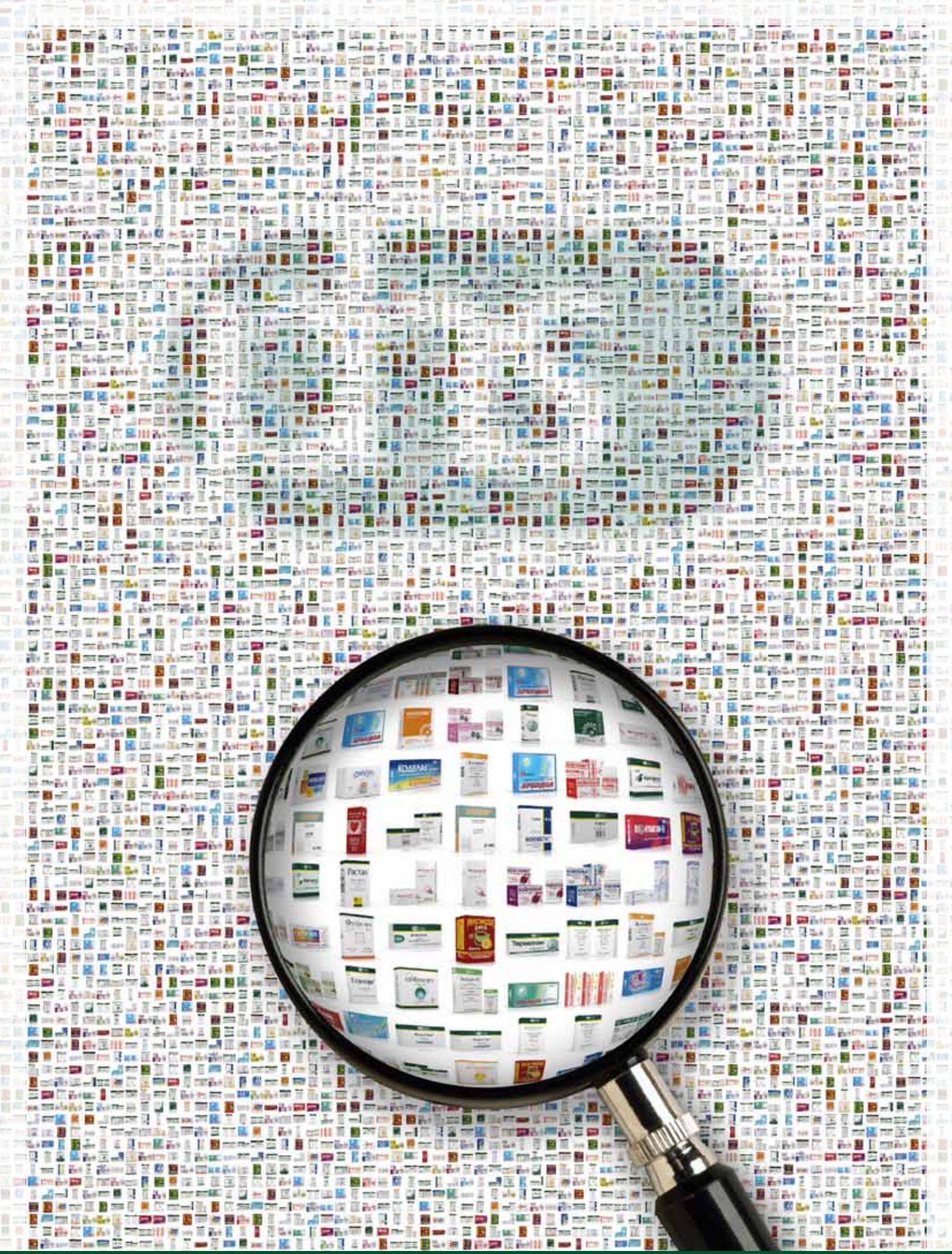


Pharmstandard annual report 2010

Pharmstandard

Wecare

Annual report 2010

Pharmstandard

Wecare®

CEO Statement

Dear shareholders and partners,

I am pleased to present to you Pharmstandard Annual Report for 2010.

This was truly a period of change, a period when new laws and regulations were enacted:

- the new law on the circulation of pharmaceuticals;
- the new regulations covering drug registration, pre-clinical and clinical trials;
- the new method of registration of maximum selling prices for Vital and Essential Pharmaceuticals.

Successful management allowed the Company to implement its plans and meet the challenges and ensured that its sales grew by 23% reaching one billion dollars, for the first time ever.

We increased our sales twofold, in comparison with 2008. This became possible due to the investment in marketing and promotion of the Company's products in the retail segment of the market; and to our active participation in the state procurement programmes at the federal and regional levels, both with our own products and with third parties products.

In 2010, we completed localisation of the final stages of production of such hi-tech pharmaceuticals as Velcade®, Mabthera® and Pulmozyme®. Pharmstandard agreed with Johnson & Johnson and Hoffmann-la Roche to localise the production of Prezista® and Tamiflu®. The possibility of our co-operation is the result of our continuing investment in production facilities and quality control management to ensure the Company is ready for the transition to the new GMP standards in 2014.

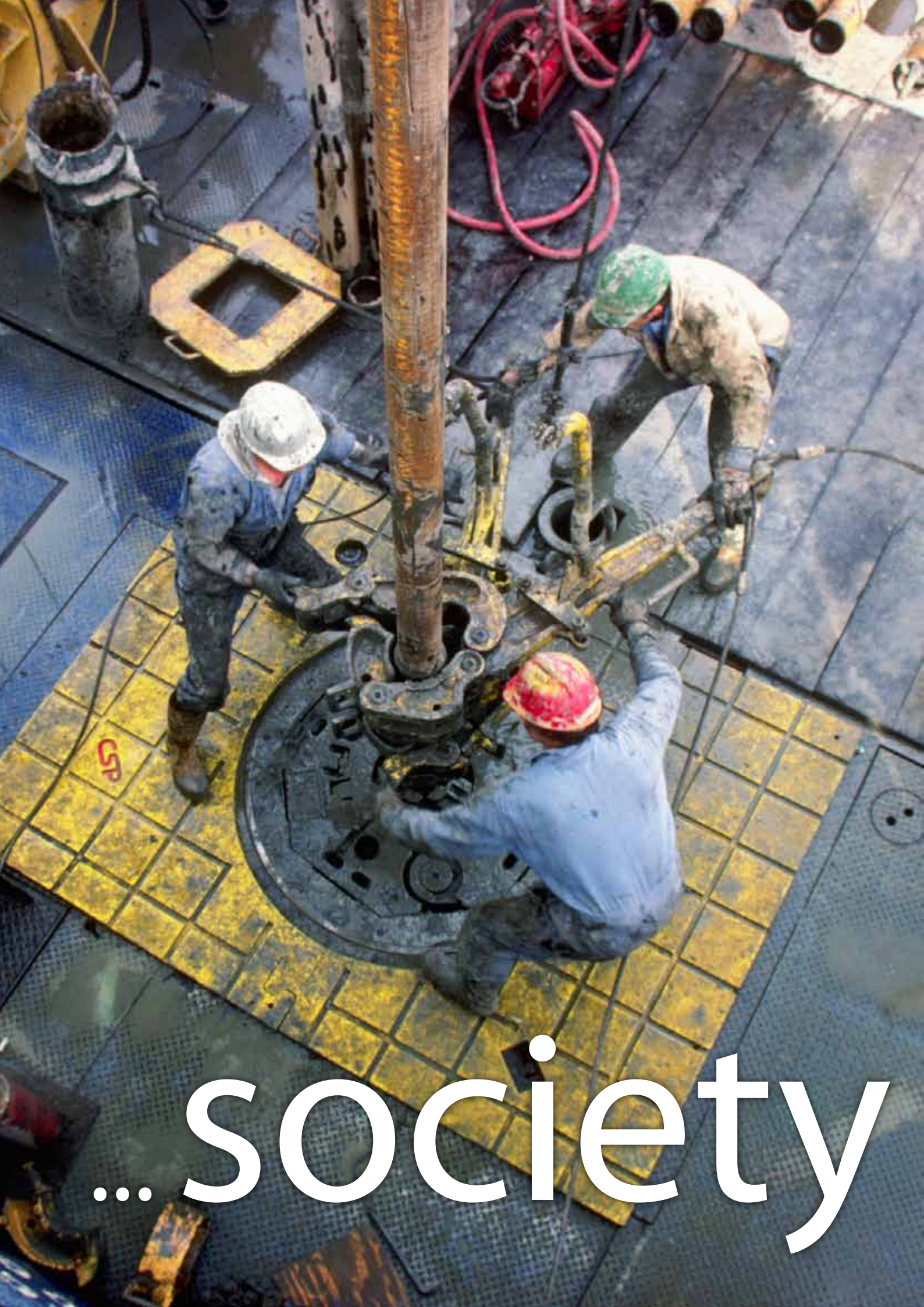
We have made a commitment to construct and develop facilities for manufacturing of solid, liquid and lyophilic forms of oncological preparations compliant with the EU GMP standards for the first time in Russia,.

We are convinced that our decisions – valid and sound – pave the way to the future growth of the Company.

For and on behalf of the Board of Directors
Sincerely yours,
Igor Krylov

Wecare®

for the health of a...



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Introduction

DIRECTORS' STATEMENT OF RESPONSIBILITIES

The Directors are responsible for preparing this Annual Report of JSC Pharmstandard («Pharmstandard» or «the Company»), including financial statements in accordance with applicable law and regulations. Each of the current Directors, whose names and functions are listed in the Corporate governance section of the Annual Report 2010 confirms that, to the best of his or her knowledge:

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

Chief Executive Officer
Igor Krylov

KEY DEVELOPMENTS AT THE COMPANY IN 2010

- In 2010, OJSC "Pharmstandard" held the second position on the Russian pharmaceutical market among all the manufacturers with market share 4,2%.[1]
- Pharmstandard keeps the leadership on the Russian pharmaceutical market among all the domestic manufacturers with the market share of 18.6% as a result of higher sales during 2010. [1]
- Pharmstandard won in the "Pharmaceutical Industry" nomination category of the national business award competition "Company of the Year 2010". [2]
- As in the previous year, Arbidol® remains the best performing retail brand. Arbidol®'s share of the total pharmaceutical retail sales in Russia was 1.5%.[3]
- In August 2010, OJSC «Pharmstandard» acquired 100% of the shares of CJSC «Vindexpharm». CJSC «Vindexpharm» owns the Acipol® trademark. Since the closure of the acquisition deal and the beginning of its sales under the Company's brand, sales of Acipol® amounted to RUR 140.7 million.
  According to «Pharmexpert» Market Research Centre, retail sales of the product in 2010 amounted to RUR 337 million which represented an increase of 17.4% in relation to RUR 287 million in 2009.
- Pharmstandard launched 12 new products: Pentalgin®, Acipol® (capsules), Formetin® (850 mg and 1000 mg tablets), Phosphogliv® forte (capsules), Artrozan® (solution for intramuscular injection 6 mg/ml), Complivit® Calcium D3 forte (tablets), Complivit® Calcium D3 for young children (powder), Complivit® Trimestrum 1,2,3, trimester (tablets), Maxicold® Rino (powder), Selmevit® Intensive (coated tablets).
- Sales proceeds of the Company for the products launched in 2010, amounted to RUR 249.2 million or 1.3% of the Company's organic sales of pharmaceuticals, RUR 140.7 million of which resulted from sales of Acipol®. It is worth taking into consideration that sales of the majority of the new pharmaceutical products commenced in the 4th quarter of 2010.
- OJSC «Pharmstandard» and «Johnson & Johnson» LLC entered into mutual agreement and successfully realized the project to localize secondary packaging of the product Velcade® (INN Bortezomib) on the Company`s production facility on OJSC «Pharmstandard-Ufavita». Sales of the product in 2010 amounted to RUR3,838 million.
- Pharmstandard registered retail prices for 98 pharmaceuticals produced by the Company (taking into account all forms and dosages) included in the Vital and Essential Pharmaceuticals (VEP) List for 2010. The Company's revenue from sales of the pharmaceutical products included in the VEP List reached RUR 9,568 million which accounted for 50.5% of the Company's organic sales revenue in 2010.
- In September 2010, OJSC «Pharmstandard» and State Corporation «ROSTEKHNOLOGII» signed a co-operation agreement. According to the agreement, the Corporation will provide assistance in the implementation of OJSC «Pharmstandard» projects related to modernization and servicing of high-tech medical facilities at medical establishments in the territory of the Russian Federation.

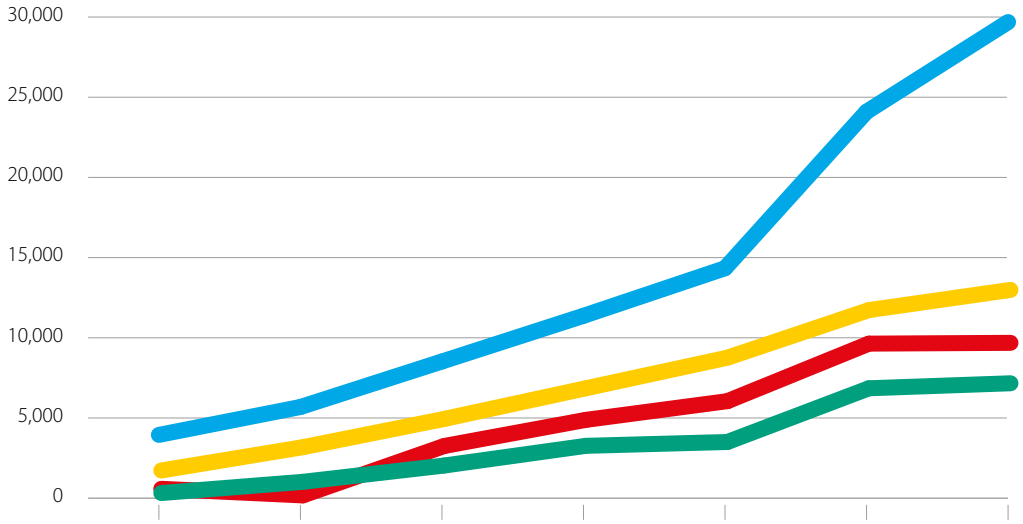
1 According to the data base of «Pharmexpert» Market Research Centre for 2010.
2 The annual national business award 'Company of the Year' is organized by RBK Holdings.
3 According to the data base of «Pharmexpert» Market Research Centre for 2010.

NAUCHTECH STROY PLUS LTD (Implementation of biotechnological project GENERIUM):

As of the end of 2010, the total investment in *Nauchtech Stroy Plus Ltd.* for construction of a R&D centre specialising in development and implementation of bioengineered pharmaceutical and diagnostics products amounted to RUR 630 million, RUR 150 million of which was the equity capital share in *Nauchtech Stroy Plus Ltd.* Construction and installation works, building communication network and construction of roads within the R&D centre have been completed. Interior furnishing and equipment installation has begun.

By the end of 2011, laboratories of molecular biology, cellular technology and bio-chemistry will be launched into operation; 41 residential buildings for R&D personnel accommodation, a cultural and business center, a general communications network and municipal amenities will be completed.

PHARMSTANDARD IN FIGURES



RUR mln	2004	2005	2006	2007	2008	2009	2010
Revenue	3,946	5,685	8,523	11,371	14,336	24,095	29,687
growth		44%	50%	33%	26%	68%	23%
Gross Profit	1,726	3,178	4,942	6,852	8,759	11,727	12,986
growth		84%	56%	39%	28%	33%	11%
EBITDA	583	1,720	3,255	4,882	6,049	9,636	9,685
growth		195%	89%	50%	24%	59%	0.5%
Net Profit	320	1,019	2,036	3,263	3,503	6,852	7,164
growth		218%	100%	60%	7%	95%	4.5%

SHAREHOLDERS STRUCTURE

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

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

The following table provides information about Pharmstandard shares ownership.

As of 31 December	2010	2009
Augment Investments Limited	54.31%	54.31%
Treasury Shares (Pharmstandard)	-	0.02%
Free Float	45.69%	45.67%
GDR	27.57%	27.57%
Local shares	18.12%	18.10%

DIVIDENDS

The Board of Directors does not recommend to paying dividends for the financial year ended December 31,2010. Like in 2007, 2008 and 2009, no dividends on ordinary shares will be paid out of 2010 earnings. The Company will retain earnings for possible M&A deals and development of biotech projects.

CORPORATE GOVERNANCE

JSC Pharmstandard is subject to applicable corporate governance regulations. In 2010, the Company continued its efforts to advance adoption of international corporate governance standards.

Throughout 2010, the Company fully complied with international ethical standards and the requirements set forward by the London Stock Exchange.

CORPORATE CODE

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

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

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

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

The Corporate Code was approved by the Company's Board of Directors on 1 October 2008.

The Company's governing bodies are:

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

ANNUAL GENERAL MEETING

The Annual General Meeting attended by all shareholders is the Company's highest decision-making body. The Company will announce the date and location of 2010 Annual General Meeting in a special press release.

BOARD OF DIRECTORS

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

The Board of Directors comprises:

Viktor Kharitonin	*Chairman of Board of Directors*	Mr. Kharitonin has served as Chairman of our Board of Directors since May 2006. Mr. Kharitonin graduated from Novosibirsk State University.
Igor Krylov	*Board Member, Chief Executive Officer*	Mr. Krylov serves as our Chief Executive Officer since 2006 and member of Board of Directors since May 2006. He has more than 16 years experience working in the pharmaceutical industry. Previously, Mr. Krylov held senior positions with Eli Lilly and Sanofi–Aventis. He graduated with honours from Kirov Military Medical Academy.
Elena Arkhangelskaya	*Board Member, Chief Financial Officer*	Ms. Arkhangelskaya has served as our Chief Financial Officer since 2006 and member of Board of Directors since June 2008. She has 13 years experience working in the pharmaceutical industry. Previously, she held senior positions at Eli Lilly. Ms. Arkhangelskaya graduated from the State Financial Academy and obtained master of business administration (MBA) degree.
Yegor Kulkov	*Board Member*	Mr. Kulkov has served as a member of our Board of Directors since May 2006. Mr. Kulkov has held a number of senior financial positions in various companies, and currently serves as General Director of Vita Realt. He graduated from Novosibirsk State University.
Pavel Mileyko	*Board Member*	Mr. Mileyko has served as a member of our Board of Directors since May 2006. Mr. Mileyko graduated from Novosibirsk State University.
Sergey Dushelikhinsky	*Board Member, Chief Commercial Officer*	Mr. Dushelikhinsky has served as our Chief Commercial Officer since 2006 and member of Board of Directors since June 2008. He has 13 years experience in sales. Previously, Mr. Dushelikhinsky worked for CJSC Veropharm and FTK Vremya. Mr. Dushelikhinsky graduated from Moscow Technical University.
Viktor Fedlyuk	*Board Member, Head of Legal Department*	Mr. Fedlyuk has served as our Head of Legal Department since 2006 and member of Board of Directors since June 2008. He has more then 11 years of experience in the legal profession, and worked for JSC Sibneft from 1996 to 2003. Mr. Fedlyuk graduated from the National Law Academy of Ukraine.
Olga Pokrovskaya	*Board Member*	Ms. Pokrovskaya has served as a member of our Board of Directors since October 2006. She also serves as a member of Evraz Group S.A Board of Directors. Ms. Pokrovskaya has more than 15 years of financial experience. Ms. Pokrovskaya graduated from the State Financial Academy and is a certified public accountant.
Roman Goryunov	*Independent Board Member*	Mr. Goryunov has been a member of Board of Directors since June 2008. Previously, he held executive positions at NP RTS Stock Exchange. Currently, Mr. Goryunov is Chairman of RTS JSC Management Board. He graduated from St. Petersburg Technical University Faculty of Economics and Management with a degree in Economics and Information Systems.
Andrei Reus	*Independent Board Member*	Andrei Reus is an independent member of the Board of Directors since 25 June 2010. Mr. Reus is general director of the "Oboronprom" United Industrial company and general director of the "United Engine-Building Corporation "Managing Company".
Ivan Tyryshkin	*Independent Board Member*	Mr. Tyryshkin has served as an independent member of our Board of Directors since October 2006. Since 2006, he has served as both Managing Director and General Director of LLC ATON. Currently, Mr. Tyryshkin is Chairman of OJSC «Rusgrain Holding» and is a member of the Board of Directors of OJSC "Rusgrain Holding". Mr. Tyryshkin graduated from the Russian Academy of Economics.

