Polyus Gold International Limited

**Interim financial report   
for the six months ended 30 June 2012**

Polyus Gold International Limited

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HIGHLIGHTS

**Financial highlights**

* Gold sales up by 36% to USD1.2 billion, reflecting increased sales volumes and higher gold price (H1 2011: USD0.9 billion);
* Total cash costs per ounce rose by 8% to USD664 per troy ounce, a significant decrease in cost growth compared to previous periods;
* EBITDA reached USD634 million, a 59% increase, while EBITDA margin increased from 43% in H1 2011 to 51%;
* Profit for the period more than doubled to USD426 million (H1 2011: USD207 million);
* EPS grew 133% to 14 US cents (H1 2011: 6 US cents); and
* Net cash position of USD532 million compared to net debt position of USD102 million at the end of 2011.

**Financial results for the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended   
31 December 2011**

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD’000, unless specified otherwise | 2012 |  | 2011 |  | p-o-p(1) |  | 2011 |
|  |  |  |  |  |  |  |  |
| Revenues from gold sales | 1,223,866 |  | 901,752 |  | 36 |  | 2,340,650 |
| Operating profit | 534,293 |  | 279,631 |  | 91 |  | 838,654 |
| Operating profit margin**(**2**)** | 43% |  | 30% |  | - |  | 35% |
| Profit for the period | 425,896 |  | 206,800 |  | 106 |  | 558,015 |
| Earnings per share – basic and diluted (US Cents) | 14 |  | 6 |  | 133 |  | 16 |
| Weighted average number of ordinary shares (‘000s) **(2)** | 2,868,789 |  | 3,082,656 |  | (7) |  | 2,960,311 |
| Capital expenditures | 330,242 |  | 181,130 |  | 82 |  | 327,843 |
| Gold production (‘000oz) | 721 |  | 611 |  | 18 |  | 1,497 |
| Gold sold (‘000oz) | 742 |  | 629 |  | 18 |  | 1,483 |
| Average realised gold price (USD/oz) | 1,649 |  | 1,433 |  | 15 |  | 1,578 |
| Adjusted EBITDA | 634,275 |  | 398,644 |  | 59 |  | 1,110,745 |
| Adjusted EBITDA margin**(**3**) (**4**)** | 51% |  | 43% |  | - |  | 46% |
| Total cash cost per ounce sold (USD/oz) | 664 |  | 616 |  | 8 |  | 661 |

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1. P-o-p – period-on-period.
2. The weighted average number of shares for the six months ended 30 June 2011 changed from 2,498,941 thousand to 3,082,656 thousand shares following the completion of the reverse takeover procedures. EPS changed from 8 to 6 US Cents per share, correspondently.
3. Calculation may not be precise due to rounding.
4. For details of the calculation of Adjusted EBITDA refer to section 2.1 of the Interim Financial Report.

**Net debt position**

|  |  |  |  |
| --- | --- | --- | --- |
| USD’000 | As at  30 June  2012 |  | As at  31 December  2011 |
|  |  |  |  |
| Net debt (cash and bank deposits) | (531,949) |  | 101,881 |

**Operational highlights and development projects**

Refined gold production up by 18% to 721 thousand ounces (H1 2011: 611 thousand ounces), mainly as   
a result of:

* 28% increase in gold output at Olimpiada due to continuous improvement in recovery rates;
* Significant increase in gold production at Blagodatnoye (+14%) and Kuranakh (+28%) on the back of sustained strong recovery rates and higher processing volumes; and
* The commissioning of the Verninskoye mine.

Capital expenditure increased 82% to USD330 million, with major investments into:

* Commissioning of the full flow sheet at Verninskoye;
* Processing optimisation at Olimpiada; and
* Construction of the Natalka mine.

Construction at Natalka is well underway with the commissioning of a 10 million tonnes of ore per year processing plant expected in December 2013. The first mining equipment and machinery has started to arrive on site. On 30 July 2012 the Company entered into a finance agreement with VTB Bank for a total amount of up to 5 billion roubles (approximately USD150 million). The VTB facility will be used to support the purchase of equipment for the Natalka project.

**Corporate update**

* On 11 May 2012 Polyus Gold International Limited completed the sale of 151,607,496 treasury shares, representing 5% less one share of the Company’s issued share capital, to Chengdong Investment Corporation, a wholly-owned subsidiary of CIC International Co. Ltd., and of 50,198,271 treasury shares and 25,153,897 Level I GDRs, representing 2.50% of the Company's issued share capital, to JSC VTB Bank. The gross proceeds received from the two transactions totalled USD635.5 million.
* On 21 May 2012 Polyus Gold International Limited sold its 100% interest in Romaltyn Limited and Romaltyn Exploration for a total consideration of USD20 million.
* On 19 June 2012 Polyus Gold International Limited’s entire issued ordinary share capital was admitted to the Premium segment of the Official List maintained by the UK Listing Authority and to trading on the London Stock Exchange’s main market for listed securities. The Company’s TIDM code on the London Stock Exchange has been changed to PGIL.

chief executive officer’S statement

**German Pikhoya, CEO of Polyus Gold International Limited, commented:**

“We are delighted to announce record profits of USD426 million in our first half yearly results since joining the Premium List of the London Stock Exchange.

The growth reflects both the operational improvements at our mines and the strong market environment for gold. Importantly, while maintaining our sector-leading rate of production growth, we were also able to control cost pressures. As a result, we have seen further improvement in margins.

Due to strong operating cash inflow and a successful placement of the treasury block of shares, our cash and cash equivalents reached USD848 million implying a significant net cash position compared to a net debt position six months earlier.

In the second half of 2012, we will continue our focus on further improving performance across a range of our projects.”

Interim management report for the six months ended 30 June 2012

The Group is an international gold mining company and the largest gold producer in Russia, according to the Russian Union of Gold Miners. The Group develops and mines hardrock gold and alluvial gold deposits, with operations in the Krasnoyarsk, Irkutsk, Magadan and Republic of Sakha (Yakutia) regions of Russia and in the Republic of Kazakhstan. In 2011, the Group produced 1,495 thousand troy ounces of gold, and   
721 thousand troy ounces of gold for the six months ended 30 June 2012.

The Group was formed as a result of the reorganisation of the OJSC Polyus Gold Group (the “Polyus Russia Group”) and its subsidiaries and KazakhGold Group Limited and its subsidiaries which resulted in KazakhGold Group Limited becoming the legal parent of OJSC Polyus Gold. Following the completion of the reorganization, KazakhGold Group Limited was renamed Polyus Gold International Limited (the “PGIL Group”). As a result, references in this report to the “Group” are to the Polyus Russia Group, including the KazakhGold Group.

**Cautionary statement**

This Interim Management Report (IMR) has been prepared solely to provide additional information to shareholders to assess the Group’s strategies. The IMR should not be relied on by any other party or for any other purpose.

The IMR contains certain forward-looking statements. These statements are made by the directors in good faith based on the information available to them up to the time of their approval of this report but such statements should be treated with caution due to the inherent uncertainties, including risk factors, underlying any such forward-looking statement. The IMR represents management’s opinion in relation to the Group’s operating and financial results.

# THE GROUP’S OPERATING RESULTS

## 1.1 External market factors affecting the Group’s financial results

The Group’s results are significantly affected by movements in currency exchange rates (principally the US dollar/rouble rate), and the prices of commodities such as gold, oil and steel.

Average rates for these main external market factors for the 6 months ended 30 June 2012 and   
30 June 2011, and for the year ended 31 December 2011were:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| Average price/ rate | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| London p.m.gold fixing price (USD per troy ounce)(1) | 1,651 |  | 1,445 |  | 14 |  | 1,572 |
| Oil (Brent brand) (USD per barrel)(2) | 114 |  | 111 |  | 2 |  | 111 |
| Steel (hot rolled) (USD per tonne)(3) | 668 |  | 722 |  | (7) |  | 726 |
| Average RUB/USD rate(4) | 30.64 |  | 28.62 |  | 7 |  | 29.39 |
| Period end RUB/USD rate | 32.82 |  | 28.08 |  | 17 |  | 32.20 |
| Average KZT/USD rate(5) | 148.15 |  | 146.00 |  | 1 |  | 146.62 |
| Period end KZT/USD rate | 149.42 |  | 146.25 |  | 2 |  | 148.40 |

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1. Source: London Bullion Market Association.
2. Source: Bloomberg.
3. Source: Steel Business Briefing.
4. Source: The Central Bank of Russia.
5. Source: The National Bank of Kazakhstan.

### Gold prices

The market price of gold is the most significant factor influencing the profitability and operating cash flow generation of the Group. The global gold price is subject to volatile movements over short periods of time. In the six months ended 30 June 2012, the average gold p.m. fixing price in London was USD 1,651.3 per ounce, with gold reaching its lowest level of USD 1,540.0 per ounce on 30 May 2012 and a high of USD 1,781.0 on 28 February 2012.

### Oil, oil products and steel prices

A significant portion of costs included in the Group's cost of sales are directly or indirectly impacted by the prices of oil and steel. Changes in oil prices impact the prices of heating oil, diesel fuel, gasoline and lubricants for mining and construction equipment. However, in Russia the impact on oil prices could be offset or enhanced by excise duty policy of the government. For example excise duty rate for diesel fuel increased in average 54% p-o-p (H1 2011 to H1 2012) and excise duty rate for gasoline increased in average 31% p-o-p. Steel forms the basis for the price of all rolled metal products, pipes, machinery and vehicles. In the reporting period average oil prices increased 2% in comparison with the first half of 2011. The price of oil products in Russia increased between 0% and 60%. Average steel prices decreased by 7% over the same period.

### Exchange rates

The Group's revenue from gold sales is denominated in US dollars, whereas most of the Group’s operating expenses are denominated in Russian roubles (“RUB”). Accordingly, an appreciation of the Russian rouble against the US dollar may negatively affect the Group’s margins by increasing the US dollar value of its RUB-denominated costs. Conversely, an appreciation of the US dollar against the Russian rouble may positively affect the Group’s margins by decreasing the US dollar value of its rouble-denominated costs. In the first six months of 2012 the average RUB/USD exchange rate increased to RUB 30.64 per US dollar from 28.62 in the first half of 2011. This contributed to a potential decrease in USD terms during the first half of 2012 in comparison with the first half of 2011 for salaries and other expenses denominated in Russian roubles, due to the effect of translation to the USD presentation currency. The increase in the closing rate to RUB 32.82 per USD (31 December 2011: 32.20) led to a decrease in the statement of financial position items in USD terms.

The Group is also exposed to KZT/USD exchange rate movements since the operating expenses of PGIL’s mining operations in Kazakhstan are incurred primarily in tenge.

## Summary of performance results

The following table shows the summary of performance results for the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD’000, unless specified otherwise(1) | Note | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |  |
| **Gold sales** | **1.2** | **1,223,866** |  | **901,752** |  | 36 |  | **2,340,650** |
| Other sales | 1.2 | 29,054 |  | 29,007 |  | 0 |  | 62,060 |
| **Total revenue** |  | **1,252,920** |  | **930,759** |  | **35** |  | **2,402,710** |
|  |  |  |  |  |  |  |  |  |
| Cost of gold sales | 1.3 | (569,030) |  | (478,053) |  | 19 |  | (1,162,019) |
| Cost of other sales | 1.3 | (21,232) |  | (23,223) |  | (9) |  | (46,343) |
| **Gross profit** |  | **662,658** |  | **429,483** |  | **54** |  | **1,194,348** |
| including: |  |  |  |  |  |  |  |  |
| Gross profit on gold sales |  | 654,836 |  | 423,699 |  | 55 |  | 1,178,631, |
|  |  |  |  |  |  |  |  |  |
| *Gross profit margin* |  | *53%* |  | *46%* |  | *-* |  | *50%* |
|  |  |  |  |  |  |  |  |  |
| Selling, general and administrative expenses | 1.4 | (110,240) |  | (93,462) |  | 18 |  | (225,618) |
| Impairment | 1.5 | (17,559) |  | (48,625) |  | (64) |  | (103,418) |
| Gain on disposal of subsidiaries | 1.6 | 6,268 |  | - |  | - |  | - |
| Research expenses |  | (1,284) |  | (1,255) |  | 2 |  | (2,581) |
| Other expenses, net |  | (5,550) |  | (6,510) |  | (15) |  | (24,077) |
| **Operating profit** |  | **534,293** |  | **279,631** |  | **91** |  | **838,654** |
|  |  |  |  |  |  |  |  |  |
| *Operating profit margin* |  | *43%* |  | *30%* |  | *-* |  | *35%* |
|  |  |  |  |  |  |  |  |  |
| Finance costs | 1.7 | (22,489) |  | (22,712) |  | (1) |  | (71,403) |
| Income from investments (net) | 1.8 | 19,540 |  | 8,232 |  | 137 |  | 3,630 |
| Foreign exchange (loss)/gain |  | 7,578 |  | 2,049 |  | 270 |  | (5,814) |
| **Profit before income tax** |  | **538,922** |  | **267,200** |  | **102** |  | **765,067** |
|  |  |  |  |  |  |  |  |  |
| Pre-tax margin**(**1**)** |  | *43%* |  | *29%* |  | *-* |  | *32%* |
|  |  |  |  |  |  |  |  |  |
| Income tax expense | 1.9 | (113,026) |  | (60,400) |  | 87 |  | (207,052) |
|  |  |  |  |  |  |  |  |  |
| **Profit for the period/year** |  | **425,896** |  | **206,800** |  | **106** |  | **558,015** |
| attributable to: |  |  |  |  |  |  |  |  |
| -Shareholders of the parent company |  | 389,315 |  | 188,847 |  | 106 |  | 468,998 |
| -Non-controlling interest |  | 36,581 |  | 17,953 |  | 104 |  | 89,017 |
|  |  |  |  |  |  |  |  |  |
| *Profit for the period margin* |  | *34%* |  | *22%* |  | *-* |  | *23%* |
| Earnings per share – basic and diluted (US cents) (2) |  | **14** |  | **6** |  | **133** |  | **16** |

The following table shows key performance indicators of the Group’s operations for the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended 31 December 2011 expressed in non-GAAP financial measures:

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD’000, unless specified otherwise | Note | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |  |
| **Adjusted EBITDA(3)** | **3.1** | **634,275** |  | **398,644** |  | **59** |  | **1,110,745** |
| *Adjusted EBITDA margin* |  | *51%* |  | *43%* |  | *-* |  | *46%* |

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1. Calculation may not be precise due to rounding.
2. The weighted average number of shares for the six months ended 30 June 2011 changed from   
   2,498,941 thousand to 3,082,656 thousand shares following the completion of the reverse takeover procedures. EPS changed from 8 to 6 US Cents per share, correspondently.
3. For details of the calculation of Adjusted EBITDA refer to section 2.1 of this document.

## 1.2 Gold sales

The following table shows the results and breakdown of the Group’s gold sales for the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
|  | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Gold sales (USD thousands) | 1,223,866 |  | 901,752 |  | 36 |  | 2,340,650 |
| Gold sales (thousand troy ounces) | 742 |  | 629 |  | 18 |  | 1,483 |
| In the domestic market (thousand troy ounces)(1) | 686 |  | 566 |  | 21 |  | 1,373 |
| In the domestic market (%) | 92 |  | 90 |  | 3 |  | 93 |
| For export (thousand troy ounces) (2) | 56 |  | 63 |  | (11) |  | 110 |
| Weighted-average realised gold price (USD per troy ounce) | 1,649 |  | 1,433 |  | 15 |  | 1,578 |
| London p.m.gold fixing price (USD per troy ounce)(3) | 1,651 |  | 1,445 |  | 14 |  | 1,571 |
| (Deficit)/excess of average realised price (under)/over average p.m. (4) fixing price (USD per troy ounce) | (2) |  | (11) |  | (78) |  | 6.7 |

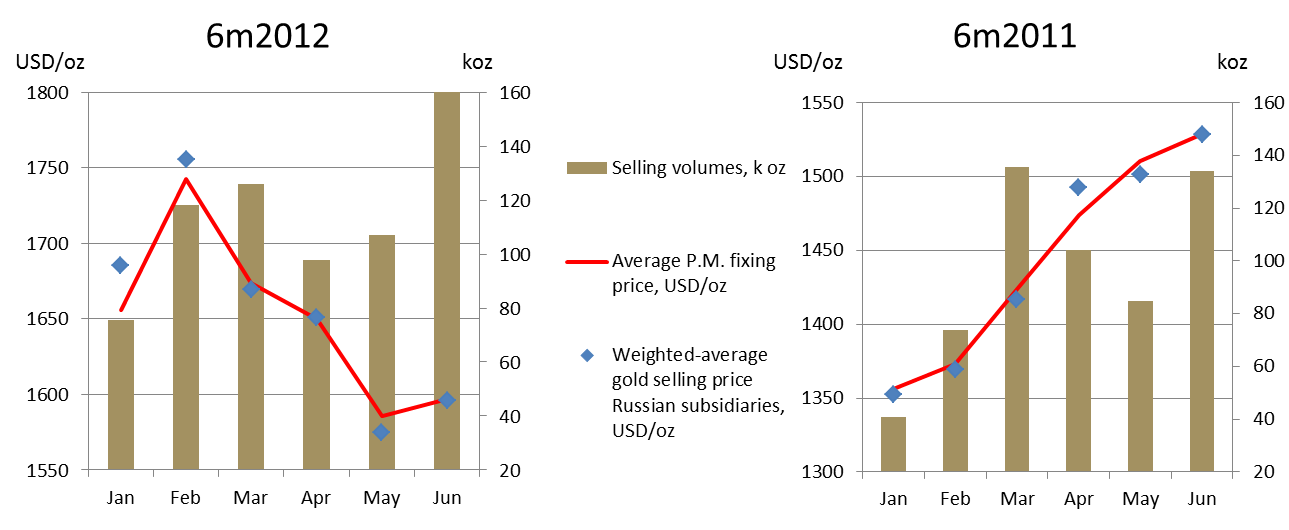
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1. Sales on the domestic market comprise of sales by the Group’s Russian subsidiaries on the Russian market.
2. Export sales comprise sales by the Kazakhstan business unit to foreign customers.
3. Source: London Bullion Market Association.
4. Calculation may not be precise due to rounding.

In the first six months of 2012, the Group’s gold sales amounted to USD1,223,866 thousand, showing an increase of 36% compared to the first six months of 2011.The increase in gold sales resulted from a combination of higher realised gold prices and increased sales volumes.

In H1 2012, the weighted-average realised gold price was USD1,649 per troy ounce, a 15% increase compared to the same period of 2011. This was just USD2 per ounce lower than the p.m. gold fixing price on the London market, as high volumes of gold were sold in February and June at a price slightly higher than the average fixing (see graph below). Therefore, the weighted-average realised gold price for refined gold sold by the Group’s Russian subsidiaries amounted to USD1,652 per ounce in H1 2012. However, this was partly offset by the impact of the Kazakhstan business unit which sells semi-products at a considerable discount to the London fixing price. In the first half of 2011, the weighted-average realised gold price was USD11 per ounce lower than the average p.m. gold fixing price due to the impact of the sale of semi-products by the Kazakhstan business unit at a considerable discount to the London fixing price, as well as the fact that in March 2011 high volumes of gold were sold at a price lower than the average p.m. fixing (see graph below).

Graph 1. Gold sales and selling price in the 6 months ended 30 June 2012 and 30 June 2011.



The sales volumes in H1 2012 were 742 thousand troy ounces, including 56 thousand ounces sold for export by the Kazakhstan business unit. The comparable sales volumes in the first half of 2011 were 629 thousand troy ounces and 63 thousand troy ounces, respectively. In the first six months of 2012 the Group produced 721 thousand ounces of gold, compared to 611 thousand ounces in the same period of the previous year.[[1]](#footnote-1)1 This 18% increase in production is primarily a result of successful work at four mines:

* The Olimpiada mine. 71 koz growth p-o-p. Successful implementation of the Group’s production optimisation programme resulted in higher recovery rate (76% vs 71% in H1 2011);
* The Blagodatnoye mine. 22 koz growth p-o-p. Continuing ramp-up and improvement in recovery rate;
* The Verninskoye mine. 18 koz growth p-o-p. New mine commissioned in December 2011 (8 koz growth p-o-p for the Irkutsk ore business unit due to the suspension of operations at the Zapadnoye mine); and
* The Kuranakh mine. 15 koz growth p-o-p. Growth in processing and mining volumes due to enhanced planning, growth in recovery rate.

This was offset by a decrease in production at the Kazakhstan business unit (6 koz decrease p-o-p) and Irkutsk alluvial business unit (1 koz decrease p-o-p).

### Other sales

Revenue from the sale of products other than gold and services (includes sales of electricity, rent services sales, revenue from transportation, handling and storage services, exploration services, and other sales) has not changed significantly in the first six months of 2012 and amounted to USD29,054 thousand compared to USD29,007 thousand in H1 2011. However, there were changes in components of other sales. USD denominated rent service sales and exploration service sales decreased 68% and 72% respectively. USD denominated electricity sales increased 30%, driven mostly by increased re-sales of electricity purchased from third parties (rate of power generation at the Mamakan hydro-power plant has not changed p-o-p). Before 2011 electricity tariffs were state-regulated.

In 2011 the pricing process was deregulated and tariffs were determined by supply and demand in the electricity market. This led to a substantial increase in electricity tariffs and consequently to higher revenue from sales of electricity received by the Group.

Other sales are mostly denominated in roubles, and in rouble terms increased by 6% on p-o-p basis, however this increase was offset by RUB depreciation.

