,898 | 114,218 |
| Bank demand deposits | 58,719 | 16,302 |
| Bank term deposits | 15,904 | 17,339 |
| | 170,423 | 486,727 |

***(Tabular amounts expressed in thousands of US dollars)***

Purchases from related parties were as follows:

| | Year ended December 31, 2006 | 2005 |
|---|---|---|
| Purchases from associates: | | |
| Non-capital expenditures | 141,630 | 85,420 |
| Purchases from other related parties: | | |
| Non-capital expenditures | 1,012,740 | 647,643 |
| Capital expenditures | 130,769 | 57,413 |

## 24. Debt finance

| | December 31, 2006 | 2005 |
|---|---|---|
| Citibank CLN — Eurobonds 2009 | 325,000 | 325,000 |
| Citibank CLN — Eurobonds 2014 | 375,000 | 375,000 |
| Other issued bonds | 113,934 | 327,446 |
| Bank financing | 1,901,046 | 1,628,709 |
| Factoring of receivables | 224,049 | 191,732 |
| Other financing | 26,163 | 57,161 |
| Accrued interest | 54,748 | 39,720 |
| Unamortized balance of transaction costs | (17,857) | (20,462) |
| | 3,002,083 | 2,924,306 |
| Total debt is denominated in the following currencies: | | |
| US dollars | 1,210,753 | 1,287,620 |
| Roubles | 342,212 | 335,381 |
| Euro | 1,449,118 | 1,301,305 |
| | 3,002,083 | 2,924,306 |
| Total debt is contractually repayable after the balance sheet date as follows: | | |
| Less than one year | 954,048 | 992,612 |
| Between one and five years | 1,488,594 | 1,496,325 |
| After more than five years | 559,441 | 435,369 |
| | 3,002,083 | 2,924,306 |

Debt finance raised from banks and unused long term credit lines are secured by charges over:

- US$ 1,081.0 million (December 31, 2005: US$ 826.7 million) net book value of plant and equipment;
- US$ 1,015.6 million (December 31, 2005: US$ 1,296.2 million) of current assets and revenues from export contracts; and,
- US$ 365.9 million (December 31, 2005: US$ 97.1 million) of financial assets.

A part of the Group's debt financing is subject to certain covenants. The Group complied with all debt covenants during the years ended December 31, 2006 and 2005.

At the balance sheet date the Group had US$ 422.1 million (December 31, 2005: US$ 319.9 million) of unused long term credit lines available to it.

*(Tabular amounts expressed in thousands of US dollars)*

## 25. Other current liabilities

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Advances received | 230,432 | 156,392 |
| Amounts payable to employees | 186,141 | 149,667 |
| Accrued expenses | 41,353 | 19,525 |
| Other liabilities | 36,296 | 35,661 |
| | 494,222 | 361,245 |

## 26. Retirement benefit liability

The following assumptions have been used to calculate the retirement benefit liability:

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Discount rates: | | |
| Russia | 6.46% | 6.85% |
| USA | 5.75% | 5.50% |
| UK | 4.90% | n/a |
| Italy and France | 4.60% | 4.0% to 5.0% |
| Future rates of benefit increase: | | |
| Russia | 6.20% | 6.20% |
| USA | n/a | n/a |
| UK | 2.80% | n/a |
| Italy and France | 3.00% | 3.0% to 3.5% |

The components of the retirement benefit liabilities were as follows:

| | December 31, 2006 | December 31, 2005 |
|---|---|---|
| Retirees | 433,965 | 291,373 |
| Other participants: | | |
| Vested | 18,304 | 13,560 |
| Non-vested | 96,740 | 82,724 |
| Present value of the defined benefit obligation | 549,009 | 387,657 |
| Fair value of the plan assets | (106,055) | (49,171) |
| | 442,954 | 338,486 |

***(Tabular amounts expressed in thousands of US dollars)***

The movements in the retirement benefit liabilities were as follows:

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Net liability at beginning of period | 338,486 | 158,023 |
| Business combinations | 10,762 | 149,110 |
| Contributions made during the year | (34,615) | (34,096) |
| Amounts recognized in the income statement: | | |
| Return on plan assets | (16,382) | (9,084) |
| Interest cost | 24,962 | 19,144 |
| Service cost | 18,767 | 12,890 |
| Actuarial losses | 67,658 | 62,380 |
| Foreign exchange loss/(gain) | 33,316 | (19,881) |
| Net liability at December 31 | 442,954 | 338,486 |

The retirement benefit expenses that are recognized in the income statement are contained in the caption: 'Selling, general and administrative expenses', except for the interest cost, which is recognized in the caption 'Net financing expense'.

## 27. Other non-current liabilities

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Decommissioning liability | 128,209 | 102,885 |
| Restructured tax liabilities | 67,731 | 97,368 |
| Provisions | 79,150 | 68,346 |
| Other | 23,011 | 30,212 |
| | 298,101 | 298,811 |

### *Decommissioning liability*

The Group has environmental liabilities related to restoration of soil and other related works, which are due upon the closures of its coal mines. These liabilities have been estimated using existing technology, at current prices, and discounted using a real discount rate of 2%. A substantial part of the decommissioning costs is expected to be incurred between 2020 and 2040.

There are no significant environmental liabilities related to steel production facilities, metalware facilities, iron ore concentrate and pellets production sites.

### *Restructured tax liabilities*

OAO Vorkutaugol and OAO Mine Vorgashorskaya had significant amounts of taxes in arrears, when they were acquired by the Group's Majority Shareholder in June 2003.

In November 2005, these subsidiaries signed restructuring agreements with the tax authorities. In accordance with these agreements, the principal amounts of taxes, and fines thereon and 15% of tax interest are payable by instalments over four years. If those payments are made on schedule, the remaining 85% of tax interest liability at the date of restructuring will be forgiven. The Group's management is confident that all payments will be in accordance with the agreed schedules, and accordingly recognized a US$ 200.9 million gain on tax restructuring in the income statement for the year ended December 31, 2005. This gain is comprised of US$ 186.8 million of tax interest, which will be forgiven, and has been derecognized from liabilities, and US$ 14.1 million of discounting of the remaining liabilities using the interest rate of 9.86%. During 2005, tax authorities have accrued US$ 26.7 million of tax interest on tax liabilities being restructured. These amounts were recognized as an expense in the income statement for the year ended December 31, 2005. During 2006, the Group was able to include part of this tax interest into restructuring, recognizing a gain of US$ 14.7 million in the income statement for the year ended December 31, 2006. Restructured tax liabilities are subject to interest rate of 5% per annum, which is included in the caption "Interest expense" since the moment of restructuring.