BOARD OF DIRECTORS COMMITTEES

The Board of Directors has the following committees

AUDIT COMMITTEE

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

Ivan Tyryshkin	Committee Chairman
Roman Goryunov	Committee Member
Andrei Reus	Committee Member

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

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

REMUNERATION AND NOMINATION COMMITTEE

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

Ivan Tyryshkin	Committee Chairman
Olga Pokrovskaya	Committee Member
Yegor Kulkov	Committee Member

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

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

MANAGEMENT BOARD

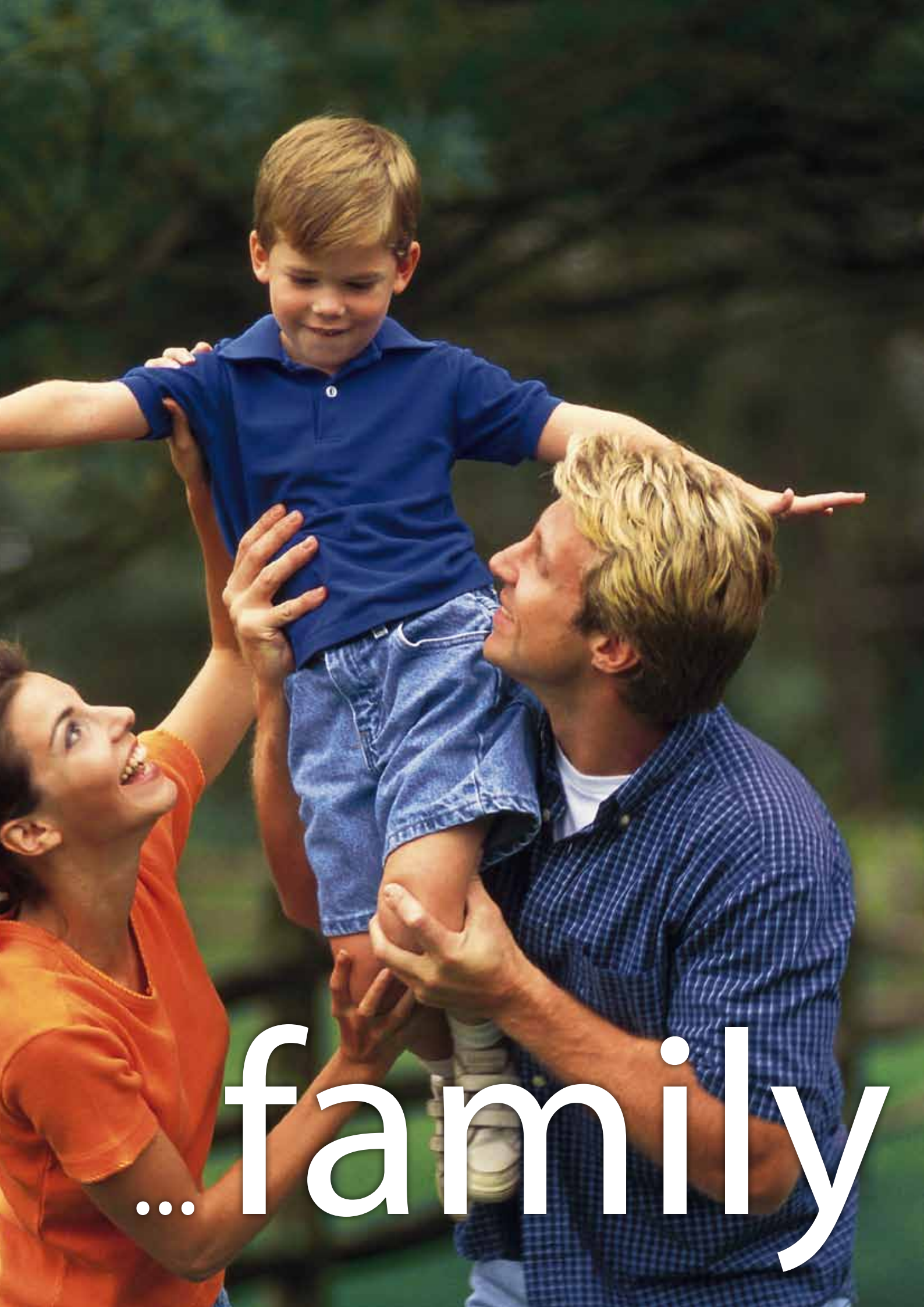
The Board has delegated to the Management Board the coordination of the Company's day-to-day business operations. The Management Board is headed by the Chief Executive Officer and also includes the following members:

Igor Krylov	*Chief Executive Officer*	Mr. Krylov serves as our Chief Executive Officer since 2006.
Pavel Mileiko	*Board Member*	Mr. Mileyko has served as a member of our Board of Directors since May 2006.
Olga Mednikova	*Chief Sales & Marketing Officer*	Ms. Mednikova has served as our Chief Sales and Marketing Officer since 2006. She has more then 14 years experience working in the healthcare industry. Previously, Ms. Mednikova held senior management positions in marketing and promotion department at Glaxo Welcome and IVAX. Ms. Mednikova graduated from Samara State Medical University and holds MD PhD degree.

Pharmstandard

We**care**

for the health of a...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Business report

MISSION

AT PHARMSTANDARD, WE ARE DEDICATED TO THE DEVELOPMENT AND PRODUCTION OF ADVANCED PHARMACEUTICAL PRODUCTS, WHICH MEET HEALTHCARE REQUIREMENTS AND PATIENTS' EXPECTATIONS.

The Company is committed to the following guiding principles:

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

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

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

STRATEGY

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

- **Promote our market-leading brands to drive sales growth and profitability.** We intend to strengthen our market position in Russia by continuing to leverage our strong brand loyalty and brand awareness through effective sales and marketing of our market-leading brands. We will continue promoting these brands by introducing line extensions of trusted and established products, such as our well-known branded product ranges Pentalgin®, Codelac®, Complivit®, Arbidol® and Flucostat®. We will also continue to focus on promoting higher value added brands – Afobazol®, Neupomax®, Biosulin®, Rastan®.
- **Launch new pharmaceutical products in a timely manner to capture market share.** We intend to maintain strong growth and capture market share by leveraging the brand loyalty and brand awareness of our market-leading brands to develop and launch new products in our Core Therapeutic Segments. We also intend to develop and launch new products in potential for our growth new therapeutic segment. Specifically, we intend to:
  - focus on the timely identification and development of new products, including the development of line-extensions of current brands;
  - focus on the timely identification and development of new products that complement our Core Therapeutic Segments and develop new products to penetrate new therapeutic areas;
  - launch these new pharmaceutical products in a timely manner to capture significant market share;
  - leverage our sales and marketing infrastructure to promote new product launches and achieve leading market positions for new branded products
- **Maintain our focus on cost control.** Our focus and ability to control costs is an important element of both our operating and financial performance. We will continue to evaluate and respond to manufacturing and distribution cost inefficiencies. We also plan to further rationalize our manufacturing costs in order to keep gross profit margins by managing our product mix on the basis of the demand for our pharmaceutical products.
- **Expand our sales and marketing capabilities.** Our sales team has more than doubled in the last two years and amounted to 579 sales people by the end of 2010. We also intend to promote further specialization of the Company sales force by therapeutic areas and expect our more specialized sales and marketing team to facilitate our increased calling efforts on medical practitioners, regional and national distributors and other customers. This measure will help to increase customer awareness of our product portfolio and drive further sales growth.
- **Grow through acquisitions and realize synergies.** We intend to complement our organic growth through the assessment and use of acquisition opportunities, including opportunities for specific brands, trademarks and patents.
- **Cooperation with leading pharmaceutical companies.** We intend to complement our organic growth through cooperation with leading pharmaceutical companies based on co-manufacturing or exclusive marketing and promotion of their most successful pharmaceutical products.
- Exploit opportunities arising from government funding of healthcare. We believe that we are well positioned to benefit from potential changes in the Federal Reimbursement Programme (FRP), which are expected to increase the participation of local producers. We plan further participation in the FRP, namely in the Federal Programme for 7 costly diseases with our GNA product Rastan (somatotropin), and in the ONLC Programme (Provision of Essential Pharmaceuticals Programme) with our insulin product Biosulin and some other Rx products (both programmes are parts of FRP). In addition, we expect growth in sterilizing devices market, where, we believe our products to have a cost-competitive advantage. This growth is expected within the framework of the National Priority Health Project ("NPHP"), which aims, among other things, to provide Russian hospitals with modern equipment.

OPERATING ENVIRONMENT

RUSSIAN PHARMACEUTICAL MARKET STRUCTURE

In 2010, the volume of the Russian pharmaceutical market amounted to RUR 523.2 billion and 4.75 billion packages.

Data comparison with the figures for 2009 indicates growth of the market both in monetary and volume terms.

Nevertheless, the market's growth by value +7.8% is the lowest figure for the last 5 years (the average growth rate before 2010 was ~+27%. By 2009 the market had grown by RUR 37.7 billion.

At the same time, a period of stagnation in consumption of pharmaceuticals changed to dynamic growth. This resulted in the market growth in volume terms by 2009 to +9.2% (while the average annual growth in the previous five years had been ~+1.7%). This figure is the highest for recent years. Consumption of pharmaceuticals by 2009 had grown by almost 400 million packages.

For the first time in recent years the average price per package of pharmaceuticals has been decreasing. In 2010, the decrease amounted to -1.3% (until 2010, price increase amounted to ~25% annually). In 2010, the average retail prise of a package of pharmaceuticals was 110 RUR.

Consequently, it is reasonable to conclude that the main market growth factor in 2010 was the growth in

Chart 1 Dynamics of the volume of the pharmaceuticals market in Russia

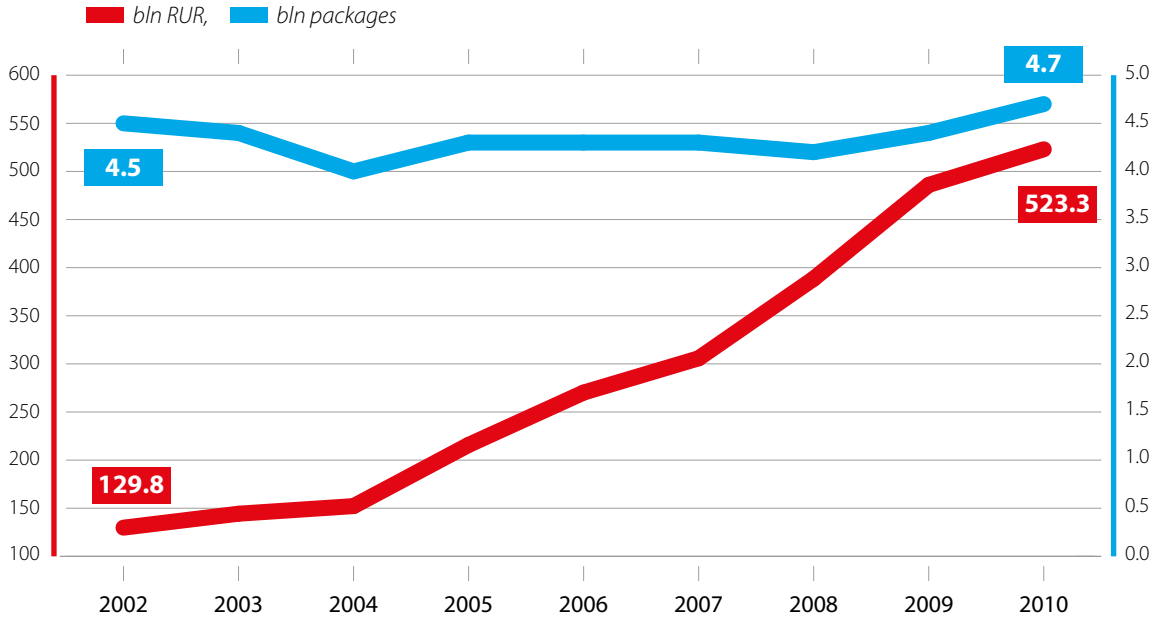
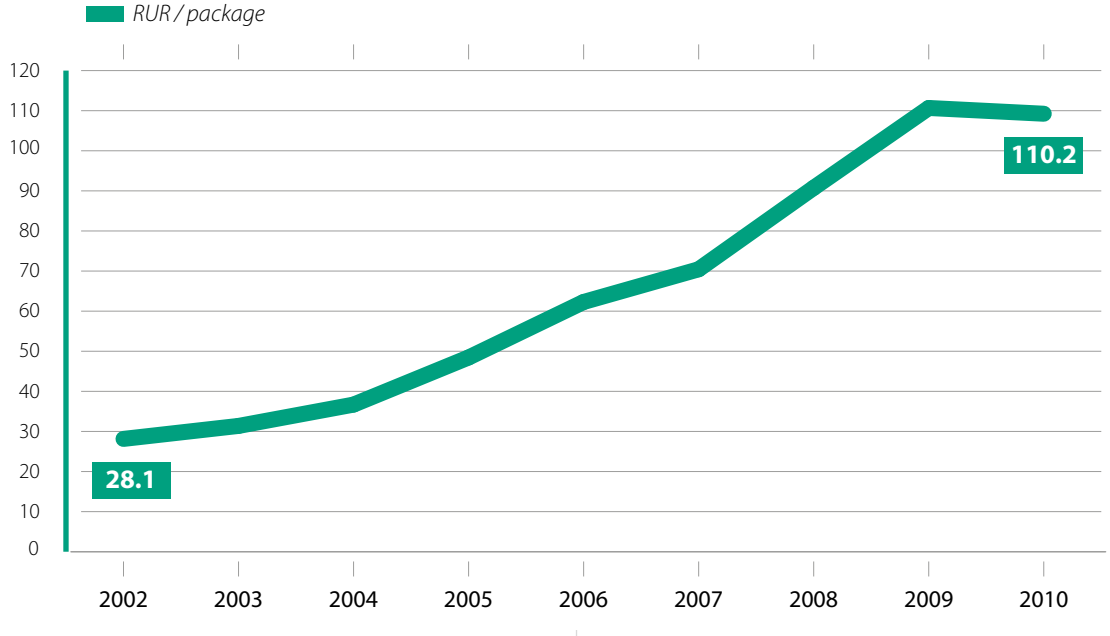


Chart 2 Dynamic of the average retail price for pharmaceuticals in Russia



consumption of pharmaceuticals due to the increase in accessibility of pharmaceuticals for the population.

It is worth noting that factor analysis demonstrates the dominant role of the pharmaceuticals price decrease factor in the growth of consumption (market growth of +7.8% by value is the effect of a -6.6% reduction in price and a consumption growth of +14.4%). This is in contrast to the tendency observed in 2009 when the influence of the price factor amounted to +20.6% while that of consumption to only +4.4%.

Thus, in 2010 the role of increasing prices as the driving factor for the growth of the pharmaceuticals market in Russia was overtaken by the increase in consumption of pharmaceuticals.

In 2010, OJSC "Pharmstandard" was the second manufacturer in value terms on the pharmaceutical market in Russia (Source: "Pharmexpert"). Market Research Centre The main factor which affected the insignificant reduction in the market share was the shift in the beginning of the epidemic period from the end of the year (2010) to the beginning of 2011. In contrast, in 2009 the peak of the epidemic season fell on October-December and was characterised by a surge of the number of cases of swine flu, which in turn led to a considerable increase in demand for antiviral and anti-cold pharmaceutical products.

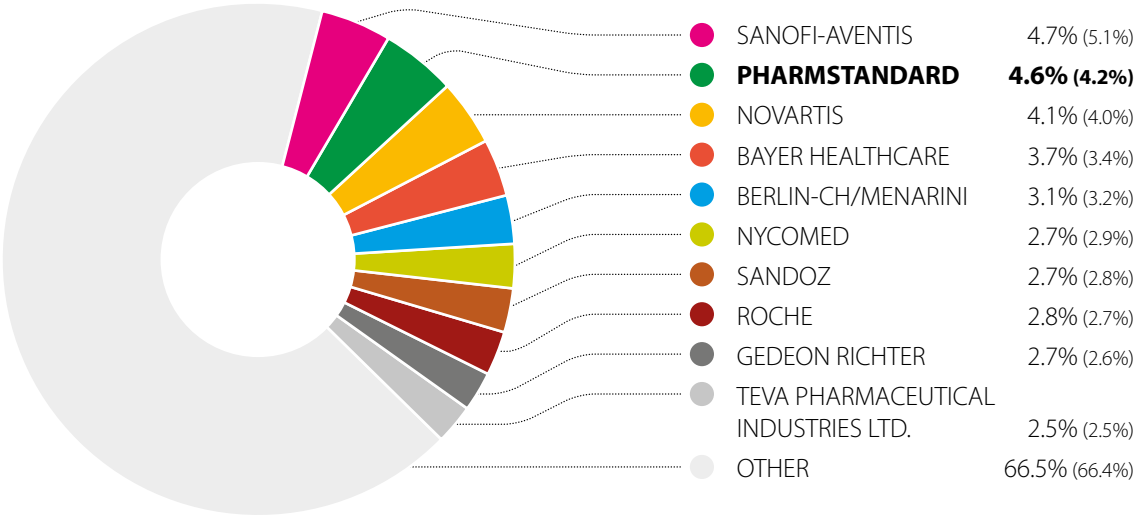
The pharmaceuticals market in Russia consists of three large segments: Retail Segment (consumer spending); Federal Reimbursement Programme – FRP (Provision of Essential Pharmaceutical Drugs plus seven costly diseases) and the Hospital Segment. Despite the varied behaviour of the segments, there were no significant changes in the market structure in 2010.

For example, the volume of the retail segment in monetary terms in 2010 amounted to RUR 404.5 billion which represented 77.3% of the market share and the growth of +8.5% over 2009 (in 2009 was RUR 372.8 billion by value and the market share was 76.8%). In 2010, the retail segment amounted to 92.5% by volume with 4.4 billion packages and an the increase of +10% over 2009 (the volume in 2009 in was 4.0 billion packages with the market share of 91.2%).

The second most significant segment of the market in terms of volume, the FRP programme, showed a decrease of its share from 18.2% to 15.6% by value; its value in 2010 amounted to RUR 81.6 billion with an increase of only +2.0% over 2009 (when its volume was RUR 80 billion). The share of this segment amounted to 1.9% by volume (~92 million packages).

The hospital segment in the last three years has been in third position with its share in volume terms amounting to ~7.1% in 2010 and it share in value terms of RUR 37.3 billion (an increase over 2009 of +13.4%).

Chart 3 **Share of leading companies in Russian pharmaceutical market** *(in value terms, 2009 data in brackets)*



All information in the chapter "Russian Pharmaceutical Market" is based on the data of the "Pharmexpert" Market Research Centre

Table 1 Structure and dynamics of the pharmaceutical market in Russia by segments *(in value terms)*

bln Rur		2008		2009		2010	09/08	10/09
Retail	288.7	74.3%	372.8	76.8%	404.5	77.3%	+29.1%	+8.5%
FRP	70.7	18.2%	80.0	16.5%	81.6	15.6%	+13.2%	+2.0%
Hospital	28.9	7.4%	32.8	6.8%	37.2	7.1%	+13.7%	+13.4%
Total Market	**388.3**	**100%**	**485.6**	**100%**	**523.3**	**100%**	**+25.1%**	**+7.8%**

Table 2 Structure and dynamics of the pharmaceutical market in Russia by segments *(by volume)*

bln Units		2008		2009		2010	09/08	10/09
Retail	3.833	90.6%	3.964	91.2%	4.390	92.5%	+3.4%	+10.7%
Hospital	0.281	6.6%	0.282	6.5%	0.265	5.6%	+0.6%	-6.0%
FRP	0.118	2.8%	0.102	2.3%	0.092	1.9%	-13.5%	-9.9%
Total Market	**4.2**	**100%**	**4.3**	**100%**	**4.7**	**100%**	**+2.8%**	**+9.2%**

Table 3 Structure and dynamics of the pharmaceutical market in Russia by segments *(by price for package)*

Price	2008	2009	2010	09/08	10/09
Retail	75.3	94.0	92.1	+24.9%	-2.0%
Hospital	103.0	116.3	140.3	+12.9%	+20.7%
FRP	600.4	785.2	888.9	+30.8%	+13.2%
Total Market	**91.8**	**111.7**	**110.2**	**+21.7%**	**-1.3%**

If we consider the market segments by manufacturers of pharmaceutical products, we do not see any changes in the structure: the share of the domestic companies amounts to 22.5% by value and to 63.7% by volume.