## 1.3 Cost of gold sales

The following table shows the results of the Group’s cost of gold sales for the 6 months ended   
30 June 2012 and 30 June 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| USD‘000 | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
|  | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Fuel, consumables and spares, out of which: | 232,550 |  | 194,171 |  | 20 |  | 410,243 |
| *Materials and spares* | *165,260* |  | *139,484* |  | *18* |  | *296,442* |
| *Fuel* | *67,290* |  | *54,687* |  | *23* |  | *113,801* |
| Labour | 157,860 |  | 122,268 |  | 29 |  | 288,866 |
| Tax on mining | 90,842 |  | 71,393 |  | 27 |  | 179,116 |
| Utilities, out of which: | 28,288 |  | 29,595 |  | (4) |  | 55,140 |
| *Power* | *27,407* |  | *28,996* |  | *(5)* |  | *53,092* |
| *Other* | *881* |  | *599* |  | *47* |  | *2,048* |
| Outsourced mining services | 7,099 |  | 3,374 |  | 110 |  | 22,147 |
| Refining costs | 2,458 |  | 1,926 |  | 28 |  | 5,067 |
| Others | 42,417 |  | 26,481 |  | 60 |  | 75,696 |
| **Cash operating costs** | **561,514** |  | **449,208** |  | 25 |  | **1,036,275** |
| Amortisation and depreciation of operating assets | 84,137 |  | 89,847 |  | (6) |  | 181,935 |
| Deferred stripping costs (capitalised)/ expensed | (2,343) |  | 17,136 |  | (114) |  | (7,335) |
| **Total cost of production** | **643,308** |  | **556,191** |  | **16** |  | **1,210.875** |
| Increase in gold-in-process and refined gold | (74,278) |  | (78,138) |  | (5) |  | (48,856) |
|  |  |  |  |  |  |  |  |
| **Cost of gold sales** | **569,030** |  | **478,053** |  | 19 |  | **1,162,019** |

The cost of gold sales increased from USD478,053 thousand in the first half of 2011 to USD569,030 thousand in the first half of 2012. This 19% increase resulted mainly from an 18% increase in the volume of gold sales, the growth in consumption of materials and spares, higher labour costs, an increase of mining tax charges in line with the gold price dynamics and growth in sundry costs.

#### Fuel, consumables and spares

Consumables and spares comprised 41% of cash operating costs in the first half of 2012 (43% in   
H1 2011). These include materials and spares (spare parts for trucks, excavators and for construction machinery, expenses on rolled metal products and cables, technological materials for plants, chemicals and other materials and spare parts used during the mining, concentration and smelting) and fuel.

### Materials and spares

The cost of materials and spares consumed in the first half of 2012 amounted to USD165,260 thousand, an increase of 18% compared with the same period in the previous year. All of the Group’s business units incurred increased expenses for the purchase of grinding balls, spare parts, tyres and chemical products. The increase in costs for materials and spares was largely driven by the increase in purchase price (ex: the average price for cyanides increased 28% p-o-p) and, in some cases by the growth in consumption.

* The Krasnoyarsk business unit: requirements for spare parts for the mining fleet increased due to higher volumes of ore mining (17% increase) and advanced growth in volumes of rock moved (stripping ratio increased from 2.00 m3/t to 2.17 m3/t). To maintain this level of mining the Group intensified drilling and blasting operations at the Vostochnyi pit and Blagodatnyi pit, which resulted in a higher consumption of explosives. Consumption of reagents, cyanides and other chemicals also increased due to overall increase in volumes of ore processing (for example consumption of cyanides increased from 8.1 tonnes in H1 2011 to 8.3 tonnes in H1 2012).
* The Irkutsk alluvial business unit: 17% increase in cost of materials and spare parts relates to the purchase price growth. The earlier commencement of preparation and mining works by the alluvial enterprises required more explosives compared to the first half of 2011 (an increase in explosives consumption of 12%).
* The Yakutia Kuranakh business unit: Chemicals and reagents, spare parts and explosives being the three largest components of material expenses. Consumption of various chemicals, including cyanides, increased due to overall increase in volumes of ore processing (11% from 1,656 thousand tonnes in H1 2011 to 1,836 thousand tonnes in H1 2012). Cost for key production materials and spare parts for repair and maintenance works also increased due to the price growth. Explosives consumption significantly increased mainly due to intensified drilling and blasting operations followed by increased volumes of ore mining (the volume of fired rock increased 41% p-o-p).
* The Irkutsk ore business unit: Commissioning of the Verninskoye mine in December 2011 and further ramp-up of the operations during the H1 2012 resulted in a higher consumption of all materials and spares in comparison to the H1 2011.
* The Kazakhstan business unit: The business unit faced a reduction in ore mining and processing in line with the transition to underground mining along with open pit reserves depletion.   
  This resulted in just 9% p-o-p growth in costs for consumables and spares in comparison to 21% growth for the Group.

It is important to note that the growth in costs for materials and spares was almost in line with the growth in ore mining.

### Fuel

The cost of fuel, diesel oil and lubricants for trucks and excavators consumed during the first half of 2012 was USD67,290 thousand, an increase of 23% in comparison to the first half of 2011. The increase was higher than the average p-o-p growth in crude oil prices, which is explained by growth in prices for oil products, as well as by additional consumption, mainly as a result of diesel consumption by the Irkutsk ore business unit (in the Q1 2012 the Verninskoye mine had diesel power generation feed only, however in May 2012 the mine was connected to the federal power grid). Higher consumption of fuel in H1 2012 was experienced at the alluvial mines (due to early commissioning of operations), as well as the Yakutia Kuranakh business unit (freight turnover increased 46% p-o-p). The Krasnoyarsk business unit decreased consumption of fuel by volume primarily as a result of decrease in in-house generation and override to the acquisition of less expensive electricity from federal grids. In addition, load reduction at coal and diesel power stations at the Krasnoyarsk business unit resulted in higher efficiency of generation at these stations.

#### Labour

Labour costs comprised 28% of cash operating costs in the first six months of 2012. These costs increased by 29% to USD157,860 thousand, with the Krasnoyarsk and Irkutsk ore business units being the major contributors to the payroll cost growth. Also, in the beginning of 2012 the Group initiated indexation of salaries for operating employees. The average indexation level (payroll increase) was 6% varying from 3% in the Magadan business unit to 13% in the Krasnoyarsk business unit.

* The Krasnoyarsk business unit: An increase in labour expenses driven by salary indexation. This was partly offset by an 18% decrease in the average number of production personnel.
* The Irkutsk ore business unit: The average number of production personnel increased by 3%   
  p-o-p. The effect was enhanced by 9% salary indexation at the beginning of the year.
* The Irkutsk alluvial business unit: The alluvial mining and preparation season in 2012 started earlier than in 2011, which led to higher payroll costs (increase of 16% p-o-p).
* The Kazakhstan business unit: Payroll costs decreased due to 1) a decrease in the number of production personnel, 2) part of labour costs has been reclassified as change in inventory and capitalised. This however was partly offset by an increase in salaries during H12012 (overall 6% industry indexation according to the Federal Law).
* CJSC Polyus Logistics: Established in 2011 to provide transportation services to the Group’s subsidiaries. The average number of personnel increased from three employees as at 30 June 2011 to 1,639 employees as at 30 June 2012.

Also in the reporting period an additional bonus for the results performance in H1 2012 for operating personnel of the Krasnoyarsk and Yakutia Kuranakh business units, as well as for personnel of CJSC Polyus Logistics, has been accrued.

#### Tax on mining

In H1 2012, mining tax expenses represented 16% of cash operating costs. In the first half of 2012, the Group accrued USD90,842 thousand of tax on mining, compared to USD71,393 thousand in   
the same period of the previous year. The increase was driven by higher realised gold prices and enhanced sales volumes. The mining tax rates in Russia and Kazakhstan were established at 6% and 5%, respectively.

#### Utilities

Utilities expenses, comprising 5% of cash operating costs, decreased from USD29,595 thousand in the first half of 2011 to USD 28,288 thousand in the first half of 2012, mainly comprising power costs. There were no significant power tariff fluctuations on p-o-p basis. However, some changes in power consumption by business units within the Group occurred.

* The Krasnoyarsk business unit increased power consumption following increased mining and processing volumes and following decrease in in-house generation. Power costs increased 14% p-o-p in rouble terms.
* The Yakutia Kuranakh business unit also increased power costs (11% increase p-o-p) following 11% increase in ore processed.
* The Irkutsk alluvial business unit. Decrease in power costs (27% in rouble terms p-o-p) mainly due to changes in principles of pricing at electricity market in Russia driven by regulators.
* The Irkutsk ore business unit. No significant changes in consumption. Newly commissioned Verninskoye mine was supplied from diesel power stations, thus expenses were recognised as fuel costs.
* The Kazakhstan business unit. Mines in Kazakhstan decreased consumption of electricity due to slow down in production as well as due to more favourable weather conditions in H1 2012 compared to the H1 2011.

#### Outsourced mining services

Outsourced mining services relates mostly to the Irkutsk alluvial business unit. In H1 2012 expenses on these services increased 110% and reached USD 7,099 thousand, which reflects early commencement of the operational season.

#### Refining costs

Refining costs increased 28% to USD2,458 thousand due to the increase in volumes of Dore gold refined during H1 2012.

#### Others

Other costs in cost of gold sales increased 60% from USD26,481 thousand in H1 2011 to USD42,417 thousand in the reporting period. These costs consist of transport, rent, repair, maintenance, insurance, security, business trips, communication expenses and other. The increase mainly relates to the increase in transport expenses (85% growth p-o-p), repair and maintenance expenses growth and rent expenses growth.

#### Amortisation and depreciation of operating assets

Amortisation and depreciation of operating assets decreased 6% and amounted to USD84,137 thousand in the first half of 2012. In the period H2 2011 to H1 2012 the Group reviewed mine plans for Olimpiada (termination year changed from 2022 to 2024), Blagodatnoye (termination year changed from 2026 to 2032) and Titimukhta (termination year changed from 2022 to 2021). This resulted in depreciation period increase, and therefore decrease in amortisation accrued in each period. Depreciation of Kuranakh deposits also decreased as a result of increase in depreciation period and the mine life. Another factor which influenced amortisation decrease is rouble depreciation of 7% p-o-p.

#### Deferred stripping costs expensed

The Group’s accounting policy stipulates that stripping costs incurred in the period are deferred to the extent that the current period stripping ratio exceeds the expected life-of-mine ratio. If the current stripping ratio falls below the average life-of-mine stripping ratio, the stripping costs are charged to operating costs.

In the first half of 2012, the Group capitalised USD8,507 thousand of deferred stripping costs at Titimukhta and other deposits at the Yakutia Kuranakh business unit and expensed USD6,164 thousand of deferred stripping costs at the Olimpiada mine. This resulted in a decrease in capitalised deferred stripping costs by USD2,343. The stripping ratio at the Vostochnyi pit of the Olimpiada mine was higher than the average life-of-mine ratio and, therefore, stripping costs were written-off, which was partly offset by the capitalisation of the stripping costs incurred in H1 2012 at Titimukhta and some deposits at the Yakutia Kuranakh business unit.

In the first half of 2011, the stripping ratio at Olimpiada was lower than the average life-of-mine ratio, therefore, previously capitalized stripping costs (partly offset by the capitalization of the excessive stripping costs incurred in H1 2011 at the Titimukhta and Kuranakh mines). As a result, deferred stripping costs in the net amount of USD17,136 thousand were charged to operating costs

#### Increase in gold-in-process and refined gold

In the first six months of 2012 total metal inventories increased from 1,130 thousand ounces at the beginning of the reporting period to 1,658 thousand ounces as at 30 June 2012. This was mainly related to the increase in ore stocks, including long-term ore stocks, at the Krasnoyarsk business unit, which contained 1,386 thousand ounces of gold, as compared to 867 thousand ounces at the beginning of the reporting period. Dore gold remaining at the Krasnoyarsk business unit which was not refined in the reporting period also increased from 21 thousand ounces as at 31 December 2011 to 42 thousand ounces as at 30 June 2012. Work-in-process at the Olimpiada mine decreased by   
26 thousand ounces following the improvement of the technological cycle.

The various types of metal inventories are valued using different approaches. Refined metals are valued at the average cost of production per saleable unit of metal. Work-in-process, metal concentrate and Dore are valued at the average production costs at the relevant stage of production. Ore stockpiles are valued at the average cost per tonne of mining ore. On the whole, metal inventories are stated at the lower of production cost or net realisable value. Production cost is determined as the sum of the applicable expenses incurred directly or indirectly in bringing inventories to their existing condition and location. The highest valued inventories – finished goods at refinery plant – significantly decreased from 17 thousand ounces as at 31 December 2011 to just 1,000 ounces at the end of the reporting period. The table below shows the balance of inventories for the Group’s Russian subsidiaries in the first 6 months 2012:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Thousand ounces | As at  30 June  2012 |  | As at  31 December 2011 |  | %  change  p-o-p |
|  |  |  |  |  |  |
| Gold contained in |  |  |  |  |  |
| Ore (short-term and long-term) | 1,386 |  | 867 |  | 60 |
| Gold-in-circuit | 213 |  | 216 |  | (1) |
| Dore gold on mine | 45 |  | 27 |  | 67 |
| Dore gold at refinery | 12 |  | 2 |  | 486 |
| Finished goods at refinery | 1 |  | 17 |  | (94) |
|  |  |  |  |  |  |
| **Total** | **1,658** |  | **1,130** |  | **47** |

The value of inventories at Kazakhstan mines also increased. Total gold-in-process of USD74,278 thousand was recorded within inventory from cost of production in the first half of 2012 (USD78,138 thousand in H1 2011).

### Cost of other sales

Cost of other sales includes, in addition to electricity costs, payroll costs related to non-mining activities, expenses on materials and fuel, and depreciation. In H1 2012, cost of other sales amounted to USD21,232 thousand. In the first half of 2012 revenue from other sales exceeded their cost of sales, which resulted in a gross profit from other sales in the amount of USD7,822 thousand, compared to USD5,784 thousand in the same period of 2011. Gross profit on other sales margin increased from 20% in the first half of 2011 to 27% in the first half of 2012. This was mainly a result of increased profitability of Mamakan HPS, where the cost of generation of 1 Kwt/h decreased by almost 39%.

## 1.4 Selling, general and administrative expenses

The following table sets forth the selling, general and administrative expenses of the Group for   
the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD‘000 | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Salaries | 68,586 |  | 43,591 |  | 57 |  | 116,295 |
| Taxes other than mining and income taxes | 12,052 |  | 21,706 |  | (44) |  | 42,630 |
| Professional services | 15,429 |  | 14,214 |  | 9 |  | 36,350 |
| Administrative overheads | 12,024 |  | 11,371 |  | 6 |  | 25,513 |
| Depreciation | 2,149 |  | 2,580 |  | (17) |  | 4,830 |
|  |  |  |  |  |  |  |  |
| **Total** | **110,240** |  | **93,462** |  | **18** |  | **225,618** |

In the first half of 2012, the Group’s selling, general and administrative expenses insignificantly increased from USD93,462 thousand to USD110,240 thousand. Administrative salaries increasing 57% were the major contributor to the growth in expenses. The major contributors to the decrease were taxes other than mining and income taxes, which decreased 44%. Depreciation of the Russian rouble in the first half of 2012 relative to the first half of 2011 also had a positive impact on the selling, general and administrative expenses of the Group.

### Salaries

In H1 2012, the Group’s administrative labour costs increased by 57% to USD68,586 thousand.   
The increase is related to bonus payments accrual for FY2011 results (calculated proportionally to the actual bonus paid for FY2011), including bonus payments to the senior management team. There was no such accrual in H1 2011. In addition, there was an increase in the average number of administrative personnel at the Yakutia (Kuranakh) and Krasnoyarsk business units.

### Taxes other than mining and income taxes

The following table shows the components of taxes, other than mining and income taxes, for the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended 31 December 2011

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD‘000 | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Property tax | 9,681 |  | 10,228 |  | (5) |  | 20,661 |
| VAT | 505 |  | 772 |  | (35) |  | 2,167 |
| Tax on dividends | - |  | 540 |  | - |  | 16,388 |
| Other taxes | 1,866 |  | 10,166 |  | (82) |  | 3,414 |
|  |  |  |  |  |  |  |  |
| **Total** | **12,052** |  | **21,706** |  | **(44)** |  | **42,630** |

In H1 2012, the Group accrued USD12,052 thousand in federal and regional taxes other than tax on mining and income tax, compared to USD21,706 thousand in the first half of 2011. Property tax charges were at the level of the previous year. First, the Group capitalised property taxes accrued at the Magadan business unit and Yakutia (Nezhdaninskoye) business unit. Also the Group suspended operations at the Zapadnoye mine in April 2011. This was partly offset by property tax increases due to commissioning of new property, plant and equipment at the Irkutsk ore business unit following the launch of the Verninskoye mine in December 2011.

### Professional services

In H1 2012, the Group incurred USD15,429 thousand of costs related to professional services, reflecting payments for advisory services provided to the Group with regard to the obtaining of the premium listing on the London Stock Exchange and negotiations related to the sale of PGIL’s operating subsidiaries in Romania, as well as an increase in software and maintenance costs. Legal, audit and consulting service payments decreased by USD1,807 thousand.

## 1.5 Impairment

The following table sets forth impairment recognised by the Group for the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD’000 | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Impairment of stockpiles | - |  | 25,881 |  | - |  | 25,209 |
| Impairment of exploration and evaluation assets | 243 |  | 15,100 |  | (98) |  | 54,708 |
| Impairment of property, plant and equipment | 17,316 |  | 7,644 |  | 127 |  | 23,501 |
|  |  |  |  |  |  |  |  |
| **Total** | **17,559** |  | **48,625** |  | **(64)** |  | **103,418** |

In H1 2012, the Group recognised USD17,559 thousand of impairment charges, which was 64% lower than in the same period of 2011. These charges were:

### Impairment of stockpiles

There was no impairment of stockpiles recognised in H1 2012, as compared to a loss on impairment of stockpiles in H1 2011 in the amount of USD25,209 thousand which was recognised in respect of ore stockpiled at the Zapadnoye mine in the Irkutsk region (1.7 million tonnes), as a result of the depletion of reserves in the pit contour of the Zapadnoye deposit.

### Impairment of exploration and evaluation assets

In H1 2012, the Group recognised impairment in the amount of USD243 thousand related to previously capitalised exploration and evaluation costs on part of the development works related to some deposits of the Exploration business unit, that had not led to the discovery of commercially viable quantities of gold resources and consequently resulted in the decision to discontinue such activities.   
In the first six months of 2011, the Group recognised an impairment loss of USD15,100 thousand at the following exploration fields: Kuzeevskaya in the Krasnoyarsk region, Doroninskoye and Tokichan in the Magadan region, Mukodek in the Irkutsk region and Kaskabulak in the Republic of Kazakhstan.

### Impairment of property, plant and equipment

In H1 2012 the Group recorded impairment of property, plant and equipment in the amount of USD17,316 thousand, which is USD9,672 million higher than in H1 2011. USD11,622 thousand relates to the impairment of mining assets following discontinuing of activities at the Omchak exploration field. The reminder relates to the Kazakhstan business unit and Irkutsk alluvial business unit, where the Group reassessed property, plant and equipment requirements and reconsidered plans for their future use. As a result, certain assets’ book values and expected useful lives exceeded their anticipated recoverable values and accordingly an impairment was recorded in respect of those assets. Their useful lives were revised downwards.

## 1.6 Gain on disposal of subsidiaries

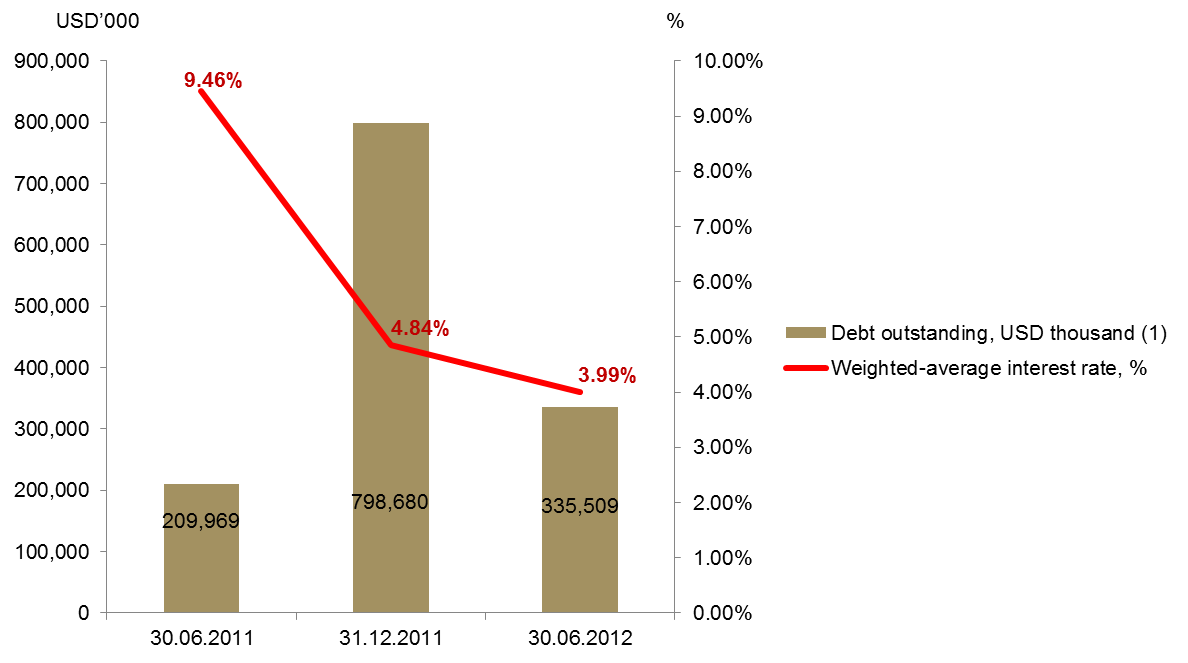
On 21 May 2012 the Group sold its 100% interest Romaltyn Mining S.R.L. and Romaltyn Exploration S.R.L to JSC SAT & Company for a total consideration of USD20 million. Romaltyn Mining owns a CIL (carbon-in-leach) gold treatment plant with an aggregate treatment capacity of 2.5 million tonnes of ore and tailings per annum. However, in order to commence operations, the owner must carry out modernisation works and obtain an Integrated Environmental Permit (IEP) before the expiry of its licence. Romaltyn Exploration holds rights to various exploration assets in Romania containing 112 koz proved and probable reserves, 114 koz measured resources and 204 koz inferred resources. The presale fair value of these assets was USD14,727 thousand where USD21,696 thousand was the net book value of the assets minus USD6,969 thousand of environmental and other obligations. Thus, the net gain from this disposal was equal to USD5,273 thousand.