***(Tabular amounts expressed in thousands of US dollars)***

Accordingly, net gain on restructuring of tax liabilities is shown in the income statement as following:

| | Year ended December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Tax interest accrued prior to restructuring | — | (26,675) |
| Gain on restructuring of tax liabilitites | 14,669 | 200,853 |
| Net gain on restructuring of tax liabilities | 14,669 | 174,178 |

Current portion of restructured tax liabilities is included in the caption 'Other taxes and social security payable'. The total amount of the restructured taxes is presented in the table below:

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Payable within one year | 43,553 | 26,059 |
| Payable after one year | 67,731 | 97,368 |
| | 111,284 | 123,427 |

***Provisions***

| | December 31, | |
|---|---|---|
| | 2006 | 2005 |
| Social security claims | 28,689 | 23,020 |
| Other employee related | 13,578 | 12,984 |
| Legal claims | 21,917 | 17,004 |
| Restructuring | 5,569 | — |
| Other | 9,397 | 15,338 |
| | 79,150 | 68,346 |

These provisions represent management's best estimate of the potential losses arising in these cases. The actual outcome of those cases is currently uncertain, and might differ from the recorded provisions.

## 28. Share capital

The Parent Company's share capital consists of ordinary shares with a nominal value of RUR 0.01 each. Authorized share capital of Severstal at December 31, 2005 comprised 551,854,800 shares and was fully issued and paid on that date. At December 31, 2006, Severstal had 1,007,701,355 issued and fully paid shares and 5,062,701,445 authorized but not issued shares.

The nominal amount of initial share capital was converted into US dollars using exchange rates during the Soviet period, when the Government contributed the original capital funds to the enterprise. These capital funds were converted into ordinary shares on September 24, 1993 and sold by the Government at privatization auctions. The Parent Company did not issue new shares until June 2006.

***Share issue in June 2006***

The Parent Company issued shares in June 2006 in consideration for the mining companies acquired from related parties. These issued shares were recognized from the date the acquired companies are included in these consolidated financial statements. The Parent Company shares issued in respect of the interests that the Majority Shareholder had at December 31, 2005 and 2004 in the acquired mining companies are recognized in the share capital at that date. Additional share issues are recognized in 2006 and 2005, in respect of ownership interests that the Majority Shareholder acquired in those companies during those periods.

***(Tabular amounts expressed in thousands of US dollars)***

As discussed in note 29, certain shareholders exercised their pre-emptive rights in connection with the share issue for acquisition of mining companies. Total proceeds for such shares issued for cash in June 2006 were US$ 162,179 thousand and comprised of US$ 5 thousand of increase in share capital and US$ 162,174 thousand of increase in share premium.

***Share issue in December 2006***

In November 2006, the Parent Company completed the listing of its global depositary receipts ('GDRs') on the London Stock Exchange. The Group's Majority Shareholder placed 85,000,000 GDRs in an initial public offering ('IPO') at a price of US$ 12.50 per GDR (one GDR represents one share). The Parent Company was not issuing new shares and has not received any proceeds in connection with this initial public offering.

However, as a part of this process, the Parent Company initiated the issue of up to 85,000,000 additional shares in the fourth quarter of 2006. In accordance with the Russian legislation, shareholders had pre-emptive rights to purchase new shares pro-rata to their shareholding in the Parent Company as at September 14, 2006 — the date of the meeting of the Board of Directors of the Parent Company where the decision to issue additional shares was approved.

On November 14, 2006, the Board of Directors set the price for pre-emptive rights purchases equal to the IPO price less pro rata expenses for the IPO transaction — RUR 322.81 per share (US$ 12.13 at November 14, 2006 exchange rate). The Board of Directors also decided that shares for which preemptive rights were not exercised would be offered through open subscription at the IPO price of RUR 332.74 per share (US$ 12.50 at November 14, 2006 exchange rate).

The Group received RUR 24,829 million (US$ 943.0 million at December 18, 2006 exchange rate — the date of closing of share issue) for 76,916,692 shares placed under pre-emptive rights subscription. The Group did not receive applications under the open subscription.

Consequently, the total value of issued share capital presented in these consolidated financial statements comprises:

| | Number of shares, thsd. | US$'000 |
|---|---|---|
| Nominal share capital at exchange rate on Dec 31, 2004 | 551,855 | 198,876 |
| Historic difference | — | 3,112,253 |
| Total historic value of statutory share capital on Dec 31, 2004 | 551,855 | 3,311,129 |
| Shares issued for acquisition of mining companies | 348,337 | 119 |
| Adjusted share capital at December 31, 2004 | 900,192 | 3,311,248 |
| Shares issued for additional stakes in mining companies | 17,076 | 6 |
| Adjusted share capital at December 31, 2005 | 917,268 | 3,311,254 |
| Shares issued for cash in June 2006 | 13,516 | 5 |
| Shares issued for cash in December 2006 | 76,917 | 29 |
| Share capital at December 31, 2006 | 1,007,701 | 3,311,288 |

All shares carry equal voting and distribution rights.

(Tabular amounts expressed in thousands of US dollars)

### *Dividends*

The maximum dividend payable is restricted to the total accumulated retained earnings of the Parent Company determined according to Russian law. As at the balance sheet date, reserves available for distribution were US$ 4,667.6 million (December 31, 2005: US$ 3,308.6 million).

On June 9, 2006, the Meeting of Shareholders approved the final dividend of RUR 4.00 (US$ 0.15) per share in respect of 2005. Owners of 551.9 million shares were entitled to this dividend, as the June 2006 share issue was completed later than the date of closing of share register for these dividends.

On September 25, 2006, the Meeting of Shareholders approved an interim dividend of RUR 3.60 (US$ 0.13) per share in respect of the first half of 2006. Owners of 930.8 million shares were entitled to these dividends.

On December 25, 2006, the Meeting of Shareholders approved an interim dividend of RUR 2.00 (US$ 0.075) per share and GDR in respect of the third quarter of 2006 with the record date November 16, 2006. Owners of 930.8 million shares were entitled to these dividends.

## 29. Subsidiary and associated companies

The following is a list of the Group's significant subsidiaries and associates and the effective ownership holdings therein:

| Company | December 31, 2006 | December 31, 2005 | Location | Activity |
|---|---|---|---|---|
| **Russian Steel segment:** | | | | |
| *Subsidiaries:* | | | | |
| ZAO Severgal | 75.0% | 75.0% | Russia | Hot dip galvanizing |
| ZAO Izhorsky Tube Factory | 100.0% | 100.0% | Russia | Wide pipes |
| OOO SSM-Tyazhmash | 100.0% | 100.0% | Russia | Repairs & construction |
| OAO Domnaremont | 82.1% | 56.4% | Russia | Repairs & construction |
| ZAO Firma Stoik | 100.0% | 100.0% | Russia | Repairs & construction |
| OAO Metallurgremont | 79.8% | 79.3% | Russia | Repairs & construction |
| OOO Energoremont | 100.0% | 100.0% | Russia | Repairs & construction |
| OOO Electroremont | 93.3% | 93.3% | Russia | Repairs & construction |
| OOO Uralmash MO | 100.0% | 100.0% | Russia | Engineering & design |
| OOO AviaCompany Severstal | 100.0% | 100.0% | Russia | Air transport |
| Severstal Export GmbH | 100.0% | 100.0% | Switzerland* | Steel sales |
| AS Severstallat | 50.5% | 50.5% | Latvia* | Steel sales |
| Latvijas Metals | 50.5% | 50.5% | Latvia* | Steel sales |
| Armaturu Servisa Centrs SIA | 25.2% | 25.2% | Latvia* | Steel service center |
| Upcroft Limited | 100.0% | 100.0% | Cyprus* | Holding company*** |
| Varndell Limited | 100.0% | 100.0% | Cyprus* | Holding company*** |
| *Associates:* | | | | |
| Severstal US Holdings LLC ** | 63.3% | 60.0% | USA* | Mini-mill |
| **Severstal North America segment:** | | | | |
| *Subsidiaries:* | | | | |
| Severstal North America Inc | 100.0% | 93.0% | USA | Iron & steel mill |
| *Associates:* | | | | |
| Double Eagle Steel Coating company | 50.0% | 46.5% | USA | Electro-galvanizing |
| Spartan Steel Coating LLC | 48.0% | 44.6% | USA | Hot dip galvanizing |
| Delaco Processing LLC | 49.0% | 45.6% | USA | Steel slitting |
| Mountain State Carbon LLC | 50.0% | 31.0% | USA | Coking coal |

**(continued on the next page)**

(*) Russian Steel segment contains Russian production entities, foreign trading companies, which are selling products primarily produced in Russia, and other foreign companies, which either provide services to Russian production entities or are managed from Russia.

(**) 20.2% and 19.9% of ordinary shares at December 31, 2006 and December 31, 2005, respectively

(***) Upcroft is holding 19.99% of Lucchini SpA and Varndell is holding 50.8% of Lucchini SpA

***(Tabular amounts expressed in thousands of US dollars)***

| Company | December 31, 2006 | December 31, 2005 | Location | Activity |
|---|---|---|---|---|
| **Lucchini segment:** | | | | |
| *Subsidiaries:* | | | | |
| Lucchini SpA | 70.8% | 70.8% | France | Holding company |
| Ascometal SAS | 70.8% | 70.8% | France | Steel manufacturing |
| Ascometal GmbH | 70.8% | 70.8% | Germany | Sales |
| Ascoforge Safe SAS | 70.8% | 70.8% | France | Forgings |
| Bari Fonderie Meridionali SpA | 70.8% | 70.8% | Italy | Forgings |
| Bi-Mec Srl | 70.8% | 70.8% | Italy | Maintenance |
| GSI Lucchini SpA | 49.1% | 49.1% | Italy | Steel spheres |
| Nitruvid SAS | 70.8% | 70.8% | France | Steel finishing |
| Lucchini Asia Pacific Pte Ltd | 70.8% | 70.8% | Singapore | Sales |
| Lucchini Holland BV | 70.8% | 70.8% | Netherlands | Investment holding |
| Lucchini HPS Gmbh | 23.5% | 46.0% | Germany | Sales |
| Lucchini Iberia Sl | 70.8% | 70.8% | Spain | Sales |
| Lucchini Poland Spzoo | 70.8% | 70.8% | Poland | Machining |
| Lucchini Servizi Srl | 70.8% | 70.8% | Italy | Dormant |
| Lucchini Sidermeccanica SpA | 70.8% | 70.8% | Italy | Casting and machining |
| Lucchini Siderprodukte AG | 46.0% | 46.0% | Switzerland | Sales |
| Lucchini Sweden AB | 70.8% | 70.8% | Sweden | Machining |
| Lucchini UK Ltd | 70.8% | 70.8% | UK | Machining |
| Lucchini USA Inc | 70.8% | 70.8% | USA | Sales |
| Servola SpA | 70.8% | 70.8% | Italy | Asset holding |
| Sideris Steel SAS | 70.8% | 70.8% | France | Investment holding |
| Simmofos Sarl | 70.8% | 70.8% | France | Asset holding |
| Sipro HPS AG | — | 46.0% | Switzerland | Sales |
| Vertek Srl | 70.8% | 70.8% | Italy | Steel finishing |
| *Associates:* | | | | |
| ESPRA SAS | 24.8% | 24.8% | France | Steel scrap |
| Logistica Servola Srl | 35.4% | 35.4% | Italy | Dormant |
| Setrans Srl | 21.2% | 21.2% | Italy | Logistics and storage |
| Tecnologie Ambientali Pulite Srl | 17.6% | 17.6% | Italy | Environmental services |
| *Companies classified as held for sale:* | | | | |
| Relco Spzoo | 70.8% | 70.8% | Poland | Land holding |
| Coimpex Spzoo | 28.3% | 28.3% | Poland | Land holding |
| **Metalware segment:** | | | | |
| *Subsidiaries:* | | | | |
| OAO Severstal-Metiz | 97.0% | 100.0% | Russia | Steel machining |
| OAO Dneprometiz | 58.2% | nil% | Ukraine | Steel machining |
| Carrington Wire Ltd | 97.0% | nil% | UK | Steel machining |
| OAO Cherepovets Steel Rolling Mill | n/a | 88.8% | Russia | Steel machining |
| OAO Orlovsky Steel Rolling Mill | n/a | 87.2% | Russia | Steel machining |
| OOO Volgometiz | 100.0% | 100.0% | Russia | Steel machining |
| OOO Policher | 87.3% | 80.0% | Russia | Polymer coatings |
| *Associates:* | | | | |
| OOO ChSPZ MKR | 48.5% | 44.4% | Russia | Mattress springs |
| **Mining segment:** | | | | |
| *Subsidiaries:* | | | | |
| OAO Karelsky Okatysh | 90.8% | 90.8% | Russia | Iron ore pellets |
| OAO Olkon | 91.8% | 91.6% | Russia | Iron ore concentrate |
| OAO Vorkutaugol | 89.2% | 88.1% | Russia | Coking coal concentrate |
| OAO Mine Vorgashorskaya | 73.6% | 70.2% | Russia | Coking coal concentrate |
| OAO Mine Pervomaiskaya | 99.1% | 99.1% | Russia | Coking coal concentrate |
| OAO Mine Berezovskaya | 96.3% | 96.0% | Russia | Coking coal concentrate |
| OAO SShEMK | 75.6% | 75.6% | Russia | Engineering |
| OAO Severokuzbasskoe PTU | 87.3% | 87.3% | Russia | Transportation |
| OAO Anzhero-Sudzhenskoe PTU | 94.4% | 94.4% | Russia | Transportation |

**(continued on the next page)**

***(Tabular amounts expressed in thousands of US dollars)***

| Company | December 31, 2006 | December 31, 2005 | Location | Activity |
|---|---|---|---|---|
| OAO Pechorugol | 99.3% | 99.3% | Russia | Holding company |
| OOO Olkon-Invest | 100.0% | 100.0% | Russia | Holding company |
| OOO Terra | 100.0% | 100.0% | Russia | Holding company |
| OOO Holding Gornaya Company | 100.0% | 100.0% | Russia | Holding company |
| ZAO Impulse-Consult | 100.0% | 100.0% | Russia | Holding company |
| OOO Investment Company Kuzbassugol | 100.0% | 100.0% | Russia | Holding company |
| **Financing and insurance segment:** | | | | |
| *Subsidiaries:* | | | | |
| OAO Metallurgical Commercial Bank | 72.9% | 72.6% | Russia | Banking |

In addition, at the balance sheet date, a further 26 (December 31, 2005: 26) subsidiaries and associates, which are not material to the Group, either individually or in aggregate, have been included in these consolidated financial statements.