Table 4 Structure and dynamics of the pharmaceutical market in Russia by manufacturing companies *(in value terms)*

bln Rur		2008		2009		2010	09/08	10/09
IMPORT	302.2	78.8%	375.9	78.0%	403.1	77.5%	+24.4%	+7.2%
DOMESTIC	81.5	21.2%	106.3	22.0%	117.3	22.5%	+30.5%	+10.3%
Total Market	**383.7**	**100%**	**482.2**	**100%**	**520.4***	**100%**	**+25.7%**	**+7.9%**

Table 5 Structure and dynamics of the pharmaceutical market in Russia by manufacturing companies *(in volume terms)*

bln Units		2008		2009		2010	09/08	10/09
IMPORT	1.479	36.5%	1.515	35.6%	1.696	36.3%	+2.4%	+12.0%
DOMESTIC	2.568	63.5%	2.735	64.4%	2.979	63.7%	+6.5%	+8.9%
Total Market	**4.05**	**100%**	**4.25**	**100%**	**4.68**	**100%**	**+5.0%**	**+10.0%**

Some dynamics is traceable in the prescription (Rx) and non-prescription (OTC) medications segments: the share of the Rx pharmaceuticals in 2010 amounted to 59.8% by value and exhibited a tendency for decrease (for example, since 2006 when the share amounted to 64.5% it has been decreasing every year) and in volume terms the share of OTC pharmaceuticals has been steady at 32% for the last four years.

* without unknown manufactures
All information in the chapter "Russian Pharmaceutical Market" is based on the data of the "Pharmexpert" Market Research Centre

Table 6 Structure and dynamics of the pharmaceutical market in Russia in relation to Rx and OTC pharmaceuticals *(in value terms)*

bln Rur		2008		2009		2010	09/08	10/09
OTC	147.7	38.0%	194.1	40.0%	210.6	40.2%	+31.4%	+8.5%
RX	240.6	62.0%	291.5	60.0%	312.7	59.8%	+21.2%	+7.3%
Total Market	**388.3**	**100%**	**485.6**	**100%**	**523.3**	**100%**	**+25.1%**	**+7.8%**

Table 7 Structure and dynamics of the pharmaceutical market in Russia in relation to Rx and OTC pharmaceuticals *(in volume terms)*

bln Units		2008		2009		2010	09/08	10/09
OTC	2.866	67.7%	2.959	68.0%	3.248	68.4%	+3.2%	+9.8%
RX	1.366	32.3%	1.390	32.0%	1.499	31.6%	+1.8%	+7.8%
Total Market	**4.23**	**100%**	**4.35**	**100%**	**4.75**	**100%**	**+2.8%**	**+9.2%**

In 2010, the share of VEP decreased to 46.6% by value. At the same time, there was no change in the structure in volume (41.0%). This is due to the introduction of state control over the VEP prices with further reduction thereof. The average price in this segment of pharmaceuticals reduced, in comparison to 2009, by 5.6% and amounted RUR 125 per package (compared to 133 RUR per package in 2009).

Table 8 Structure and dynamics of the pharmaceutical market in Russia in relation to non-VEP and VEP pharmaceuticals *(in value terms)*

bln Rur		2008		2009		2010	09/08	10/09
NON-VEP	195.7	50.4%	247.1	50.9%	279.6	53.4%	+26.3%	+13.2%
VEP	192.6	49.6%	238.6	49.1%	243.7	46.6%	+23.8%	+2.2%
Total Market	**388.3**	**100%**	**485.6**	**100%**	**523.3**	**100%**	**+25.1%**	**+7.8%**

Table 9 Structure and dynamics of the pharmaceutical market in Russia in relation to non-VEP and VEP pharmaceuticals *(in volume term)*

bln Units		2008		2009		2010	09/08	10/09
NON-VEP	2.528	59.7%	2.549	58.6%	2.801	59.0%	+0.9%	+9.9%
VEP	1.704	40.3%	1.799	41.4%	1.946	41.0%	+5.6%	+8.2%
Total Market	**4.23**	**100%**	**4.35**	**100%**	**4.75**	**100%**	**+2.8%**	**+9.2%**

Table 10 Table 10. Structure and dynamics of the pharmaceutical market in Russia in relation to non-VEP and VEP pharmaceuticals *(by price per package)*

Price	2008	2009	2010	09/08	10/09
NON-VEP	77.4	96.9	99.8	+25.2%	+3.0%
VEP	113.0	132.6	125.2	+17.3%	-5.6%
Total Market	**91.8**	**111.7**	**110.2**	**+21.7%**	**-1.3%**

RETAIL SEGMENT

The retail segment represents the biggest share of the pharmaceutical market in Russia. In 2010, its share amounted to 77.3% by value and to 92.5% by volume.

The contribution of the retail segment in the overall market growth in 2010 in relation to 2009 amounted to 84% (RUR 31.7 billion of the total increase amount of 37.7 RUR). This was due to the faster growth of the segment in volume terms in comparison to the market as a whole, the increase amounted to +8.5%. However, only the retail segment exhibits steady positive growth dynamics, including in 2009, and it is the increase in consumption in this segment that drives the growth of the market as a whole.

The increase of 10.7% by volume in this segment represents a record figure for the last few years (while the range of figure over the years has been fluctuating from -7.9% in 2004/2003 to +5.9% in the periods of 2005/2004 and 2007/2006).

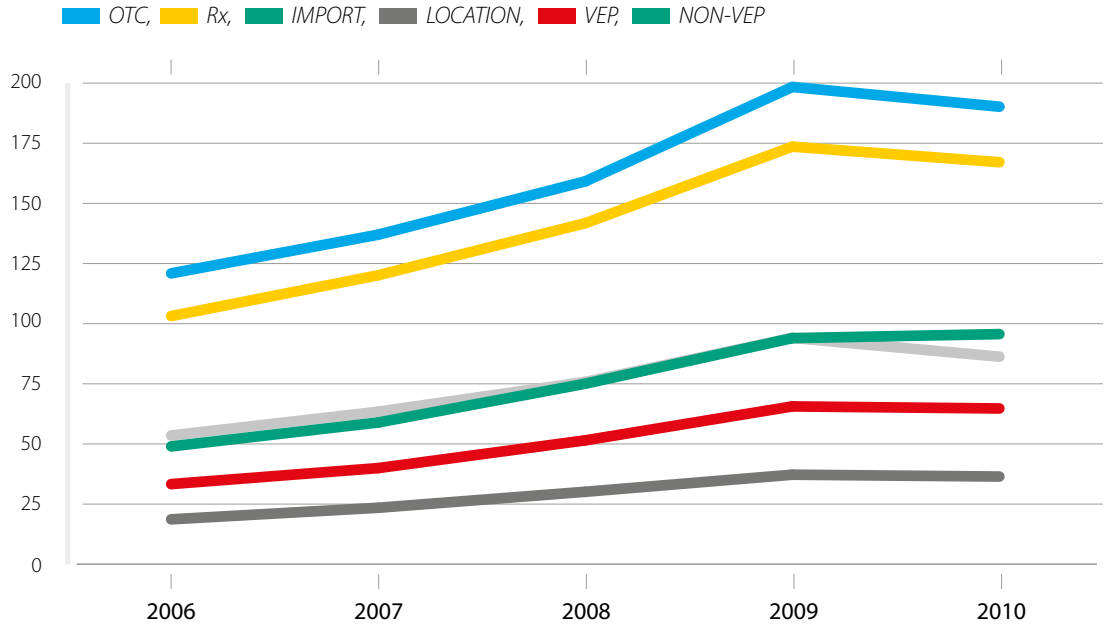
This increase was caused by the end of the period of pharmaceuticals price growth (the reduction in an average price in 2010 amounted to 2.0%). It is noteworthy that the most significant reduction occurred in the expensive product segments (Rx pharmaceuticals price decreased by 3.7% and pharmaceuticals manufactured by foreign companies price decreased by 4.1%).

It is worth mentioning that this decrease became possible due to two factors: the state regulation of the prices of pharmaceuticals on the VEP list which dropped by 8-9% throughout all the segments (Rx and OTC preparations, pharmaceuticals produced domestically and imported) and the decrease in prices in relation to 2009. It is important that the reduction in prices happened in 2010 after a period of growth in prices in 2009 during the crisis, when the price was the only factor driving the growth of the market. Despite the reduction in prices in 2010 in relation to 2009, the average prices for pharmaceuticals remained higher than in the pre-crisis period. But such adjustment / stagnation of prices in 2010 was sufficient for revitalising the consumption of pharmaceuticals, in comparison to 2009.

In 2010, we observed equal growth of consumption both in the VEP segment (+11.1%) and in the segment of other pharmaceutical preparations (+10.5%) notwithstanding that the price dynamics in these segments is different, and the absolute value of prices in 2009 were equal (94 RUR per package). By 2009, the average price in the VEP segment fell by 5.6%; and in the segment of other pharmaceuticals the average price grew by 3%. This increase in the average price of the latter segment resulted from the change in the consumption structure: prices for the more expensive products had fallen which lead to an increase in their consumption and consequently to the increase in the average price for one package of pharmaceuticals in the retail segment.

The analysis of the situation in the therapeutic categories of the segment shows that there are no major differences from 2009. For instance, the average rate of growth for the TOP-5 categories (which represent 67% in value terms and 70% in volume terms) amounted, in 2010, to 10.1% (from +9% to +12%) in value terms and 11.3% (from 8% to +16%) in volume terms.

Chart 4 **Dynamics of selling prices as per various sectors of the retail segment of the pharmaceutical market in Russia** *(RUR/package)*



All information in the chapter "Russian Pharmaceutical Market" is based on the data of the "Pharmexpert" Market Research Centre

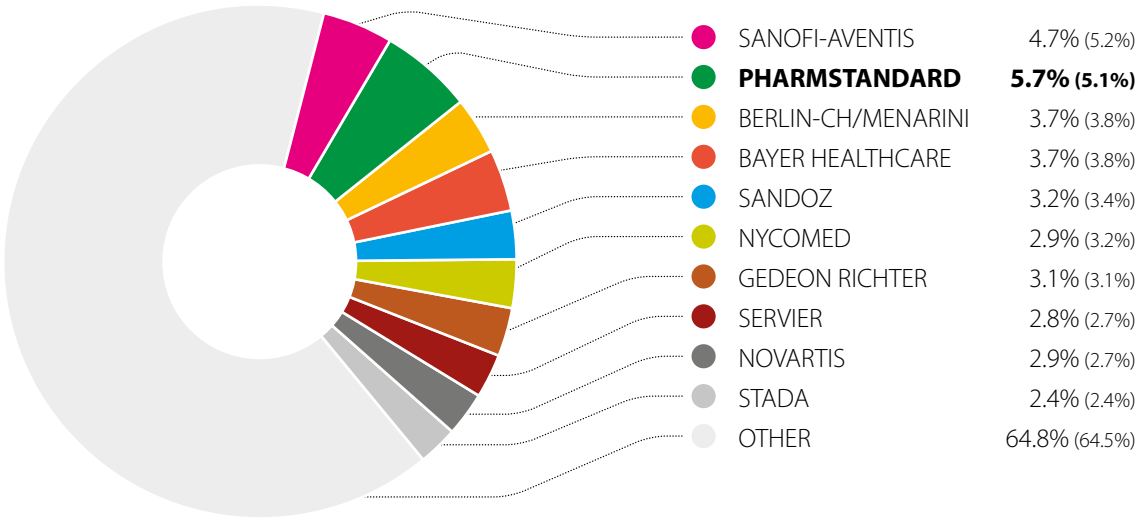
Table 11 Structure and dynamics of the pharmaceutical market in Russia in relation to the anatomical-therapeutic categories *(in value terms)*

bln Rur		2008		2009		2010	09/08	10/09
Alimentary tract and metabolism	53.8	18.6%	69.8	18.7%	78.0	19.3%	+29.8%	+11.8%
Respiratory system	43.3	15.0%	56.2	15.1%	61.4	15.2%	+29.8%	+9.3%
Cardiovascular system	40.7	14.1%	52.3	14.0%	58.4	14.4%	+28.6%	+11.7%
Central nervous system	30.0	10.4%	38.0	10.2%	41.5	10.3%	+26.9%	+9.1%
Genito-urinary system and sex hormones	25.2	8.7%	31.9	8.6%	34.7	8.6%	+26.4%	+8.7%
Other	95.8	33.2%	124.6	33.4%	130.5	32.2%	+30.1%	+4.7%
Total Market	**288.7**	**100%**	**372.8**	**100%**	**404.5**	**100%**	**+29.1%**	**+8.5%**

Table 12 Structure and dynamics of the pharmaceutical market in Russia in relation to the anatomical-therapeutic categories *(in volume terms)*

bln Units		2008		2009		2010	09/08	10/09
Alimentary tract and metabolism	789.2	20.6%	807.7	20.4%	894.5	20.4%	+2.3%	+10.8%
Respiratory system	635.3	16.6%	669.9	16.9%	728.2	16.6%	+5.4%	+8.7%
Cardiovascular system	415.7	10.8%	410.8	10.4%	474.7	10.8%	-1.2%	+15.6%
Central nervous system	786.5	20.5%	829.2	20.9%	896.3	20.4%	+5.4%	+8.1%
Genito-urinary system and sex hormones	93.2	2.4%	91.7	2.3%	104.2	2.4%	-1.6%	+13.6%
Other	1 113.5	29.0%	1 155.1	29.1%	1 292.2	29.4%	+3.7%	+11.9%
Total Market	**3 833.5**	**100%**	**3 964.4**	**100%**	**4 390.1**	**100%**	**+3.4%**	**+10.7%**

Chart 5 Share of companies in the retail segment of the pharmaceutical market in Russia *(in value terms, 2009 data in brackets)*



Thus, it is obvious that the tendency to respond with stagnation of prices to sufficiency, is common for the market.

According to the results of 2010, "Pharmstandard" holds the second place in the retail segment with its share of 5.1% in value terms. This change in the Company's position and reduction of its share (in 2009 it was in the first place with a share of 5.7%) in comparison to previous periods was only due to the shift in the epidemic season from December 2010 to January 2011.

However, the January 2011 results put the Company back to the first place and according to the February results, it strengthened its leading position (for rolling years February 2010 – January 2011 and March 2010 – February 2011 respectively).

Two of the Company's pharmaceutical products have been in the TOP-10 brands of the retail segment: Arbidol® and Pentalgin®. It is worth noting that Arbidol® has been in the leading position for the last five years. Pentalgin® moved one line up in the list as compared to 2009.

Table 13 **TOP-10 brands of the retail segment** *(in value terms)*

1	ARBIDOL
2	ESSENTIALE
3	VIAGRA
4	ACTOVEGIN
5	CONCOR
6	NUROFEN
7	LINEX
8	PENTALGIN
9	THERAFLU
10	OSCILLOCOCCINUM

The TOP-10 domestic manufacturers' brands of the retail segment include four products of the Company: Arbidol® (No.1), Pentalgin® (No.2), Complivit ® (No.6) and Flucostat ® (No.9).

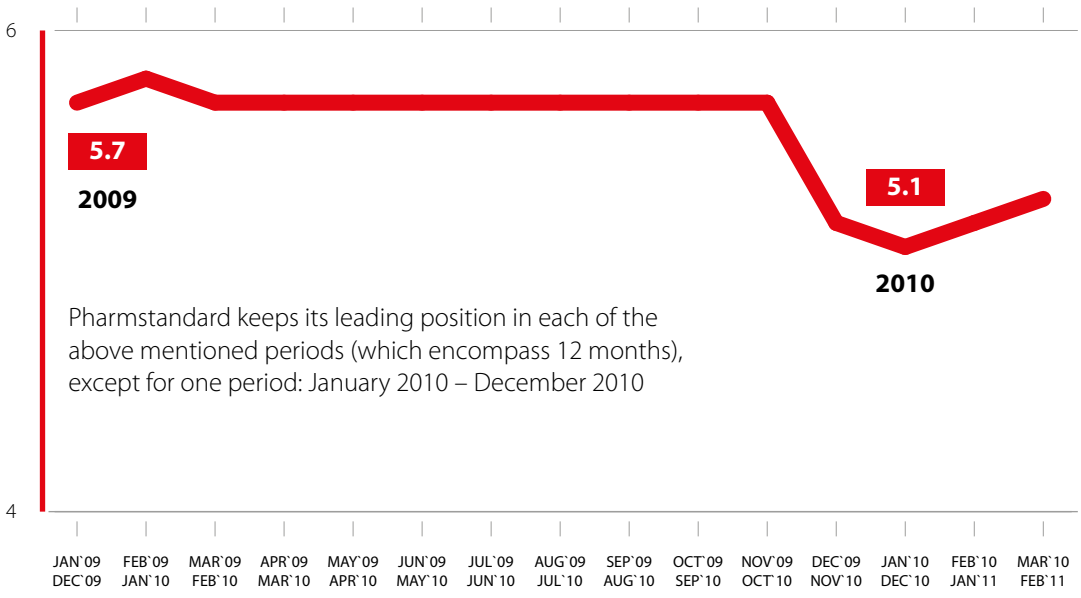
Table 14 **TOP-10 domestic manufacturers' brands of the retail segment** *(in value terms)*

1	ARBIDOL
2	PENTALGIN
3	ANAFERON
4	MEXIDOL
5	VIFERON
6	COMPLIVIT
7	ANTIGRIPPIN
8	MYDOCALM
9	FLUCOSTAT
10	ESSLIVER

The Company's portfolio, in terms of its presence on the market, is characterized by the Company being represented in virtually all significant therapeutic categories of the retail segment. The Company's preparations are present in 106 categories out of 273. These categories' share of the retail segment is 74% in value terms, and in volume terms it is 89%. The share of the Company in the total of these segments is different from the share of the Company in the whole of the retail segment. The share of Pharmstandard in these 106 competitive therapeutic categories amounts to 6.9% in value terms and 13.3% in volume terms.

This means that the Company's portfolio of pharmaceutical products has a significant representation in the most important categories of the retail segment of the

Chart 6 **Monthly share of "Pharmstandard" in the retail segment of the pharmaceutical market in Russia in January 2010 – February 2011**



pharmaceutical market, which reduces the risks of portfolio concentration and allows expansion of Company's presence without any obstacles at the start up stage.

FORECAST. RETAIL SEGMENT

The results of 2010 indicate that the tendency of consumption increase is the dominant driving factor of the market growth. This increase goes alongside the changing structure of consumption with a shift towards the preparations with stable or decreasing prices. If we also look at the influence of the VEP factor which made pharmaceuticals with a higher price more accessible, it becomes clear that the increase in consumption will go alongside a gradual trend of the average package price growth, due to the shift in the consumption structure towards more expensive preparations.

So, 2010 has become a transitional period: before its commencement, the main factor of growth was growth in prices; during the course of the year the main factor was the increase in consumption; and after its end, both factors will be affecting the market – the price and consumption increase. However, it will not be the real growth of average prices due to their increase that will constitute the main distinguishing feature of the price factor; rather it will be the growth of average prices owing to the structural shift in consumption.

As we noted in the previous annual report, one of the main factors influencing the growth of the pharmaceutical market, will be increase in consumption of medicines, which currently is a likely scenario of development due to the slower rate of increase in pharmaceutical prices.