Also in the reporting period the Group disposed of GRK Bargold Ltd and Yakutskoe GRP Ltd, which hold rights to a number of exploration assets in Russia. The net gain on the disposal of these assets was USD995 thousand.

## 1.7 Finance costs

The level of borrowings increased significantly within the last 12 months: 280% increase from   
30 June 2011 to 31 December 2011, and 60% from 30 June 2011 to 30 June 2012. This relates to the Mandatory Tender Offer in November financed through two bridge facilities with a total consideration of USD460,000 thousand, as well as the following loans from Societe Generale, Unicredit and HSBC with a consideration of USD100,000 thousand each (On 06 October 2011 USD50,000 thousand from Societe Generale loan had been transferred to Unicredit). The Group’s finance costs slightly decreased by 5.5% to USD22,489 thousand in H1 2012, owing to lower interest rates.

Graph 2. Debt outstanding and weighted-average interest rate as of 30 June 2011, 31 December 2011 and 30 June 2012.



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1. Debt outstanding recognised at fair value and carried at amortised cost (as shown in the Group’s statement of financial position). Actual debt outstanding was USD337,540 thousand as at 30 June 2012, USD794,160 thousand as at 31 December 2011 and USD231,922 thousand as at 30 June 2011.

## 1.8 Income from investments (net)

In H1 2012, the Group received income from investments totaling USD19,540 thousand, compared to USD8,232 thousand in the first half of 2011. 89% of this income (or USD17,325 thousand) relates to the interest income on bank deposits. The reminder relates to the income received from investments in listed companies. At the end of the reporting period the fair value of these investments increased by USD2,215. This was recognised as investment income.

At the end of the reporting period the fair value of available-for-sale investments decreased by USD1,791. There was no disposal of available-for-sale investments in the reporting period.

## 1.9 Income tax expense

Income tax expense in the first half of 2012 was USD113,026 thousand, which was 87% more than in the same period of 2011. The increase in income tax expense for H1 2012 was driven by higher profit before taxation in comparison with the first half of 2011 (an increase of 102% p-o-p). The effective income tax rate (ratio of current and deferred tax expense to IFRS income before tax) was 21% (23% in the first half of 2011), while the statutory income tax rate in Russia was 20% in both periods. The difference between the statutory and the effective tax rates was due to a number of non-deductible items for tax purposes and other permanent differences.

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# SUMMARY OF PERFORMANCE RESULTS BY BUSINESS UNITS

The following table shows the Group’s performance results by business units for the 6 months ended 30 June 2012 and 30 June 2011, and for the year ended 31 December 2011.

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  | Six months ended 30 June | | | | | | | | | | | | | | | | | | | | | | |  | Year ended 31 December | | | | | | | | | | |
|  |  | 2012 | | | | | | | | | | |  | 2011 | | | | | | | | | | |  | 2011 | | | | | | | | | | |
|  |  | **Production** | | |  | **Sales** | | |  | **Gold sales** | | |  | **Production** | | |  | Sales | | |  | Gold sales | | |  | **Production** | | |  | Sales | | |  | Gold sales | | |
|  | Note | **‘000 ounces** |  | **%** |  | **‘000 ounces** |  | **%** |  | USD‘000 |  | % |  | **‘000 ounces** |  | **%** |  | ‘000 ounces |  | % |  | USD‘000 |  | % |  | ‘000 ounces |  | % |  | ‘000 ounces |  | % |  | USD‘000 |  | % |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| Krasnoyarsk business unit | 2.1 | 538 |  | 75 |  | 554 |  | 75 |  | 916,086 |  | 75 |  | 445 |  | 73 |  | 464 |  | 74 |  | 669,570 |  | 74 |  | 1,038 |  | 69 |  | 1,040 |  | 70 |  | 1,641,380 |  | 70 |
| Irkutsk alluvial business unit | 2.2 | 44 |  | 6 |  | 44 |  | 6 |  | 72,781 |  | 6 |  | 45 |  | 7 |  | 45 |  | 7 |  | 66,644 |  | 7 |  | 210 |  | 14 |  | 210 |  | 14 |  | 350,213 |  | 15 |
| Yakutia Kuranakh business unit | 2.3 | 70 |  | 10 |  | 70 |  | 9 |  | 114,873 |  | 9 |  | 55 |  | 9 |  | 55 |  | 9 |  | 78,662 |  | 9 |  | 117 |  | 8 |  | 117 |  | 8 |  | 184,735 |  | 8 |
| Irkutsk ore business unit | 2.4 | 18 |  | 3 |  | 18 |  | 2 |  | 29,134 |  | 2 |  | 10 |  | 2 |  | 3 |  | - |  | 3,590 |  | - |  | 16 |  | 1 |  | 3 |  | - |  | 3,497 |  | - |
| Kazakhstan business unit | 2.5 | 51 |  | 7 |  | 56 |  | 8 |  | 90,992 |  | 7 |  | 57 |  | 9 |  | 63 |  | 10 |  | 83,286 |  | 9 |  | 117 |  | 8 |  | 113 |  | 8 |  | 160,825 |  | 7 |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Group total(1)** |  | **721** |  | **100** |  | **742** |  | **100** |  | **1,223,866** |  | **100** |  | **611** |  | **100** |  | **629** |  | **100** |  | **901,752** |  | **100** |  | **1,497** |  | **100** |  | **1,483** |  | **100** |  | **2,340,650** |  | **100** |

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1. In this table and in the tables in notes 2.1-2.5 to IMS totals may not sum completely due to rounding.

## 2.1 The Krasnoyarsk business unit (Olimpiada, Blagodatnoye and Titimukhta deposits)

The Krasnoyarsk business unit is the Group’s largest mining operation. The table below shows selected financial data for this unit for the 6 months ended 30 June 2012 and 2011 and for the year ended   
31 December 2011.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| USD’000, | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| unless otherwise indicated | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Olimpiada production  (thousand ounces) | 318 |  | 248 |  | 28 |  | 566 |
| Titimukhta production  (thousand ounces) | 46 |  | 44 |  | 4 |  | 109 |
| Blagodatnoye production  (thousand ounces) | 174 |  | 152 |  | 14 |  | 363 |
| Total gold production  (thousand ounces) | 538 |  | 445 |  | 21 |  | 1,038 |
| Gold sales | 916,086 |  | 669,570 |  | 37 |  | 1,641,380 |
| Gold sales (thousand ounces) | 554 |  | 464 |  | 20 |  | 1,040 |
| Segment profit | 465,059 |  | 342,265 |  | 36 |  | 918,078 |
| Segment profit margin (%) | 51% |  | 51% |  | (1) |  | 56% |
| TCC per ounce sold (USD/ounce) | 614 |  | 577 |  | 6 |  | 606 |

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Source: Management accounting data.

In H1 2012, the Krasnoyarsk business unit produced 538 thousand ounces of refined gold, compared to 445 thousand ounces in H1 2011.

Mills No.2 and 3 of the Olimpiada mine produced 318 thousand ounces of refined gold in the first six months of 2012, compared to 248 thousand ounces in the same period of 2011. Gold output increased primarily due to the growth in recovery rate from 71.1% in H1 2011 to 75.6% in H1 2012 following implementation of a series of measures aimed at increasing density of flotation concentrate and optimisation of the leaching process. Also the stabilisation in average grade (3.5 g/t in H1 2012 vs. 3.4 g/t in H1 2011) improved production results.

The Titimukhta project (Mill No.1 of the Olimpiada mine) produced 46 thousand ounces of refined gold in H1 2012, compared to 44 thousand ounces in the same period of 2011. The 4% increase mainly relates to improved grades.

The Blagodatnoye mine produced 174 thousand ounces of gold, compared to 152 thousand ounces in H1 2011. The 14% increase in production was primarily a result of the achieved maintenance of recovery rates at levels exceeding design parameters.

Gold sales of the Krasnoyarsk business unit in H1 2012 were USD916,086 thousand, compared to USD669,570 thousand in H1 2011. The 37% increase in gold sales resulted from a combination of higher realised gold prices and increased sales volumes. During the first six months of 2012   
554 thousand ounces of refined gold were sold. The comparative sales volume for the H1 2011 was 464 thousand ounces.

The total cash costs per ounce of gold sold for the Krasnoyarsk business unit amounted to USD614 in H1 2012, compared to USD577 in H1 2011. In addition to the factors impacting on cash costs throughout the Group in H1 2012 as well as detailed analysis by business units (see paragraph 1.3 “Cost of Gold Sales – Cash operating costs”), the increase in TCC per ounce sold at the Krasnoyarsk business unit was also attributable to the increase of cost of ore mining at the Blagodatnoye and Titimukhta mines, including expenditures on transportation. Labour costs also increased due to an approximately 13% salary indexation starting from the beginning of 2012 (the highest indexation level in the Group). Consumption of explosives also increased due to overall growth in drilling and blasting operations aimed to deepening and forming of open pits, as well as due to instability in physical characteristics of the ore body at Olimpiada. Transportation expenses also increased. Material expenses have been the largest component of cost of gold sales at the Krasnoyarsk business unit.

## 2.2 The Irkutsk alluvial business unit (Alluvial deposits)

The Irkutsk business unit operates alluvial deposits. The table below shows selected financial data for this unit for the 6 months ended 30 June 2012 and 2011, and for the year ended 31 December 2011.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| USD’000, | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| unless otherwise indicated | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Gold production (thousand ounces) | 44 |  | 45 |  | (3) |  | 210 |
| Gold sales | 72,781 |  | 66,644 |  | 9 |  | 350,213 |
| Gold sales (thousand ounces) | 44 |  | 45 |  | (3) |  | 210 |
| Segment profit | 24,715 |  | 6,588 |  | 275 |  | 102,795 |
| Segment profit margin (%) | 34% |  | 10% |  | 244 |  | 29% |
| TCC per ounce sold (USD/ounce) | 866 |  | 628 |  | 38 |  | 776 |

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Source: Management accounting data.

In H1 2012, refined gold production at the Group’s alluvial deposits in the Irkutsk region was at the level of the H1 2011 and amounted to 44 thousand ounces. In the reporting period, alluvial enterprises washed lesser volume of sands, but with higher gold content.

Gold sales of the Irkutsk alluvial business unit increased from USD66,644 thousand in H1 2011 to USD72,781 thousand in H1 2012 on the back of the growing realised gold price. All gold produced in the reporting period was sold within the period.

Total cash costs per ounce of gold sold amounted to USD866 in H1 2012, compared to USD628 in H1 2011. In addition to the factors impacting on cash costs throughout the Group in H1 2012 as well as detailed analysis by business units (see paragraph 1.3 “Cost of gold sales – Cash operating costs”), the increase in TCC per ounce sold at the Irkutsk alluvial business unit was mainly attributable to increased payroll costs (due to bonus payments for exceeding the production plan) and consumption of consumables and tires for mining fleet, resulting from the early commencement of the mining season, increased volumes of repair works and the increased cost of outsourced mining services. Labour costs have been the largest component of cost of gold sales at the Irkutsk alluvial business unit.

## 2.3 The Yakutia Kuranakh business unit (the Kuranakh mine)

The Yakutia Kuranakh business unit operates the Kuranakh mine in the Sakha Republic (Yakutia). The table below shows selected financial data for this unit for six months ended 30 June 2012 and 2011, and for the year ended 31 December 2011.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| USD’000, | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| unless otherwise indicated | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Gold production (thousand ounces) | 70 |  | 55 |  | 28 |  | 117 |
| Gold sales | 114,873 |  | 78,662 |  | 46 |  | 184,735 |
| Gold sales (thousand ounces) | 70 |  | 55 |  | 28 |  | 117 |
| Segment profit | 23,487 |  | (3,735) |  | (729) |  | 13,797 |
| Segment profit margin (%) | 20% |  | - |  | - |  | 7% |
| TCC per ounce sold (USD/ounce) | 967 |  | 851 |  | 14 |  | 890 |

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Source: Management accounting data.

The Kuranakh mine produced 70 thousand ounces of refined gold in the first six months of 2012, compared to 55 thousand ounces in H1 2011. The increase in production was a combination of several factors, including increase in ore mining, ore processing and recovery rate improvement.

In H1 2012, gold sales of the Yakutia Kuranakh business unit amounted to USD114,873 thousand, compared to USD78,662 thousand in H1 2011. The 46% increase was the result of the growth in production and the realised gold price.

Total cash costs per ounce of gold sold increased from USD851 in H1 2011 to USD967 in H1 2012. In addition to the factors impacting on cash costs described in paragraph 1.3 “Cost of Gold Sales – Cash operating costs”, the increase in TCC per ounce sold at the Yakutia Kuranakh business unit was also attributable to the increased costs for metal-roll for operating activity (increased mainly due to the purchase price growth), and costs for tires (as a result of growth in price, as well as mileage increase following pits enlargement). Labour costs and material expenses have been the largest components of cost of gold sales at the Yakutia Kuranakh business unit, expenses on transport services (in many cases provided by third parties) are also traditionally high at the Kuranakh mine.

The segment profit of the Yakutia Kuranakh business unit improved in H1 2011 due to successful elimination of watering in the pits. However, the processing plant is the oldest in the Group’s portfolio, which results in high TCC level.

## 2.4 The Irkutsk ore business unit (the Verninskoye mine)

The Irkutsk ore business unit conducts hard-rock mining operations at the Verninskoye mine. The table below shows selected financial data for this unit for the 6 months ended 30 June 2012 and 2011, and for the year ended 31 December 2011.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| USD’000, | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| unless otherwise indicated | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Gold production (thousand ounces) | 18 |  | 10 |  | 81 |  | 13 |
| Total sales | 55,184 |  | 25,022 |  | 121 |  | 46,802 |
| Gold sales | 29,134 |  | 3,590 |  | 712 |  | 3,497 |
| Gold sales (thousand ounces) | 18 |  | 3 |  | 614 |  | 3 |
| Segment profit/ (loss) | 7,044 |  | 1,797 |  | 292 |  | (13,042) |
| Segment profit margin (%) | 13% |  | 7% |  | - |  | - |
| TCC per ounce sold (USD/ounce) | 756 |  | 1,045 |  | (28) |  | 841 |

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Source: Management accounting data.

In the reporting period, the Irkutsk ore business unit produced 18 thousand ounces of gold, compared to 10 thousand ounces produced in H1 2011. All gold was produced from the ore of the Verninskoye deposit. The Group mined 567 thousand tonnes of ore at the Verninskoye deposit, which was processed at Verninskoye plant (for 85%) and at Pervenets plant (for 15%).

Gold sales of the Irkutsk ore business unit in H1 2012 amounted to USD29,134 thousand, compared to USD3,590 thousand in the same period of 2011. The increase in sales is a result of the Verninskoye mine commissioning in December 2011. Gold sales volumes in the reporting period amounted to 18 thousand ounces.

Other sales also increased as a result of re-sales of electricity purchased from third parties and sales of in-house generated electricity by Mamakan hydro-power station.

The profitability of the Irkutsk ore business unit improved in H1 2012, and was a result of the Verninskoye mine launch, suspension of subeconomic operations at the Zapadnoye mine, as well as improved profitability of power generation.

## 2.5 The Kazakhstan business unit

The Kazakhstan business unit comprises the Aksu, Bestobe, Zholymbet and Akzhal mines. The Group acquired these operations through its acquisition of a controlling stake in KazakhGold Group Limited (now PGIL) in August 2009. The table below shows selected financial data for this unit for the 6 months ended 30 June 2012 and 2011, and for the year ended 31 December 2011.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| USD’000, | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| unless otherwise indicated | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Gold production (thousand ounces) | 51 |  | 57 |  | (10) |  | 117 |
| Total sales | 91,883 |  | 83,863 |  | 10 |  | 162,538 |
| Gold sales | 90,992 |  | 83,286 |  | 9 |  | 160,825 |
| Gold sales (thousand ounces) | 56 |  | 63 |  | (11) |  | 113 |
| Segment profit/(loss) | 22,906 |  | 2,843 |  | 706 |  | 5,773 |
| Segment profit margin (%) | 25% |  | 3% |  | - |  | 4% |
| TCC per ounce sold (USD/ounce) | 707 |  | 642 |  | 10 |  | 653 |

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Source: Management accounting data.

In the first six months 2012, the Kazakhstan business unit produced 51 thousand ounces of gold in semi-finished products, compared to 57 thousand ounces in the same period of 2011. The decrease of 13% was a result of 51% reduction in ore processed at heap leaching site due to expiration of the licence for geological exploration of the Akzhal deposit, as well as due to reduction of open pit mining at the Aksu mine.

Gold sales amounted to USD90,992 thousand in H1 2012, compared to USD83,286 thousand in the first six months of 2011. The increase resulted from higher realised gold prices offset by decrease in production. Sales volumes amounted to 56 thousand ounces in H1 2012, compared to 63 thousand ounces in H1 2011. There were no other sales in H1 2012.

Total cash costs per ounce of gold sold in H1 2012 amounted to USD707, compared to   
USD642 in the same period of the previous year. Besides the factors impacting on the Kazakhstan business unit cash costs described in paragraph 1.3, the increase in TCC per ounce sold at the Kazakhstan mines was driven by a material decline in the average gold grade in the ore processed at plants, decrease in volumes of cheap processing at heap leaching facilities, deterioration of ore quality.

In H1 2012, the segment profit of the Kazakhstan operations amounted to USD22,906 thousand, compared to USD2,843 thousand in H1 2011. The improvement of the financial results of the business unit was a result of the average realised gold price increase, as well as redeemtion of Senior Notes in March 2012. In H1 2011 interest expenses on Senior notes were consolidated in the result of the Kazakhstan business unit.

# NON-GAAP FINANCIAL MEASURES

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

## 3.1 EBITDA

“Adjusted EBITDA” is defined by the Group as profit before finance costs, income tax, income/(losses) from investments, depreciation, amortisation and interest, and is further adjusted by certain items included in the table below. The Group has made these adjustments in calculating Adjusted EBITDA to provide a clearer view of the performance of its underlying business operations and to generate   
a metric that it believes will give greater comparability over time with peers in its industry. The Group believes that Adjusted EBITDA is a meaningful indicator of its profitability and performance. This measure should not be considered as an alternative to profit for the year and operating cash flows based on IFRS and should not necessarily be construed as a comprehensive indicator of the Group’s measure of profitability or liquidity.

The following table sets forth the Group’s Adjusted EBITDA for the 6 months ended 30 June 2012 and 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD’000 | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Profit for the period | 425,896 |  | 206,800 |  | 106 |  | 558,015 |
| + Income tax charged | 113,026 |  | 60,400 |  | 87 |  | 207,052 |
| + Depreciation and amortisation for the period | 87,279 |  | 93,645 |  | (7) |  | 187,949 |
| + Interest expense | 22,489 |  | 22,712 |  | (1) |  | 71,403 |
| - Interest income | (17,325) |  | (6,902) |  | 151 |  | (16,252) |
| - Gain on disposal of investments | - |  | (17,023) |  | - |  | (17,023) |
| + Gain from investments in listed companies held for trading | (2,215) |  | 7,032 |  | (131) |  | 20,984 |
| - Foreign exchange gain | (7,578) |  | (2,049) |  | 270 |  | 5,814 |
| + Loss from disposal of property, plant and equipment and work-in-progress | 1,412 |  | 2,62,624 |  | (46) |  | 5,933 |
| + Impairment of property, plant and equipment | 17,559 |  | 22,744 |  | (23) |  | 78,209 |
| + Change in fair value of derivative | - |  | 8,661 |  | (100) |  | 8,661 |
| - Gain on disposal of subsidiaries | (6,268) |  | - |  | - |  | - |
| **Adjusted EBITDA** | **634,275** |  | **398,644** |  | **59** |  | **1,110,745** |

The Group’s Adjusted EBITDA in the first half of 2012 was USD634,275 thousand, compared to USD398,644 thousand in the first half of 2011.The increase of 59% over the levels of the first half of 2011 reflects higher realised gold prices combined with the increased sales volumes.

## 3.2 Total cash costs

The Group presents the financial items “total cash costs” (“TCC”) and “total cash costs per troy ounce” which have been calculated and presented by management as TCC presentation is common industry practice, although its calculations of these items may differ from those of its industry peers. These items are non IFRS measures. An investor should not consider these items in isolation or as alternatives to cost of sales, profit for the year attributable to shareholders of the parent company, net cash generated from operating activities or any other measure of financial performance presented in accordance with IFRS.

Total cash costs per troy ounce are the total attributable cash costs divided by the attributable troy ounce of gold sold during the period.

The following table shows the Group’s TCC for the six months ended 30 June 2012 and 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| USD’000, | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| unless otherwise indicate | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Cost of gold sales | 569,030 |  | 478,053 |  | 19 |  | 1,162,019 |
| - property, plant and equipment depreciation | (84,137) |  | (89,847) |  | (6) |  | (181,935) |
| - provision for annual vacation payment | (3,202) |  | (5,299) |  | (40) |  | (3,774) |
| - employee benefit obligations cost | (1,697) |  | (2,184) |  | (22) |  | (1,620) |
| - change in allowance for obsolescence of inventory | 3,072 |  | (2,189) |  | (240) |  | (2,819) |
| + non-monetary changes in inventories(1) | 9,213 |  | 12,638 |  | (97) |  | 6,795 |
| + non-monetary changes in deferred stripping costs(2) | 375 |  | (3,582) |  | (357) |  | 1,174 |
| **Тotal cash costs (3)** | **492,653** |  | **387,590** |  | **27** |  | **979,840** |
| Gold sales (“000 troy ounces) | 742 |  | 629 |  | 18 |  | 1,483 |
| **TCC (USD/oz)** | **664** |  | **616** |  | **8** |  | **661** |
| TCC (RUB/oz) | 20,336 |  | 17,634 |  | 15 |  | 19,427 |

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1. “Non-monetary changes in inventories” is a calculation to estimate the non-cash portion of costs included in the change in the amount of inventory, primarily representing depreciation and amortisation.
2. “Non-monetary changes in deferred stripping costs” is a calculation to estimate the non-cash portion of costs included in the change in the amount of deferred stripping costs, primarily representing depreciation and amortisation.
3. Totals may not sum completely due to rounding.