Information on carrying amounts, acquisitions and disposals of associated companies is disclosed in Note 20 of these consolidated financial statements.

During 2006, Severstal completed acquisitions of controlling stakes in a number of companies previously controlled by Severstal's Majority Shareholder. These consolidated financial statements take account of such acquisitions as if they had occurred at the beginning of the earliest comparative period presented or, if later, at the date on which control was obtained by the common controlling shareholder. These acquisition transactions are described in the following paragraphs.

***Acquisition of Lucchini SpA from Majority Shareholder during 2006***

On April 26, 2005 Severstal and its related parties (financed by Severstal) subscribed for new ordinary shares issued by Lucchini SpA (Italy), a European steel and metalware products producer, such that Severstal obtained 19.99% of the outstanding share capital of Lucchini SpA for Euro 138.9 million and its related parties obtained 41.9% of Lucchini SpA for Euro 291.1 million. Related parties, financed by Severstal, acquired from third parties additional 8.9% of the outstanding share capital of Lucchini SpA for Euro 68.5 million in May-November 2005.

On October 2, 2006, the Group completed the acquisition from the Group's Majority Shareholder of 50.82% in Lucchini SpA for Euro 550.0 million, comprising redemption of loans issued by the Group to related parties and a Euro 182.3 million (US$ 234.3 million) cash payment. The Group's management commissioned a leading international investment bank to appraise the value of this controlling stake and conducted the acquisition at a price determined in accordance with this valuation. This acquisition was undertaken to strengthen the Group's position in the European market.

***Acquisition of Mining companies from Majority Shareholder during 2006***

On March 27, 2006, the Meeting of Shareholders of the Parent Company approved the additional share issue to acquire controlling stakes in coal and iron ore mining assets controlled by its Majority Shareholder and approved an independent appraiser.

On March 29, 2006, having received a fairness opinion on the proposed transaction from Citigroup, the Board of Directors approved the independent appraiser's valuations of the Parent Company shares being issued at RUR 320.74 per share (US$ 11.24 at the exchange rate on the date of valuation — October 1, 2005) and of the mining assets being acquired at RUR 117,202 million (US$ 4,107 million at the exchange date on the date of valuation — October 1, 2005).

On May 29, 2006, an extraordinary shareholder meeting approved the price and other terms of the share issue for acquiring the mining assets and on June 6, 2006, the transaction was completed.

Shareholders of the Parent Company, which were entitled to voting on March 27, 2006 but did not participate in it or voted against the deal, had the right to participate in the additional share issue by purchasing for cash the amount of shares that maintained their current shareholding interest at a price of RUR 320.74 per share. The market price of shares on March 27, 2006 was RUR 384 (US$ 13.79) per share. The Parent Company issued 13,516,489 shares to the shareholders that used these preemptive purchase rights.

***Acquisition of service and construction companies from Majority Shareholder during 2006***

In May 2006, the Group completed the process of purchasing back controlling stakes in certain service and construction companies, which were disposed by the Group on December 31, 2004 to related parties. Purchase prices totalled US$ 60.8 million, which is not significantly different from the amounts received by the Group for disposal of these entities on December 31, 2004.

***Acquisition of ZAO Severstal-Resource from Majority Shareholder during 2006***

In December 2006, the Group completed the process of acquiring 100% ownership interest in ZAO Severstal-Resource from Severstal's Majority Shareholder for a negligible consideration. ZAO Severstal-Resource is the management company for the companies of Mining segment.

***Acquisition of stake in Severstal North America from related parties during 2006***

In December 2006, the Group completed the process of acquiring 7% ownership interest in Severstal North America Inc for US$ 54.5 million.

***Acquisitions of subsidiaries from third parties during 2006***

In February 2006, the Group acquired 60% ownership interest (57.9% effective ownership interest) in joint stock company Dneprometiz for US$ 33 million. Severstal also obtained an option to buy an additional 27% stake of the share capital after one year for a consideration in the range from US$ 14.0 to US$ 20.0 million. Dneprometiz produces wire and certain other metalware products at its production facilities located in Ukraine.

In April 2006, the Group acquired 100% of Carrington Wire Ltd., a UK wire and other metalware products producer, for US$ 30.5 million.

These acquisitions were conducted to strengthen the Group's position in the metalware market.

*(Tabular amounts expressed in thousands of US dollars)*

A summary of assets and liabilities acquired from third parties during 2006 and 2005 is presented below:

| | 2006 | 2005 |
|---|---|---|
| Cash and cash equivalents | 5,875 | 657 |
| Trade accounts receivable | 26,463 | 1,311 |
| Inventories | 18,841 | 4,906 |
| Other current assets | 7,601 | 792 |
| Property, plant and equipment | 93,368 | 4,036 |
| Assets held for sale | — | 16,365 |
| Trade accounts payable | (33,557) | (199) |
| Other taxes and social security payable | (70) | (144) |
| Deferred tax liabilities | (10,421) | — |
| Retirement benefit liability | (10,762) | — |
| Debt finance | (8,623) | (841) |
| Other liabilities | (5,773) | (151) |
| Net identifiable assets and liabilities acquired | 82,942 | 26,732 |
| Minority interest | (17,792) | — |
| Severstal's share of net identifiable assets and liabilities acquired | 65,150 | 26,732 |
| Consideration paid | (63,500) | (21,902) |
| Negative goodwill | 1,650 | 4,830 |

***Reorganization of Metalware segment during 2006***

OAO Severstal-Metiz (renamed from ZAO Severstal-Metiz on July 1, 2006) was a holding company that managed the activities of the Metalware segment, provided all administrative services to the companies of the Metalware segment and was the sole sales and procurement organization for the Metalware segment.

During 2005 Severstal transferred to OAO Severstal-Metiz its ownership interests in the metalware companies OAO Cherepovets Steel Rolling Mill ("ChSPZ") and OAO Orlovsky Steel Rolling Mill ("OSPaZ"). Effective January 1, 2006, ChSPZ and OSPaZ legal entities were merged into OAO Severstal-Metiz. As a result of this merger, Severstal's ownership in OAO Severstal-Metiz reduced on January 1, 2006 from 100% to 92.8%. In December 2005, OOO Volgometiz transferred all its principal assets and liabilities to OAO Severstal-Metiz. As a result of these transactions, from January 1, 2006 OAO Severstal-Metiz is the principal operating company of metalware segment.