It is our opinion that the tendency of increase in consumption of pharmaceuticals that emerged in 2010, may prove to become the foundation for further growth of the Russian pharmaceutical market. As this tendency only formed in 2010, it would be reasonable to suggest that in future, the rate of the market increase, owing to the growing consumption of pharmaceuticals, may be more significant.

FRP\HOSPITAL

SUPPLIES OF PHARMACEUTICALS UNDER THE STATE OPEN AUCTIONS IN 2010

In November 2010, Pharmstandard won a number of state auctions for the procurement of costly pharmaceuticals to meet the demand thereof in 2011, in compliance with the Russian Federation Government Decree No. 682 dated 17 October 2007 'On procurement in 2010 of pharmaceutical products for the treatment of patients for Malignant neoplasms of lymphoid, hematopoietic and similar tissues, haemophilia, cystic fibrosis, pituitary dwarfism, Gaucher disease, multiple sclerosis, as well as after organ and/or tissue transplants' (7 nosologies programme)*.

Supplies of Coagil VII (93% in 2010 and 7% in 2011) amounting to RUR 1,384.6 million succeeded in meeting the demand of Russian haemopilia patients in three dosage forms of INN Eptacog Alpha [activated]. According to the terms of the state contract, the next supply is due before 31 May 2011. Preparation Coagil VII is produced within the framework of the joint biotechnological project "Generum".

In October 2010, pusuaint to the sub-programme 'Tuberculosis' of the Federal Targeted Programme 'Russian Federal Target Program on Prevention and Fight against Social Diseases', Pharmstandard supplied Diaskintest® (a tuberculosis diagnostic drug produced by CJSC "Lekko") for RUR 147 million.

FEDERAL LAW ON CIRCULATION ON MEDICAL PRODUCTS

On 1 September 2010, Federal Law No. 61-FZ 'On the Circulation of Pharmaceuticals in the Russian Federation' came into force. In 2010, the law was amended by Federal Law 'On amendments to Federal Law 'On the circulation of Pharmaceuticals" No. 271-FZ dated 11 October 2010 as well as by Federal Law 'On amending certain Russian Federation legislative acts, due to the adoption of the Federal Law 'On compulsory medical insurance in the Russian Federation" No. 313-FZ dated 29 November 2010.

This law brought considerable changes to the area of circulation of pharmaceuticals. The law contains precise provisions for stages of registration of pharmaceuticals and establishes the maximum period for such registration (210 working days).

The law clearly stipulates that imported preparations are subject to the same registration procedures which apply to domestic ones. Russia establishes mutual recognition of clinical trial data of pharmaceuticals with other countries provided there is an appropriate bilateral agreement.

The law, for the first time, addresses the issues of state regulation of pharmaceutical prices, provision of accessibility of pharmaceuticals for the countryside population, compulsory monitoring of pharmaceuticals safety and also determines the responsibilities of all participants of the pharmaceuticals market at all stages. The law also clearly defines the objectives of clinical trials.

The thorough work carried out on the draft documents is reflected in the new law in clarification and introduction of new definitions and terms, including the list of vital and essential pharmaceuticals, dosage forms, post-registration trials, prescription for a drug etc.

OJSC «Pharmstandard» took an active part in the work on the drafts of the law 'On the Circulation of Pharmaceuticals in the Russian Federation' and on Amendments to this law. Altogether the Company's experts studied and analyzed 9 drafts of the law and made their proposals, corrections and comments about each of these drafts.

The objective of our work was to make improvements in the legislative regulation of the legal structure of relations in the area of pharmaceuticals circulation taking into account the interests of all the participants of the process of circulation and also the priorities of the domestic pharmaceutical industry.

The most significant and complex areas of work were the sections on clinical trials, registration and production of pharmaceuticals, labeling, import and export of pharmaceuticals and the main concepts and notions of the law.

A number of these proposals were taken into account both in the law itself and in the two Amendments to it,

* SUMMARY OF THE 7 NOSOLOGIES PROGRAMME

The Federal "7 nosologies" programme which provides for free outpatient treatment using the most costly pharmaceuticals, was drawn up as a separate item included in to the Federal Reimbursement Programme.

In 2007, in accordance with the federal legisative acts, drug supply to the citizens entitled to the state social provisions the Federal Reimbursement Programme, was split into two items:

1. Provision of citizens entitled to receive state social provisions (federal and regional beneficiaries) with pharmaceuticals and medical products, including the products of medical application, from the federal budget resources.
2. Centralised provision, from the federal budget resources, of pharmaceuticals for the 7 costly nosologies, for treatment of patients with haemophilia, cystic fibrosis, Gaucher disease, pituitary dwarfism, multiple sclerosis, Malignant neoplasms of lymphoid, hematopoietic and similar tissues as well as after organ and/or tissue transplants.

The Decree of the Government of the Russian Federation No. 682 dated 17 October 2007 enacted the Provision regarding the centralised procurement, in 2008-2009, of pharmaceuticals for the treatment of patients with haemophilia, cystic fibrosis, pituitary dwarfism, Gaucher disease, multiple sclerosis, Malignant neoplasms of lymphoid, hematopoietic and similar tissues, as well as after organ and/or tissue transplants.

Provision of the Government of the Russian Federation No. 115 dated 14 February 2009 'Amendments to the Provision of the Government of the Russian Federation No. 682 dated 17 October 2007' extended the programme to 2011 inclusive.

The "7 nosologies" programme is the most effective state programme of assistance to patients with rare diseases which provides free costly pharmaceuticals to about 100 thousand seriously ill Russians.

Each patient entitled to reimbursement of pharmaceuticals is automatically included in the Federal Register. In each subject of the Russian Federation, specialists responsible for the treatment of this group of citizens, draw up orders for pharmaceuticals and submit them to the local health care managing bodies. Then the orders from each region are authorised and consolidated by the federal procurement body. In 2007, the role of the procurement body was played by Federal Agency for Healthcare and Social Development and in subsequent years by the Ministry of Healthcare and Social Development of the Russian Federation.

Procurement of pharmaceutical products under the "7 nosologies" programme is done through public tenders. Purchased pharmaceutical products are supplied to the regions according to the distribution lists drawn up on the basis of the orders from the regions.

Patients included in the register and entitled to receive medicines under the "7 nosologies" programme, are prescribed the necessary amount of drugs by their district doctor in the local polyclinic. The patients take the prescription to the authorised pharmacy to receive the medicine.

Owing to the realisation of the Federal Reimbursement Programme, Russian patients suffering from the most serious diseases have experienced, for the first time, an improvement in the quality of their lives.

The "7 nosologies" programme is seen by specialists as a prototype of wider reaching programmes designed to combat rare diseases. Its implementaion effectively represented the first steps to the systematisation of rare diseases and drawing up of their register, to creation of an orderly system of circulation of rare and expensive pharmaceuticals, giving impetus to the production of rare preparations in the country.

In October 2010, President Dmitry Medvedev confirmed his intention to expand the "7 nosologies" programme.

which contributed to resolving a part of the complex issues and contradictions, including those relating to the transition period.

The enactment of the law 'On the Circulation of Pharmaceuticals in the Russian Federation' led to development of a whole number of bylaws, such as Good Distribution Practice (GDP), Pharmaceutical storage regulations, Regulations of safe disposal of faulty, counterfeit and smuggled pharmaceuticals, Method of establishing the maximum selling price for pharmaceuticals included in the VEP etc.

Good Clinical Practice (GCP) and Regulations of production and quality control of pharmaceuticals (GMP) are still being developed in 2011.

The law 'On the Circulation of Pharmaceuticals in the Russian Federation' introduced certain changes in the procedure of pharmaceuticals registration, reduced the number of stages and state structures participating in the process of registration. These changes considerably increase the responsibility of a developer for the quality of preparation of the drug master file, the preparation and the methods of drug control.

Enactment of the law 'On the Circulation of Pharmaceuticals in the Russian Federation' resulted in a redistribution of the authorities of the federal executive agencies. Pursuant to the Government of the Russian Federation Decree No. 650, dated 20 August 2010, 'On Amending Several Acts of the Government of the Russian Federation in Connection with the Adopted Federal Law 'On the Circulation of Pharmaceuticals" the functions of registration of pharmaceuticals, including issuing permissions for conducting evaluation and clinical trials, registration of maximum selling prices for the pharmaceuticals producers, issuing permissions for import of each batch of non-registered pharmaceuticals have been transferred from Roszdravnadzor (Federal Service on Surveillance in Healthcare and Social Development of Russian Federation) to the Ministry of Healthcare and Social Development. The main function of Roszdravnadzor in the area of circulation of pharmaceuticals, following the coming into effect of the new law, are federal control over all the stages of circulation of pharmaceuticals – from pre-clinical development to disposal, including monitoring of safety of pharmaceuticals and monitoring of range and prices of VEP.

Apart from that, the Ministry of Healthcare and Social Development acquired new functions such as certification of evaluation experts from federal state budget-funded entities as well as of authorised representatives of the pharmaceuticals producers.

The new registry of researchers, drawn up pursuant to the new law, in addition to the already existing registry of accredited entities, will markedly simplify selection and search for potential partners in the area of clinical research.

The system of insuring patients participating in clinical trials has been fully revised; the term 'insurable event' has been clearly defined; and insurance premiums resulting from such events have been precisely determined. Underwriting rates have been established and determined depending on the objectives of the research and the number of patients, which allows to plan expenses connected to the compulsory insurance of patients in advance.

New requirements of the Federal Law in relation to the labeling of pharmaceuticals created an urgent objective, for Russian producers and importers of pharmaceuticals, to bring the labeling of their pharmaceuticals in line with the letter of the law. Pharmstandard, within the period of four months, prepared and introduced relevant changes in the normative documents of 182 pharmaceutical preparations.

PHARMACEUTICALS

OVERALL REVIEW

As of 31 December 2010 the list of pharmaceuticals sold by the Company included more than 250 items.

The portfolio of Pharmstandard is diversified and is represented in 52,106 anatomic and therapeutic groups (ATC) which comprises 38% of their total number (ATC segment of the third level). The anatomic and therapeutic segments in which the Company's pharmaceutical products are represented, occupy 69% of the total pharmaceutical market and 75% of its retail segment in value terms.

The TOP-10 preparations of Pharmstandard occupy key positions in their respective segments: Arbidol® and Amixin® (J05B Antivirals, excluding anti-HIV products), Pentalgin® (N02B Non-narcotics and anti-pyretics), Complivit® (A11A Multivitamins and minerals), Terpincod® and Codelac® (R05D Antitussives), Flucostat® (J02A Systemic agents for fungal infections), Afobazol® (N05C Tranquillisers) and Corvalol (N05B Hypnotics/Sedatives), Phosphogliv® (A05B Hepatic protectors, lipotropics). Arbidol®, Pentalgin®, Flucostat®, Terpincod®, Complivit® and Afobazol® are the leaders in their segments (in value terms).

In 2010, two brands, Arbidol® and Pentalgin® were included in the TOP-15 brands as per volume of sales in the whole of the pharmaceutical market in Russia, and in TOP-10 in the retail segment.

In 2010, two brands, Arbidol® and Pentalgin® were included in the TOP-15 brands as per volume of sales in the whole of the pharmaceutical market in Russia, and in TOP-10 in the retail segment.

Seven of the Company's brands were included in the TOP-30 among the domestically manufactured preparations: Arbidol®, Pentalgin®, Complivit®, Flucostat®, Codelac®, Amixin® and Phosphogliv®.

The following segments of the pharmaceutical market for Pharmstandard are of prime importance: J05 Antivirals for systemic use, N02 Analgesics, R05 Cough and cold preparations, A11 Vitamins, N05 Psycholeptics, J02 Systemic agents for fungal infections, A05 Cholagogues and hepatic protectors. In 2009, all the above mentioned segments exhibited an increase in the volume of sales, in comparison to 2008. In 2010, growth continued in all segments, except for "Antiviral systemic preparations" and "Vitamins", which was due to the post-epidemic shift in the peak period of flu and cold infections from the last months of 2010 to the first quarter 2011.

RESULTS

2010 STRATEGY

Depending on the registration status and the type of retail in pharmacies, the portfolio of the Company is divided into Over-the-counter pharmaceuticals (OTC) and Prescription pharmaceuticals (Rx). The Company's portfolio also includes preparations which are sold under trade names and INN. In 2009, the annual report included TPP (third parties products) as a separate group which has also been included in the 2010 report, with a number of additional positions.

The Company's portfolio of preparations, as in the previous years, is divided into two groups on the basis of their promotion: preparations in the active promotion stage, which generate most of the growth for the Company, and preparations which are not being promoted, which have reached a level of stable sales and consumption.

Branded preparations which are in the active stage of promotion, make the main contribution the business structure of the Company, i.e. 85.5%. This segment of preparations includes:

- Those brands which form the current basis of sales (the most significant preparations from the point of view of the volume of sales in value terms);
- The brands generate growth in value terms ("the drivers of growth", both new preparations and those preparations which have a history of being sold in the Russian market).

For the successful realisation of the strategy to achieve an increase in Company's sales by means of promoting branded preparations, we should take care of maintaining the volume of their sales and actively support the positive sales trend. In 2010, the main means of achieving the above objective for this group of pharmaceuticals, were:

- Maintaining the dominant position in terms of "quality" and / or "quantity" of advertising exposure to the target audience;
- Expansion of the current brands in terms of the sales by means of increasing the share of sub-brands or new SKU to attract new customers.

Among these brands are the leading brands such as Arbidol®, Pentalgin®, Complivit®, Codelac®, Flucostat®.

As for the portfolio of preparations which were responsible for most of sales growth gain ("growth drivers") in 2010, below are the key elements of our tactics approach in this respect:

- Development and launch of new Company's preparations, including by means of acquisition of third parties brands;
- Active investment approach which insures taking over a larger market share;
- Expansion of the target audience and its inclusion in new therapeutic sub-segments;
- Expansion of the market for such pharmaceuticals (by means of working with the end consumer, using the federal target programmes etc.).

Among these brands are Acipol®, Afobazol®, Phosphogliv®, Rastan®, Biosulin®, Combilipen® etc.

To successfully implement the strategy of increasing the share of Rx brands in the Company's sales structure, in 2010 the possibilities provided by the Federal Reimbursement Programme (FRP) were used. Thus, the drugs sold under the FRP, dominate the sales structure of a number of Pharmstandard's preparations, such as, for instance, the group of Endocrinology products. Within the framework of this strategy with respect to the FRP, in 2010, as in 2009, Pharmstandard played the role of a distributor participating in the state auctions of third parties pharmaceuticals (TPP group of products) under the FRP.

PORTFOLIO REVIEW. STRUCTURE

In 2010, Pharmstandard's total revenue from sales of pharmaceuticals amounted to RUR 28.8 billion which represents an increase of RUR 5.4 billion, i.e. 23.3% in relation to 2009 in value terms.

SALES IN 2010	2010 (RUR mln)	% of the total sales	2009 (RUR mln)	% of the total sales	Growth 2010/2009 (RUR mln)	Growth 2010/2009 (%)
Pharmaceutical products	**28,769.1**	**100.0%**	**23,335.1**	**100.0%**	**5,434.0**	**23.3%**
OTC	**16,238.8**	**56.4%**	**15,734.6**	**67.4%**	**504.2**	**3.2%**
Branded	13,339.0	46.4%	12,684.4	54.4%	654.6	5.2%
Non-branded	2,242.1	7.8%	2,130.8	9.1%	111.4	5.2%
TPP	657.7	2.3%	919.5	3.9%	-261.8	-28.5%
RX	**12,530.3**	**43.6%**	**7,600.5**	**32.6%**	**4,929.8**	**64.9%**
Branded	2,806.9	9.8%	2,022.4	8.7%	784.5	38.8%
Non-branded	487.3	1.7%	315.7	1.4%	171.5	54.3%
TPP	9,236.1	32.1%	5,262.4	22.6%	3,973.7	75.5%

The volume of sales of pharmaceutical products manufactured by Pharmstandard (without TPP) grew by 10% over 2009. The main contribution to this growth was made by the Rx preparations (56% in the structure of product growth, i.e. RUR 956 million out of RUR 1.7 billion) in comparison to the OTC preparations (43% in the structure of product growth representing RUR 766 million out of RUR 1.7 billion). It is noteworthy that the Rx preparations grew by 41% in relation to 2009 and the OTC preparations grew by 3.2%. The OTC growth figures resulted from the low growth dynamics of the branded preparations group which increased by 5.2% in relation to the previous year. In 2009, this figure was 43% which was due to the sharp increase in sales of anti-viral and anti-cold drugs during the flu and cold pandemic caused by the A/H1N1 virus. The growth of OTC products was mainly driven by Arbidol® which grew by 101.5%. Nevertheless, despite the fact that in 2009 the high growth rate of sales was attributable to the sharp increase in the consumption of anti-viral and anti-cold products, in 2010 we managed to maintain the positive trend of sales growth and the high growth dynamics of OTC products.

The structure of sales of pharmaceutical products, in terms of branded and non-branded products, practically has not changed. Branded products are the drivers of growth in volume terms. Their share in the sales structure amounts to 85.5%.

SALES IN 2010 (Excluding TPP)	2010 (RUR mln)	% of the total sales	2009 (RUR mln)	% of the total sales	Growth 2010/2009 (RUR mln)	Growth 2010/2009 (%)
Pharmaceutical products	**18,875.3**	**100.0%**	**17,153.3**	**100.0%**	**1,722.0**	**10.0%**
Branded	16,145.9	85.5%	14,706.8	85.7%	1,439.1	9.8%
Non-branded	2,729.4	14.5%	2,446.5	14.3%	282.9	11.6%

In 2010, the volume of sales of the top 10 brands amounted to 71.6% in the sales structure; their share reduced, in comparison to 2009. This is primarily due to the high rate of sales of anti-viral and anti-cold products during the flu pandemic in 2009 and the absence of such an epidemic wave in 2010.

№	BRAND	2010			2009			Volume 10/09		Sales 10/09	
		Volume (mln packs)	Sales (mln RUR)	% of total sales	Volume (mln packs)	Sales (mln RUR)	% of total sales	Change	%	Change	%
1	Arbidol	42.640	5,589	29.6%	45.736	5,503	32.1%	-3.095	-6.8%	87	1.6%
2	Pentalgin	38.124	1,988	10.5%	40.608	2,100	12.2%	-2.484	-6.1%	-111	-5.3%
3	Complivit	14.903	1,228	6.5%	16.818	1,188	6.9%	-1.915	-11.4%	40	3.4%
4	Terpincod	7.470	1,047	5.5%	6.442	889	5.2%	1.028	16.0%	158	17.8%
5	Phosphogliv	2.083	699	3.7%	1.721	596	3.5%	0.362	21.0%	103	17.3%
6	Codelac	8.317	692	3.7%	8.386	752	4.4%	-0.069	-0.8%	-61	-8.1%
7	Flucostat	5.609	653	3.5%	5.534	661	3.9%	0.075	1.3%	-8	-1.2%
8	Afobazol	4.093	607	3.2%	3.649	531	3.1%	0.444	12.2%	76	14.4%
9	Amixin	1.367	564	3.0%	1.322	558	3.3%	0.044	3.4%	6	1.0%
10	Rastan	0.336	439	2.3%	0.153	186	1.1%	0.182	118.9%	254	136.4%
TOP 10 total		**124.941**	**13,507**	**71.6%**	**130.369**	**12,964**	**75.6%**	**-5.429**	**-4.2%**	**544**	**4.2%**
Other brands		540.412	5,368	28.4%	577.233	4,190	24.4%	-36.821	-6.4%	1,178	28.1%
TOTAL SALES		**665.353**	**18,875**	**100.0%**	**707.602**	**17,153**	**100.0%**	**-42.249**	**-6.0%**	**1,722**	**10.0%**

* All forms of Flucostat® (tablets and injections)
** All Amixin® (No. 125 and No. 60)

In 2010, the share of TPP in the sales structure increased from 26.5% to 34.4%. This was due to the addition of two new third parties products to the portfolio of the Company: Coagil and Prezista®. In December 2009, Pharmstandard won the state open auction for the procurement of Coagil 7 (epta-cog alpha – coagulation factor VII) under the FRP. In the first quarter of 2010, this preparation was successfully procured, according to the state contract. Procurement of preparations Prezista® (Darunavir, manufactured by Janssen Cilag) for the treatment of HIV infection and AIDS took place in the

third quarter of 2010 within the framework of the Priority National Project "Health" (in compliance with the Decree of the Government of the Russian Federation No. 1143 dated 31 December 2009 "On procurement and delivery, in 2010, of diagnostics and antiviral preparations for the prevention, diagnosis and treatment of individuals infected with HIV and hepatitis B and C viruses, and of equipment and expendable supplies and materials for neonatal and audiological screening within the healthcare system").