In the first six months of 2012, TCC per troy ounce increased by 15% on a rouble basis. The increase of 8% on a USD basis was lower due to the strengthening of the US dollar relative to the Russian rouble.

During the first half of 2012, total cash costs were affected mainly by a material increase in costs resulting primarily from significant increase in consumption of materials, fuel and spare parts, salaries indexation, increase in the average number of personnel, growth in prices for some materials and components and increase in mining tax charges on the back of gold price growth (Refer to paragraph 1.3 “Cost of gold sales”). Despite improvements in the Group’s mines processing efficiency, the increase in gold production and sales volumes was not sufficient to meet the growth of costs, which led to an increase in the Group’s TCC indicator.

# REVIEW OF FINANCIAL SUSTAINABILITY AND SOLVENCY

## 4.1 Analysis of statement of financial position items

The table below sets forth key items from the Group’s consolidated statement of financial position as at 30 June 2011 and 31 December 2011:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| USD‘000 | 30 June  2012 |  | 31 December 2011 |  | %  Change |
|  |  |  |  |  |  |
| **ASSETS** |  |  |  |  |  |
| **Non-current assets** |  |  |  |  |  |
| Property, plant and equipment | 2,177,202 |  | 2,056,417 |  | 6 |
| Exploration and evaluation assets | 412,322 |  | 399,846 |  | 3 |
| Deferred stripping costs | 65,428 |  | 64,460 |  | 2 |
| Inventories | 220,360 |  | 207,789 |  | 6 |
| Investments in securities and other financial assets | 3,330 |  | 3,643 |  | (9) |
| Other non-current assets | - |  | 35 |  | - |
| **Total non-current assets** | **2,878,642** |  | **2,732,190** |  | **5** |
|  |  |  |  |  |  |
| **Current assets** |  |  |  |  |  |
| Inventories | 604,505 |  | 543,023 |  | 11 |
| Investments in securities and other financial assets | 63,707 |  | 63,468 |  | 0 |
| Cash and cash equivalents | 847,954 |  | 657,448 |  | 29 |
| Other current assets(1) | 254,994 |  | 222,882 |  | 14 |
| **Total current assets** | **1,771,160** |  | **1,486,821** |  | **19** |
|  |  |  |  |  |  |
| **TOTAL ASSETS** | **4,649,802** |  | **4,219,011** |  | **10** |
|  |  |  |  |  |  |
| **EQUITY AND LIABILITIES** |  |  |  |  |  |
| Equity attributable to shareholders of the parent company | 3,367,157 |  | 2,595,356 |  | 30 |
| Non-controlling interest | 289,518 |  | 235,317 |  | 23 |
| **TOTAL EQUITY** | **3,656,675** |  | **2,830,673** |  | **29** |
|  |  |  |  |  |  |
| **Non-current liabilities** |  |  |  |  |  |
| Site restoration and environmental obligations | 150,083 |  | 149,876 |  | 0 |
| Borrowings | 302,176 |  | 123,048 |  | 146 |
| Deferred tax liabilities | 187,139 |  | 180,741 |  | 4 |
| Other non-current liabilities | 22,854 |  | 24,008 |  | (5) |
| **Total non-current liabilities** | **662,252** |  | **477,673** |  | **39** |
|  |  |  |  |  |  |
| Current liabilities |  |  |  |  |  |
| Borrowings | 33,333 |  | 675,632 |  | (95) |
| Trade and other payables and accrued expenses | 252,581 |  | 192,077 |  | 31 |
| Taxes payable | 44,961 |  | 42,956 |  | 5 |
| **Total current liabilities** | **330,875** |  | **910,665** |  | **(64)** |
|  |  |  |  |  |  |
| **TOTAL LIABILITIES** | **993,127** |  | **1,388,338** |  | **(28)** |
|  |  |  |  |  |  |
| **TOTAL EQUITY AND LIABILITIES** | **4,649,802** |  | **4,219,011** |  | **10** |

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1. Other current assets consist of deferred expenditures, trade and other receivables, advances paid to suppliers and prepaid expenses and taxes receivable.

### 4.1.1 Assets

### Non-current assets

### Property, plant and equipment

The table below sets forth the components of the Group’s property, plant and equipment at 30 June 2011 and 31 December 2011:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| USD‘000 | 30 June  2012 |  | 31 December 2011 |  | %  change |
|  |  |  |  |  |  |
| Mining assets | 1,612,742 |  | 1,651,929 |  | (2) |
| Non-mining assets | 47,685 |  | 32,820 |  | 45 |
| Capital construction-in-progress | 516,775 |  | 371,668 |  | 39 |
|  |  |  |  |  |  |
| **Total property, plant and equipment** | **2,177,202** |  | **2,056,417** |  | **6** |

As at 30 June 2012 the value of property, plant and equipment totalled USD2,177,202 thousand, compared to USD2,056,417 thousand at 31 December 2011. The 6% increase primarily was due to the increase in capital construction-in-progress.

The value of mining assets decreased in spite of assembling and commissioning of some new equipment at the Verninskoye mine. It was fully offset by USD17,316 thousand impairment loss of property, plant at the Omchak exploration field and at the Kazakhstan business unit, disposal of Romanian assets, and the rouble depreciation.

The value of capital construction-in-progress on the contrary increased 39% p-o-p, and mostly related to the development of the Natalka mine and Verninskoye mine. The Natalka mine: in H1 2012 the following equipment has been delivered on site and recorded as capital construction: eight trucks, three bulldozers, two excavators and three cars, construction of camp and some other facilities continued. The Verninskoye mine: In H1 2012 the Group installed the following flotation and hydrometallurgical equipment on the plant: hydro cyclones, thickeners, centrifugal concentrators, cyanidation reactors, carbon in leach and elution units, various pumps and ancillary equipment. All equipment was recorded as capital construction ore mining assets. In addition, the average number of personnel at LLC Polyus Stroy, for which salary costs are capitalised as capital construction-in-progress, increased, mainly as a result of continuing development of the Natalka mine.

### Exploration and evaluation assets

As at the end of June 2012 the value of exploration and evaluation assets increased by 3% to USD412,322 thousand (the Nezhdaninskoye deposit represented 53% of all Exploration and evaluation assets). This was a result of capitalisation of exploration expenses incurred at all business units of the Group (the major contributors were: the Nezhdaninskoye deposit an addition of USD4,847 thousand in H1 2012 and the Medvezhy-Zapadnyi deposit – an addition of USD3,621 thousand in H1 2012), as well as reclassification of the Smezhnyi deposit into exploration assets from mining assets   
(an addition of USD5,337 thousand). The increase has been offset by disposal of exploration expenses on development works in GRK Bargold Ltd and Yakutskoe GRP Ltd (the Exploration business unit), as well as due to the effect of translation to US dollars.

### Deferred stripping costs

In the reporting period deferred stripping costs increased by 2% and equaled USD65,428 thousand. The increase mostly reflects capitalisation of stripping costs incurred at the Titimukhta deposit   
(the Krasnoyarsk business unit) and several deposits at the Yakutia Kuranakh business unit in the total amount of USD8,507 thousand. This was partly offset by expensing of previously capitalised stripping costs at the Olimpiada deposit (the Krasnoyarsk business unit) in the total amount of USD6,164 thousand, as the stripping ratio there was lower than the average life-of-mine ratio for these deposits.

### Inventories

In the first half of 2012 long-term inventories increased by 6% from USD207,789 thousand at   
31 December 2011 to USD220,360 thousand at 30 June 2012. This relates to the increase in   
long-term ore stocks at the Krasnoyarsk business unit (please refer to 1.3 Cost of sales, Change in gold-in-process and refined gold). This increase was partly offset by rouble depreciation p-o-p.

When the Group was processing oxide ores at the Olimpiada mine, stockpiles of sulphide ore   
(6.8 million tonnes) were considered as waste and accounted for at zero cost. During the period 2008-2010 the Group did not process any zero-value stockpiles. During 2011 and the H1 2012   
the Group processed zero-value inventory, so the remaining volume of zero-valued stockpiles as at 30 June 2012 was 5.1 million tonnes (5.6 million tonnes as at 31 December 2011). This zero-value stockpile could have a significant impact on operations if processed at the present time, since the only cost associated with this inventory would be the processing cost. The impact of processing the remaining stockpiles would be an approximate USD92 million increase to profit for the year in which processed. The benefit of processing of 0.5 million tonnes of zero cost stockpiles during the reporting period is estimated at USD11 million.

### Current assets

As at 30 June 2012 the Group’s current assets amounted to USD1,771,160 thousand, compared to USD1,486,821 thousand at 31 December 2011. This increase of 19% resulted primarily from growth of inventories and increased cash balance.

### Inventories

During the first half of 2012, inventories increased by 11% to USD604,505 thousand mostly due to the increase in metal inventories from USD188,515 thousand at 31 December 2011 to   
USD235,732 thousand at 30 June 2012. Gold-in-process increased mainly at the Krasnoyarsk business unit (mostly short-term stockpiles). At 30 June 2012 the balance of Dore gold remaining at the plant and refinery amounted to 54 thousand troy ounces (22 thousand ounces at 31 December 2011). This increase was enhanced by an increase in the cost of production at which metal inventories were recorded to the statement of financial position and the impact of the exchange rate factor. All these factors resulted in a 25% increase in cost of gold-in-process to USD229,174 thousand.

Stocks of unsold finished goods declined from USD24,757 thousand at the beginning of the year to USD6,558 thousand at 30 June 2012.

The value of stores and materials increased 4% from USD354,508 thousand at the beginning of the year to USD368,773 thousand as at 30 June 2012, which was largely driven by the increase in purchase prices for consumables and spares.

### Investments in securities and other financial assets

At 30 June 2012, the short-term investments in securities and other financial assets totalled USD75,932 thousand, compared to USD63,468 thousand at 31 December 2011, reflecting a 20% increase. Annualised return on investments in the first half of 2012 amounted to 6.9%. Annualised effective return on bank deposits equalled 6.6%.

Short-term investments during the six months ended 30 June 2012 are presented in the table below:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| USD‘000 | 30 June  2012 |  | 31 December 2011 |  | %  change |
|  |  |  |  |  |  |
| **Available-for-sale investments**  Mainly represented by shares of Rosfund. There was no disposal or acquisition of available-for-sale investments during the reporting period. In the first half of 2012, the fair value of these investments declined by USD1,791 thousand. This decrease was recognised in equity within the investment revaluation reserve. | 32,953 |  | 34,744 |  | (5) |
|  |  |  |  |  |  |
| **Equity investments in listed companies held for trading**  Represented by financial assets carried at fair value through profit and loss. During the first half of 2012, the Group disposed of USD6,645 thousand of these investments. By the end of the reporting period, the fair value of held for trading investments increased by USD2,215 thousand. The balance of USD232 thousand relates to currency differences. | 10,659 |  | 14,857 |  | (28) |
|  |  |  |  |  |  |
| **Bank deposits**  In the reporting period, the Group deposited cash to bank accounts in the total amount of USD7,329 thousand. Bank deposits are denominated in roubles and US dollars and bear interest of 6.7-9.0% per annum. | 19,504 |  | 12,175 |  | 60 |
|  |  |  |  |  |  |
| **Other** | 591 |  | 1,692 |  | (65) |
|  |  |  |  |  |  |
| **Total investments in securities and other financial assets:** | **63,707** |  | **63,468** |  | - |

### Cash and cash equivalents

At 30 June 2012, the balance of cash and cash equivalents amounted to USD847,954 thousand,   
an increase of 29% as compared to 31 December 2011 due to the strong operating cash inflow during the period.

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| USD‘000 | 30 June  2012 |  | 31 December 2011 |  | %  change |
|  |  |  |  |  |  |
| Bank deposits | 524,802 |  | 487,467 |  | 8 |
| Current accounts |  |  |  |  |  |
| RUB | 106,616 |  | 146,761 |  | (27) |
| other currencies | 215,880 |  | 21,992 |  | 882 |
| Other cash | 656 |  | 1,228 |  | (47) |

Bank deposits increased by 8% from USD487,467 thousand at the beginning of the reporting period to USD524,802 as of June 30,2012. The increase primarily relates to the Krasnoyarsk business unit.

## 4.1.2 Equity and liabilities

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| USD‘000 | 30 June  2012 |  | 31 December 2011 |  | %  change |
|  |  |  |  |  |  |
| Share capital | 482 |  | 482 |  | - |
| Additional paid-in capital | 2,151,765 |  | 2,189,240 |  | (2) |
| Treasury shares | - |  | (765,013) |  | (100) |
| Investments revaluation reserve | 2,766 |  | 4,557 |  | (39) |
| Translation reserve | (343,885) |  | (258,426) |  | 33 |
| Retained earnings | 1,556,029 |  | 1,424,516 |  | 9 |

### Capital and reserves

As at 30 June 2012, capital and reserves were USD3,656,675 thousand compared to   
USD2,830,673 thousand as at 31 December 2011. In the first half of 2012, the Group’s capital and reserves changed mostly as a result of the sale of treasury block in May 2012. The issued and fully paid-up share capital of PGIL comprised 3,032,149,962 ordinary shares as at 30 June 2012 (the same amount as at 31 December 2011) at a par value of £0.0001 per share.

On 11 May 2012 the Company completed the sale of its 151,607,496 shares, representing 5% less one share of it's issued share capital, to Chengdong Investment Corporation, a wholly-owned subsidiary of CIC International Co. Ltd., and of 50,198,271 shares and 25,153,897 Level I GDRs, representing 2.50% of the Company's issued share capital, to JSC VTB Bank. Thus, the value of treasury shares decreased from USD765,013 as at 31 December 2011 to zero as at 30 June 2012.

The investment revaluation reserve decreased by USD1,791 thousand in the first half of 2012, which reflected the decline in the fair value of available-for-sale investments. At the reporting date the investment revaluation reserve amounted to USD2,776 thousand.

The translation reserve changed by USD85,459 thousand as a result of RUB/USD exchange rate increase from 32.1961 RUB/USD as at 31 December 2011 to 32.8169 RUB/USD as at 30 June 2012.

During the reporting period, the Group’s retained earnings increased by 9% to USD1,556,029 thousand, reflecting a net profit attributable to shareholders of the parent company of USD 389,315 thousand, which was partly offset by a net loss on disposal of treasury shares of the Company in the amount of USD103,166 thousand. This net loss is calculated as the difference between net proceeds from the sale of shares of USD624,372 thousand and the book value of the disposed treasury shares of USD727,538 thousand.

### Non-current liabilities

In the first half of 2012, non-current liabilities increased by 39% to USD 662,252 thousand at 30 June 2012. The major change relates to the increase in long-term borrowings.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| USD‘000 | 30 June  2012 |  | 31 December  2011 |  | %  change |  |
|  |  |  |  |  |  |  |
| Site restoration and environmental obligations | 150,083 |  | 149,876 |  | 0 |  |
| Borrowings | 302,176 |  | 123,048 |  | 146 |  |
| Deferred tax liabilities | 187,139 |  | 180,741 |  | 4 |  |
| Other non-current liabilities | 22,854 |  | 24,008 |  | (5) |  |
|  |  |  |  |  |  |  |
| **Total non-current liabilities** | **662,252** |  | **477,673** |  | **39** |  |

There was no significant change in site restoration and environmental obligations during the reporting period. The Group sold assets in Romania which bear environmental obligations in the amount of USD5,022 thousand, which was fully offset by unwinding of discount rates applicable to these obligations in the amount of USD6,102 thousand.

Long-term borrowings of the Group at the reporting date were represented by USD100 million loan from Societe Generale due in October 2014 (50% of this loan transferred to Unicredit Bank on   
06 October 2011), loans payable to Gold Lion, previously PGIL’s major shareholder, due in November 2014, USD100 million loan from HSBC and USD100 million loan from Unicredit Bank. Societe Generale credit facility is provided to OJSC Pervenets (the Irkutsk ore business unit) and assigned for general corporate purposes, including repayment of intra-group loan to CJSC Polyus and capital expenditures. The sum due under the loans payable to Gold Lion at 30 June 2012 was USD37,072 thousand (USD34,160 thousand at 31 December 2011). The level of borrowings significantly increased within the last 12 months: 280% increase from 30 June 2011 to 31 December 2011, and 60% from 30 June 2011 to 30 June 2012. This relates to the Mandatory Tender Offer in November 2011 financed through two bridge facilities with a total consideration of USD460,000 thousand, as well as following loans from Societe Generale, Unicredit and HSBC with a consideration of USD100,000 thousand each. Senior Notes were redeemed in March 2012, both bridge facilities redeemed in May 2012.

The Group also has a number of unused credit facilities: a three year RUB10 billion (approximately USD305 million) credit line with VTB to fund its general corporate purposes, and USD67,502 thousand export financing credit facility agreement with Societe Generale.

Deferred tax liabilities increased from USD180,741 thousand at 31 December 2011 to USD187,139 thousand at 30 June 2012, which was also primarily due to the effect of the rouble depreciation.

### Current liabilities

Current liabilities include short-term borrowings, trade and other payables and accrued expenses and taxes payable. In the reporting period current liabilities decreased by 64% from USD910,665 thousand at 31 December 2011 to USD330,875 thousand at 30 June 2012 due to the decrease in borrowings.

Short-term borrowings decreased 95% from USD675,632 thousand at 31 December 2011 to USD33,333 thousand at 30 June 2012. At the beginning of the reporting period short-term borrowings were presented mainly with USD200 million Senior Notes and USD460 million bridge facilities from Societe Generale and VTB bank. Following the acquisition of a controlling stake in PGIL, the liability under Senior Notes was reflected in the Group’s statement of financial position at fair value at the acquisition date and carried at amortised cost. Senior Notes were redeemed in March 2012, both bridge facilities redeemed in May 2012. The remaining USD33,333 thousand relates to current portion of long-term borrowings due within twelve months.

Trade, other payables and accrued expenses increased by 31% from USD192,077 thousand at   
31 December 2011 to USD252,581 thousand at 30 June 2012. This relates first of all to the accrual of additional bonuses for operational and financial performance in H1 2012 for operational and administrative personnel of the Krasnoyarsk and Yakutia Kuranakh business units, as well as   
the Moscow HQ of the Group for an amount of USD24,426 thousand (the bonus was calculated proportionally to the actual bonus paid for the FY2011). The rest of the increase relates to the advances payable for the disposal of Kazakh assets.

In the first half of 2012, income tax payable slightly increased from USD42,956 thousand to USD44,961 thousand. This increase was due to the increase in unified social tax as well as tax on mining payable.

## 4.2 Cash flow analysis

The following table sets forth the main components of the Group’s consolidated interim statement of cash flows for the 6 months ended 30 June 2012 and 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | Year ended  31 December |
| USD‘000 | 2012 |  | 2011 |  | 2011 |
|  |  |  |  |  |  |
| **Operating activities** |  |  |  |  |  |
| **Profit before income tax** | **538,922** |  | **267,200** |  | **765,067** |
| Adjustments(1) | 94,737 |  | 188,524 |  | 391,849 |
| **Operating profit before working capital changes** | **633,659** |  | **455,724** |  | **1,156,916** |
| Changes in working capital | (59,209) |  | (89,603) |  | (137,345) |
| **Cash flows from operations** | **574,450** |  | **366,121** |  | **1,019,571** |
| Interest paid | (21,620) |  | (9,375) |  | (23,423) |
| Income tax paid | (101,590) |  | (65,872) |  | (230,743) |
| **Net cash generated from operating activities** | **451,240** |  | **290,874** |  | **765,405** |
| **Investing activities** |  |  |  |  |  |
| CAPEX, acquisition of subsidiaries and deferred stripping costs(2) | (278,937) |  | (180,273) |  | (359,396) |
| Other investing activities (3) | 16,016 |  | (28,456) |  | 99,033 |
| **Net cash (used in)/generated from investing activities** | **(262,921)** |  | **(208,729)** |  | **(260,363)** |
| **Net cash used in financing activities** | **12,304** |  | **(9,097)** |  | **(134,958)** |
| Effect of translation to presentation currency | (10,117) |  | 23,016 |  | (39,541) |
| **Net increase in cash and cash equivalents** | 200,623 |  | 73,048 |  | 370,084 |
| **Cash and cash equivalents at beginning of the period** | **657,448** |  | **326,905** |  | **326,905** |
|  |  |  |  |  |  |
| **Cash and cash equivalents at end of the period** | **847,954** |  | **422,969** |  | **657,448** |

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

1. Adjustments for non-cash items include: amortisation and depreciation, finance costs, loss on disposal of property, plant and equipment, impairment of property, plant and equipment, expensed stripping costs, change in allowance for reimbursable value added tax, income/(loss) from investments, change in fair value of derivative, net foreign exchange gain and other items.
2. Capital expenditures, acquisition of subsidiaries and deferred stripping costs include purchases of property, plant and equipment, deferred stripping costs capitalised and proceeds from sale of property, plant and equipment.
3. Other investing activities include interest received, purchase of promissory notes and other financial assets, proceeds from sale of promissory notes and other financial assets.

### Operating activities

In the first six months of 2012, the Group generated profit before income tax in the amount of USD538,922 thousand, compared to USD267,200 thousand in the first six months of 2011. The increase in profit before taxation resulted from a combination of the increasing selling prices and higher gold sales volumes. Operating profit before working capital changes was USD633,659 thousand, which was 39% more than in the same period of the previous year. In the first half of 2012 changes in working capital were substantially lower than in the first half of 2011, when the Group recorded a material increase in inventories. Net cash generated from operating activities increased from USD290,874 thousand in the first half of 2011 to USD451,240 thousand in the first half of 2012.