During 2006, the Group bought additional 3.8% of OAO Severstal-Metiz for US$ 6.3 million and participated in the additional share issue by OAO Severstal-Metiz, increasing its ownership to 97.01% at December 31, 2006. The fair value of net assets of OAO Severstal-Metiz at the time of acquisition was US$ 214.3 million, resulting in recognition of US$ 1.8 million of negative goodwill.

## 30. Subsequent events

***Dividends proposed***

On March 30, 2007, the Board of Directors recommended the final dividend for 2006 of RUR 5.00 (US$ 0.19) per share and GDR.

***Acquisition of ZAO Vtorchermet***

In January 2007, the Group completed the acquisition of ZAO Vtorchermet and its subsidiaries and certain related companies for US$ 45.4 million. ZAO Vtorchermet is a scrap processing and wholesale company, and the majority of its operations is located in Saint Peterburg. Currently, ZAO Vtorchermet exports to Europe substantially all of the scrap that it purchases, and the Group expects to continue this. The acquisition was conducted to secure a reliable source of scrap for the Russian steel mill in case of future changes in the Russian scrap market. Management has not yet completed the estimation of fair values of the acquired assets and liabilities and, accordingly, does not currently possess all necessary information to disclose the effect of this subsequent period acquisition on the Group's financial position or results of operations.

*Disposal of Lucchini Sidermeccanica S.p.A.*

On March 29, 2007, the Board of Directors of Lucchini S.p.A., a Group's subsidiary, approved the disposal of 100% shares (representing an effective Group's ownership of 70.8%) in Lucchini Sidermeccanica SpA to the Lucchini family, following a binding offer received from a Lucchini family company. Lucchini S.p.A. would receive approximately Euro 125 million (US$ 167 million at March 29, 2007 exchange rate) for these shares, subject to possible insignificant changes related to final determination of net financial indebtedness, and approximately Euro 68 million (US$ 93 million at March 29, 2007 exchange rate) for the loans previously issued by Lucchini S.p.A. to Lucchini Sidermeccanica S.p.A.

Revenues for the year ended December 31, 2006 and net equity at December 31, 2006 of Lucchini Sidermeccanica S.p.A. and its subsidiaries included in these consolidated financial statements were Euro 249 million (US$ 313 million) and Euro 95 million (US$ 125 million at December 31, 2006 exchange rate), respectively. The transaction is expected to be closed within the second quarter of 2007 and the Group expects to recognize a pre-tax gain on the disposal of Lucchini Sidermeccanica S.p.A. of approximately Euro 30 million (US$ 40 million at March 29, 2007 exchange rate). A fairness opinion from a reputable Italian bank has been obtained by the Board of Directors of Lucchini SpA for the transaction.

***(Tabular amounts expressed in thousands of US dollars)***

## 31. Segment information

Segmental income statements for the year ended December 31, 2006:

| | Russian Steel segment | Severstal North America | Lucchini segment | Metalware segment | Mining segment | Financing segment | Inter segment transactions | Consolidated |
|---|---|---|---|---|---|---|---|---|
| **Sales** | | | | | | | | |
| Sales — external | 5,352,801 | 1,868,426 | 3,182,119 | 780,086 | 520,922 | — | — | 11,704,354 |
| Sales — to related parties | 921,647 | — | 175,347 | 58,837 | 943,555 | — | (1,381,222) | 718,164 |
| | 6,274,448 | 1,868,426 | 3,357,466 | 838,923 | 1,464,477 | — | (1,381,222) | 12,422,518 |
| **Cost of sales** | (4,036,411) | (1,712,355) | (2,829,402) | (741,925) | (1,005,324) | — | 1,381,989 | (8,943,428) |
| **Gross profit** | 2,238,037 | 156,071 | 528,064 | 96,998 | 459,153 | — | 767 | 3,479,090 |
| Selling, general and administrative expenses | (267,763) | (27,561) | (186,470) | (31,082) | (135,667) | (2,036) | — | (650,579) |
| Distribution expenses | (456,340) | — | (56,256) | (43,560) | (92,966) | — | — | (649,122) |
| Indirect taxes and contributions | (53,568) | — | (64,374) | (2,982) | (48,369) | (158) | — | (169,451) |
| Share of associates' (losses)/profits | (2,644) | 2,971 | 202 | (1,722) | — | — | — | (1,193) |
| Net income from bank lending operations | — | — | — | — | — | 5,322 | 4,072 | 9,394 |
| Net income from securities operations | 20,525 | — | 3,713 | 314 | 6,934 | 4,817 | (3,376) | 32,927 |
| (Loss)/gain on disposal of property, plant and equipment | (46,247) | 469 | (3,412) | (1,385) | (19,423) | 9 | — | (69,989) |
| Net other operating (expenses)/income | (10,078) | 1,827 | (13,564) | 5 | (1,409) | 907 | (4,642) | (26,954) |
| **Profit from operations** | 1,421,922 | 133,777 | 207,903 | 16,586 | 168,253 | 8,861 | (3,179) | 1,954,123 |
| Impairment of property, plant and equipment | (8,222) | — | (9,778) | (23,364) | (16,372) | — | — | (57,736) |
| Net gain on restructuring of tax liabilities | — | — | — | — | 14,669 | — | — | 14,669 |
| (Write off of goodwill)/negative goodwill, net | (187) | — | — | 1,650 | 224 | — | 2,526 | 4,213 |
| Net other non-operating expenses | (40,867) | — | — | (1,261) | (11,437) | — | — | (53,565) |
| **Profit before financing and taxation** | 1,372,646 | 133,777 | 198,125 | (6,389) | 155,337 | 8,861 | (653) | 1,861,704 |
| Net financing expense | (1,938) | (9,262) | (45,552) | (7,632) | (40,638) | — | (4,054) | (109,076) |
| **Profit before income tax** | 1,370,708 | 124,515 | 152,573 | (14,021) | 114,699 | 8,861 | (4,707) | 1,752,628 |
| Income tax expense | (388,539) | (41,189) | (53,790) | 3,022 | (60,894) | (2,297) | 174 | (543,513) |
| **Profit from continuing operations** | 982,169 | 83,326 | 98,783 | (10,999) | 53,805 | 6,564 | (4,533) | 1,209,115 |
| Profit from discountinued operations | — | — | 22,212 | — | — | — | — | 22,212 |
| **Profit for the year** | 982,169 | 83,326 | 120,995 | (10,999) | 53,805 | 6,564 | (4,533) | 1,231,327 |
| Additional information: depreciation expense | 546,196 | 8,783 | 117,910 | 30,619 | 250,583 | 64 | — | 954,155 |

(Tabular amounts expressed in thousands of US dollars)