These two preparations accounted for RUR 2.7 billion (73% in the growth structure in the TPP segment) of the total growth of RUR 3.7 billion in 2010 (Total sales of TPP achieved RUR 9.9 billion in 2010, RUR 6.2 billion in 2009). Pulmozyme® (dornaze alpha, manufactured by Hoffman La Roche) also made a considerable contribution to the growth of TPP: in 2010, the volume of sales of this medication under the FRP exhibited more than a fourfold increase.

In 2010, Pharmstandard continued the successful implementation of the joint venture project with Latvian Company Grindeks, launched in 2008, for exclusive sales and promotion of Mildronate® in the Russian pharmaceutical market. The sales of Mildronate® in 2010 amounted to RUR 1.2 billion. The data relating to Mildronate® is included in the TPP section of the accounts.

Thus, the organic growth of TPP (not taking into account Coagil and Prezista®) amounted to 15.7%, in relation to 2009, and the structure of product sales, in comparison to 2009, remained virtually the same.

SALES IN 2010	2010 (RUR mln)	% of the total sales	2009 (RUR mln)	% of the total sales	Growth 2010/2009 (RUR mln)	Growth 2010/2009 (%)
Pharmaceutical products	**28,769.1**	**100.0%**	**23,335.1**	**100.0%**	**5,434.0**	**23.3%**
Produced by Pharmstandard	18,875.3	65.6%	17,153.3	73.5%	1,722.0	10.0%
OTC	15,581.1	54.2%	14,815.2	63.5%	765.9	5.2%
RX	3,294.2	11.5%	2,338.1	10.0%	956.1	40.9%
TPP	**9,893.8**	**34.4%**	**6,181.9**	**26.5%**	**3,712.0**	**60.0%**
Velcade®	3,838.2	13.3%	3,661.9	15.7%	176.3	4.8%
Coagil®	1,799.5	6.3%	0.0	0.0%	1,799.5	-
Mildronate®	1,211.7	4.2%	1,194.3	5.1%	17.3	1.5%
Prezista®	942.5	3.3%	0.0	0.0%	942.5	-
Pulmozim®	610.2	2.1%	143.9	0.6%	466.4	324.1%
IRS®-19, Imudon®	533.5	1.9%	645.6	2.8%	-112.1	-17.4%
Other TPP	958.3	3.3%	536.1	2.3%	422.2	78.7%

Below is a detailed description of our leading brands, dynamics of the positions they occupy in the respective market segments (on the basis of the data of the "Pharmexpert" Research Centre), the changes in the indicators related to the perception of the brands by representatives of target audiences (on the basis of the data of COMCON-Pharma, TGI-Russia "The Russian index of target groups"), as well as the dynamics of these brands' sales in 2010 (on the basis of the Company's own data).

PORTFOLIO REVIEW. OTC PREPARATIONS

The revenue from the sales of the OTC products increased by RUR 740.4 million (or 5%) from RUR 14,840.7 million in 2009 to RUR 15,581.1 million in 2010.

The main drivers of growth in the branded OTC preparations were: Arbidol®, Afobazol®, Complivit®. The sales of Arbidol® in 2010 exceeded the figures for 2009 despite a high rate of growth of this product in 2009 due to the A/H1N1 flu and cold pandemic.

TOP-10 OTC ALL		2010			2009			Volume 10/09		Sales 10/09	
№	BRAND	Volume (mln packs)	Sales (mln RUR)	% of total sales	Volume (mln packs)	Sales (mln RUR)	% of total sales	Change	%	Change	%
1	Arbidol	42.640	5,589	35.9%	45.736	5,503	37.1%	-3.095	-6.8%	87	1.6%
2	Pentalgin	38.124	1,988	12.8%	40.608	2,100	14.2%	-2.484	-6.1%	-111	-5.3%
3	Complivit	14.903	1,228	7.9%	16.818	1,188	8.0%	-1.915	-11.4%	40	3.4%
4	Terpincod	7.470	1,047	6.7%	6.442	889	6.0%	1.028	16.0%	158	17.8%
5	Codelac	8.317	692	4.4%	8.386	752	5.1%	-0.069	-0.8%	-61	-8.1%
6	Flucostat	5.609	653	4.2%	5.458	649	4.4%	0.151	2.8%	4	0.7%
7	Afobazol	4.093	607	3.9%	3.649	531	3.6%	0.444	12.2%	76	14.4%
8	Amixin	1.208	514	3.3%	1.162	507	3.4%	0.046	3.9%	6	1.3%
9	Coal activated	71.233	247	1.6%	56.587	180	1.2%	14.646	25.9%	68	37.7%
10	Corvalol	41.986	230	1.5%	46.298	222	1.5%	-4.312	-9.3%	7	3.4%
TOP 10 total		**235.583**	**12,796**	**82.1%**	**231.144**	**12,521**	**84.5%**	**4.439**	**1.9%**	**275**	**2.2%**
Other brands		376.167	2,785	17.9%	432.936	2,294	15.5%	-56.769	-13.1%	491	21.4%
TOTAL SALES		**611.750**	**15,581**	**100.0%**	**664.080**	**14,815**	**100.0%**	**-52.330**	**-7.9%**	**766**	**5.2%**

* Only Flucostat® tablets
** Only Amixin® No. 125

Multivitamins and minerals. Complivit®.

"Multivitamins and minerals" historically is one of the most significant segments for Pharmstandard. In 2010, the volume of this segment in value terms amounted to RUR 7.2 billion, with the growth of +1% in relation to 2009. This is the lowest growth indicator in this segment in value terms for the last five years. This is due to the fact that in 2010, for the first time, this segment exhibited a reduction of price per package, which in turn led to a fairly insignificant increase in consumption within this segment in volume terms (+2%). A similar tendency (stagnation of prices and growth of consumption in volume terms) could also be observable in 2006-2007. Hence we can arrive at a conclusion that prices in this segment possess a certain elasticity, which, amongst other things, could be attributed to the fact that consumption of products belonging to this segment is not of a vital nature.

Pharmstandard's share in this segment is 20% in value terms and 36% in volume terms. It is worth noting that in the last five years our leading position within this segment, in volume terms, has been fairly stable. This means that our strategic potential for growth within this segment is determined, and more and more so, by the increase in the relative brand "value" in the eyes of the consumers, which should enable us to introduce changes in the price positioning of our products and, consequently, to increase our share in value terms.

Among all the products of Pharmstandard presented in this segment, the largest share belongs to Complivit®. At present, it is 15% in value terms which puts it in the second place among all the branded preparations in this segment.

Moreover, in 2010, Complivit® with respect to its consumption in volume terms was a clear leader among all the leading brands in this segment, and at the same time it exhibited the highest rate of growth among the TOP-4 brands in value terms, in relation to 2009. None of the near competitor preparations, comparable to Complivit® in terms of the sales volume, shows a similar rate of growth in value terms.

As regards the indicators of consumer attitude to the Complivit® brand, it shows an increase in the rates of knowledge, consumption and brand loyalty.

We believe that this became possible due to the consistent implementation of the strategy to expand the Complivit® line: new sub-brands have been added to the line, including in other segments.

One of the sub-brands of Complivit®, Complivit® Calcium D3 made an impressive progress. A vigorous media campaign and an effective communication component resulted in the increase of the market share of this sub-brand in the segment "A12A Calcuim Products" from 6.9% to 9.7% (the growth according to the market audit amounted to +61.1%, and the growth of the segment amounted to 14.5%).

On the whole, the strategy of promoting the Complivit® umbrella brand in 2010 was directed at the expansion of the consumer base of the brand among the female audience, which was reflected in the conclusions of RTGI monitoring: in the second half of 2010 the percentage of consumers among all the female consumers of this segment increased, in relation to the same period of 2009, from 10.6% to 11.1%. This was partly due to the launch, in 2010, of a new Complivit® sub-brand, Complivit® for women 45+ which specifically targets female consumers.

The above developments resulted in an increase of the share of sub-brands in the sales structure of the Complivit® brand. In 2010, it reached 48% in comparison to 32% in 2009.

In 2010, Complivit®, with its 6.5% share in the overall sales structure of the Company, was one of its most significant brands. In 2010, the sales of Complivit® in value terms increased by 3.4% vs 2009. The reason for such a low growth (in comparison to that in 2009/2008 when it was 76.6%) is that the fourth quarter of 2009 witnessed the peak of the epidemic and, consequently, a dramatic increase in consumption and sales of both antiviral and general health supplements (in particular, vitamins and minerals). Hence, the usual peak of consumption and sales shifted from the first quarter of 2010 to the fourth quarter of 2009 which led to changes in the structure of shipments during these periods.

Non-narcotics analgesics and antipyretics. Pentalgin®.

The category "Non-narcotics analgesics and antipyretics" is one of the largest segments in terms of the volume of consumption, both in volume and in value terms. Virtually all socio-demographic groups of the population of Russia consume preparations from this segment. The rate of consumption growth in this segment, according to the sales volume data, in the last three years slightly increased in relation to the same indicator for earlier periods (2008-2010 versus 2006-2008). In the last five years, we have been observing an increase in the average price per package in this category, which was caused by both the actual increase in prices and by consumers switching from the "traditional" analgesics of the bottom price segment to the brands of the middle and premium segments. This segment exhibits a low-level price elasticity: the unimpeded growth of the average price per package does not lead to a negative trend with respect to consumption in volume terms.

The volume of this category in 2010 amounted to RUR 12.8 billion and RUR 538 million packages. The share of Pharmstandard in this category, in the last five years, has been relatively stable and amounts, on average, to 29% in value terms. The changes in the share of the Company in volume and value terms are caused primarily by the changes in the structure of sales of "traditional" analgesics (Citramon, Analgin – the bottom price segment) and of Pentalgin® (middle price segment).

Among all the preparations of the Company, the Pentalgin® brand has the largest share of the market. In 2010, it amounted to 22% in value terms. Pentalgin® is the leader in this category. Furthermore, its sales in volume terms exceed by several times the sales volume of its nearest competitors for market share in value terms.

Moreover, in 2010, Pentalgin® showed a growth rate which was comparable with other participants included in this category's TOP-10 brands in value terms.

Taking into account the highly competitive nature of the analgesics market, in 2010, Pharmstandard selected a new strategy to maintain the leading position in this cat-

egory by means of increasing the number of loyal consumers and the number of those consumers who are switching from the "traditional" analgesics of a lower price segment to Pentalgin®. The second important element of the 2010 strategy was the launch in the Russian market of a new form of Pentalgin® (Pentalgin® No. 12) which has a new formulation (including, among other components, a spasmolytic) and a wider range of indications.

In 2010, the loyalty of the target group (females aged 25-55) to Pentalgin® grew by 12% (according to Gallup), and the national numerical and weighted distribution of the new form of Pentalgin® amounted, as of December 2010, to 21% and 52% respectively which points to high retail penetration reached in the shortest possible timeframe (three months of active sales).

In 2010, Pentalgin® with its 10.5% share in the overall sales structure of the Company, was one of its most significant brands. In 2010, the sales of Pentalgin® in value terms reduced by 5.3% in relation to 2009. This dynamic is related to the dramatic increase in sales of the Pentalgin® brand in the fourth quarter of 2009, which, in turn, is related to changes in the stocking policy of national distributors during the "swine" flu pandemic. The increase in stock in the fourth quarter of 2009 was a response to the dramatic increase in consumer demand for both antiviral medicines and also for symptomatic medications which alleviate the effects of the disease (in particular, products from the category "Non-narcotics analgesics and antipyretics").

Systemic agents for fungal infections. Flucostat®.

Pharmastandard's active penetration into the category of "Systemic agents for fungal infections" is directly connected with its purchase, in 2006, of CJSC "Masterlek" and the Flucostat® brand. This category has a significant potential, as in the last five years it has been showing a stable growth both in value and in volume terms (in the 2006-2010 period the growth was 41% and 42% respectively). In 2010 this category's volume was RUR 4.9 billion and 23.9 mln. packages. This segment is price elastic: while during 2006-2009 the average price per package was in stagnation and, at the same time, the consumption was steadily growing, in the 2009-2010 period the average price reduced to the 2006 level which accounted for the segment's growth by 16% in volume terms. This indicator is the highest in the last five years.

In 2010, Pharmstandard's share in the "Systemic agents for fungal infections" segment was 21% in value terms and 23% in volume terms. Moreover, during the 2009-2010 period the Company's share increased which was due to the growth in sales at a faster rate than the growth of the segment itself, both in volume and in value terms.

Pharmstandard is represented in this segment by the Flucostat® brand. With its share of 20% in value terms, Flucostat® is the leading brand in the segment and, moreover, it shows a higher growth than the growth of the segment itself. It is worth noting that Flucostat® is a clear leader of the sales in volume terms among its nearest competitor brands, and at the same time its rate of growth exceeds that of the majority of its competitors.

The strategy of Flucostat® promotion in 2010 focused on maintaining its market share by means of strengthening the position of the brand in the retail segment. It was essential because the market of preparations containing fluconazole is highly competitive (more than 18 trademarks and more than 30 manufacturers in 2010).

An effective media campaign in combination with the BTL activities at outlet level allowed us not only to maintain but also to increase the share of the brand in the respective segment. It is also worth mentioning that the volume of prescriptions of Flucostat® by gynaecologists in 2010 increased threefold which ensured a leading position for the brand (Comcon data, 2010). According to the latest research, Flucostat® is the only brand in this category which exhibits a positive dynamic in terms of the volume of its prescriptions by gynaecologists.

The promotional campaign of the Flucostat® brand resulted in an increase in the number of its loyal consumers by 20% (the target group: females aged 25-45, based on data from Gallup). There is also an observable increase in the levels of knowledge, consumption and brand loyalty among the consumers of the category of preparations for the treatment of candidiadis (data from Gallup).

In 2010, Flucostat® was in the seventh place with a share of 3.5% in the Company's structure of sales. The growth of sales, in relation to 2009, amounted to 1.3% in volume terms, while in value terms we observed an insignificant decrease of 1.2%. Such results are attributable to the changes in the structure of sales of the forms of production of the Flucostat® brand. First, in 2010, the Company temporarily halted sales of the injectable form of Flucostat® which was related to the process of renewal of its registration certificate. Second, the share of the more expensive form of production of Flucostat® (Flucostat®, 50 mg, No. 7) in the structure of sales reduced, while the share of the 150 mg form of production, No. 1, increased. This change is of a strategic significance, as the main area of application of the Flucostat® brand by consumers is the treatment of vulvovaginal candidiasis (vaginal thrush), and the 150 mg form of production, capsule No. 1, is most suitable for the therapy of this disease.

Antivirals, excluding anti-HIV products. Arbidol®. Amixin®.

Sales of systemic antivirals is one of the strategic directions of the Company. Pharmstandard's presence and progression in this segment is another example of the successful implementation of the Company strategy of growth through acquisition of brands possessing a high potential for development in relevant segments.

The category "Antivirals, excluding anti-HIV products" has, for the last few years, been exhibiting high rates of growth both in volume and in value terms. The main external factor determining the rate of development of this category, is the severity of flu epidemics during the autumn-winter periods. It is precisely for this reason that this category is characterised by the "shifting" of peak consumption periods and, consequently, of peak sales. A perfect example of such "shifting" could be observed during the season of 2009-2010 when a sharp increase in sales in 2009 was followed by a decrease in sales in 2010.

For the last few years the sales of Arbidol® in value terms amounted to 50% of the overall volume of sales in this segment. The second position is occupied by another Pharmstandard preparation, Amixin® (its share in 2010 amounted to 6.4%). As already mentioned above, the dynamics of sales volume in this segment is largely determined by external factors, primarily by the outbreaks of flu and cold-related diseases. For example, during the winter season of 2009-2010 the flu pandemic peaked at the end of 2009 which is the reason why the sales of antivirals in 2010 reduced, in comparison to 2009, by 11.2%. According to Comcon Pharma, in 2010, 14.6% of the population of Russian over the age of 16 were consumers of Arbidol®, over 9.9% in 2009.

It is noteworthy that in 2010 the Company launched a new form of production of Arbidol® which contained 40 capsules. Effectively, we created a special form of production for loyal consumers which was conducive to completion of the recommended course of treatment with this preparation. This, in turn, resulted in a reduction of the market share of Arbidol® with respect to the number of packages sold. However, if we recalculate the sum total of all forms of Arbidol® sales as though it were sold in packages containing 10 capsules each, we shall come to the conclusion that in 2010 Arbidol® maintained its share in volume terms and that the tendency of sales variations fully correlates with the market (segment) dynamics which equals -7.8%.

Dynamics of Arbidol® sales (based on the form of production No. 40) and of the segment.

			Packages, mln
	2009	2010	Growth, %
Market (segment) volume	50,6	46,7	-7,8%
Arbidol® volume (on the basis of the sum total of all forms of production)	34,3	30,0	-12,5%
Arbidol® volume (recalculation of all forms of production into the No. 10 package)	37,5	34,5	-7,8%
Arbidol® market share (on the basis of the sum total of all forms of production), %	67,8%	64,3%	
Arbidol® market share (recalculation of all forms of production into the No. 10 package), %	74,0%	74,0%	

The marketing strategy of the Arbidol® brand was focused on maintaining the adherence of doctors and patients to administration of etiotropic antiviral preparations in the post-pandemic period. An infection outbreak caused by the Mexican type 'A' flu virus (H1N1) was pronounced to be a pandemic by the World Health Organisation on 11 June 2009. According to the experts, during the course of 2010, the effects of the flu pandemic conformed with the most favourable scenario which could be expected. This gave ground to some criticisms purporting that the measures undertaken to confront the pandemic, were disproportionately excessive in relation to the actual threat. However, such a misinterpretation of the role of a scientifically sound approach to the development of a healthcare technology, which was so beneficial to the whole world and to Russia in particular, may result in grave peril for the cause of health protections against future threats (2).

According to leading virusology experts, the following factors required thorough monitoring in the post-pandemic period:

- a possible change in the virulence (pathogenicity) of the virus caused by the next wave of infection;
- development of a resistance to antiviral preparations as a result of mutation (2).

It is obvious that promotion of Arbidol® in 2010 had to based on reliable clinical and laboratory research confirming the efficacy of Arbidol® in the post-pandemic period. For this reason, in 2010, we dedicated a lot of attention to the issue of the flu virus' potential resistance to Arbidol®. Eventually, neither the monitoring organised in Russia to ascertain the resistance of circulating 'A' flu strains, nor the clinical studies done with the volunteers taking Arbidol® found any strains resistant to Arbidol® (3, 4).

Another important tactical component was the launch of a new form of production, Arbidol® in capsules No. 40. The effect of this new form was to enhance consumer loyalty to treatment with Arbidol® as one package contained the quantity of capsules sufficient for a proper course of treatment.

The effectiveness of our 2010 strategy is confirmed by the dynamics of indexes of awareness, consumption and brand loyalty with respect to Arbidol® among the representatives of the target audience: in 2010, we witnessed a considerable increase in the share of Arbidol® consumers in the category of anti-flu and anti-cold medications.