### Investing activities

In the first half of 2012, the Group spent USD262,921 thousand on investing activities, while in the first half of 2011 it spent USD208,729 thousand. The largest spending during the reporting period comprised capital expenditures and deferred stripping costs totalling USD278,937 thousand, compared to USD180,273 thousand in the same period of 2011. This outflow was partly offset by proceeds from sale of investments in securities, proceeds from disposal of Romanian assets and interest received.

### Financing activities

Cash inflow from financing activities in the six months ended 30 June 2012 totalled USD12,304 thousand (outflow of USD9,097 thousand in the six months ended 30 June 2011). The proceeds from placement of treasury block and attraction of new loans (total USD822,584 thousand) were almost fully offset by outflow for loans repayments and dividends pay-out (totally USD810,280).

## 4.3 Capital expenditures

Capital expenditures represent the Group’s purchase of property, plant and equipment.

The following table shows the Group’s capital expenditures for the six months ended 30 June 2012 and 2011, and for the year ended 31 December 2011:

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June | | |  | %  change |  | Year ended  31 December |
| USD’000 | 2012 |  | 2011 |  | p-o-p |  | 2011 |
|  |  |  |  |  |  |  |  |
| Capital expenditures  (management accounts) | 297,130 |  | 183,148 |  | 62 |  | 455,730 |
| Differences between IFRS and management accounts | 33,112 |  | (2,018) |  | - |  | (127,887) |
|  |  |  |  |  |  |  |  |
| **Capital expenditures** | **330,242** |  | **181,130** |  | **82** |  | **327,843** |

In the first six months of 2012, the Group’s capital expenditures amounted to USD330,242 thousand, an increase of 82% as compared with the first six months of 2011.

The major part of funds was invested into the construction of the Verninskoye and Natalka mine.

## 4.4 Net debt

Net debt is defined as short-term and long-term debt less cash and cash equivalentsand short-term bank deposits. Short-term bank deposits with original maturity of more than 3 months can be withdrawn on demand and therefore have the same liquidity as cash and cash equivalents. Net debt should not be considered as an alternative to current and non-current loans and borrowings based on IFRS and should not necessarily be construed as a comprehensive indicator of the Group’s measure of profitability or liquidity.

The following table sets forth the Group’s net debt as at 30 June 2012 and 31 December 2011:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| USD’000 | 30 June 2012 |  | 31 December 2011 |  | %  change |
|  |  |  |  |  |  |
| Non-current borrowings | 302,176 |  | 123,048 |  | 146 |
| + Current borrowings | 33,333 |  | 675,632 |  | (95) |
| - Cash and cash equivalents | (847,954) |  | (657,448) |  | 29 |
| - Bank deposits | (19,504) |  | (39,351) |  | (50) |
|  |  |  |  |  |  |
| **Net debt (cash and bank deposits)** | **(531,949)** |  | **101,881** |  | **-** |

# Description of principal risks

The activities of the Group are associated with a number of risks that may affect the Group’s production and financial results.

The Group is committed to achieving successful development, including through ensuring an effective risk management system designed to achieve optimal results, an efficient distribution of resources, and a strengthening of the Group’s competitiveness.

Successful risk management requires, amongst other things, the identification and assessment of potential threat parameters, and the development of measures aimed at mitigating potential risks. The Group has developed internal procedures governing the process through which risks are managed. Such procedures require that each business unit has a designated risk manager, identifies risks facing the unit, and takes measures aimed at lowering its risk levels.

## Operational risks

### Ore and mineral reserves are difficult to quantify; actual volumes may differ from estimated, and therefore reserve estimates are subject to significant correction

The Group’s activities are heavily reliant upon its available ore reserves and mineral resources.   
The evaluation of ore reserves and mineral resources depends to a certain extent on statistical conclusions made on the basis of the results of limited volumes of drilling and other analyses that may turn out to be incorrect. The evaluation and classification of ore and mineral reserves may also be affected by the changes in the prices of gold. If the quantity and quality of the explored reserves are not confirmed, the production efficiency may deteriorate as a result of labor consuming mining operations. The Group periodically engages independent experts to conduct audits on prospective and existing deposits and to provide reports on the results of the exploration activity, mineral resources and ore reserves.

### Risks connected with mining and production activity

The Group’s production activities are carried out in remote regions, which are subject to severe climatic conditions. As a result, the delivery of equipment, technological materials and spare parts is more difficult, thus affecting production costs. Mining machinery, transport and new technologies, including those developed by the Group, are used for operations in areas which have complicated geological and climatic conditions.

There are increased risks of flooding, pit slope and rim slide, accidents caused by the use of the mining transport equipment and preparation and performance of explosion works in the pit, reduction of gold production due to adverse weather conditions and problems in the power supply facilities and recovery plants. These risks could result in suspended ore production and recovery, increased costs, and health, safety and environmental issues and affect the Group’s production activities.

The Group aims to mitigate the risks associated with unplanned production interruptions through various processes, including probability analysis and effective risk management. Such risk management includes the identification of potential threat parameters, the identification of defined risk categories and the adoption of measures designed to prevent accidents and emergencies. A risk reduction programme is also currently in the process of being developed.

### Risks of non-compliance with contracts and delivery of equipment and materials

Interruption of material and technical supplies as a result of a failure of contractors and suppliers to fulfill their contractual obligations for the construction of new production facilities, or interruptions in the delivery of spare parts, and equipment could adversely affect the timing of the introduction of new production capacity and production plans.

To attempt to mitigate the risk of late delivery, the Group monitors the financial status of its major counterparties on a regular basis and takes measures to increase the number of counterparties with which it conducts business.

### Risks connected with acquisition and merger transactions

The Group considers M&A options that would reinforce its asset portfolio, offer attractive growth potential and geographic diversification. Such transactions may entail a variety of risks. To reduce the risks connected with any acquisition and merger transaction, the Group conducts a comprehensive analysis of the pending transactions and an assessment of the consequences with due regard for political, economic, ecological and social factors.

## Financial risks

### Inflation and market risks

Increased inflation induced by the current economic climate may have an adverse impact on the Group’s financial results. Costs which are subject to inflationary changes are denominated in Russian Roubles and the Kazakhstan Tenge and include materials and utilities, wages and services. Increased tariff rates of the natural monopolies may also result in increased costs.

In order to reduce the impact of increasing tariff rates, the Group seeks to develop and modernise its own energy-generating facilities and to purchase and consume energy resources based on long-term fixed-price contracts. Prospective inflationary changes are also considered as a part of the analysis when preparing budgets and estimating costs of implementing investment projects.

The Group’s income is primarily derived from gold sales, which are generally effected at spot prices. Gold prices are quoted in international markets in US dollars. Accordingly, the economic results of the Group depend, to a considerable extent, on the fluctuations in the gold price. The gold market is cyclical and sensitive to any economic changes. The price of gold is subject to substantial fluctuations and is affected by a number of factors which are beyond the control of the Group. A substantial gold price reduction may result in a reduction in the profitability of the Group.

### Liquidity risk

Management of liquidity risk is intended to maintain a sufficient level of monetary resources to fund production-, management-, and investment-related needs, to ensure stability of compliance with the financial obligations of the Group and to develop an appropriate capital structure. The Group monitors on a regular basis the following risks: production levels, operational expenditures, prices of raw materials, volumes of floating assets and capital expenditure. The enterprises of the Group implement   
a co-ordinated and automatic program of cash asset record-keeping.

## Regulatory risks

### The activities of the Group may be adversely impacted by the termination or non-renewal of its licences or the failure to obtain or comply with new licences

The ability of the Group to carry out its activities depends on its licences, in particular those licences relating to the use of mineral resources, and on being able to obtain new licences and comply with their terms. The terms of the licence agreements require the Group to comply with a number of industrial standards, employ qualified personnel, ensure that the necessary equipment and operational quality control systems are available, maintain relevant documentation and provide information to   
the licensing authorities when requested. Failure to comply with any such terms may result in the termination of the licences critical to the operations of the Group or impose obligations on the Group, which may decrease its profitability.

The Group is focused on improving its systems control over compliance with licence agreements and industrial standards requirements. These control activities include the analysis and response to comments or reports made by state regulatory and supervisory authorities in connection with inspections of the Group’s business activities.

### Tax risks

The Group pays a significant amount of taxes in the regions in which it operates. The tax obligations of the Group can result in uncertainties due to the ambiguity of certain tax legislation. The risks include: ambiguous interpretation of law, inconsistent application of legislation, amendments to tax legislation or change in application. Such risks may result in fines, penalties and other sanctions.

### Changes in environmental legislation

The Group’s activities are subject to environmental control and regulation as a result of the use of environmentally hazardous substances, and the disposal of operational waste and hazardous substances into the environment, soil disturbance, potential harm to wildlife and other factors. The Group seeks to comply with its environmental obligations and follows the requirements of Russian and international standards, agreements, conventions and protocols applicable to it. The task of enhancing the efficiency of Group performance is intended, among other things, to reduce emissions of hazardous substances and develop waste disposal sites. Changes in environmental legislation and introduction of stricter licensing requirements may result in additional expenditures to modify industrial processes and an increase in environmental charges and fines.

## Risks associated with the implementation of investment projects

The implementation of the Group’s investment projects is subject to market and operational risks. Market risks include the impact of changes in the price of gold, exchange rates and inflation.

Operational risks include:

* Delays in commissioning projects;
* Errors in design, construction and installation, which may result in increased planned project costs, or deficiencies in operations; and
* Shortages of skilled technicians due to competition in the recruitment of workers and employers and the difficulty in recruiting caused by the remote location of the associated projects.

## Risks related to the Euro zone

One of the possible outcome of the crisis in the Euro zone could be an essential worsening of the financial position of some companies, producing equipment, reagents, materials. The possibility that these companies would discontinue operations could lead to a failure to act under the contract obligations and breach the schedule of material and maintenance supply of the Group. This could negatively effect commissioning of new production facilities and production plans fulfillment. In order to eliminate this risk the Group diversifies its procurement portfolio globally and determines the use of interchangeable parts and materials.

# Related-parties transactions

The Company’s ordinary shares were admitted to the premium segment of the Official List maintained by the UK Listing Authority and to trading on the London Stock Exchange’s main market for listed securities on 19 June 2012. As a result the Company and each company within the Group is subject to requirements, set out in Listing Rule 11 of the Listing Rules, in respect of any transaction or arrangement entered into with a Related Party.

On 8 June 2012, in order to meet the requirements the Board of Directors of the Company approved Related Party Transaction Procedures (the Procedures). The Procedures set out a process of prompt identification of any potential transaction with a Related Party. The Group developed the Related Party List, which is maintained and controlled by the List Controller (General Council). According to the Procedures a Person responsible for identifying the Related Party transactions by reference to the Related Parties List (Responsible Person) is appointed in each company of the Group.

In the instance of such a transaction being identified, the Responsible Person informs the List Controller. The List Controller together with the Sponsor bank (Sponsor) assesses whether it is a Related Party transaction, and then values the nature and size of the expected Related Party transaction by reference to the parameters set out in Listing Rules.

Thus, based on the Listing Rules and based on the specific nature and size of the transaction it   
1) does not require any approval 2) requires approval by the Board 3) requires the approval by the Board and further FSA notification 4) requires the pre-approval by the Board and final approval by shareholders of the Company.

By 30 June 2012 the Group has deposited USD9,694 thousand and accumulated USD112,257 thousand as cash on the accounts with Bank “Mezhdunarodnyi Finansovyi Klub” (MFK), which is identified as a Related Party. However, all transactions with MFK had been implemented before the Company’s shares were admitted to the Premium list (and the Company met an obligation to follow LR 11) and do not require retrospective review and approval.

# Going concern statement

As stated in note 2 to the condensed consolidated interim financial statements for the 6 months ended 30 June 2012, the Directors are satisfied that the Group has sufficient resources to continue in operation for the foreseeable future, a period of no less than 12 months from the date of this report. Accordingly, they continue to adopt the going concern basis in preparing the condensed consolidated interim financial statements.

# production OUTLOOK for the year ending 31 December 2012

Based on the results of H1 2012, the Group confirms its FY 2012 production guidance of 1.6 million ounces, including assets in Kazakhstan. This will be achieved through production growth at alluvial operations (subject to seasonality), further ramp-up of the Verninskoye mine, and production growth at Titimukhta (as a result of capacity increase to 2.4 million tonnes per annum).

STATEMENT OF directors’ RESPONSIBILITIES

We confirm that to the best of our knowledge:

* The condensed consolidated interim financial statements has been prepared in accordance with IAS 34 Interim Financial Reporting;
* The interim management report includes a fair review of the information required by DTR4.2.7R (indication of important events during the first six months and description of principal risks and uncertainties for the remaining six months of the year), and;
* The Interim Management Report includes a fair review of the information required by DTR4.2.8R (related parties’ transactions and changes therein).

The names of the Directors of Polyus Gold International Limited are as follows:

* Robert Buchan;
* [Adrian Coates](http://www.polyusgold.com/eng/about/boardofdirectors/656/);
* [Bruce Buck](http://www.polyusgold.com/eng/about/boardofdirectors/Buck/);
* The Earl of Clanwilliam;
* [Anna Kolonchina](http://www.polyusgold.com/eng/about/boardofdirectors/anna_kolonchina/);
* [Kobus Moolman](http://www.polyusgold.com/eng/about/boardofdirectors/moolman/);
* [Alexander Mosionzhik](http://www.polyusgold.com/eng/about/boardofdirectors/547/);
* [German Pikhoya](http://www.polyusgold.com/eng/about/boardofdirectors/pikhoya/);
* Dmitry Razumov.

The responsibility statement was approved by the Board of Directors on 29 August 2012 and signed on its behalf by:

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**Pikhoya G.R.**

Chief Executive Officer

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**Ignatov O.V.**

Chief Financial Officer

29 August 2012

**INDEPENDENT REVIEW REPORT TO POLYUS GOLD INTERNATIONAL LIMITED**

We have been engaged by the Company to review the condensed set of consolidated interim financial statements in the half-yearly financial report for the six months ended 30 June 2012 which comprises the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of financial position, the consolidated statement of changes in equity, the consolidated statement of cash flows and related notes 1 to 21. We have read the other information contained in the half-yearly financial report and considered whether it contains any apparent misstatements or material inconsistencies with the information in the condensed set of financial statements.

This report is made solely to the Company in accordance with International Standard on Review Engagements (UK and Ireland) 2410 “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Auditing Practices Board. Our work has been undertaken so that we might state to the Company those matters we are required to state to it in an independent review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company, for our review work, for this report, or for the conclusions we have formed.

**Directors’ responsibilities**

The half-yearly financial report is the responsibility of, and has been approved by, the directors. The directors are responsible for preparing the half-yearly financial report in accordance with the Disclosure and Transparency Rules of the United Kingdom’s Financial Services Authority.

As disclosed in note 2, the annual financial statements of the Group are prepared in accordance with IFRSs as adopted by the European Union. The condensed set of financial statements included in this half-yearly financial report has been prepared in accordance with International Accounting Standard 34, “Interim Financial Reporting,” as adopted by the European Union.

**Our responsibility**

Our responsibility is to express to the Company a conclusion on the condensed set of financial statements in the half-yearly financial report based on our review.

**Scope of review**

We conducted our review in accordance with International Standard on Review Engagements (UK and Ireland) 2410 “Review of Interim Financial Information Performed by the Independent Auditor of the Entity” issued by the Auditing Practices Board for use in the United Kingdom. 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 (UK and Ireland) 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 condensed set of financial statements in the half-yearly financial report for the six months ended 30 June 2012 is not prepared, in all material respects, in accordance with International Accounting Standard 34 as adopted by the European Union and the Disclosure and Transparency Rules of the United Kingdom’s Financial Services Authority.

**Deloitte LLP**

Chartered Accountants and Statutory Auditor

London, United Kingdom

29 August 2012

POLYUS GOLD International Limited

condensed CONSOLIDATED interim INCOME STATEMENT

FOR the six months ended 30 June 2012

(in thousands of US Dollars, except for earnings per share and number of shares data)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Notes | Six months ended 30 June  2012  (unaudited) |  | Six months ended 30 June  2011  (unaudited) |  | Year ended  31 December 2011  (audited) |
|  |  |  |  |  |  |  |
| Gold sales | 5 | 1,223,866 |  | 901,752 |  | 2,340,650 |
| Other sales |  | 29,054 |  | 29,007 |  | 62,060 |
|  |  |  |  |  |  |  |
| **Total revenue** |  | **1,252,920** |  | **930,759** |  | **2,402,710** |
|  |  |  |  |  |  |  |
| Cost of gold sales | 6 | (569,030) |  | (478,053) |  | (1,162,019) |
| Cost of other sales |  | (21,232) |  | (23,223) |  | (46,343) |
|  |  |  |  |  |  |  |
| **Gross profit** |  | **662,658** |  | **429,483** |  | **1,194,348** |
|  |  |  |  |  |  |  |
| Selling, general and administrative expenses | 7 | (110,240) |  | (93,462) |  | (225,618) |
| Impairment of stockpiles |  | - |  | (25,881) |  | (25,209) |
| Impairment of exploration and evaluation assets |  | (243) |  | (15,100) |  | (54,708) |
| Impairment of property, plant and equipment | 10 | (17,316) |  | (7,644) |  | (23,501) |
| Gain on disposal of subsidiaries | 3 | 6,268 |  | - |  | - |
| Research expenses |  | (1,284) |  | (1,255) |  | (2,581) |
| Other expenses, net |  | (5,550) |  | (6,510) |  | (24,077) |
|  |  |  |  |  |  |  |
| **Operating profit** |  | **534,293** |  | **279,631** |  | **838,654** |
|  |  |  |  |  |  |  |
| Finance costs | 8 | (22,489) |  | (22,712) |  | (71,403) |
| Income from investments, net | 9 | 19,540 |  | 8,232 |  | 3,630 |
| Foreign exchange gain/(loss) |  | 7,578 |  | 2,049 |  | (5,814) |
|  |  |  |  |  |  |  |
| **Profit before income tax** |  | **538,922** |  | **267,200** |  | **765,067** |
|  |  |  |  |  |  |  |
| Current income tax expense |  | (102,851) |  | (52,715) |  | (200,297) |
| Deferred income tax expense |  | (10,175) |  | (7,685) |  | (6,755) |
|  |  |  |  |  |  |  |
| **Profit for the period / year** |  | **425,896** |  | **206,800** |  | **558,015** |
|  |  |  |  |  |  |  |
| Profit for the period / year attributable to: |  |  |  |  |  |  |
| Shareholders of the Company |  | 389,315 |  | 188,847 |  | 468,998 |
| Non-controlling interests |  | 36,581 |  | 17,953 |  | 89,017 |
|  |  |  |  |  |  |  |
|  |  | **425,896** |  | **206,800** |  | **558,015** |
|  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
| Weighted average number of ordinary shares in issue during the period (‘000s) |  | 2,868,789 |  | 3,082,656 |  | 2,960,311 |
|  |  |  |  |  |  |  |
| Earnings (loss) per share (US Cents) \* |  |  |  |  |  |  |
| Basic and diluted |  | 14 |  | 6 |  | 16 |

\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

\* There were no financial instruments or any other instances which could cause antidilutive effect on earnings per share calculation.