Segmental income statements for the year ended December 31, 2005:

| | Russian Steel segment | Severstal North America | Lucchini segment[(1)] | Metalware segment | Mining segment | Financing segment | Inter segment transactions | Consolidated |
|---|---|---|---|---|---|---|---|---|
| **Sales** | | | | | | | | |
| Sales — external | 5,174,637 | 1,822,573 | 1,805,903 | 562,630 | 409,143 | — | — | 9,774,886 |
| Sales — to related parties | 789,677 | — | 41,630 | 56,200 | 962,520 | — | (1,193,147) | 656,880 |
| | 5,964,314 | 1,822,573 | 1,847,533 | 618,830 | 1,371,663 | — | (1,193,147) | 10,431,766 |
| **Cost of sales** | (3,407,625) | (1,716,332) | (1,586,801) | (556,963) | (729,785) | — | 1,164,450 | (6,833,056) |
| **Gross profit** | 2,556,689 | 106,241 | 260,732 | 61,867 | 641,878 | — | (28,697) | 3,598,710 |
| Selling, general and administrative expenses | (227,649) | (29,539) | (120,140) | (36,882) | (104,051) | (1,903) | — | (520,164) |
| Distribution expenses | (509,943) | — | (29,728) | (27,848) | (52,986) | — | — | (620,505) |
| Indirect taxes and contributions | (26,439) | — | (45,454) | (3,444) | (41,968) | (129) | — | (117,434) |
| Share of associates' (losses)/profits | (4,969) | 2,749 | 77 | (2,047) | — | — | — | (4,190) |
| Net income from bank lending operations | — | — | — | — | — | 6,250 | 3,732 | 9,982 |
| Net income from securities operations | 20,837 | 505 | 1,761 | 470 | 3,728 | 3,461 | (2,858) | 27,904 |
| Loss/(gain) on disposal of property, plant and equipment | (29,611) | (184) | (1,169) | (1,885) | (3,931) | 10 | — | (36,770) |
| Net other operating (expenses)/ income | (3,406) | 1,981 | (12,868) | (273) | (4,352) | 1,531 | — | (17,387) |
| **Profit from operations** | 1,775,509 | 81,753 | 53,211 | (10,042) | 438,318 | 9,220 | (27,823) | 2,320,146 |
| Reversal of impairment/ (impairment) of property, plant and equipment, net | 85,249 | — | (8,552) | (914) | (10,624) | — | — | 65,159 |
| Net gain on restructuring of tax liabilities | — | — | — | — | 174,178 | — | — | 174,178 |
| Negative goodwill | 4,830 | — | — | — | — | — | 2,800 | 7,630 |
| Net other non-operating expenses | (30,444) | — | — | (4,142) | (8,378) | — | (9,789) | (52,753) |
| **Profit before financing and taxation** | 1,835,144 | 81,753 | 44,659 | (15,098) | 593,494 | 9,220 | (34,812) | 2,514,360 |
| Net financing expense | (129,534) | (12,524) | (27,858) | 197 | (23,654) | — | (4,751) | (198,124) |
| **Profit before income tax** | 1,705,610 | 69,229 | 16,801 | (14,901) | 569,840 | 9,220 | (39,563) | 2,316,236 |
| Income tax expense | (414,175) | (27,088) | 9,166 | (2,819) | (117,390) | (2,378) | 9,016 | (545,668) |
| **Profit from continuing operations** | 1,291,435 | 42,141 | 25,967 | (17,720) | 452,450 | 6,842 | (30,547) | 1,770,568 |
| Loss from discountinued operations | — | — | (10,784) | — | — | — | — | (10,784) |
| **Profit for the year** | 1,291,435 | 42,141 | 15,183 | (17,720) | 452,450 | 6,842 | (30,547) | 1,759,784 |
| Additional information: depreciation expense | 234,202 | 7,159 | 74,659 | 19,550 | 155,902 | 146 | — | 491,618 |

(1) As discussed in note 29, Lucchini S.p.A. is included in these financial statements for eight months from end of April to December 2005.

## Notes to the consolidated financial statements for the year ended December 31, 2006
### *(Tabular amounts expressed in thousands of US dollars)*

Segmental balance sheets as at December 31, 2006:

| | Russian Steel segment | Severstal North America | Lucchini segment | Metalware segment | Mining segment | Financing segment | Inter segment balances | Consolidated |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| **Current assets:** | | | | | | | | |
| Cash and cash equivalents | 1,242,963 | — | 225,854 | 9,584 | 87,203 | 309,674 | (174,983) | 1,700,295 |
| Short-term bank deposits | 1,293,364 | — | — | 41,092 | 7 | — | (187,193) | 1,147,270 |
| Short-term financial investments | 264,429 | — | 6,587 | 1,598 | 77,839 | 191,358 | (219,969) | 321,842 |
| Trade accounts receivable | 252,209 | 128,768 | 843,737 | 62,577 | 36,806 | — | — | 1,324,097 |
| Amounts receivable from related parties | 118,309 | 1,184 | 9,601 | 7,009 | 61,927 | — | (70,517) | 127,513 |
| Inventories | 946,247 | 427,502 | 695,041 | 102,320 | 122,757 | — | (54,220) | 2,239,647 |
| VAT receivable | 213,022 | — | 49,476 | 30,436 | 45,188 | — | — | 338,122 |
| Income tax receivable | 9,010 | 16,361 | 8,404 | 294 | 1,787 | — | — | 35,856 |
| Other current assets | 132,084 | 17,070 | 29,320 | 16,091 | 50,701 | 13,138 | — | 258,404 |
| **Total current assets** | 4,471,637 | 590,885 | 1,868,020 | 271,001 | 484,215 | 514,170 | (706,882) | 7,493,046 |
| **Non-current assets:** | | | | | | | | |
| Intangible assets | 7,086 | — | 17,408 | 1,418 | 35,747 | 7 | — | 61,666 |
| Property, plant and equipment | 6,435,882 | 157,824 | 1,519,357 | 328,042 | 2,107,620 | 475 | 19 | 10,549,219 |
| Investment in associates | 139,231 | 212,154 | 2,656 | 865 | — | — | — | 354,906 |
| Long-term financial investments | 1,632,668 | — | 31,934 | 42,183 | 2,682 | 25,705 | (1,535,232) | 199,940 |
| Amounts receivable from related parties | — | — | — | — | — | — | — | — |
| Assets held for sale | — | — | 113,516 | — | — | — | — | 113,516 |
| Deferred tax assets | — | — | 29,926 | — | — | — | — | 29,926 |
| Other non-current assets | — | — | 2,659 | — | 1,185 | — | — | 3,844 |
| **Total non-current assets** | 8,214,867 | 369,978 | 1,717,456 | 372,508 | 2,147,234 | 26,187 | (1,535,213) | 11,313,017 |
| **Total assets** | 12,686,504 | 960,863 | 3,585,476 | 643,509 | 2,631,449 | 540,357 | (2,242,095) | 18,806,063 |
| **Liabilities and shareholders' equity** | | | | | | | | |
| **Current liabilities:** | | | | | | | | |
| Trade accounts payable | 216,454 | 116,681 | 620,668 | 23,823 | 60,712 | — | — | 1,038,338 |
| Bank customer accounts | — | — | — | — | — | 396,176 | (365,033) | 31,143 |
| Amounts payable to related parties | 73,372 | 17,303 | 36,651 | 21,460 | 13,900 | 74,623 | (66,886) | 170,423 |
| Short-term debt finance | 393,184 | 10,024 | 414,480 | 18,999 | 99,606 | 17,755 | — | 954,048 |
| Income taxes payable | 28,880 | — | 8,921 | 15 | 6,506 | — | — | 44,322 |
| Other taxes and social security payable | 38,506 | 2,357 | 85,952 | 3,127 | 69,851 | 5 | — | 199,798 |
| Dividends payable | 23,243 | — | — | — | — | — | — | 23,243 |
| Other current liabilities | 286,672 | 21,672 | 96,461 | 35,320 | 53,911 | 186 | — | 494,222 |
| **Total current liabilities** | 1,060,311 | 168,037 | 1,263,133 | 102,744 | 304,486 | 488,745 | (431,919) | 2,955,537 |
| **Non-current liabilities:** | | | | | | | | |
| Long-term debt finance | 1,222,147 | 138,404 | 605,827 | 55,423 | 242,470 | 23 | (216,259) | 2,048,035 |
| Deferred tax liabilities | 936,255 | 77,730 | 89,662 | 43,364 | 248,770 | 1,152 | (15,148) | 1,381,785 |
| Retirement benefit liability | 133,854 | 43,574 | 167,855 | 24,615 | 73,056 | — | — | 442,954 |
| Liabilities related to assets held for sale | — | — | 1,792 | — | — | — | — | 1,792 |
| Other non-current liabilities | 218 | 4,307 | 93,883 | — | 199,693 | — | — | 298,101 |
| **Total non-current liabilities** | 2,292,474 | 264,015 | 959,019 | 123,402 | 763,989 | 1,175 | (231,407) | 4,172,667 |
| **Equity** | 9,333,719 | 528,811 | 1,363,324 | 417,363 | 1,562,974 | 50,437 | (1,578,769) | 11,677,859 |
| **Total equity and liabilities** | 12,686,504 | 960,863 | 3,585,476 | 643,509 | 2,631,449 | 540,357 | (2,242,095) | 18,806,063 |