In 2010, as in 2009, the Arbidol® brand held the leading position in the Company's structure of sales with a share of 30% in value terms. The growth of sales, in relation to 2009, amounted to 1.6% in value terms while sales in volume terms reduced by 6.8%. Such changes are connected primarily to the differences in the sales structure between the two seasons (autumn 2009 and winter 2010) caused by the pandemic flu outbreak's shift to the fourth quarter 2009. The second reason was that the sales dynamics was affected by the changes in the forms of production: the more expensive form of production containing 40 capsules increased its share which, in turn, led to the reduction in consumption of the form of production containing 10 capsules and to establishing, nevertheless, of a positive trend of sales in value terms.

Tranquilizers. Afobazol®

The segment of tranquilizers includes a wide-range of preparations united by the area of application: all of them are administered either episodically or as a course of treatment to relieve the states of increased agitation and neuroses. In 2010, the sales in this category amounted to 252.5 million packages. Moreover, in the 2009-2010 period, this category grew by 9.2% which exceeded its sum total

growth in the 2006-2009 period (when the category only grew by 8%). We believe that the increased rate of growth in the last two years was, to a great extent, attributable to the fact that the issues of agitation and stress have become more relevant for the public. In 2010, the growth of sales in this category in value terms amounted only to 5% (or RUR 8.6 billion). It is worth nothing that in the period from 2006 to 2009 the sales in this category increased twofold in value terms.

The share of Pharmstandard in this segment in 2010 amounted to 14.6% in value terms and 22.7% in volume terms. The rate of growth within this segment exceeds that of the segment itself, which is primarily due to the outstanding effect of promotion of the innovative preparation Afobazol® which was acquired from Russian company Masterpharm in 2008. Since the acquisition of Afobazol®, the share of Pharmstandard in this segment of the market increased by 1.5 times (from 10% to 15% in value terms).

In 2010 the share of the Afobazol® brand in this segment amounted to 9% in value terms which corresponded to the third place in the list of TOP products in this category.

Afobazol® is one of the drivers of this segment: its growth in value terms in 2010 amounted to 23%, in relation to 2009. Moreover, Afobazol® is one of the fastest growing leading brands in this category with its rate of growth exceeding that of the segment itself.

This was achieved largely due to an intensive media campaign (according to Gallup, in 2010 Pharmstandard moved to the leading position in terms of its share of voice among all the advertising campaigns of preparations from the same category) encompassing national television, press and Internet. One of the effects of the campaign was that the share of those who are aware of the Afobazol® brand, within the target group, increased, in comparison to 2009, from 22% to 29%; and at the same time the number its consumers grew from 8% to 9% (Gallup data). The following factors of success are also worth mentioning: the action mechanism of the preparation which defined its clinical profile (in particular, it does not cause such side effects as drowsiness, dependency and addiction) (6); and also our work with a wide range of medical specialists (general practitioners, cardiologists, gynaecologists, dermatologists, neurologists and gastroenterologists) aimed at increasing awareness and relevance of the issue of disorders characterised by agitation among the patients with somatic diseases.

In 2010, sales of Afobazol® amounted to RUR 600 million (4.1 million packages) representing an increase of 14% (in value terms) and 12% (in volume terms) respectively. The rate of growth of the brand's sales corresponds to the positive dynamics of the brand reflected in the market audits and is the result of an effective promotional campaign.

Cough and cold preparations. Codelac® and Terpincod®

This category unites preparations included in two segments: "cough preparations" and "expectorant preparations". It includes pharmaceuticals used for clearance of the cough syndrome which may acCompany multiple diseases of the upper and lower respiratory tracts (including infectious diseases, such as, for example, flu and cold. In 2010, the sales of this category of drugs grew by 8% in value terms over 2009. This category has been showing a stable growth in this area for the last five years. However, in volume terms it has been in stagnation in the last five years (195.9 million packages were sold in 2010) which is due to the "historically" high level of market saturation with this type of medications.

The share of Pharmstandard in this segment in 2010 amounted to 14.8% in value terms and 11.4% in volume terms. It has been experiencing a downturn tendency during the last two years. This is due to changes in the regulation of pharmaceutical circulation at the regional level with respect to the group of preparations which include, among others, such preparations as Codelac® and Terpincod®.

In 2010, Codelac® and Terpincod® were in the third and fourth places, their market share amounting to 6% each (in value terms).

In 2010, the main strategic emphasis was on the promotion of the new form of Codelac®, Codelac® Broncho (tablets and syrup). The combined preparation was found, in clinical trials, to be more efficient in the treatment of cough accompanied by stubborn phlegm in comparison to single preparations containing ambroxol (5). Our promotional efforts, directed primarily at general practitioners and pediatricians, as well as at pharmacies, resulted in a fourfold increase of Codelac® Broncho's market share in the segment in 2010. In 2010, the share of Codelac® Broncho (tablets and syrup) in the general sales structure of the Codelac® brand increased from 5% (2009) to 12% (2010).

On the whole, the sales of the Codelac® brand in 2010 showed an insignificant reduction in volume terms. However, in value terms the reduction was more pronounced (-8% in relation to the sales of 2009). This was due to the changes in the structure of the Codelac® brand sales with respect to certain forms of production (the increase in sales of Codelac® Broncho and reduction in sales of Codelac® and Codelac® Phyto). In 2010, Codelac® held sixth place, with a share of 3.7% in value terms, in the Company's structure of sales.

Antidiarrheal microorganisms (probiotics). Acipol®

In 2010, Pharmstandard acquired the Acipol® brand which enabled us to enter the market of probiotics (antidiarrheal microorganisms). In 2010 this segment was worth RUR 6.2 billion, with a volume of consumption of 29.1 million packages (the growth in relation to 2009 was 13% and 15% respectively).

The share of Acipol®, in 2010, amounted to 5.4% in value terms (in the last five years the brand increased its share more than ten times). Its share in volume terms was 6%. It is also worth mentioning that the growth of the Acipol® brand in 2010 exceeded the growth of the segment itself, both in value and in volume terms, which allowed it to move to fourth place in the market.

In 2011, Acipol® is in the stage of active promotion overseen by Pharmstandard's marketing and promotion team. Work with pediatricians forms the backbone of its promotional strategy, as preparations from this category are actively prescribed for the treatment of various forms of disbacteriosis occurring in children.

PORTFOLIO REVIEW. PRESCRIPTION DRUGS (RX)

In 2010, the Rx portfolio grew by 41%. This is the most significant segment which is responsible for the largest contribution to the Company's structure of sales in value terms. Rx preparations are sold both in the commercial segment of the pharmaceutical market, through the FRP, and in the hospital segment of the market. The priorities for our work in each segment are defined depending on the work strategy for each preparation at the stage of promotion. For the majority of Rx preparations at the stage of promotion, the focus was on the commercial segment as the largest segment of the market with a 51.2% share of Rx preparations, in value terms. Given that the share of Rx preparations in the Company's sales structure has until now been lower than the share of Rx preparations in the sales structure of the Russian market, there is an obvious strategic potential for the development of the Company's business. We are working on the realisation of this potential at present and will continue in the future.

Sales of prescription drugs increased by RUR 956.1 million (or 40.9%) from RUR 2,338.1 million in 2009 to RUR 3,294.2 million in 2010. The following preparations made a considerable contribution to the increase in prescription drugs sales: Rastan® (somatotropin) grew by RUR 253.5 million or 136.4%, Biosulin® (insulin) grew by RUR 150.4 million or 71.4%, Phosphogliv® grew by RUR 103.2 million or 17.3%, Combilipen® grew by RUR 83.8 million or 42.9% and Octolipen® grew by RUR 64.2 million or 224.1%.

TOP-10 RX ALL		2010			2009			Volume 10/09		Sales 10/09	
№	BRAND	Volume (mln packs)	Sales (mln RUR)	% of total sales	Volume (mln packs)	Sales (mln RUR)	% of total sales	Change	%	Change	%
1	Phosphogliv	2.083	699	21.2%	1.721	596	25.5%	0.362	21.0%	103	17.3%
2	Rastan	0.336	439	13.3%	0.153	186	8.0%	0.182	118.9%	254	136.4%
3	Biosulin	0.731	361	11.0%	0.442	211	9.0%	0.289	65.4%	150	71.4%
4	Combilipen	2.919	279	8.5%	1.811	195	8.4%	1.108	61.2%	84	42.9%
5	Cocarboxylase	4.402	216	6.5%	3.165	109	4.7%	1.237	39.1%	106	97.6%
6	Picamilon	3.959	155	4.7%	4.299	129	5.5%	-0.341	-7.9%	26	20.5%
7	Cyclodol	2.730	120	3.7%	2.506	107	4.6%	0.224	9.0%	13	12.4%
8	Sulfocamphocain	2.620	103	3.1%	1.989	69	3.0%	0.631	31.8%	34	49.3%
9	Azitrox	0.631	99	3.0%	0.655	108	4.6%	-0.023	-3.5%	-9	-8.1%
10	Octolipen	0.482	93	2.8%	0.149	29	1.2%	0.333	222.7%	64	224.1%
	TOP 10 total	**20.893**	**2,565**	**77.9%**	**16.890**	**1,738**	**74.3%**	**4.003**	**23.7%**	**826**	**47.5%**
Other brands		32.710	729	22.1%	26.632	600	25.7%	6.078	22.8%	130	21.6%
	TOTAL SALES	**53.603**	**3,294**	**100.0%**	**43.522**	**2,338**	**100.0%**	**10.081**	**23.2%**	**956**	**40.9%**

Hepatic protectors/lipotropics. Phosphogliv®

In 2010, the volume of the category of "Hepatic protectors/lipotropics" exceeded RUR 11.5 billion. In the last five years this category has grown more than twofold. In the period of 2009-2010 the rate of growth of this category amounted to 16% in value and in volume terms.

In 2010, Pharmstandard's share of this segment amounted to 6.8% in value terms and 6.6% in volume terms. Moreover, since 2006 the share increased five times exceeding, on an annual basis, the rate of growth of this segment.

In this segment, the Company is represented by Phosphogliv® containing natural phospholipids which have a hepatoprotective effect, and also glycyrrhetinic acid which has hepatoprotective, anti-inflammatory and antiviral effects.

In 2010, Phosphogliv® held the fifth position in the Company's sales structure, with a share of 3.7%. In relation to 2009, Phosphogliv® grew by 21% in volume terms and by 17% in value terms. The success of the Phosphogliv® promotional campaign in 2010 was determined by the following factors: an extended reach to the main target audiences (gastroenterologists, infectiologists, general practitioners) which became possible through the reorganisation of the field force; and also the launch of the nation-wide educational programme on chronic hepatitis (together with the scientific association "Russian Society for the Study of the Liver"). The programme enabled us to create awareness about the issue of diagnosing and treating hepatitis and subsequently to establish such programmes for patients at a regional level. It is also worth noting that in 2010 Phosphogliv® was included in the VEP, on the basis of the scientifically sound evidence of its efficacy.

Other prescription drugs of the Company

One of the most successful launches of a new prescription drug was Combilipen®, a multivitamin preparation for the comprehensive treatment of neurological diseases, including polyneuropathy of various etiologies, which has been at the stage of active promotion after its launch in 2008. In the third year the sales of the preparation reached RUR 280 million in value terms, and in 2010 they showed an increase of 43% in relation to 2009. According to the market data, in 2010, the share of Combilipen® in its segment amounted to 13%, while the increase in value terms equalled 7% and the brand growth was over 60%.

It is also worth noting that in 2010, Octolipen® which is administered for the treatment of neurological disorders and also for complications of diabetes, grew by 224%.

The Company's success in the segment of hi-tech preparations H04C Growth Hormones deserves a special mention. In 2010, the Rastan® brand's share of this segment was 81.5% and its sales increase was +309% over 2009. This success was connected to the launch, in 2010, of a new dosage of Rastan® (solution for subcutaneous injection) as well as of a new device for a more comfortable injection – Biomatik® Pen system. These factors, along with the competitive price, account for the considerable advantage enjoyed by the Rastan® brand in comparison with its foreign competitors.

A similar positive dynamics of Pharmstandard's position was also observable in the segment "A10 Human Insulin and Analogues". Despite the reduction of the segment in value terms (-5%), Biosulin® showed an 18.4% increase in value terms. Such a dynamic is attributable to the extension of the reach to the endocrinological target group, as well as to the state's preferences regarding the status of Russian manufacturers.

VEP LIST 2011 vs 2010

PRICE REGULATION FOR PREPARATIONS INCLUDED IN THE LIST OF VITAL AND ESSENTIAL PHARMACEUTICALS

To keep down the prices for those pharmaceuticals which satisfy the priority healthcare needs such as prevention and treatment of diseases, including those prevailing in the structure of diseases in the Russian Federation, the Government of the Russian Federation, in 2010, passed a number of legislative acts (Federal Law No. 61-FZ 'On the circulation of pharmaceuticals', Federal Laws dated 27.07.2010 No. 192-FZ, dated 11.10.2010 No. 271-FZ, dated 29.11.2010 No. 313-FZ) which regulate the circulation of VEP in the territory of the Russian Federation and transferred the functions of supervision of their enforcement to the Ministry of Healthcare and Social Development of the Russian Federation.

In connection with these changes the following has been drawn up and endorsed:

- by the Decree of the Government of the Russian Federation No. 865 dated 29.10.2010

1. The rules of state registration of maximum selling prices of the producers of pharmaceuticals included in the list of vital and essential pharmaceuticals.
2. The rules of maintaining the state register of maximum selling prices of the producers of pharmaceuticals included in the list of vital and essential pharmaceuticals.
3. The rules of establishing maximum wholesale and maximum retail mark-ups on the actual selling prices of the producers of pharmaceuticals included in the list of vital and essential pharmaceuticals, in the subjects of the Russian Federation.

- VEP list for 2011 (Government Decree No. 1938-r of 11 November 2010)
- The method of establishing, by the producers of pharmaceuticals, the maximum selling prices for pharmaceutical preparations included in the list of vital and essential pharmaceuticals (it was enacted by the Decree of the Ministry of Healthcare and Social Development and the Federal Tariff Service on 3 November 2010, No. 961n/527-a).

In accordance with the Decree of the Government of the Russian Federation No. 865 dated 29.10.2010, all maximum selling prices for vital and essential pharmaceuticals of domestic producers registered before 26.10.2010 are indexed, from 11.11.2010, at 8%.

In addition to the preparations included in the previous List, in 2011 the VEP list contains the following types of pharmaceuticals produced by Pharmstandard: Acetylsalicylic Acid, Paracetamol tablets, Mildronate.

The method applied by manufacturers for establishing maximum selling prices for pharmaceuticals in the list

of VEP, determines that prices for those pharmaceuticals in circulation in the territory of the Russian Federation are calculated:

- for Russian produced pharmaceuticals – as weighted average actual selling price for the year prior to price registration;
- for foreign producers – as weighted average actual price of import for a year taking into account customs clearance and transportation expenses;
- and for pharmaceuticals which have not been in circulation in the territory of the Russian Federation for one year and original pharmaceutical preparations:
  - Russian manufacturers provide a calculation of expenses, related to development, production and realisation of pharmaceuticals, as well as the method of distribution of general running costs;
- foreign manufacturers provide information regarding minimum selling prices in the producer state and other states which are listed in Appendix No. 5 to the Method.

The process of registration of maximum selling prices for manufacturers takes into account registered maximum selling prices for analogous pharmaceutical preparations (based on the brand names, INN, dosage, dosage form):

- the maximum asking selling price of a Russian manufacturer is compared with the maximum selling prices for analogous pharmaceuticals manufactured in Russia; and if they do not exist, then it is compared with the maximum registered price of an analogous preparation manufactured in a foreign country and present in civil circulation in the territory of the Russian Federation;
- the maximum asking selling price of a foreign manufacturer is compared with the maximum selling prices for analogous pharmaceuticals in civil circulation in the territory of the Russian Federation.

Re-registration of maximum selling prices for domestic manufacturers is envisaged to take place within a period of no less than one year. The method does not stipulate re-registration frequency for foreign manufacturers.

98 maximum selling prices have been registered for VEP manufactured by Pharmstandard in 2010 (in relation to 43 international non-proprietary names or in relation to 46 branded names).

The main entries:

№	INN	Brand Name
1	Azithromycin	Azitrox
2	Arbidol	Arbidol
3	Insulin soluble (human genetically engineered)	Biosulin
4	Insulin-isophan (human genetically engineered)	Biosulin
5	Somatropin	Rastan
6	Tilorin	Amixin
7	Flukonazon	Flukostat
8	Phospholipids	Phosphogliv
9	Phospholipids+Glycyrrhizinic Acid	Phosphogliv

In 2010 the share of pharmaceuticals produced by Pharmstandard itself and related to the vital and essential pharmaceuticals, amounted to 56.4% of pharmaceuticals manufactured by the Company.

EXPORT SALES FOR 2010

Selling its products at the export markets is one of the strategic directions of Pharmstandard. Though the volume of export in 2010 amounted only to 2% of the Company's revenue, the markets of the CIS countries show a high rate of growth. Promotion of the most modern branded products to foreign markets constitutes the core of the Company's strategy in relation to export sales.

Export of the Company's pharmaceutical products in 2010 increased by 38.8% and amounted to RUR 593 million vs RUR 427 million in 2009. The share of Top-10 exported pharmaceuticals amounts to 79% (RUR 472 million) of the Company's revenue from export. The Top-10 exported pharmaceuticals include Arbidol®, Complivit®, Pentalgin®, Afobazole®, Citramon P, Ingalipt®, Phosphogliv®.

The Company exports its products to 14 countries, mostly to the CIS countries: Ukraine (41.8%), Uzbekistan (34.8%), Belarus (7.7%).

The Company's strategic planning includes active development and expansion not only the CIS countries but also Latin and South America (Venezuela, Argentina, Nicaragua), Africa (Nigeria, Egypt), Near and Middle East (Iran, Iraq, Afghanistan, UAE).

PRODUCT DEVELOPMENT IN 2010

In 2010, we have introduced 15 new pharmaceutical products (10 OTC products and 5 prescription products) including new dosage form of growth hormone, which accounted for 0.3% of our pharmaceutical product sales in 2010.

The following table sets forth certain information concerning our registration applications by therapeutic segment for both prescription products and OTC products as of 31 December 2010.

Product		Date	Description (Therapeutic Segment)	Sales Value, RUR mln	AT C value, 2010, RUR mln
OTC	Complivit® Woman 45+	Jan 10	A11A – multivitamins with minerals	18.3	9455.5
	Complivit® Active (Chewing), 3–10 years	Dec 10	A11A – multivitamins	-	9455.5
	Complivit® "Trimestrum"	Dec 10	A11A – multivitamins with minerals	5.5	9455.5
	Complivit® Ca D3 forte	Oct 10	A12A- calcium products	9.1	2211.2
	Codelac® Broncho syrup with thyme	Feb 10	R05D – antitussives	35.5	3089.5
	Complivit® Multivitamin (powder for oral liquid), up to 3 years	Dec 10	A11A – multivitamins with minerals	-	9455.5
	Complivit® Ca D3 (powder for oral liquid), up to 3 years	Nov 10	A12A- calcium products	0.5	2211.2
	Pentalgin® (codeine free)	Dec 10	N02B – non-narcotics analgesics	-	14016.7
	Zinnokap® aerosol	Feb 10	D05A – topical antipsoriasis product	6.0	842.9
	Znnokap® liniment	Apr 10	D05A – topical antipsoriasis product	5.8	842.9
RX	Artrozan® solution 6 mg/ml	Sept 10	M01A1-Anti-Rheumatics, Non-Steroidal Plain	2.8	13662.5
	Phosphogliv® forte capsules	Jun 10	A05B – Hepatic protectors, lipotropics	14.1	11739.2
	Formetin® tablets 850 mg, 1000 mg	Dec 10	A10J1 – Biguanide Antidiabetics, Plain	-	1669
	Glimepiride tablets 2 mg, 3mg	Dec 10	A10H – Sulphonylurea Antidiabetics	-	2162.8
	Rastan® solution, 5IU/ml	Nov 10	H04C0-Growth Hormones	-	578.7

Following our strategic intentions we are going to launch 6 OTC and 5 prescription products in 2011 including extension for our Maxicold®, Neosmektine®, Azitrox®, Terpincode® umbrella brands and new topical non-narcotics analgesics product Next®.