POLYUS GOLD International Limited

condensed CONSOLIDATED interim statement of comprehensive income

FOR the six months ended 30 June 2012

(in thousands of US Dollars)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Notes | Six months ended 30 June 2012  (unaudited) |  | Six months ended 30 June 2011  (unaudited) |  | Year ended  31 December 2011  (audited) |
|  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
| **Profit for the period / year** |  | **425,896** |  | **206,800** |  | **558,015** |
|  |  |  |  |  |  |  |
| Available for sale financial assets: |  |  |  |  |  |  |
| (Loss)/gain from change in fair value of available-for-sale investments |  | (1,791) |  | (410) |  | (8,976) |
| Losses recycled to profit or loss on disposal or impairment of available-for-sale investments | 9 | - |  | (17,023) |  | (17,023) |
|  |  |  |  |  |  |  |
|  |  | **(1,791)** |  | **(17,433)** |  | **(25,999)** |
|  |  |  |  |  |  |  |
| Effect of translation to presentation currency |  | (88,432) |  | 257,703 |  | (194,307) |
|  |  |  |  |  |  |  |
| **Other comprehensive (loss) / income  for the period / year** |  | **(90,223)** |  | **240,270** |  | **(220,306)** |
|  |  |  |  |  |  |  |
| **Total comprehensive income  for the period / year** |  | **335,673** |  | **447,070** |  | **337,709** |
|  |  |  |  |  |  |  |
| Attributable to: |  |  |  |  |  |  |
| Shareholders of the Company |  | 302,065 |  | 415,942 |  | 304,309 |
| Non-controlling interests |  | 33,608 |  | 31,128 |  | 33,400 |
|  |  |  |  |  |  |  |
|  |  | **335,673** |  | **447,070** |  | **337,709** |

POLYUS GOLD International Limited

condensed CONSOLIDATED interim statement of financial position

AT 30 June 2012

(in thousands of US Dollars)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Notes | 30 June  2012  (unaudited) |  | 30 June  2011  (unaudited) |  | 31 December 2011  (audited) |
|  |  |  |  |  |  |  |
| ASSETS |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
| **Non-current assets** |  |  |  |  |  |  |
| Property, plant and equipment | 10 | 2,177,202 |  | 2,277,769 |  | 2,056,417 |
| Exploration and evaluation assets | 11 | 412,322 |  | 462,552 |  | 399,846 |
| Deferred stripping costs |  | 65,428 |  | 48,770 |  | 64,460 |
| Investments in securities and other financial assets | 12 | 3,330 |  | 4,467 |  | 3,643 |
| Inventories | 13 | 220,360 |  | 187,559 |  | 207,789 |
| Other non-current assets |  | - |  | 55 |  | 35 |
|  |  |  |  |  |  |  |
|  |  | **2,878,642** |  | **2,981,172** |  | **2,732,190** |
|  |  |  |  |  |  |  |
| **Current assets** |  |  |  |  |  |  |
| Inventories | 13 | 604,505 |  | 598,956 |  | 543,023 |
| Deferred expenditures |  | 54,735 |  | 53,893 |  | 18,512 |
| Trade and other receivables |  | 32,280 |  | 29,681 |  | 24,712 |
| Advances paid to suppliers and prepaid expenses |  | 31,804 |  | 24,938 |  | 29,636 |
| Investments in securities and other financial assets | 12 | 63,707 |  | 213,066 |  | 63,468 |
| Taxes receivable |  | 136,175 |  | 159,325 |  | 150,022 |
| Cash and cash equivalents | 14 | 847,954 |  | 422,969 |  | 657,448 |
|  |  |  |  |  |  |  |
|  |  | **1,771,160** |  | **1,502,828** |  | **1,486,821** |
|  |  |  |  |  |  |  |
| **TOTAL ASSETS** |  | **4,649,802** |  | **4,484,000** |  | **4,219,011** |
|  |  |  |  |  |  |  |
| **EQUITY AND LIABILITIES** |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
| **Capital and reserves** |  |  |  |  |  |  |
| Share capital | 15 | 482 |  | 482 |  | 482 |
| Additional paid-in capital |  | 2,151,765 |  | 2,308,863 |  | 2,189,240 |
| Treasury shares | 15 | - |  | (884,636) |  | (765,013) |
| Investments revaluation reserve |  | 2,766 |  | 13,123 |  | 4,557 |
| Translation reserve |  | (343,885) |  | 124,792 |  | (258,426) |
| Retained earnings |  | 1,556,029 |  | 1,119,224 |  | 1,424,516 |
|  |  |  |  |  |  |  |
| **Equity attributable to shareholders of the Company** |  | **3,367,157** |  | **2,681,848** |  | **2,595,356** |
| Non-controlling interests |  | 289,518 |  | 882,211 |  | 235,317 |
|  |  |  |  |  |  |  |
|  |  | **3,656,675** |  | **3,564,059** |  | **2,830,673** |
|  |  |  |  |  |  |  |
| **Non-current liabilities** |  |  |  |  |  |  |
| Site restoration and environmental obligations |  | 150,083 |  | 151,010 |  | 149,876 |
| Borrowings | 16 | 302,176 |  | 209,969 |  | 123,048 |
| Deferred tax |  | 187,139 |  | 204,183 |  | 180,741 |
| Other non-current liabilities |  | 22,854 |  | 25,097 |  | 24,008 |
|  |  |  |  |  |  |  |
|  |  | **662,252** |  | **590,259** |  | **477,673** |
|  |  |  |  |  |  |  |
| **Current liabilities** |  |  |  |  |  |  |
| Borrowings | 16 | 33,333 |  | - |  | 675,632 |
| Trade, other payables and accrued expenses |  | 252,581 |  | 287,852 |  | 192,077 |
| Taxes payable |  | 44,961 |  | 41,830 |  | 42,956 |
|  |  |  |  |  |  |  |
|  |  | **330,875** |  | **329,682** |  | **910,665** |
|  |  |  |  |  |  |  |
| **TOTAL LIABILITIES** |  | **993,127** |  | **919,941** |  | **1,388,338** |
|  |  |  |  |  |  |  |
| **TOTAL EQUITY AND LIABILITIES** |  | **4,649,802** |  | **4,484,000** |  | **4,219,011** |

POLYUS GOLD International Limited

condensed CONSOLIDATED interim STATEMENT OF CHANGES IN EQUITY

FOR THE six months ENDED 30 june 2012

(in thousands of US Dollars)

|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  | Number of |  | Equity attributable to shareholders of the Company | | | | | | | | | | | | |  |  |  |  |
|  | Notes | outstanding shares, thousand |  | Share  capital |  | Additional paid-in capital |  | Treasury  shares |  | Investments revaluation reserve |  | Translation reserve |  | Retained earnings |  | Total |  | Non-controlling  interests |  | Total |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Balance at 31 December 2010 (audited)** |  | **3,082,656** |  | **519** |  | **2,087,978** |  | **(626,313)** |  | **30,556** |  | **(119,736)** |  | **1,810,641** |  | **3,183,645** |  | **56,886** |  | **3,240,531** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| Profit for the six months ended 30 June 2011 |  | - |  | - |  | - |  | - |  | - |  | - |  | 188,847 |  | **188,847** |  | 17,953 |  | **206,800** |
| Other comprehensive income/(loss) |  | - |  | - |  | - |  | - |  | (17,433) |  | 244,528 |  | - |  | **227,095** |  | 13,175 |  | **240,270** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Total comprehensive income** |  | - |  | - |  | - |  | - |  | **(17,433)** |  | **244,528** |  | **188,847** |  | **415,942** |  | **31,128** |  | **447,070** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| Effect of reorganization |  | (312,955) |  | (37) |  | 220,885 |  | (258,323) |  | - |  | - |  | (807,937) |  | **(845,412)** |  | 807,937 |  | **(37,475)** |
| Dividends declared to shareholders of  the Company | 15 | - |  | - |  | - |  | - |  | - |  | - |  | (72,327) |  | **(72,327)** |  | - |  | **(72,327)** |
| Dividends declared to shareholders of  non-controlling interests |  | - |  | - |  | - |  | - |  | - |  | - |  | - |  | **-** |  | (13,740) |  | **(13,740)** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Balance at 30 June 2011 (unaudited)** |  | **2,769,701** |  | **482** |  | **2,308,863** |  | **(884,636)** |  | **13,123** |  | **124,792** |  | **1,119,224** |  | **2,681,848** |  | **882,211** |  | **3,564,059** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| Profit for the six months ended  31 December 2011 |  | - |  | - |  | - |  | - |  | - |  | - |  | 280,151 |  | **280,151** |  | 71,064 |  | **351,215** |
| Other comprehensive loss |  | - |  | - |  | - |  | - |  | (8,566) |  | (383,218) |  | - |  | **(391,784)** |  | (68,792) |  | **(460,576)** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Total comprehensive income** |  | - |  | - |  | - |  | - |  | **(8,566)** |  | **(383,218)** |  | **280,151** |  | **(111,633)** |  | **2,272** |  | **(109,361)** |
|  |  | - |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| Effect of reorganisation |  | - |  | - |  | - |  | - |  | - |  | - |  | 390,477 |  | **390,477** |  | (390,477) |  | **-** |
| Increase of ownership in subsidiary |  | 35,489 |  | - |  | (119,623) |  | 119,623 |  | - |  | - |  | (365,336) |  | **(365,336)** |  | (223,480) |  | **(588,816)** |
| Dividends declared to shareholders of  non-controlling interests |  | - |  | - |  | - |  | - |  | - |  | - |  | - |  | **-** |  | (35,209) |  | **(35,209)** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Balance at 31 December 2011 (audited)** |  | **2,805,190** |  | **482** |  | **2,189,240** |  | **(765,013)** |  | **4,557** |  | **(258,426)** |  | **1,424,516** |  | **2,595,356** |  | **235,317** |  | **2,830,673** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| Profit for the six months ended 30 June 2012 |  | - |  | - |  | - |  | - |  | - |  | - |  | 389,315 |  | **389,315** |  | 36,581 |  | **425,896** |
| Other comprehensive loss |  | - |  | - |  | - |  | - |  | (1,791) |  | (85,459) |  | - |  | **(87,250)** |  | (2,973) |  | **(90,223)** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Total comprehensive income** |  | - |  | - |  | - |  | - |  | **(1,791)** |  | **(85,459)** |  | **389,315** |  | **302,065** |  | **33,608** |  | **335,673** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| Dividends declared to shareholders of  the Company | 15 | - |  | - |  | - |  | - |  | - |  | - |  | (124,318) |  | **(124,318)** |  | - |  | **(124,318)** |
| Sale of treasury shares | 15 | 226,960 |  | - |  | - |  | 727,538 |  | - |  | - |  | (133,484) |  | **594,054** |  | 30,318 |  | **624,372** |
| Transfer of balance relating to call option | 15 | - |  | - |  | (37,475) |  | 37,475 |  | - |  | - |  | - |  | - |  | - |  | - |
| Dividends declared to shareholders of  non-controlling interests |  | - |  | - |  | - |  | - |  | - |  | - |  | - |  | **-** |  | (9,725) |  | **(9,725)** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Balance at 30 June 2012 (unaudited)** |  | **3,032,150** |  | **482** |  | **2,151,765** |  | **-** |  | **2,766** |  | **(343,885)** |  | **1,556,029** |  | **3,367,157** |  | **289,518** |  | **3,656,675** |

POLYUS GOLD International Limited

condensed CONSOLIDATED interim STATEMENT of CASH FLOWs

FOR THE six months ENDED 30 june 2012

(in thousands of US Dollars)

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Notes | Six months ended 30 June  2012  (unaudited) |  | Six months ended 30 June 2011  (unaudited) |  | Year ended  31 December  2011  (audited) |
|  |  |  |  |  |  |  |
| **Net cash generated from operating activities** | 17 | **451,240** |  | **290,874** |  | **765,405** |
|  |  |  |  |  |  |  |
| **Investing activities** |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
| Purchases of property, plant and equipment |  | (293,671) |  | (170,566) |  | (343,037) |
| Proceeds from subsidiaries’ disposal, net of cash disposed | 3 | 20,973 |  | - |  | - |
| Payments for deferred stripping |  | (8,507) |  | (9,934) |  | (18,270) |
| Proceeds on sales of property, plant and equipment |  | 2,268 |  | 227 |  | 1,911 |
| Interest received |  | 15,423 |  | 5,815 |  | 15,359 |
| Purchases of investments in securities and placement of deposits in banks |  | (14,252) |  | (137,564) |  | (37,596) |
| Proceeds on sales of investments in securities and redemption of bank deposits |  | 14,845 |  | 103,293 |  | 121,270 |
|  |  |  |  |  |  |  |
| **Net cash utilised in investing activities** |  | **(262,921)** |  | **(208,729)** |  | **(260,363)** |
|  |  |  |  |  |  |  |
| **Financing activities** |  |  |  |  |  |  |
|  |  |  |  |  |  |  |
| Acquisition of subsidiary’s shares |  | - |  | - |  | (588,816) |
| Proceeds from borrowings | 16 | 198,212 |  | - |  | 560,000 |
| Repayment of borrowings | 16 | (664,688) |  | - |  | - |
| Proceeds from sale of treasury shares | 15 | 624,372 |  | - |  | - |
| Dividends paid to shareholders of the Company | 15 | (124,318) |  | - |  | (73,191) |
| Dividends paid to shareholders of non-controlling interests |  | (21,274) |  | (3,738) |  | (26,225) |
| Other |  | - |  | (5,359) |  | (6,726) |
|  |  |  |  |  |  |  |
| **Net cash utilised in financing activities** |  | **12,304** |  | **(9,097)** |  | **(134,958)** |
|  |  |  |  |  |  |  |
| **Net increase in cash and cash equivalents** |  | **200,623** |  | **73,048** |  | **370,084** |
|  |  |  |  |  |  |  |
| **Cash and cash equivalents at beginning of the period** | 14 | **657,448** |  | **326,905** |  | **326,905** |
|  |  |  |  |  |  |  |
| Effect of foreign exchange rate changes on cash and cash equivalents |  | (10,117) |  | 23,016 |  | (39,541) |
|  |  |  |  |  |  |  |
| **Cash and cash equivalents at end of  the period** | 14 | **847,954** |  | **422,969** |  | **657,448** |

# GENERAL

The principal activities of Polyus Gold International Limited (“PGIL” or the “Company”) and its controlled entities (the “Group”) are the extraction, refining and sale of gold. Mining and processing facilities of the Group are located in the Krasnoyarsk and Irkutsk regions and Sakha Republic of the Russian Federation and in the Republic of Kazakhstan.

The Group also performs research, exploration and development works, primarily at the Natalka license area located in the Magadan region, Nezhdaninskoe license areas located in the Sakha Republic, Kyrgyzstan and the Republic of Kazakhstan. Further details regarding the nature of the business and of the significant subsidiaries of the Group are presented in note 21.

# BASIS OF PREPARATION AND PRESENTATION

## Going concern

In assessing its going concern status, the Directors have taken account of the Group’s financial position, expected future trading performance, its borrowings and available credit facilities and its capital expenditure commitments and plans, together with other risks facing the Group. After making appropriate enquiries, the Directors consider that the Group has adequate resources to continue in operational existence for at least the next 12 months from the date of these condensed consolidated interim financial statements and that it is appropriate to adopt the going concern basis in preparing these condensed consolidated interim financial statements.

## Compliance with the International Financial Reporting Standards

The same accounting policies, presentation and methods of computation have been followed in these condensed consolidated interim financial statements as were applied in the Group’s consolidated financial statements for the year ended 31 December 2011.

The condensed consolidated interim financial statements have been prepared in compliance with International Accounting Standard (“IAS”) 34 “*Interim Financial Reporting”.*

## Basis of presentation

The entities of the Group maintain their accounting records in accordance with the laws, accounting and reporting regulations of the jurisdiction in which they are incorporated and registered. The accounting principles and financial reporting procedures in these jurisdictions may differ substantially from those generally accepted under IFRS as adopted by the EU. Accordingly, such financial information has been adjusted to ensure that the condensed consolidated interim financial statements are presented in accordance with IFRS as adopted by the EU.

The condensed consolidated interim financial statements of the Group are prepared on the historical cost basis, except for mark-to-market valuation of certain financial instruments, in accordance with IAS 39 *“Financial Instruments: recognition and measurement”.*

**2. BASIS OF PREPARATION AND PRESENTATION (continued)**

## Standards and Interpretations in issue not yet adopted

At the date of approval of the condensed consolidated interim financial statements, the following new or amended IFRS standards have been issued by the IASB during the six months ended 30 June 2012, but are not mandatory for the current reporting period and therefore have not been applied:

|  |  |
| --- | --- |
|  | Effective  for annual periods beginning on or after |
|  |  |
| IFRS 7 “Financial Instruments: Disclosures” – amendment | 1 January 2013 |
| IFRS 9 “Financial Instruments – Classification and Measurement” | 1 January 2013 |
| IFRS 10 “Consolidated financial statements” | 1 January 2013 |
| IFRS 11 “Joint arrangements” | 1 January 2013 |
| IFRS 12 “Disclosure of interests in other entities” | 1 January 2013 |
| IFRS 13 “Fair value measurement” | 1 January 2013 |
| IAS 19 “Employee benefits” – amendment | 1 January 2013 |
| IAS 27 “Separate financial statements” – amendment | 1 January 2013 |
| IAS 28 “Investments in associates and joint ventures” – amendment | 1 January 2013 |
| IAS 32 “Financial instruments: Presentation” – amendment | 1 January 2014 |
| IAS 34 “Interim Financial Reporting” – amendment | 1 January 2013 |
| IFRIC 20 “Stripping costs in the Production Phase of a Surface mine” | 1 January 2013 |

The impact of the adoption of these standards and interpretations in the preparation of the consolidated financial statements in future periods is currently being assessed by Group’s management; however, no material effect on the Group’s financial position or results of its operations is anticipated.

## Critical accounting judgments, estimates and assumptions

The critical accounting judgments, estimates and assumptions made by management of the Group and applied in the accompanying condensed consolidated interim financial statements for the six months ended 30 June 2012 are consistent with those applied in the preparation of annual consolidated financial statements of the Group for the year ended 31 December 2011.

## Exchange rates

Exchange rates used in the preparation of the condensed consolidated interim financial statements were as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended 30 June 2012 |  | Six months ended 30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| **Russian Rouble/US Dollar** |  |  |  |  |  |
| Period end rate | 32.82 |  | 28.08 |  | 32.20 |
| Average for the period | 30.64 |  | 28.62 |  | 29.39 |
|  |  |  |  |  |  |
| **Kazakh Tenge/US Dollar** |  |  |  |  |  |
| Period end rate | 149.42 |  | 146.25 |  | 148.40 |
| Average for the period | 148.15 |  | 146.00 |  | 146.62 |

# disposal of subsidiaries

During the six months ended 30 June 2012 the following subsidiaries of the Group

* Romaltyn Mining S.R.L., Romaltyn Exploration S.R.L., Romaltyn Limited (previously attributable to Kazakhstan business unit);
* GRK Bargold Ltd and Yakutskoe GRP Ltd (previously attributable to the Exploration business unit),

were sold to independent not related parties.

Romaltyn Mining and Romaltyn Exploration (together, “the Romanian assets”) hold rights to various mining assets in Romania including a gold treatment plant with an annual processing capacity of   
2.5 million tonnes (currently not in operation) and a number of exploration properties. Romanian assets were acquired in 2009, together with the Group’s subsidiaries in Kazakhstan. The disposal of the Romanian assets was driven by the strategic objectives of the Group and the increased focus on our core large-scale operations.

GRK Bargold and Yakutskoe GRP hold rights to a number of exploration properties in Russia. The Group’s investment in GRK Bargold was fully impaired during the year ended 31 December 2011.

There were no contingent liabilities or deferred consideration applicable to the sale. All the proceeds were received in cash.

The following assets and liabilities were disposed during the six months ended 30 June 2012:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Romanian assets |  | GRK Bargold and Yakutskoe GRP assets |  | Total |
|  |  |  |  |  |  |
| Property, plant and equipment | 16,344 |  | - |  | 16,344 |
| Exploration and evaluation assets | 3,880 |  | 544 |  | 4,424 |
| Cash | 572 |  | 686 |  | 1,258 |
| Other assets | 900 |  | 18 |  | 918 |
| Site restoration and environmental obligations | (5,022) |  | - |  | (5,022) |
| Other liabilities | (1,947) |  | (12) |  | (1,959) |
|  |  |  |  |  |  |
| **Total net assets disposed** | **14,727** |  | **1,236** |  | **15,963** |
| Proceeds | 20,000 |  | 2,231 |  | 22,231 |
|  |  |  |  |  |  |
| **Gain on disposal** | **5,273** |  | **995** |  | **6,268** |

# segment information

For management purposes, the Group is organised in separate business segments defined by   
a combination of operating activities and geographical area. Separate financial information is available for each segment and reported regularly to the chief operating decision maker (“CODM”) and the Executive Committee. The Group’s seven identified reportable segments are located and described as follows:

* ***Krasnoyarsk business unit*** (Krasnoyarsk region of the Russian Federation) – Extraction, refining and sales of gold from the Olimpiada, Blagodatnoe and Titimukhta mines, as well as research, exploration and development work at Olimpiada deposits;
* ***Kazakhstan business unit*** (Republic of Kazakhstan and Kyrgyzstan), formed by the Kazakh Gold Group Limited – Extraction, refining and sales of gold from Aksu, Bestobe, Akzhal, Zholymbet mines, as well as exploration and evaluation works in Southern Karaultube;
* ***Irkutsk alluvial business unit*** (Irkutsk region, Bodaibo district of the Russian Federation) – Extraction, refining and sales of gold from several alluvial deposits;
* ***Irkutsk ore business unit*** (Irkutsk region, Bodaibo district of the Russian Federation) – Extraction, refining and sales of gold from Verninskoe, research, exploration and development works at Pervenetc, Verninskoe and Medvezhiy Ruchei deposits, and electricity and utilities production and sales in the Bodaibo district of the Irkutsk region;
* ***Yakutsk Kuranakh business unit*** (Sakha Republic of the Russian Federation) – Extraction, refining and sales of gold from the Kuranakh ore field;
* ***Exploration business unit*** – Comprising two operating segments that are combined into one reportable segment as they satisfy the criteria for aggregation:
* Yakutsk (Nezhdaninskoe) business unit (Sakha Republic of Russian Federation) – Research and exploration works at the Nezhdaninskoe deposit; and
* (Krasnoyarsk region, Irkutsk region, Amur region, and others) – Research and exploration works in several regions of the Russian Federation; and
* ***Magadan business unit*** (Magadan region of the Russian Federation) – Represented by   
  OJSC “Matrosov Mine” which performs development works at the Natalka deposit.

The reportable segments derive their revenue primarily from gold sales. The CODM performs an analysis of the operating results based on these separate business units and evaluates the reporting segment’s results, for purposes of resource allocation, based on the segment measure; segment profit before income tax excluding the finance costs, other sales, costs of other sales and income from investments.

Business segment assets and liabilities are not reviewed by the CODM and therefore are not disclosed in these condensed consolidated interim financial statements. Segment financial information provided to the CODM is prepared from the management accounts which are based on Russian or Kazakhstan accounting standards, respectively.

**4. SEGMENT INFORMATION** (**continued**)

The Group does not to allocate segment results of companies that perform management, investing activities and certain other administrative functions within its internal reporting.