***(Tabular amounts expressed in thousands of US dollars)***

Segmental balance sheets as at December 31, 2005:

| | Russian Steel segment | Severstal North America | Lucchini segment | Metalware segment | Mining segment | Financing segment | Inter segment balances | Consolidated |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| **Current assets:** | | | | | | | | |
| Cash and cash equivalents | 784,676 | — | 384,624 | 3,921 | 67,316 | 143,246 | (56,353) | 1,327,430 |
| Short-term bank deposits | 718,705 | — | — | 18,274 | 1,071 | — | (63,538) | 674,512 |
| Short-term financial investments | 263,072 | — | 7,935 | 15,619 | 25,922 | 143,999 | (188,696) | 267,851 |
| Trade accounts receivable | 274,020 | 166,541 | 676,208 | 27,652 | 29,252 | — | — | 1,173,673 |
| Amounts receivable from related parties | 205,092 | 970 | 15,035 | 9,411 | 129,276 | — | (186,262) | 173,522 |
| Inventories | 579,076 | 401,146 | 633,068 | 59,457 | 103,876 | — | (52,891) | 1,723,732 |
| VAT receivable | 317,262 | — | 50,540 | 33,797 | 39,755 | — | — | 441,354 |
| Income tax receivable | 757 | — | 11,097 | 914 | 15,803 | — | — | 28,571 |
| Other current assets | 98,557 | 22,964 | 22,824 | 8,041 | 23,536 | 5,186 | — | 181,108 |
| **Total current assets** | 3,241,217 | 591,621 | 1,801,331 | 177,086 | 435,807 | 292,431 | (547,740) | 5,991,753 |
| **Non-current assets:** | | | | | | | | |
| Intangible assets | 5,731 | — | 19,787 | 1,418 | 29,537 | 50 | — | 56,523 |
| Property, plant and equipment | 5,810,984 | 83,863 | 1,376,460 | 111,734 | 1,462,571 | 391 | — | 8,846,003 |
| Investment in associates | 63,209 | 142,988 | 2,335 | 2,120 | — | — | — | 210,652 |
| Long-term financial investments | 1,271,105 | — | 31,645 | 7,601 | 3,855 | — | (1,224,665) | 89,541 |
| Amounts receivable from related parties | — | — | 13,069 | — | 22,026 | — | — | 35,095 |
| Assets held for sale | — | — | 66,117 | — | — | — | — | 66,117 |
| Deferred tax assets | — | — | 35,076 | — | — | — | — | 35,076 |
| Other non-current assets | — | — | 2,582 | — | 523 | — | — | 3,105 |
| **Total non-current assets** | 7,151,029 | 226,851 | 1,547,071 | 122,873 | 1,518,512 | 441 | (1,224,665) | 9,342,112 |
| **Total assets** | 10,392,246 | 818,472 | 3,348,402 | 299,959 | 1,954,319 | 292,872 | (1,772,405) | 15,333,865 |
| **Liabilities and shareholders' equity** | | | | | | | | |
| **Current liabilities:** | | | | | | | | |
| Trade accounts payable | 197,978 | 129,040 | 496,110 | 7,354 | 34,633 | — | 1,231 | 866,346 |
| Bank customer accounts | — | — | — | — | — | 218,673 | (119,806) | 98,867 |
| Amounts payable to related parties | 390,248 | 14,149 | 21,504 | 10,610 | 138,590 | 33,725 | (122,099) | 486,727 |
| Income taxes payable | 30,075 | 14,183 | 40,701 | 104 | 938 | — | — | 86,001 |
| Other taxes and social security payable | 23,054 | 1,681 | 106,584 | 16,063 | 110,063 | — | — | 257,445 |
| Short-term debt finance | 244,708 | 143,818 | 646,803 | 20,560 | 83,511 | — | (146,788) | 992,612 |
| Dividends payable | 12,275 | — | — | — | — | — | — | 12,275 |
| Other current liabilities | 163,370 | 22,169 | 114,635 | 10,587 | 50,384 | 100 | — | 361,245 |
| **Total current liabilities** | 1,061,708 | 325,040 | 1,426,337 | 65,278 | 418,119 | 252,498 | (387,462) | 3,161,518 |
| **Non-current liabilities:** | | | | | | | | |
| Long-term debt finance | 1,430,488 | — | 490,391 | 4,483 | 60,442 | — | (54,110) | 1,931,694 |
| Deferred tax liabilities | 909,382 | 62,508 | 91,107 | 8,462 | 149,130 | 466 | (14,975) | 1,206,080 |
| Retirement benefit liability | 79,034 | 38,888 | 135,029 | 21,354 | 64,181 | — | — | 338,486 |
| Liabilities related to assets held for sale | — | — | 172 | — | — | — | — | 172 |
| Other non-current liabilities | 75 | 6,452 | 90,795 | — | 201,489 | — | — | 298,811 |
| **Total non-current liabilities** | 2,418,979 | 107,848 | 807,494 | 34,299 | 475,242 | 466 | (69,085) | 3,775,243 |
| **Equity** | 6,911,559 | 385,584 | 1,114,571 | 200,382 | 1,060,958 | 39,908 | (1,315,858) | 8,397,104 |
| **Total equity and liabilities** | 10,392,246 | 818,472 | 3,348,402 | 299,959 | 1,954,319 | 292,872 | (1,772,405) | 15,333,865 |