PRODUCT APPROVALS AND LAUNCHES 2011

Product		Date	Description (Therapeutic Segment)	AT C value, RUR mln
OTC	Medira® caps	Apr 11	C01E – metabolics	2043.3
	Maxicold® coated tablets	Apr 11	N02B – non-narcotics analgesics	14016.7
	Next® coated tablets	Jun 11	N02B – non-narcotics analgesics	14016.7
	Cyclovita® coated tablets	Jul 11	A11A – multivitamins with minerals	9455.5
	Maxispray® spray	Dec 11	A01A2 – Mouth Antiseptics And Anti-Infectives	751.8
	Neosmektine® powder (new flavors)	Dec 11	A07B – intestinal absorbent antidiarrhoeals	3005.3
RX	Gluconorm® coated tablets	Aug 11	A10J2 Biguanide And Sulphonylurea Antidiabetic Combinations	681.1
	Water for injections in vials, 2,4,5,8,10 ml	May 11	V07AB – solvent	234.5
	Terpincode® N	Oct 11	R05D – antitussives	3089.5
	Akorta® coated tablets	Nov 11	C10A – Hypolipidemics	4315.8
	Azitrox® caps 500 mg №2	Sept 11	J01F – Macrolides and similar types	5473.1

NAUCHTECH STROY PLUS LTD

Its role in the project consists of development and implementation of bioengineered pharmaceutical and diagnostics products.

The main areas of activity of the R&D Centre:

- Replication of know-how of manufacturing vital bio-technological pharmaceuticals
- Development of new promising forms by means of cellular and protein technologies and genetic enginieering
- Following the completion of the centre's construction it is expected that it will annually develop and market 8–10 new genetically-engineered pharmaceutical preparations

- Interaction with the leading Russian scientific centres
- Sourcing and employment of reseach scientist with working experience in western and Russian pharmaceutical companies
- Creation of a local and international scientific consultation committee
- The plan of development of the R&D centre:
- Territory – 70 hectares in the central region of Russia (80 km from Moscow)
- Research and production complex – 4.5 thousand m^2.
- Personnel – 150 research scientists with international working experience in the areas of biotechnology, chemistry and pharmacology.
- Residential buildings – more than 10 thousand m^2 including all the necessary infrustructure for 600 people.

Planned investment – RUR 990 million.

Investment (September 2010) – RUR 630 million, RUR 150 million of which was the equity capital share.

Project completion – the end of 2012.

In February 2010, Nauchtech Stroy Plus Ltd. (NTS+ Ltd.) was registered, with 50% Pharmstandard ownership. At the current stage a R&D centre with the necessary infrastructure is being constructed in the Vladimir region. As of the end of 2010, the total investment in Nauchtech Stroy Plus Ltd. for construction of the R&D centre amounted to RUR 630 million, RUR 150 million of which was the equity capital share in Nauchtech Stroy Plus Ltd. Construction and installation works, building communication network and construction of roads within the R&D centre have been completed. Interior furnishing and equipment installation has begun.

By the end of 2011, laboratories of molecular biology, cellular technology and bio-chemistry will be operational; 41 residential buildings for R&D personnel accommodation, a cultural and business centre, a general communications network and municipal amenities will be completed.

There are clinical trials underway at present concerning 4 new preparations which are being developed within the framework of the biotechnological project GENERIUM.

INN	Theraputic indications
Blood-coagulation factor VIII	Haemophilia
Blood-coagulation factor IX	Haemophilia
PEG filgrastim	Neutropenia
Alteplase (tissue-type plasminogen activator)	Acute ishemic stroke / Myocardial infarction

SALES & MARKETING (STRUCTURE, CHANGES)

A more vigorous promotion of the Company's preparations is the strategic platform for success which will allow us to expand our sales and marketing capabilities. The Sales and Marketing department is responsible for the branded drugs which are promoted through our Sales Force and advertising activities directly to medical and pharmaceutical professionals and consumers. The list of promoted products in 2010 included 30 brands. The contribution of the promoted products to the total sales of pharmaceutical products without TPP in 2010 was 65%. One of the promoted brands from the TPP group is Mildronate®; its sales volume in 2010 amounted to RUR 1.2 billion. 2010 was a year of recovery, after the crisis, and was notable for the considerable reinvigoration of the leading industry players. This meant we had to review our strategy and enhance our field presence.

In 2010, the following tactical principles formed the foundation of our strategy:

- further specialisation of our production portfolio work force;
- a more precise targeting and an increase in the "voice share" of each strategic brand, as well as of new preparations which are launched for the first time;
- an extended reach to the main target audiences.

In the first quarter of 2010, the Sales and Marketing department underwent a reorganisation during which two additional lines of promotion were established.

In 2009 the structure of promotion included:

- the division of Rx products promotion with 4 specialised teams for promotion in the areas of (1) Cardiology, (2) Neurology, (3) Hepatology and Dermatology, (4) Hospitals
- he division of OTC products promotion with 2 specialised teams for promotion in the areas of (1) Pharmacies, (2) Pediatrics and Gynecology
- he division of endocrine products promotion.

In 2010, the structure of the divisions of Rx products promotion and of the Endocrine products promotion did not experience significant changes. However, the division of OTC products promotion was expanded up to four specialised lines: (1) Pharma-1 (pharmacies line 1) (2) Pharma-2 (pharmacies line 2) (3) pediatrics and general therapy line (4) gynecology line.

This change reflects the need to increase the level of promotional targeting for the preparations sold through pharmacies as their number in the portfolio of promoted products increased in 2010 both in terms of brands and in terms of new forms of production. It also reflects the business-driven requirement to extend the promotion reach to the general therapy and gynecololy groups.

Another important structural change in 2010 was the establishment of the division responsible for working with pharmacy chains and its expansion to the regions. Thus, in 2010, we have successfully set up a regional group of managers specialising in working with pharmacy chains whose main responsibilities include building up and supervising distribution, as well as launching BTL programmes in the regional pharmacy chains.

As at 31 December 2010, marketing and promotion staff headcount was 579 people, which represents an increase of +29% in relation to the same period of 2009.

The motivating payment system continues to function, successfully, in the Sales and Marketing department. It is based on a variable part of wages which is paid every quarter. The amount of a bonus depends on the fulfilment of quantitative goals (such as the resale plan for the period) and also of qualitative goals. In 2010, 71% of the staff were awarded.

All staff are trained to promote on a regular basis, which in our opinion is an important factor ensuring the fulfilment of business objectives and an additional motivating factor for the success of the Company. In 2010, the average figure for the number of training days per medical representative equalled 33.4 (the comparative figure for 2009 was 27), the average figure for a number of training days per line manager equalled 34.5 (the comparative figure for 2009 was 29). In addition to auditorium-based training, a system of distant learning was introduced in 2010, which resulted in an increase in efficacy of training in general and in the savings made by the promotional divisions (15% of the training budget for 2010) and did not affect the successful implementation of the training programme for 2010.

In the Sales and Marketing department the system of regular reporting continues to operate successfully : monitoring retail sales, stock distributors, monitoring of retail prices, sales reports, P&L analysis of each brand. These approaches allow the regular assessment of key performance indicators and facilitation of operational decisions for the future.

Implementation of the above strategy as a whole enabled us to meet our targets, including sales growth in respect to most promoted brands as compared to the previous period.

MANUFACTURING LICENSES / GMP STANDARDS

MANUFACTURING LICENSES

Pursuant to the law 'On the Circulation of Pharmaceuticals in the Russian Federation', the Government of the Russian Federation Decree 'On Amending Several Acts of the Government of the Russian Federation in Connection with the Adopted Federal Law «On the Circulation of Pharmaceuticals», the authority to license the production of pharmaceuticals and keeping the registry of the issued licenses has been transferred to the Ministry of Industry and Trade of the Russian Federation.

According to the new Provisions for Licensing the Production of Pharmaceuticals, in addition to the already existing requirements and conditions, to receive a license the producer should have, among its employees, an authorised person who confirms compliance of the pharmaceuticals to the requirements established during their registration and guarantees that the pharmaceutical preparations have been produced in accordance with the Rules of GMP. Apart from that, the licensee should be in conformity with the requirement regarding state registration of maximum selling prices for pharmaceuticals and regarding the rules of disposal of poor-quality, fake and counterfeit pharmaceuticals.

At the present moment, the enterprises of Pharmstandard have all the necessary licenses for production of various forms of sterile and non-sterile pharmaceutical preparations.

GMP STANDARDS

Pharmaceuticals producing subsidiaries of OJSC «Pharmstandard» work in accrodance with the standards containing strict requirements to quality provision in respect of the pharmaceuticals during their development, production and control.

During the registration process all pharmaceuticals produced by the holding's subsidiaries are tested by a competent authorized body to establish their compliance to the up-to-date requirements in relation to their safety, quality and efficacy. The manufacturing authorization process insures that all the products of OJSC «Pharmstandard» permitted for sale in the territory of Russia, come out of the holding's plants which hold a relevant license and are regularly inspected by competent authorized bodies. Production licenses are compulsory for all pharmaceutical producers in Russia.

All the pharmaceutical producing subsidiaries of OJSC «Pharmstandard» have implemented a fully functioning and continuously evolving quality control management. The current quality control management system has been developed and implemented in strict compliance to the requirements of the EU Directive 2003/94/EU, Russian manufacturing standards GOST R 52249-2009 (GMP) 'Rules for the Production and Quality Control of Pharmaceuticals' and GOST R ISO 9001-2008 (ISO 9001-2008) 'Quality Management System. Requirements'.

In 2010, three subsidiaries of the Company (OJSC "Pharmstandard-Leksredstva", Kursk; OJSC "Pharmstandard-Ufavita", Ufa; OJSC "Pharmstandard-Tomskhimpharm", Tomsk) received certificates confirming their compliance with the requirements of the national standards of the Russian Federation GOST R 52249-2009 (GMP) "Rules for the Production and Quality Control of Pharmaceuticals" and GOST R ISO 9001-2008 (ISO 9001-2008) "Quality Management System. Requirements".

In 2008, Tyumen Plant of Medical Equipment and Tools received certificates of compliance with the requirements of EN ISO 9001:2000 "Quality Management System. Requirements" and the requirements of EN ISO 13485:2003 "Medical devices – Quality management systems – Requirements for regulatory purposes" and of Annex V, Section 3 of the EU Council Directive 93/42/EEC (on medical devices, dated 14 June 1993) regarding the introduction and implementation of guarantees of quality in respect to sterile syringes and needles.

This aspiration to comply with the standards of GMP is the prerequisite for our extending co-operation with companies in the EU and worldwide. In 2009, six production lines (65% of the production facilities) of OJSC «Pharmstandard» received certificates of conformity with the standards of the EU Good Manufacturing Practice (EU

GMP). These EU GMP certificates are available to see in the EudraGMP database at the following link http://eudragmp.emea.europa.eu/

The main directions and objectives of the subsidiaries of OJSC «Pharmstandard» as regards the issues of quality, which have been officially adopted by the management, are reflected in the internal Quality Policy.

The system of quality management includes a set of measures which, applied systematically, ensures that the manufactured goods are compliant with the established normative requirements regarding their quality and possess the necessary consumer properties (quality, efficacy, safety). Quality of pharmaceuticals is defined as their conformity with all the registration requirements, production requirements (technology, production sites, personnel) and specification data. It is the main objective of the management of OJSC «Pharmstandard» to ensure that the manufactured pharmaceuticals comply with the quality requirements.

OJSC «Pharmstandard» has a system of document keeping which complies with the requirements of GMP, ISO. The documents of the quality management system contain principles and the mechanism of realisation of such principles in accordance with each chapter of Good Manufacturing Practice dedicated to a specific aspect of quality.

The objective of such a system is a timely provision to each subdivision of the enterprises of necessary up-to-date documentation which would enable them to organise the production processes in all their complexity and result in the production of high-quality, effective and safe pharmaceuticals.

All the measures concerning production, control and licensing are contained in such documentation.

All specialists working for the Company undertake compulsory GMP studies in leading Russian establishments which specialise in teaching pharmaceutical professionals the requirements of expedient production and control of pharmaceuticals on the basis of the best international practices. Pharmstandard's continuing success and its leading position in the Russian pharmaceutical market are secured by its highly skilled and competent personnel.

One of the elements of the quality management system is the quality service which has been set up at the enterprises of OJSC «Pharmstandard». Control over the quality of raw materials and supplies, intermediates and bulk products and finished products is carried out by highly skilled specialists of the quality service according to the authorised methods and using modern high-value testing equipment. Only those raw materials and supplies are admitted for the production process which have passed the acceptance test and received permission to be used in production. During the production process the following monitoring procedures are carried out: monitoring of the main parameters of manufacturing processes, monitoring of the environmental parameters (microbiological air control, control of equipment, clothes, personnel's hands etc.) and control of the quality of intermediates and bulk products. Finished products are only ready for sale when a representative of the quality control management confirms in writing that each batch of the finished product has been produced and undergone quality control in compliance with the requirements of the master file.

The quality service also undertakes investigation regarding product quality claims and complaints. Each claim and complaint is registered and investigated in accordance with the established procedures. On the basis of the investigation conclusions a plan of rectification and prevention measures is drawn up. The performance of such a plan is meticulously monitored, and the efficacy and performance of the undertaken rectifying and preventative measures is evaluated.

In order to comply with the GMP standards, construction and furnishing of new production lines, as well as modernisation of existing ones, at the enterprises of OJSC «Pharmstandard» are carried out using modern materials, innovative technologies and equipment of leading European companies are used: Bosch, Marchesini, Killian, Fetta, IMA, BMT, Glatt, Coster and Favea.

COMPANY'S DEVELOPMENT PLANS UNTIL 2014

THE FOLLOWING IS ENVISAGED TO BE REALISED AT OJSC «PHARMSTANDARD-LEKSREDSTVA» IN THE PERIOD UP TO 2014:

- To complete, until the end of 2011, the construction of the 11,500-pallet warehouse for finished products. It will have sufficient storage space to rule out any possible shortage of such space for storing finished products, raw materials and packaging materials.
- Construction of production facilities for filling sprays: introducing new pharmaceuticals to be produced and increase in the pharmaceuticals being produced.
- Construction of production facilities for asthma sprays which will lead to the increase in the output of sprays and aerosol sprays.
- Acquisition of a universal tablet and capsule packaging line. Acquisition of such a line will for packaging tablets and capsules will allow to increase the monthly output with respect to packaging to 5,000 packages per months.
- Creation of a research centre: a complex comprising laboratory (new technologies department) and production facilities which will ensure scalability during the period of organising of new pharmaceuticals production, development of the production process of technologically complex pharmaceuticals, production of small batches of expensive preparations.
- Reconstruction of the warehouse building to create space for storing raw materials and packaging materials to increase space allocated to storage of raw and other materials and rule out shortages of warehouse space and to provide required storage conditions.
- Reconstruction of production of tablets and coated tablets in production room No. 2 as well as of production of tablet dosage forms in production room No. 3 and section No. 4, of production of active pharmaceutical ingredients in order to replace equipment and increase volume of production.

THE FOLLOWING IS ENVISAGED TO BE REALISED AT OJSC «PHARMSTANDARD-UFAVITA» UNTIL 2014:

- Construction of a warehouse building with a 5862 m² storage space and 5346 pallet capacity for storing raw materials, packaging materials and finished products in GMP compliant conditions in order to rule out shortages of warehouse space and to provide required storage conditions.
- Construction of a section of injection preparations to increase the volume and range of produced injection pharmaceuticals by 120 million ampoules per year.
- Creation of a separate production facility for cytoreductive drugs in order to increase the range of produced pharmaceuticals. The investment will amount to 40 million Euros.
- Construction of a new, 10,000 m² building for the production of finished pharmaceutical preparations with new production sections for:
  - production of injection preparations (including lyophilized preparations) on six newly-purchased automatic lines for the production of preparations in ampoules and bottles and their packaging;
  - production of bioactive additives;
  - production of sugar-coated tablets;
  - packaging;
  - research laboratories of the Central Laboratory Department.
- Quality Control Department, Central Laboratory Department and the Validation Team of the Quality Control Department upgrade with devices and equipment for performing all the necessary measurements.

THE FOLLOWING IS ENVISAGED TO BE REALISED AT OJSC «PHARMSTANDARD-TOMSKHIMPHARM» IN THE PERIOD UP UNTIL 2014:

- Construction of a 3,000 m² laboratory building including the cleanrooms of the Quality Control Department and the Production Testing Section of the Central Laboratory Department as well as office, sanitary and welfare, laboratory and other rooms of the Quality Control Department and the Central Laboratory.
- Construction and setting into operation of a warehouse complex (1500 pallets, 2,000 m²) to rule out any shortage of warehouse space for storing raw materials, packaging materials and finished products in required conditions.
- Reconstruction of tablet preparations production floor in order to carry out its technical refurbishment and increase its production output.
- Fitting additional modern technological equipment in the reconstructed cleanrooms of the 3rd – 5th floors of section No. 1 of the tablet production facilities.
- Acquisition of additional modern of measurement and testing equipment for the Quality Control Department and the Central Laboratory.
- Reconstruction of the laundry section of the tablet production facilities; creation of cleanrooms.

All the new processes, equipment, rooms, methods and systems are validated. Validation is an element of the system of quality control management and is an integral part of the entire process of development of a pharmaceutical product and the technology of its manufacturing.

Validation is a set of measures which result in documented confirmation that a certain established manufacturing procedure, certain control measures relating to the object of validation lead to a guaranteed expected quality of pharmaceutical product.

A system of internal audits which has been developed and implemented at the enterprises of the Company, is successfully functioning. Such audits are carried out by a group of competent specialists working at the enterprises. The objective of the external audits of manufacturers of raw materials and supplies, of third-party contractors is verification of compliance of the manufacturing processes management with the requirements of GMP, ISO and with those of OJSC «Pharmstandard» as well as of compliance of product and services supply with a guaranteed, proper standard. The purpose of internal audits (self-audits) at the enterprises of OJSC «Pharmstandard» is to evaluate efficacy of the quality control management, to improve its performance and to determine further actions aimed at developing and improving it. External and internal audits are performed in accordance with annually drawn-up schedules and at regular intervals.

All the enterprises of OJSC «Pharmstandard» are subject to regular external audits both by the state bodies of the Russian Federation (Federal Service on Surveillance in Healthcare and Social Development of the Russian Federation) and by independent European and Russian auditors.

The laboratory of the Quality Control Department of OJSC «Pharmstandard-Ufavita». OJSC «Pharmstandard-Ufavita», has received its accreditation certificate of technical competence.

Due to the expiry of their state certificates the laboratories of the Quality Control Department of OJSC «Pharmstandard-Tomskhimpharm», Tomsk, and of OJSC «Pharmstandard-Leksredstva», Kursk, are planning to receive certificates of accreditation of technical competence in 2011 and 2012 respectively.

To confirm the validity of their certified status, in 2011 a scheduled re-audit of the quality control management will be carried out at the following subsidiaries of the Company: OJSC «Pharmstandard-Leksredstva», Kursk; OJSC «Pharmstandard-UfaVITA», Ufa; OJSC «Pharmstandard-Tomskhimpharm», Tomsk.

From January 2014 all Russian enterprises are to be compliant with the requirements of Good Manufacturing Practice in accordance with Federal Law No. 61-FZ 'On Circulation of Pharmaceuticals in the Russian Federation' which came into force on 1 September 2010. The Company's management are confident about the future and believe that, as a result of the work being done, the production facilities of the Company will be well prepared to pass the necessary audits in due time and in accordance with Good Manufacturing Practice.