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Gold  sales |  | Segment profit/(loss) |  | Capital expenditures |  | Depreciation and amortisation |
|  |  |  |  |  |  |  |  |
| For the six months ended  30 June 2012 |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |
| Krasnoyarsk business unit | 916,086 |  | 465,059 |  | 132,267 |  | 48,119 |
| Irkutsk alluvial business unit | 72,781 |  | 24,715 |  | 16,938 |  | 5,062 |
| Yakutsk Kuranakh business unit | 114,873 |  | 23,487 |  | 11,649 |  | 3,767 |
| Irkutsk ore business unit | 29,134 |  | 7,044 |  | 86,956 |  | 3,063 |
| Exploration business unit | - |  | (7,912) |  | 5,186 |  | 850 |
| Kazakhstan business unit | 90,992 |  | 22,906 |  | 20,988 |  | 9,700 |
| Magadan business unit | - |  | (10,606) |  | 23,146 |  | 1,577 |
|  |  |  |  |  |  |  |  |
| **Segment result** | **1,223,866** |  | **524,693** |  | **297,130** |  | **72,138** |
|  |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |
| **For the six months ended  30 June 2011** |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |
| Krasnoyarsk business unit | 669,570 |  | 342,265 |  | 105,278 |  | 46,352 |
| Irkutsk alluvial business unit | 66,644 |  | 6,588 |  | 15,685 |  | 3,981 |
| Yakutsk Kuranakh business unit | 78,662 |  | (3,735) |  | 1,475 |  | 3,845 |
| Irkutsk ore business unit | 3,590 |  | 1,797 |  | 37,493 |  | 3,528 |
| Exploration business unit | - |  | (6,305) |  | 3,100 |  | 434 |
| Kazakhstan business unit | 83,286 |  | 2,843 |  | 16,858 |  | 5,626 |
| Magadan business unit | - |  | (6,871) |  | 3,259 |  | 1,833 |
|  |  |  |  |  |  |  |  |
| **Segment result** | **901,752** |  | **336,582** |  | **183,148** |  | **65,599** |
|  |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |
| **For the year ended  31 December 2011** |  |  |  |  |  |  |  |
|  |  |  |  |  |  |  |  |
| Krasnoyarsk business unit | 1,641,380 |  | 918,078 |  | 236,780 |  | 104,821 |
| Irkutsk alluvial business unit | 350,213 |  | 102,795 |  | 22,808 |  | 6,550 |
| Yakutsk Kuranakh business unit | 184,735 |  | 13,797 |  | 12,569 |  | 8,298 |
| Irkutsk ore business unit | 3,497 |  | (13,042) |  | 111,751 |  | 7,307 |
| Exploration business unit | - |  | (14,107) |  | 11,213 |  | 973 |
| Kazakhstan business unit | 160,825 |  | 5,773 |  | 38,583 |  | 14,939 |
| Magadan business unit | - |  | (16,313) |  | 22,026 |  | 3,784 |
|  |  |  |  |  |  |  |  |
| **Segment result** | **2,340,650** |  | **996,981** |  | **455,730** |  | **146,672** |

Gold sales reported above represent revenue generated from external customers. There were no inter-segment gold sales during the periods ended 30 June 2012 and 2011 and the year ended   
31 December 2011.

**4. SEGMENT INFORMATION** (**continued**)

The segment measure of profit/(loss) reconciles to the IFRS profit before income tax as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| **Segment result** | **524,693** |  | **336,582** |  | **996,981** |
|  |  |  |  |  |  |
| *Differences between IFRS and management accounts:* |  |  |  |  |  |
| Capitalised exploration works | 20,750 |  | 3,368 |  | (206) |
| Provisions and accruals | (2,383) |  | (17,995) |  | (49,109) |
| Additional depreciation charge and amortisation of mineral rights | (15,141) |  | (28,046) |  | (41,277) |
| Calculation of gold-in-process at net production cost | 12,361 |  | (28,882) |  | (31,918) |
| Difference in stripping costs capitalisation | 5,058 |  | (3,812) |  | 20,711 |
| Other | 904 |  | (1,264) |  | (3,219) |
|  |  |  |  |  |  |
| Adjusted segment result | **546,242** |  | **259,951** |  | **891,963** |
| Unallocated central costs, results of financing and investing activities and differences in accounting treatment under IFRS | (7,320) |  | 7,249 |  | (126,896) |
|  |  |  |  |  |  |
| **Profit before income tax** | **538,922** |  | **267,200** |  | **765,067** |
|  |  |  |  |  |  |
| **Segment capital expenditures** | **297,130** |  | **183,148** |  | **455,730** |
|  |  |  |  |  |  |
| *Differences between IFRS and management accounts:* |  |  |  |  |  |
| Differences at the moment of recognition of capital expenditures | 8,081 |  | (11,653) |  | (85,268) |
| Reclassification of advances paid for property, plant and equipment and construction works | (5,455) |  | (10,365) |  | 20,148 |
| Reclassification of materials related to construction works | 21,511 |  | 4,455 |  | (9,322) |
| Differences in capitalised exploration and evaluation costs | 4,429 |  | 16,417 |  | (12,635) |
| Other | 2,877 |  | (1,397) |  | (1,821) |
|  |  |  |  |  |  |
| Adjusted segment capital expenditure | 328,573 |  | 180,605 |  | 366,832 |
| Unallocated central capital expenditures | 1,669 |  | 525 |  | 1,307 |
|  |  |  |  |  |  |
| **Capital expenditures** | **330,242** |  | **181,130** |  | **368,139** |
|  |  |  |  |  |  |
| **Segment depreciation and amortisation** | **72,138** |  | **65,599** |  | **146,672** |
|  |  |  |  |  |  |
| Additional depreciation charge | 13,608 |  | 17,824 |  | 27,878 |
| Amortisation of mineral rights | 1,533 |  | 10,222 |  | 13,399 |
|  |  |  |  |  |  |
| **Depreciation and amortisation** | **87,279** |  | **93,645** |  | **187,949** |

The Group’s information about its non-current assets other than financial instruments by geographical location is as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| Russian Federation | 2,529,958 |  | 2,634,359 |  | 2,371,841 |
| Republic of Kazakhstan | 313,659 |  | 291,931 |  | 308,358 |
| Kyrgyzstan | 31,617 |  | 33,805 |  | 31,084 |
| Romania | - |  | 16,501 |  | 17,170 |
| United Kingdom | 78 |  | 109 |  | 94 |
|  |  |  |  |  |  |
| **Total** | **2,875,312** |  | **2,976,705** |  | **2,728,547** |

**4. SEGMENT INFORMATION** (**continued**)

The impairment losses under IFRS in relation to Exploration and evaluation assets attributable to each reportable segment are presented as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Exploration business unit | 243 |  | 7,848 |  | 43,596 |
| Kazakhstan business unit | - |  | 1,594 |  | 1,707 |
| Krasnoyarsk business unit | - |  | 5,226 |  | 5,054 |
| Irkutsk ore business unit | - |  | 432 |  | 4,351 |
| Irkutsk alluvial business unit | - |  | - |  | - |
|  |  |  |  |  |  |
| **Total** | **243** |  | **15,100** |  | **54,708** |

The impairment losses under IFRS in relation to Property, plant and equipment attributable to each reportable segment are presented as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Kazakhstan business unit | 4,636 |  | - |  | 11,417 |
| Krasnoyarsk business unit | - |  | - |  | 4,891 |
| Irkutsk ore business unit | 1,058 |  | 7,644 |  | 7,193 |
| Magadan business unit | 11,622 |  | - |  | - |
|  |  |  |  |  |  |
| **Total** | **17,316** |  | **7,644** |  | **23,501** |

# GOld sales

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Refined gold | 1,132,874 |  | 818,466 |  | 2,179,825 |
| Other gold-bearing products | 90,992 |  | 83,286 |  | 160,825 |
|  |  |  |  |  |  |
| **Total** | **1,223,866** |  | **901,752** |  | **2,340,650** |

# COST OF GOLD SALES

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Fuel, consumables and spares | 232,550 |  | 194,171 |  | 410,243 |
| Labour | 157,860 |  | 122,268 |  | 288,866 |
| Tax on mining | 90,842 |  | 71,393 |  | 179,116 |
| Utilities | 28,288 |  | 29,595 |  | 55,140 |
| Outsourced mining services | 7,099 |  | 3,374 |  | 22,147 |
| Refining costs | 2,458 |  | 1,926 |  | 5,067 |
| Other | 42,417 |  | 26,481 |  | 75,696 |
|  |  |  |  |  |  |
| **Sub-total** | **561,514** |  | **449,208** |  | **1,036,275** |
|  |  |  |  |  |  |
| Amortisation and depreciation of operating assets (note 10) | 84,137 |  | 89,847 |  | 181,935 |
| (Capitalisation)/amortisation of deferred stripping costs, net | (2,343) |  | 17,136 |  | (7,335) |
| Increase in gold-in-process and refined gold inventories | (74,278) |  | (78,138) |  | (48,856) |
|  |  |  |  |  |  |
| **Total** | **569,030** |  | **478,053** |  | **1,162,019** |

# SELLING, GENERAL AND ADMINISTRATIVE EXPENSES

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Salaries | 68,586 |  | 43,591 |  | 116,295 |
| Professional services | 15,429 |  | 14,214 |  | 36,350 |
| Taxes other than mining and income taxes | 12,052 |  | 21,706 |  | 42,630 |
| Amortisation and depreciation | 2,149 |  | 2,580 |  | 4,830 |
| Other | 12,024 |  | 11,371 |  | 25,513 |
|  |  |  |  |  |  |
| **Total** | **110,240** |  | **93,462** |  | **225,618** |

# FINANCE COSTS

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Interest on borrowings | 16,387 |  | 16,546 |  | 31,241 |
| Unwinding of discounts | 6,102 |  | 6,166 |  | 11,999 |
| Debt modification expense | - |  | - |  | 26,928 |
| Other | - |  | - |  | 1,235 |
|  |  |  |  |  |  |
| **Total** | **22,489** |  | **22,712** |  | **71,403** |

# INCOME/(LOSS) FROM INVESTMENTS, net

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| **Income / (loss) from financial assets at fair value through profit and loss** |  |  |  |  |  |
| Loss on derivatives classified as held for trading | - |  | (8,661) |  | (8,661) |
| Income / (loss) from investments in listed companies held for trading | 2,215 |  | (7,032) |  | (20,984) |
|  |  |  |  |  |  |
| **Income from AFS investments** |  |  |  |  |  |
| Gain on disposal of AFS investments | - |  | 17,023 |  | 17,023 |
|  |  |  |  |  |  |
| Interest income on bank deposits | 17,325 |  | 6,902 |  | 16,252 |
|  |  |  |  |  |  |
| **Total** | **19,540** |  | **8,232** |  | **3,630** |

# PROPERTY, PLANT AND EQUIPMENT

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | Mining assets |  | Non-mining assets |  | Capital construction-in-progress |  | Total |
|  |  |  |  |  |  |  |  |
| **Cost** |  |  |  |  |  |  |  |
| **Balance at 31 December 2010** | **2,356,373** |  | **70,313** |  | **312,258** |  | **2,738,944** |
| Additions | 125,909 |  | 840 |  | 41,306 |  | **168,055** |
| Transfers from capital construction-in-progress | 2,297 |  | 280 |  | (2,577) |  | **-** |
| Change in decommissioning liabilities | (1,791) |  | - |  | - |  | **(1,791)** |
| Disposals | (11,466) |  | (278) |  | (86) |  | **(11,830)** |
| Disposal of subsidiary | (73) |  | - |  | - |  | **(73)** |
| Effect of translation to presentation currency | 194,987 |  | 5,803 |  | 24,484 |  | **225,274** |
| **Balance at 30 June 2011** | **2,666,236** |  | **76,958** |  | **375,385** |  | **3,118,579** |
| Additions | 34,765 |  | 13,546 |  | 120,079 |  | **168,390** |
| Transfers from capital construction-in-progress | 88,396 |  | (26,803) |  | (61,593) |  | **-** |
| Transfers from exploration and evaluation assets (note 11) | 264 |  | - |  | - |  | **264** |
| Change in decommissioning liabilities | 9,624 |  | - |  | - |  | **9,624** |
| Disposals | (14,159) |  | (190) |  | (374) |  | **(14,723)** |
| Effect of translation to presentation currency | (325,580) |  | (8,322) |  | (45,733) |  | **(379,635)** |
| **Balance at 31 December 2011** | **2,459,546** |  | **55,189** |  | **387,764** |  | **2,902,499** |
| Additions | 90,332 |  | 16,988 |  | 202,520 |  | **309,840** |
| Transfers from capital construction-in-progress | 29,354 |  | 3,191 |  | (32,545) |  | - |
| Transfers to exploration and evaluation assets (note 11) | (5,337) |  | - |  | - |  | **(5,337)** |
| Change in decommissioning liabilities | 1,364 |  | - |  | - |  | **1,364** |
| Disposals | (8,846) |  | (1,246) |  | (791) |  | **(10,883)** |
| Disposals of subsidiaries | (13,580) |  | - |  | (6,572) |  | **(20,152)** |
| Effect of translation to presentation currency | (48,648) |  | (2,230) |  | (17,179) |  | **(68,057)** |
| **Balance at 30 June 2012** | **2,504,185** |  | **71,892** |  | **533,197** |  | **3,109,274** |
|  |  |  |  |  |  |  |  |
| **Accumulated amortisation, depreciation and impairment** |  |  |  |  |  |  |  |
| **Balance at 31 December 2010** | **(634,041)** |  | **(29,591)** |  | **(16,676)** |  | **(680,308)** |
| Charge for the period | (102,518) |  | (2,718) |  | - |  | **(105,236)** |
| Disposals | 8,597 |  | 256 |  | - |  | **8,853** |
| Impairment | (7,639) |  | (5) |  | - |  | **(7,644)** |
| Effect of translation to presentation currency | (53,019) |  | (2,550) |  | (906) |  | **(56,475)** |
| **Balance at 30 June 2011** | **(788,620)** |  | **(34,608)** |  | **(17,582)** |  | **(840,810)** |
| Charge for the period | (98,505) |  | (1,998) |  | - |  | **(100,503)** |
| Transfers | (10,335) |  | 10,335 |  | - |  | **-** |
| Disposals | 9,575 |  | 354 |  | - |  | **9,929** |
| Impairment | (15,857) |  | - |  | - |  | **(15,857)** |
| Effect of translation to presentation currency | 96,127 |  | 3,548 |  | 1,486 |  | **101,161** |
| **Balance at 31 December 2011** | **(807,617)** |  | **(22,369)** |  | **(16,096)** |  | **(846,082)** |
| Charge for the period | (101,812) |  | (2,625) |  | - |  | **(104,437)** |
| Disposals | 7,029 |  | 171 |  | - |  | **7,200** |
| Disposals of subsidiaries | 3,808 |  | - |  | - |  | **3,808** |
| Impairment | (17,103) |  | - |  | (213) |  | **(17,316)** |
| Effect of translation to presentation currency | 24,252 |  | 616 |  | (113) |  | **24,755** |
| **Balance at 30 June 2012** | **(891,443)** |  | **(24,207)** |  | **(16,422)** |  | **(932,072)** |
|  |  |  |  |  |  |  |  |
| **Net book value** |  |  |  |  |  |  |  |
| **30 June 2011** | **1,877,616** |  | **42,350** |  | **357,803** |  | **2,277,769** |
|  |  |  |  |  |  |  |  |
| **31 December 2011** | **1,651,929** |  | **32,820** |  | **371,668** |  | **2,056,417** |
|  |  |  |  |  |  |  |  |
| **30 June 2012** | **1,612,742** |  | **47,685** |  | **516,775** |  | **2,177,202** |

**10. PROPERTY, PLANT AND EQUIPMENT (continued)**

During the six months ended 30 June 2012 impairment of mining assets in the amount of   
USD 11,622 thousand and USD 1,058 thousand were recognised following the decision to abandon activities related to the Omchak deposit and other deposits in Irkutsk ore business unit respectively.

The remaining amount of impairment charge was a result of impairment at the Kazakhstan business unit, due to reassessment of property, plant and equipment requirements and plans for their future use. As the result, certain assets’ net book value and expected economic useful life exceeded the anticipated recoverable value.

The carrying values of mineral rights included in mining assets were as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| Mineral rights | 326,096 |  | 368,303 |  | 335,470 |

Amortisation and depreciation charge is allocated as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Cost of gold sales (note 6) | 84,137 |  | 89,847 |  | 181,935 |
| Selling, general and administrative expenses and cost of other sales | 3,142 |  | 3,798 |  | 6,014 |
| Capitalised within property, plant and equipment | 17,158 |  | 11,591 |  | 17,790 |
|  |  |  |  |  |  |
| **Total** | **104,437** |  | **105,236** |  | **205,739** |

The carrying values of property, plant and equipment pledged against a bank guarantee liability were as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| Pledged property, plant and equipment | - |  | 3,620 |  | 4,613 |

# exploration and evaluation assets

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Six months ended  31 December 2011 |
|  |  |  |  |  |  |
| **Balance at beginning of the period** | **399,846** |  | **442,316** |  | **462,552** |
| Additions | 20,402 |  | 13,075 |  | 18,619 |
| Transfers from / (to) mining assets (note 10) | 5,337 |  | - |  | (264) |
| Impairment | (243) |  | (15,100) |  | (39,608) |
| Disposals of subsidiaries | (4,424) |  | - |  | - |
| Effect of translation to presentation currency | (8,596) |  | 22,261 |  | (41,453) |
|  |  |  |  |  |  |
| **Balance at end of the period** | **412,322** |  | **462,552** |  | **399,846** |

# INVESTMENTS IN SECURITIES AND OTHER FINANCIAL ASSETS

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| Non-current |  |  |  |  |  |
| Loans receivable | 3,330 |  | 4,128 |  | 3,643 |
| Other | - |  | 339 |  | - |
|  |  |  |  |  |  |
| **Total** | **3,330** |  | **4,467** |  | **3,643** |
|  |  |  |  |  |  |
| **Current** |  |  |  |  |  |
| AFS equity investments | 32,953 |  | 43,311 |  | 34,744 |
| Bank deposits | 19,504 |  | 134,669 |  | 12,175 |
| Equity investments in listed companies held for trading | 10,659 |  | 33,400 |  | 14,857 |
| Other | 591 |  | 1,686 |  | 1,692 |
|  |  |  |  |  |  |
| **Total** | **63,707** |  | **213,066** |  | **63,468** |

## AFS investments, carried at fair value

At 30 June 2012 and 2011 and at 31 December 2011 AFS equity investments primarily comprised shares owned in Rosfund, SPC (Cayman Islands) acquired in July 2006.

Rosfund, SPC invests in securities and other financial assets (equity investments in listed companies, bonds and depositary receipts).

## Bank deposits

Bank deposits at 6.66-9.00% (30 June 2011: 2.14-5.75%, 31 December 2011: 2.14-8.05%) per annum are denominated in RUB with a maturity date at the end of September 2012.

# INVENTORIES

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| **Inventories expected to be recovered after twelve months** |  |  |  |  |  |
| Stockpiles | 220,360 |  | 187,559 |  | 207,789 |
|  |  |  |  |  |  |
| **Total** | **220,360** |  | **187,559** |  | **207,789** |
|  |  |  |  |  |  |
| **Inventories expected to be recovered in the next twelve months** |  |  |  |  |  |
| Gold-in-process at net production cost | 229,174 |  | 257,419 |  | 163,758 |
| Refined gold at net production cost | 6,558 |  | 4,047 |  | 24,757 |
|  |  |  |  |  |  |
| **Total metal inventories** | **235,732** |  | **261,466** |  | **188,515** |
|  |  |  |  |  |  |
| Stores and materials at cost | 368,773 |  | 337,490 |  | 354,508 |
|  |  |  |  |  |  |
| **Total** | **604,505** |  | **598,956** |  | **543,023** |

# CASH AND CASH EQUIVALENTS

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| Bank deposits - RUB | 344,339 |  | 71,933 |  | 487,467 |
| - foreign currencies | 180,463 |  | - |  |  |
| Current bank accounts - RUB | 106,616 |  | 237,104 |  | 146,761 |
| - foreign currencies | 215,880 |  | 111,833 |  | 21,992 |
| Other cash and cash equivalents | 656 |  | 2,099 |  | 1,228 |
|  |  |  |  |  |  |
| **Total** | **847,954** |  | **422,969** |  | **657,448** |

Bank deposits are denominated in RUB and USD and bear interest of 1.65-8.50% per annum with original maturity date within three months.

# SHARE CAPITAL

Issued and fully paid up ordinary shares of PGIL as of 30 June 2012 comprised 3,032,150 thousand shares. Number of the authorised share capital of the Company comprised 3,600,000 thousand shares with a par value of GBP0.0001 per share.

## Treasury shares

On 11 May 2012, Jenington International Inc, a subsidiary of the Group, completed the sale of   
the Company’s treasury shares. 151,608 thousand shares were sold to Chengdong Investment Corporation, a wholly-owned subsidiary of CIC International Co. Ltd., and 50,198 thousand shares and 25,154 thousand Level I GDRs (one GDR is equal to one ordinary share) to JSC VTB Bank. The gross proceeds received from the two transactions were equal to USD635,487 thousand, less USD11,115 thousand of arrangement fees directly attributable to the sale of the treasury shares.

In connection with the sale of treasury shares, the Group transferred the balance of USD37,475 thousand relating to the call options to acquire all the rights and obligations under the Gold Lion Holdings convertible loan agreements [see note 16(ii)] from treasury share account to additional paid-in capital.

## Dividends to shareholders of the Company

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Six months  ended  31 December  2011 |
|  |  |  |  |  |  |
| Dividend declared during the period, USD thousand | 124,318 |  | 72,327 |  | - |
| Dividend declared during the period, US cents per share | 0.04 |  | 0.02 |  | - |

# Borrowings

|  |  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  |  | 30 June 2012 | | |  | 30 June 2011 | | |  | 31 December 2011 | | |
|  |  | Nominal  rate % |  | Outstanding balance |  | Nominal  rate % |  | Outstanding balance |  | Nominal  rate % |  | Outstanding balance |
|  |  |  |  |  |  |  |  |  |  |  |  |  |
| Guaranteed senior notes | (i) | - |  | - |  | 9.37% |  | 178,047 |  | 9.875% |  | 204,520 |
| Loans payable to Gold Lion Holdings Limited | (ii) | 10.00% |  | 37,072 |  | 10.00% |  | 31,922 |  | 10.00% |  | 34,160 |
| Societe Generale credit facility | (iii) | - |  | - |  | - |  | - |  | 1 months USD LIBOR + 1.95% |  | 230,000 |
| VTB credit facility | (iv) | - |  | - |  | - |  | - |  | 3 months USD LIBOR + 2.25% |  | 230,000 |
| Societe Generale credit facility  (OJSC “Pervenets”) | (v) | 3 months USD LIBOR + 2.4% |  | 50,000 |  | - |  | - |  | 3 months USD LIBOR + 2.4% |  | 50,000 |
| Unicredit Bank credit facility  (OJSC “Pervenets”) | (vi) | 3 months USD LIBOR + 2.4% |  | 50,000 |  |  |  | - |  | 3 months USD LIBOR + 2.4% |  | 50,000 |
| HSBC credit facility | (vii) | 3 months USD LIBOR+3%. |  | 99,125 |  | - |  | - |  | - |  | - |
| Unicredit Bank credit facility | (viii) | 3 months USD LIBOR+2.95%. |  | 99,312 |  | - |  | - |  | - |  | - |
|  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Total** |  |  |  | **335,509** |  |  |  | **209,969** |  |  |  | **798,680** |
|  |  |  |  |  |  |  |  |  |  |  |  |  |
| Less: current portion due within twelve months |  |  |  | 33,333 |  |  |  | - |  |  |  | 675,632 |
|  |  |  |  |  |  |  |  |  |  |  |  |  |
| **Long-term borrowings** |  |  |  | **302,176** |  |  |  | **209,969** |  |  |  | **123,048** |

### Summary of borrowing agreements

1. **Guaranteed senior notes**

On 15 March 2012, USD200 million guaranteed senior notes were redeemed at 102.344% of nominal value funded by two USD100 million loans from HSBC and Unicredit Bank, see note (vii) and (viii) below.