## 32. Commitments and contingencies

### a. For litigation, tax and other liabilities

The taxation system and regulatory environment of the Russian Federation are relatively new and characterized by numerous taxes and frequently changing legislation, which is often unclear, contradictory and subject to varying interpretations between the differing regulatory authorities and jurisdictions, who are empowered to impose significant fines, penalties and interest charges. Events during the recent years suggest that the regulatory authorities within the Russian Federation are adopting a more assertive stance regarding the interpretation and enforcement of legislation. This situation creates substantial tax and regulatory risks. Management believes that it has complied in all material respects with all relevant legislation.

At the balance sheet date, the Russian tax authorities had made claims for taxes, fines and penalties in the amount of approximately US$ 60 million, mostly related to mineral extraction tax and water usage tax by certain of the Group's entities in the Mining segment. Management does not agree with the tax authorities' claims and believes that the Group has complied with existing legislation in all material respects. Management is unable to assess the ultimate outcome of the claims and the outflow of financial sources to settle such claims, if any. Management believes that it has made adequate provisions for other possible tax claims.

### b. Long term purchase and sales contracts

In the normal course of business group companies enter into long term purchase contracts for raw materials, and long term sales contracts. These contracts allow for periodic adjustments in prices dependent on prevailing market conditions.

### c. Capital commitments

At the balance sheet date the Group had contractual capital commitments of US$ 291.1 million (December 31, 2005: US$ 435.4 million).

### d. Insurance

The Group has insured its property and equipment to compensate for expenses arising from accidents. In addition, the Group has insurance for business interruption on a basis of reimbursement of certain fixed costs. The Group has also insured third party liability in respect of property or environmental damage. However, the Group does not have a full insurance coverage.

### e. Guarantees

At the balance sheet date the Group had US$ 22.2 million (December 31, 2005: US$ 23.8 million) of guarantees issued.

## 33. Financial instruments

Exposure to credit, liquidity, interest rate and currency risk arises in the normal course of the Group's business. The Russian Steel, Metalware and Mining segments of the Group have not used derivative financial instruments to reduce exposure to fluctuations in foreign exchange rates and interest rates. The use of Severstal North America and Lucchini segments of derivatives to hedge their interest rates, commodity inputs and foreign exchange rate exposures were not material to these consolidated financial statements. As at December 31, 2006 and December 31, 2005, the Financing segment had no outstanding foreign exchange contracts.

(Tabular amounts expressed in thousands of US dollars)

Management believes that the fair value of its financial assets and liabilities approximates their carrying amounts except for the following long-term fixed rate borrowings:

| | December 31, 2006 | | |
|---|---|---|---|
| | Market value | Book value | Difference |
| Citibank CLN — Eurobonds 2009 | 337,857 | 325,000 | 12,857 |
| Citibank CLN — Eurobonds 2014 | 407,616 | 375,000 | 32,616 |
| | 745,473 | 700,000 | 45,473 |

| | December 31, 2005 | | |
|---|---|---|---|
| | Market value | Book value | Difference |
| Citibank CLN — Eurobonds 2009 | 336,830 | 325,000 | 11,830 |
| Citibank CLN — Eurobonds 2014 | 407,438 | 375,000 | 32,438 |
| Other bonds | 225,552 | 223,216 | 2,336 |
| | 969,820 | 923,216 | 46,604 |

The above amounts exclude accrued interest.

### *Credit risk*

The maximum exposure to credit risk is represented by the carrying amount of each financial asset in the balance sheet and guarantees (see note 32e). The Group has developed policies and procedures for the management of credit exposures, including the establishment of credit committees that actively monitors credit risk. At the balance sheet date there was a significant concentration of credit risk in respect of trade accounts receivable from related parties and originated loans to related parties.

### *Liquidity risk*

The Group maintains liquidity management with the objective of ensuring that funds will be available at all times to honour all cash flow obligations as they become due.

### *Foreign exchange rate risk*

The Group incurs currency risk when an entity enters into transactions and balances not denominated in its functional currency. The Group has assets and liabilities denominated in several foreign currencies. Foreign currency risk arises when the actual or forecasted assets in a foreign currency are either greater or less than the liabilities in that currency.

### *Interest rate risk*

Interest rates on the Group's debt finance are either fixed or variable, at a fixed spread over LIBOR or Euribor for the duration of each contract. Changes in interest rates impact primarily loans and borrowings by changing either their fair value (fixed rate debt) or their future cash flows (variable rate debt). Management does not have a formal policy of determining how much of the Group's exposure should be to fixed or variable rates. However, at the time of raising new loans or borrowings management uses its judgment to decide whether it believes that a fixed or variable rate would be more favourable to the over the expected period until maturity.

***(Tabular amounts expressed in thousands of US dollars)***

The following table indicates weighted average effective interest rates of income-earning financial assets and interest-bearing financial liabilities at the balance sheet dates:

| | Rouble | US dollar | Euro |
|---|---|---|---|
| **As at December 31, 2006:** | | | |
| **Interest bearing assets** | | | |
| Short term bank deposits | 6.7% | 6.1% | 3.9% |
| Placements at financial institutions | 4.8% | 5.2% | 3.3% |
| Loans to bank customers | 9.9% | 11.5% | — |
| Held-for-trading securities | 6.0% | — | — |
| Loans | 10.6% | 15.0% | — |
| **Interest bearing liabilities** | | | |
| Bank customer accounts | 3.9% | 4.7% | 2.2% |
| Bank loans and issued bonds | 10.8% | 8.2% | 4.8% |

| | Rouble | US dollar | Euro |
|---|---|---|---|
| **As at December 31, 2005:** | | | |
| **Interest bearing assets** | | | |
| Short term bank deposits | 5.9% | 5.2% | — |
| Placements at financial institutions | 6.2% | 2.4% | 2.2% |
| Loans to bank customers | 8.8% | 11.2% | — |
| Held-for-trading securities | 6.2% | — | — |
| Loans | 9.9% | 7.9% | 3.9% |
| **Interest bearing liabilities** | | | |
| Bank customer accounts | 4.3% | 1.9% | 1.3% |
| Bank loans and issued bonds | 9.9% | 8.0% | 4.9% |

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