1. **Loans payable to Gold Lion Holdings Limited**

On 11 June 2009, PGIL (formerly KazakhGold) signed two loan agreements with Gold Lion Holdings Limited, an entity that was, at that time, a related party. The loan agreements have a 10% interest rate per annum. Principal amounts of USD21,650 thousand and USD9,375 thousand together with accrued interest are payable on 6 November 2014 in full or a part is convertible into PGIL’s (formerly KazakhGold) ordinary shares (see note 15) at a rate of USD 1.50 per one share. Conversion is subject to several restrictions, including the Republic of Kazakhstan’s regulatory approval and approval from the Company. In September 2009, Gold Lion Holdings Limited granted a call option to Jenington, or any other direct or indirect subsidiary of Polyus Gold, to acquire all the rights and interests under these loan agreements, including the conversion right.

The effective interest rate on these loans was 16% per annum.

1. **Societe Generale credit facility**

On 15 May 2012 the Societe Generale credit facility and corresponding accrued interest were fully repaid.

**16. BORROWINGS (continued)**

1. **VTB credit facility**

On 15 May 2012, the VTB credit facility and corresponding accrued interest were fully repaid.

1. **Societe Generale credit facility to OJSC “Pervenets”**

On 4 October 2011, OJSC “Pervenets”, a subsidiary of the Group, entered into a three year   
USD 100 million term loan facility agreement with Societe Generale as a lender to fund general corporate purposes. On 6 October 2011 Societe Generale transferred USD50 million of the facility to a new lender, Unicredit Bank [see note (vi) below]. As of 30 June 2012 USD50 million had been drawn down. The facility is to be repaid in nine equal instalments in intervals of three months starting from 4 October 2012.

1. **Unicredit Bank credit facility to OJSC “Pervenets”**

On 6 October 2011 Societe Generale transferred USD50 million of the facility [see note (v) above] to a new lender Unicredit Bank. As of 30 June 2012 USD50 million had been drawn down. The facility is to be repaid in nine equal instalments in intervals of three months starting from 4 October 2012.

1. **HSBC credit facility**

On 10 February 2012, the Group entered into a three year USD100 million credit facility with HSBC to fund the redemption of Guaranteed senior notes [see note (i)]. The interest rate is set at 3 months USD LIBOR+3%. The facility was fully utilised as of 30 June 2012.

1. **Unicredit Bank credit facility**

On 29 December 2011, PGIL entered into a two year USD100 million facility agreement arranged by Unicredit Bank to fund the redemption of Guaranteed senior notes [see note (i)]. The interest rate is set at LIBOR + 2.95%. The facility was fully utilised as of 30 June 2012.

1. **Unused credit facilities**

On 15 March 2012, CJSC “Gold Mining Company Polyus”, a subsidiary of the Group, entered into   
a three year RUB 10 billion (approximately USD 305 million) credit line with VTB to fund its general corporate purposes. The interest rate is subject for a separate agreement under each of the credit line drawdowns but could not exceed 20% or MosPrime Rate + 6.5% for RUB denominated drawdown and 14% or LIBOR/EURIBOR + 13.5% – for USD/EURO denominated drawdown.

As of 30 June 2012 a USD67,502 thousand export financing credit facility agreement with Societe Generale as a lender for making available the extension of financing to be used for the purchase of goods and services and related exposure fees was not used. The establishment of the facility is for facilitation of exports from the United States of America and guaranteed by Export-Import Bank of the United States.

HSBC, Unicredit Bank and Societe Generale credit facilities contain certain financial covenants.   
The Group believes that it was in compliance with these covenants as of 30 June 2012.

# Notes to the consolidated statement of Cash flows

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | Note | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |  |
| **Profit before income tax** |  | **538,922** |  | **267,200** |  | **765,067** |
|  |  |  |  |  |  |  |
| Adjustments for: |  |  |  |  |  |  |
| Amortisation and depreciation | 10 | 87,279 |  | 93,645 |  | 187,949 |
| Finance costs | 8 | 22,489 |  | 22,712 |  | 71,403 |
| Expensed stripping cost |  | 6,164 |  | 27,070 |  | 10,935 |
| Impairment of stockpiles |  | - |  | 25,881 |  | 25,209 |
| Impairment of exploration and evaluation assets | 11 | 243 |  | 15,100 |  | 54,708 |
| Impairment of property, plant and equipment | 10 | 17,316 |  | 7,644 |  | 23,501 |
| Loss on disposal of property, plant and equipment |  | 1,412 |  | 2,624 |  | 5,933 |
| Change in allowance for reimbursable value added and tax provision |  | (91) |  | (288) |  | 6,602 |
| Gain from disposal of subsidiaries | 3 | (6,268) |  | - |  | - |
| Income from investments | 9 | (19,540) |  | (8,232) |  | (3,630) |
| Change in allowance for doubtful debts |  | 42 |  | 805 |  | (546) |
| Foreign exchange (gain) loss, net |  | (7,578) |  | (2,049) |  | 5,814 |
| Other |  | (6,731) |  | 3,612 |  | 3,971 |
|  |  |  |  |  |  |  |
|  |  | **633,659** |  | **455,724** |  | **1,156,916** |
|  |  |  |  |  |  |  |
| Movements in working capital |  |  |  |  |  |  |
| Inventories |  | (91,389) |  | (103,325) |  | (168,688) |
| Trade and other receivables |  | (8,174) |  | (7,047) |  | (5,811) |
| Advances paid to suppliers and prepaid expenses |  | (1,392) |  | (857) |  | (354) |
| Taxes receivable |  | 4,781 |  | (11,090) |  | 8,029 |
| Deferred expenditures |  | (39,173) |  | 26,459 |  | (230) |
| Trade and other payables and accrued expenses |  | 67,499 |  | 1,720 |  | 29,813 |
| Other non-current liabilities |  | 1,885 |  | 4,322 |  | 4,026 |
| Other taxes payable |  | 6,754 |  | 215 |  | (4,130) |
|  |  |  |  |  |  |  |
| **Cash flows from operations** |  | **574,450** |  | **366,121** |  | **1,019,571** |
|  |  |  |  |  |  |  |
| Interest paid |  | (21,620) |  | (9,375) |  | (23,423) |
| Income tax paid |  | (101,590) |  | (65,872) |  | (230,743) |
|  |  |  |  |  |  |  |
| **Net cash generated from operating activities** |  | **451,240** |  | **290,874** |  | **765,405** |

# RELATED PARTIES

Related parties include substantial shareholders, entities under common ownership and control with the Group and members of key management personnel. The Company and its subsidiaries, in the ordinary course of business, enter into purchase and service transactions with related parties. The terms of these transactions would not necessarily be on similar terms had the Group entered into the transactions with third parties.

The Group had no transactions with its substantial shareholders during the six-month periods ended 30 June 2012 and 30 June 2011 and for the year ended 31 December 2011, except for the Reorganisation described in the annual consolidated financial statements for the year ended 31 December 2011.

## Entities under common ownership

The Group had the following outstanding balances with entities under common control:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| Cash and cash equivalents at Bank “Mezhdunarodniy finansoviy club” | 112,257 |  | 107,018 |  | 149,323 |
| Investments in securities and other financial assets at “Mezhdunarodniy finansoviy club” | 9,694 |  | - |  | 1,553 |
| Prepayments to suppliers | 679 |  | 1,305 |  | 216 |

The amounts outstanding at 30 June 2012 are unsecured and expected to be settled in cash. No expense has been recognised in the reporting period for bad or doubtful debts in respect of the amounts owed by related parties.

The Group entered into the following transactions with entities under common control:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Purchase of goods and services | 1,863 |  | 2,261 |  | 2,224 |
| Interest income | 4,323 |  | 1,335 |  | 5,136 |

## Key management personnel

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | Six months ended  30 June 2012 |  | Six months ended  30 June 2011 |  | Year ended  31 December 2011 |
|  |  |  |  |  |  |
| Short-term compensation of key management personnel amounted to | 24,224 |  | 8,317 |  | 24,495 |

# COMMITMENTS AND CONTINGENCIES

## Commitments

### Capital commitments

The Group’s contracted capital expenditure commitments are as follows:

|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
| --- | --- | --- | --- | --- | --- |
|  |  |  |  |  |  |
| Contracted capital expenditure commitments | 234,183 |  | 186,138 |  | 107,019 |

### Operating leases: Group as a lessee

The land in the Russian Federation on which the Group’s production facilities are located is owned by the state. The Group leases this land through operating lease agreements, which expire in various years through 2060.

Future minimum lease payments due under non-cancellable operating lease agreements at the end of the period were as follows:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |
| Due within one year | 3,676 |  | 3,760 |  | 4,275 |
| From one to five years | 7,428 |  | 8,975 |  | 7,629 |
| Thereafter | 16,423 |  | 20,282 |  | 17,199 |
|  |  |  |  |  |  |
| **Total** | **27,527** |  | **33,017** |  | **29,103** |

## Contingencies

### Litigations

In the ordinary course of business, the Group is a party to litigation matters in a number of jurisdictions, the outcome of which is uncertain and could give rise to adverse outcomes. At the date of issuance of these condensed consolidated interim financial statements the Group was party to a number of claims and litigation, most of which are not material, except:

* A lawsuit against Kazakhaltyn MMC JSC with a potential exposure of USD15,000 thousand. The lawsuit is at the initial stage of investigation. Management believes that this claim will not have a material adverse impact on the Group;
* A dispute between the former and current principal shareholders of PGIL is described in paragraph “KazakhGold dispute” below.

**19. COMMITMENTS AND CONTINGENCIES (continued)**

## KazakhGold dispute

A dispute between the former and current principal shareholders of PGIL, whereby the current shareholders were asserting that the former shareholders were negligent in their fiduciary responsibilities related to KazakhGold, herewith the sequence of events, to date:

* on 10 April 2011, the Group entered into a Restated and Amended Principal Agreement   
  (the “RAPA”), and a Settlement Deed in respect of the claims which provides for a conditional settlement and release of the orders, judgments and claims, whether in litigation, arbitration or otherwise, initiated, inter alia in the UK, Jersey, the BVI, or Jenington and Kazakhaltyn, on the one hand, and the Assaubayev family, on the other hand, and all of their respective subsidiaries and affiliates, relating to the matters referred to in those proceedings or otherwise arising in respect of the original acquisition of 65 percent of KazakhGold by Jenington, without any admission of liability on either part (the “Settlement Deed”). Pursuant to the RAPA, AltynGroup (Assaubayev family) agreed to acquire the Company’s operating subsidiaries in Kazakhstan, Romania and Kyrgyzstan in tranches. The aggregate transaction price for all the shares is USD 509 million, as well as the provision of funds required to repay the loan provided to KazakhGold by Jenington. The sale of the operating subsidiaries is subject of numerous conditions, most of which are outstanding, and uncertain as to resolution at the date of these condensed consolidated interim financial statements;
* in May 2011, the Ministry of Industry and New Technologies of Kazakhstan (the “MINT”) granted its approval to the proposed Reorganisation of KazakhGold and Polyus Gold and to the sale of 100% of the shares in Kazakhaltyn MMC JSC to AltynGroup. MINT has also revoked its previous letters, which annulled the waiver obtained for the partial offer by Jenington International Inc. for 50.1% of shares in KazakhGold, which was completed in August 2009, and the waivers obtained in September 2010 for the proposed Reorganisation between Polyus Gold and KazakhGold and the US$100 million equity placing completed by KazakhGold on 1 July 2010;
* in May 2011, criminal investigations by the Agency on Economic and Corruption Crimes of the Republic of Kazakhstan (“AECC”) against three members of KazakhGold's Board of Directors were terminated.
* On 12 September 2011, the Company entered into a deed of amendment (the “RAPA Amendment”) to the RAPA dated 10 April 2011 for the sale of its operating subsidiaries in Kazakhstan, Romania and Kyrgyzstan with AltynGroup, under which the parties have agreed to extend the date of the First Tranche Completion until 12 October 2011 and made a number of consequential changes to reflect a corresponding extension of other deadlines set forth in the RAPA and the documentary stand-by letter of credit for USD 100,000,000 obtained by the Company pursuant to the terms of the RAPA.
* On 13 October 2011, the Group announced that it entered into a second deed of amendment to the RAPA dated 10 April 2011 for the sale of its operating subsidiaries and related matters, as amended by the deed of amendment dated 12 September 2011, with AltynGroup, under which the parties agreed to further extend the date of the First Tranche Completion until 12 December 2011 and made a number of consequential changes to reflect a corresponding extension of other deadlines set forth in the RAPA and the documentary stand-by letter of credit for USD100,000 thousand obtained by the Company pursuant to the terms of the RAPA.
* The Company has terminated the RAPA with AltynGroup given that the First Tranche Completion under the RAPA did not occur by the First Tranche Cut-Off Date. The Letter of Credit, which was issued in favour of PGIL under the terms of the RAPA, has been extended until 29 June 2012 and remains in full force and effect.
* At 8 June 2012 Sale and Purchase Agreement between the Company, Romanshorn, Jenington (all part of PGIL Group) and AltynGroup Holdings Korlatolt Felelossegu Tarsasag controlled by the Assaubayev family (further AltynGroup Holdings) was signed, according to which all Kazakhstan and Kirgizia subsidiaries of the Group were to be sold to AltynGroup Holdings.

**19. COMMITMENTS AND CONTINGENCIES (continued)**

* By the end of June 2012 year the following SPA conditions were satisfied:

1. At 14 June 2012 Gold Lion Holdings Limited signed a Deed of Novation of the Company’s loans to Jenington, according to which all rights for loans payable by the Company to Gold Lion Holdings Limited will be transferred to Jenington for zero consideration upon the earlier of the Completion Date under SPA or 30 September 2012;
2. At 20 June 2012 AltynGroup Holdings has made a prepayment to the Company in amount of USD40 million by making a drawing under the documentary stand-by letter of credit for USD100 million. The amount was treated as an advance received.

* The SPA contains certain conditions and some of them are beyond the Company’s control (see note 20). Besides required approvals from Kazakhstan authorities, the deal can be cancelled by any party at any time, until the consideration is paid by AltynGroup Holdings, thus the Company concluded that Kazakhstan and Kirgizia assets shall be treated as continuous operations, until the sale becomes highly probable.

### Insurance

The insurance industry is not yet well developed in the Russian Federation and the Republic of Kazakhstan and many forms of insurance protection common in more economically developed countries are not yet available on comparable terms. The Group does not have full insurance coverage for its mining, processing and transportation facilities, for business interruption, or for third party liabilities in respect of property or environmental damage arising from accidents on the Group’s property or relating to the Group’s operations, other than limited coverage required by law.

The Group, as a participant in exploration and mining activities may become subject to liability for risks that cannot be insured against, or against which it may elect not to be insured because of high premium costs. Losses from uninsured risks may cause the Group to incur costs that could have a material adverse effect on the Group’s business and financial condition.

### Taxation contingencies in the Russian Federation

Commercial legislation of Russian Federation, including tax legislation, is subject to varying interpretations and frequent changes. In addition, there is a risk of tax authorities making arbitrary judgments of business activities. If a particular treatment, based on management’s judgment of the Group’s business activities, was to be challenged by the tax authorities, the Group may be assessed additional taxes, penalties and interest.

Generally, taxpayers are subject to tax audits with respect to three calendar years preceding the year of the audit. However, completed audits do not exclude the possibility of subsequent additional tax audits performed by upper-level tax inspectorates reviewing the results of tax audits of their subordinate tax inspectorates. Also according to the clarification of the Russian Constitutional Court the statute of limitation for tax liabilities may be extended beyond the three year term set forth in the tax legislation, if a court determines that the taxpayers has obstructed or hindered a tax inspection.

The management of the Group is confident that applicable taxes have all been accrued and, consequently, creation of respective provisions is not required.

In terms of Russian tax legislation, authorities have a period of up to three years to re-open tax declarations for further inspection. Changes in the tax system that may be applied retrospectively by authorities could affect the Group’s previously submitted and assessed tax declarations.

With regards to matters where practice concerning payment of taxes is unclear, management estimated the there was no tax exposure at 30 June 2012 (USD2,607 thousand at 31 December 2011 and USD3,842 thousand at 30 June 2011).

**19. COMMITMENTS AND CONTINGENCIES (continued)**

### Environmental matters

The Group is subject to extensive federal, local environmental controls and regulations in the regions in which it operates. The Group’s operations involve the discharge of materials and contaminants into the environment, disturbance of land that could potentially impact on flora and fauna, and give rise to other environmental concerns.

The Group’s management believes that its mining and production technologies are in compliance with the existing environmental legislation in the countries in which it operates. However, environmental laws and regulations continue to evolve. The Group is unable to predict the timing or extent to which those laws and regulations may change. Such change, if it occurs, may require that the Group modernise technology to meet more stringent standards.

The Group is obliged in terms of various laws, mining licenses and ‘use of mineral rights’ agreements to decommission mine facilities on cessation of its mining operations and to restore and rehabilitate the environment. Management of the Group regularly reassesses site restoration and environmental obligations for its operations. Estimations are based on management’s understanding of the current legal requirements and the terms of the license agreements. Should the requirements of applicable environmental legislation change or be clarified, the Group may incur additional site restoration and environmental obligations.

# subsequent EVENTS

On 25 July 2012, OJSC “Matrosov Mine”, a subsidiary of the Company, entered into a finance agreement with VTB Bank for a total amount of up to RUB5 billion (approximately USD152 million). The facility will be utilised in the form of letters of credit issued by VTB Bank on the subsidiary’s request, with the repayment period not later than 5 years after the drawdown date at an interest rate of 10% per year. The facility will be used to support the purchase of equipment for the Natalka project. CJSC “Gold Mining Company Polyus” guaranteed liabilities of the subsidiary under all the finance agreements.

Certain conditions of the SPA with AltynGroup Holdings (see note 19) were not met and negotiations are on-going.

With the exception of the above there have been no material reportable events since 30 June 2012.

# INVESTMENTS IN SIGNIFICANT SUBSIDIARIES

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  |  |  | Effective % held1 | | | | |
| Subsidiaries | Incorporation | Nature of business | 30 June  2012 |  | 30 June  2011 |  | 31 December 2011 |
|  |  |  |  |  |  |  |  |
| OJSC “Polyus Gold”2 | Russian Federation | Management company | 95 |  | 89 |  | 95 |
| CJSC “Gold Mining Company Polyus” | Russian Federation | Mining | 95 |  | 89 |  | 95 |
| OJSC “Aldanzoloto GRK” | Russian Federation | Mining | 95 |  | 89 |  | 95 |
| OJSC “Lenzoloto” | Russian Federation | Market agent | 61 |  | 57 |  | 61 |
| LLC “Lenskaya Zolotorudnaya Company” | Russian Federation | Market agent | n/a |  | 89 |  | n/a |
| CJSC “ZDK Lenzoloto” | Russian Federation | Mining | 63 |  | 59 |  | 63 |
| CJSC “Lensib” 3 | Russian Federation | Mining | 38 |  | 36 |  | 38 |
| CJSC “Svetliy” | Russian Federation | Mining | 53 |  | 50 |  | 53 |
| CJSC “Marakan” | Russian Federation | Mining | 53 |  | 50 |  | 53 |
| CJSC “Dalnaya Taiga” | Russian Federation | Mining | 52 |  | 48 |  | 52 |
| CJSC “Sevzoto” 3 | Russian Federation | Mining | 41 |  | 38 |  | 41 |
| CJSC “GRK Sukhoy Log” | Russian Federation | Mining | n/a |  | 89 |  | n/a |
| OJSC “Matrosov Mine” | Russian Federation | Mining  (development stage) | 95 |  | 89 |  | 95 |
| CJSC “Tonoda” | Russian Federation | Mining  (exploration stage) | 95 |  | 89 |  | 95 |
| OJSC “Pervenets” | Russian Federation | Mining  (development stage) | 95 |  | 89 |  | 95 |
| OJSC “South-Verkhoyansk Mining Company” | Russian Federation | Mining  (development stage) | 95 |  | 89 |  | 95 |
| Polyus Exploration Limited | British Virgin Islands | Geological research | 95 |  | 89 |  | 95 |
| JSC “MMC Kazakhaltyn” | Republic of Kazakhstan | Mining | 100 |  | 100 |  | 100 |
| Jenington International Inc. | British Virgin Islands | Market agent | 95 |  | 89 |  | 95 |
| Polyus Investments Limited | Cyprus | Market agent | 95 |  | 89 |  | 95 |

1. Effective % held by the Company, including holdings by other subsidiaries of the Group.
2. Effective % includes 92.95% of ordinary shares held directly by the Company as at 30 June 2012 and 31 December 2011 and 89.14% as at 30 June 2011.
3. The Company maintains control of these entities as it continues to govern their financial and operating policies through its ability to appoint the Board of Directors. A majority of the Board members for these entities are representatives of the Company and are therefore consolidated even though the effective interest is less than 50%.

1. 1 H1 2012 production volumes include 670 thousand ounces of refined gold produced by the Group’s mines in Russia and 51 thousand ounces of gold produced by the Kazakhstan operations in the form of sludge, flotation and gravitation concentrates and other semi-products. H1 2011 production volumes include 554 thousand ounces of refined gold produced by the Group’s mines in Russia and 57 thousand ounces of gold produced by the Kazakhstan operations in the form of sludge, flotation and gravitation concentrates and other semi-products. [↑](#footnote-ref-1)