PRODUCTION FACILITIES

The following table provides information about the Company`s pharmaceutical manufacturing facilities:

Factory	Approximate size (sq. m.)	Formulation	Shifts	Capacity 000's thousands packs 2009	Utilisation 2009	Capacity 000's thousands packs 2010	Utilisation 2010	Month of new capacity launch 2010
LEKSREDSTVA (KURSK)	14'900 (lease)	Syrops & liquid forms	3	71,898	81%	71,112	56%	
		Tablets	3	631,575	60%	602,059	59%	
		Sprays	3	13,893	99%	14,964	95%	Feb 2010
		Powders	3	9,775	12%	8,966	34%	
		Capsules	3	57,990	67%	82,877	77%	Jan 2010
UFAVITA (UFA)	5'850 (lease)	Ampules	3	13,646	56%	18,294	76%	
		Frozen-dried preparation	3	4,705	37%	4,945	63%	
		Syrops & liquid forms	3	9,053	28%	8,940	27%	
		Tablets	3	151,620	42%	149,093	54%	
		Vitamin bars (ferrohematogen)	3	35,640	64%	35,482	69%	
		Insulin	3	14,400	3%	14,400	5%	
PHYTOFARM (N. NOVGOROD)	1'200 (lease)	Ointments	3	744	26%	-		
		Powders	3	-	0%	-		
		Syrops & liquid forms	3	-	0%	-		
		Tablets	3	-	0%	-		
TOMSKHIM-PHARM (TOMSK)	29'000 (own)	Syrops & liquid forms	3	5,400	6%	5,400	9%	
		Tablets	3	327,368	44%	355,993	36%	Jun 2010
		Sprays	3	,600	12%	9,600	16%	
		Ointments	3	744	8%	2,178	18%	
Total:				**1,358,052**		**1,384,303**		

OJSC «PHARMSTANDARD-LEKSREDSTVA»

In 2010, the acquisition of new equipment allowed OJSC «Pharmstandard-Leksredstva» to increase its capacity for production of pharmaceuticals in capsules by 42% over 2009. Actual increase in output of preparations in capsules was 230 million capsules (Arbidol, Phosphogliv, Flucostat, Azitrox). Also, there was a 7% increase in the production output of aerosol sprays and sprays (Nitrospray, Termicon and Cinocap) in 2010 in relation to 2009 which was due to equipment modernisation in 2010.

Chief Executive Officer OJSC «Pharmstandard-Leksredstva» – **Prohoda Evgeniy.**

OJSC «PHARMSTANDARD-UFAVITA»

Following the launch of a new injection preparations line in August 2009, production capacity for preparations in ampoules at OJSC «Pharmstandard-Ufavita» in 2010 grew in comparison to 2009 by 34% which amounts to an increase of preparations in ampoules (Combilipen, Octolipen, Artrozan) by 69.2 million ampoules. In the fourth quarter of 2010, reconstruction of lipophilic preparations (Phosphogliv, Rastan) production facilities was carried out. This will lead to doubling the production of these pharmaceuticals in 2011.

Chief Executive Officer OJSC «Pharmstandard-Ufavita» – **Kreyman Vladimir.**

OJSC «PHARMSTANDARD-TOMSKHINPHARM»

As a result of the improvement of technological processes in 2010 OJSC «Pharmstandard-Tomskhinpharm» increased its capacity for production of oinment form preparations by 46% over 2009; and productions of such preparations as Termicon and Cinocap grew by 54%. Also, due to reconstruction of the facilities for production of tablets in August 2010, production capacity for tablet preparations increased in 2010 by 9% in relation to 2009.

Through modernisation and introduction of new equipment, in 2010 the output capacity of the pharamaceutical plants of the Pharmstandard group of companies grew by up to 1.38 billion packages which amounts to an increase of 26.2 million packages over 2009.

Chief Executive Officer OJSC «Pharmstandard-Tomskhinpharm» – **Skorokhod Andrei.**

The following is planned for 2011:

- At OJSC «Pharmstandard-Ufavita»: reconstruction of the facilities for production of lipophilic preparations in order to increase their capacity for the production of Phospholigliv and Rastan.
- OJSC «Pharmstandard-Tomskhinpharm»: an increase in the capacity for the production of new tablet form preparations.
- OJSC «Pharmstandard-Leksredstva»: an increase in the capacity for production of coated tablets.

MEDICAL EQUIPMENT AND DISPOSABLES. JSC TZMOI

JSC "Tyumen Plant of Medical Equipment and Tools" (TZMOI), a leader of domestic market of medical equipment and disposables.

Range of products includes models with sterilizing chamber volume from 10 to 2,250 dm^3. The following types of devices have been produced: simple models of sterilizers with semi-automatic microprocessor control, forvacuum, devices for documentation and recording of sterilization cycles and possibility of computerized diagnostics as well as all-purpose sterilizers (for sterilizing of medical devices, textile and medicinal solutions). In addition to sterilizers, the medical equipment includes also water distillers, water storage collectors, disinfection boilers and spare parts.

Chief Executive Officer JSC TZMOI – **Nizovcev Alexander.**

In 2010 the Company's revenue from the sales of medical equipment amounted to RUR 630 million. Despite a reduction in sales in 2010 compared to 2009 by 8.5%, it would be reasonable to say that this segment of the Company's business has stabilized, considering that in 2009 reduction in sales of medical equipment compared to 2008 was 36%.

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

	2010, mln RUR	2009, mln RUR	Difference,%
Medical Equipment	420.5	445	-5.5
Syringes & Disposables	185.3	207	-10.5
Spare Parts	24.4	24	1.6
Other	0.3	13	-97.7
	630.5	**689**	**-8.5**

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

	2010, mln RUR	2009, mln RUR	Difference, %
Retail Segment	521.7	591	-11.7
Export	84.4	71	18.9
Other	0	18	-100
Open auctions	24.4	9	171.1
	630.5	**689**	**-8.5**

PROCUREMENT

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

The following table shows procurement structure.

Nomenclature	2010,%	2009,%
Raw materials	88.5%	86.0%
API	80.7%	76.0%
Others	7.8%	10.0%
Auxiliary materials	0.2%	0.2%
Packaging	11.3%	13.8%
Total materials & supplies	**100.0%**	**100.0%**

The majority of the materials are supplied from a variety of external sources, primarily brokers. As of 31 December 2010, we had approx. 406 raw materials, and we obtained approximately 82% of our raw material requirements from our top-10 suppliers in 2010. We import the majority of our raw materials for our pharmaceutical products since certain types of raw materials are not produced in Russia, fail to meet quality standards or are produced in insufficient quantities. We import our raw materials from a number of countries, including China, Europe and India.

The following table shows breakdown of procurement contracts by currency.

Currency	2010,%	2009,%
Euro	15.7%	18%
US Dollar	66.4%	62%
Russian rouble	17.9%	20%
Total materials&supplies	**100%**	**100%**

In 2010, the share of the amount of procured API under USD denominated contracts was 66.4%, in comparison to 62% in the year before. This was due to the increase in the amount of procured API and the increase of prices by the suppliers: in 2010, the Company spent RUR 5.2 billion on the procurement of API vs RUR 3.4 billion in 2009. Another factor which had a notable effect on the procurement structure was the increase in the amount of API purchased for the production of Arbidol® and Afobazol®.

The share of the Euro denominated contracts reduced from 18% in 2009 to 15.7% in 2010, while in value terms the expenses grew from RUR 1,023 million in 2009 to RUR 1,229 million in 2010.

The volume and prices with respect to the procurement of API under RUR denominated contracts did not change considerably. The share of such contracts was 17.9%.

Throughout 2010, the currency rates were subject to conflicting trends. For example, while in the first quarter of 2010 USD experienced considerable loss in value, in the second quarter it reached its peak level of 31.77 RUR, and in the third and fourth quarters the tendency veered towards volatility of its rate. Pharmstandard did not incur any material loss due to changes in the currency rates.

Currently, all 2011 contracts for API are signed and prices are mostly fixed in USD.

SELLING API IN THE RUSSIAN MARKET

In February 2010, the management of Pharmstandard decided to create a new line of business specialising in wholesale of API supplied directly by foreign manufacturers, primarily from China, India and Western Europe.

The Company's analysts are of the opinion that the volume of demand for imported API by Russia-based manufacturers of antibiotics and finished pharmaceutical products, amounts to USD 150 million. Given the current business trends and the prospects of the Russian market, the Company decided to develop this line of business and increase its share on the API market.

The development strategy for 2011:

- to increase the volume of sales;
- to improve the quality of Customer service by means of optimisation of paperwork and shipment of goods from warehouses;
- to increase the number of customers;
- to expand the range of goods;
- to monitor and control accounts receivable.

TOP 10

List of API	Value, RUR (incl. VAT 10%)
Analgin (Metamizole sodium)	38 509 183
Ascorbic acid	26 531 137
Enalapril Maleate	20 305 893
Ruin/Vitamin P	18 842 406
Acetylsalicylic acid	14 672 689
Ampicillin sodium	13 410 278
Omeprazole (Pellets)	11 911 025
Lipoic acid	11 326 592
Azithromycin dihydrate	10 247 447
Pancreatin 6 NF	10 130 575
Others	105,791,677
Total	**271,548,326**

DISTRIBUTION

In general, the list of principal product distributors did not change in 2010 as compared to 2009.

In 2010, the share of sales under the Ministry of Health and Social Development's contracts accounted for 10% of the Company's total sales. Reduction of the share of sales in the overall structure of sales from 16% (2009) to 10% (2010) was due to Velcade being supplied, in 2010, through "Pharmastandard-Ufavita".During 2010, the Company supplied products under 40 main contracts. In 2010, 5 top distributors accounted for 71% of sales, except for the state supplies, while in 2009 they accounted for 69%.

Increase in the share of sales of the TOP-5 distributors was primarily due to the Company's credit policy aimed at mitigation of risks (including failure to collect receivables). Such a policy provides for establishment by the Credit Committee of credit limits for counter parties on the basis of the analysis of their financial position and solvency. Another factor which had an effect on this was the general market tendency towards reduction in the number of distributors and, as a consequence, the increase of the share of the largest national distributors.

Payment terms under the main distribution contracts remained similar to those of 2009 i. e., 90–120 days in Russia and 180 days for export.

The table below introduces the main distributors' share in sales. The data below do not include any state contracts.

Distibutor	2009, % of sales	2010, % of sales
Katren	17%	17%
Protek	16%	17%
SIA International	14%	13%
Альянс Хелскеа (Аптека-Холдинг)	10%	13%
Rosta	12%	11%
	69%	**71%**

The average stock is equal to 60 days product sales neglecting any out of stock situations.

EMPLOYEES

As of 31 December 2010, there were 5,584 full-time employees working for the group of companies Pharmstandard. 51% of them were trade unions members. During 2010, the employer did not experienced any business interruptions resulting from labour disputes. That is why we believe that our employees are satisfied with the working conditions.

The following table shows our headcount as of 31December 2009

	2009	2010	Difference %
Production/Logistics	3,689	3,750	1.7%
Research and Development	136	144	5.9%
Marketing and Promotion	760	987	29.9%
Management and Administrative	689	703	2.0%
	5,274	**5,584**	**5.9%**

The following table shows the headcount at each manufacturing facility as of 31 December 2009:

	Kursk	Ufa	Tomsk	Tyumen	Moscow	N. Novgorod	TOTAL
Production/ Logistics	1,340	1,311	497	602	0	0	3,750
Research and Development	25	34	15	14	56	0	144
Marketing and Promotion	0	0	0	0	987	0	987
Management and Administrative	99	155	114	72	263	0	703
TOTAL	**1,464**	**1,500**	**626**	**688**	**1,306**	**0**	**5,584**

The increase in the number of personnel working in Marketing and Promotion in 2010, was due to the continued realisation of our strategy of specialisation whose objective is an increase in the efficiency working with clients.

SOCIAL POLICY

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

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

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

RISK MANAGEMENT

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

category	category specification	definition	possible risks for Pharmstandard Group	regulation methods	risk probability for Pharmstandard Group
OPERATIONAL	**PERSONNEL RISK**	risk of improper discharge of duties/rules/procedures	■ risk of material errors andmalpractices	■ enhancement of internal control measures	medium
		risk of inefficient corporate structure	■ risk of inefficient delegation of authority; ■ creation of additional bureaucratic barriers, loss of operational efficiency of information flows established between distant enterprises	■ use of appropriate evaluation instruments for the existing business processes evaluation; ■ organization of training sessions for the Company personnel	low
		risk of key managers andspecialists loss	■ risk of key managers andspecialists loss	■ adequate compensation package	medium
		risk of qualified personnel shortage	■ risk of qualified personnel shortage	■ The Company's approach to building up its relationship with employees is based on Russian labour legislation and advanced human resource management methods and techniques. The standard of social provisions for employees meets the current requirements of the labour market. Regular training is organised by the Company for employees using its own and outside resources.	medium
	PROCESSES RISK	risk of incorrect organization of processes schedules and procedures	■ risk of incorrect organization of processes schedules and procedures	■ qualified personnel; ■ a system of internal standards and procedures compliance control	low
		lack (inadequacy) of the information security system and/or information access procedure	■ information security system inadequacy	■ creation of information access control; ■ implementation of regular measures for identification and elimination of risk factors	medium
	IT SYSTEMS RISK	technological risk of hardware or software failure	■ technological risk of hardware or software failure	■ creation of reserve database storage facilities/servers; ■ qualified technical staff formation	low
	EXTERNAL FACTOR RISKS	risk of unrecorded competitive expansion	■ risk of competition within the pharmaceutical industry	■ development of R&D capabilities; ■ analysis of the new pharmaceutical products market; ■ portfolio diversification; ■ expansion into new market segments through participation in government-sponsored schemes; ■ support of import substitution strategy	low
		risk of inefficient acquisition	■ risk of losses resulting from the integration of acquired assets combined with the risk of weakened financial performance	■ thorough preliminary analysis; ■ development of new methods	medium
		risk of participation in government-sponsored schemes	■ risk of overdue receivables (reserve) resulting from the sales of products under the FRP	■ collection of information; ■ control of compliance with contractual terms and conditions; ■ control of receivables structure and adequate diversification	medium
	RISK OF DIRECT FINANCIAL LOSSES	stock exchange risk	■ non-compliance with capital requirements or other legal (stock exchange) requirements	■ timely updating of information; ■ distribution of responsibility areas among the corporate internal services; ■ regular monitoring	medium
	LEGAL RISKS	state regulatory risk	■ risks due to changes in law and taxation	■ the Company focuses its attention to timely response to changes in law related to all areas in the industry; ■ the functional of each Company's division implies monitoring of the RF statutes; ■ in everyday affairs the Company applies up-to-date legal infoware; ■ responsible officers of the Company regularly circularize amendments to law.	medium

We**care**

for the high standard of disclosure

Management's Discussion and Analysis

of Financial Condition and Results of Operations development

OUR (COMPANY'S) FINANCIAL POSITION AND PERFORMANCE SHOULD BE FURTHER REVIEWED ALONG WITH THE CONSOLIDATED FINANCIAL STATEMENTS, COMMENTS THERETO AND OTHER INFORMATION DISCLOSED IN THIS ANNUAL REPORT.

PERFORMANCE

The table below presents an overview of the Company's performance, with the key figures as of 31 December 2010 and 2009, in absolute values and percentage sales.

In this table, third parties products (hereinafter TPP) in the revenue section are presented separately. The purpose of such analytics is a more detailed reflection of specific business features. Thus, for the purpose of comparative analysis, such classification was also applied to the results of 2009. It is worth noting that such a portfolio structuringprinciple has no effect whatsoever on the results of sales of pharmaceutical products.

	Year ended 31 December 2010		Year ended 31 December 2009	
	RUR in mln	%	RUR in mln	%
Revenue	**29 686.6**	**100.0**	**24 095.4**	**100.0**
Pharmaceutical products	29 056.1	97.9	23 406.7	97.1
OTC products	15 581.1	52.5	14 840.7	61.6
Branded	13 339.0	44.9	12 709.9	52.7
Non-branded	2 242.1	7.6	2 130.8	8.8
Prescription products	3 294.2	11.1	2 338.1	9.7
Branded	2 806.9	9.5	2 022.4	8.4
Non-branded	487.3	1.6	315.7	1.3
Third parties products	9 893.8	33.3	6 156.4	25.5
Other sales	287.0	1.0	71.5	0.3
Medical equipment	630.5	2.1	688.7	2.9
Cost of sales	-16 700.8	56.3	-12 367.9	51.3
Gross profit	**12 985.8**	**43.7**	**11 727.5**	**48.7**
Selling and distribution costs	-2 916.2	9.8	-2 463.1	10.2
General and administrative expenses	-892.0	3.0	-711.2	3.0
Other expenses	-300.8	1.0	105.3	0.4
Financial income	315.2	1.1	132.9	0.6
Financial expense	-47.7	0.2	-146.0	0.6
Profit before income tax	9 144.3	30.8	8 645.3	35.9
Income tax expense	-1 980.5	6.7	-1 792.8	7.4
Profit for the period	**7 163.8**	**24.1**	**6 852.4**	**28.4**
Attributable to equity holders of the parent	7 149.5		6 836.4	
Attributable to non-controlling interest	14.3		16.0	

SALES OF PRODUCTS

The Company's core business is manufacture and sales of pharmaceutical products and medical equipment and disposables. Sales of pharmaceutical products and medical equipment and disposables account for 97.9% and 2.1% of the total sales, respectively. Pharmaceutical products and medical equipment and disposables are mainly sold under direct delivery contracts with wholesale distributors and/or medical institutions. In 2010, total sales amounted to RUR 29,686.6 million, which is 23.2% above the corresponding 2009 figure (RUR 24,095.4 million).

In 2009, total sales of pharmaceutical products increased by 24.1%. Of this increase 46% was attributable to sales excluding third parties products.

A number of drugs representing third parties products contributed substantially to the increase in total sales of pharmaceutical products. For the purposes of this analysis, they have been presented as separate entries (TPP):

In 2010, sales of third parties products amounted to RUR 9,893.8 million or 34.1% of the Company's total sales. The positive dynamics of these figures reflects the increase in production output of these pharmaceuticals as well as in their range resulting from the state open auctions won by the Company. The biggest share of the proceeds from TPP sales in 2010, namely 90.3%, related to the sales of Velcade®, Coagil, Mildronate®, Prezista®, Pulmozim, IRS® 19 and Imudon®.

			2010			2009		
Brand	**Atc**	**Category**	**Sales, mln RUR**	**% in Group**	**% of Pharma sales**	**Sales, mln RUR**	**% in Group**	**% of Pharma sales**
Velcade®		RX	3 838.2	38.8	13.2	3 661.9	59.5	15.6
Coagil		RX	1 799.5	18.2	6.2	0.0	0.0	0.0
Mildronate®		RX	1 211.7	12.2	4.2	1 194.3	19.4	5.1
Prezista®		RX	942.5	9.5	3.2	0.0	0.0	0.0
Pulmozim		RX	610.2	6.2	2.1	143.9	2.3	0.6
IRS® 19, Imudon®		OTC	533.5	5.4	1.8	645.6	10.5	2.8
Other TPP			958.2	9.7	3.3	510.6	8.3	2.2
TOTAL			**9 893.8**	**100.0**	**34.1**	**6 156.4**	**100.0**	**26.3**

PHARMACEUTICAL PRODUCTS

Sales of OTC medications increased by RUR 740.4 million (5.0%) from RUR 14,840.7 million in 2009 to RUR 15,581.1 million in 2010.

The following drugs were the key contributors to the increase: Acipol®, Arbidol®, Afobazol®, Magnelis B6®, Complivit®. The sales of these preparations in monetary terms increased in 2010 by the following amounts: Arbidol® – RUR 86.8 million, Afobazol® – RUR 76.3 million, Magnelis B6® - RUR 66.0 million, Complivit® – RUR 40.0 million. In relative terms this increase amounted to 1.6%, 14.4 %, 276.6% and 3.4% respectively. The sales of Arbidol® exceeded the level of the previous year when the main driving factor of the growth was the AH1/N1 flue and cold pandemic in the fourth quarter of 2009. Acipol®, the brand purchased in the middle of 2010, is a new product in the Company's portfolio. Its sales, since August 2010, amounted to RUR 140.7 million.

The following preparations were driving the growth in sales of non-branded pharmaceuticals: Mukaltin grew by RUR 100.9 million (or 148.5%), Activated Charcoal – by RUR 67.7 million (37.7%) , Inhalipt – by RUR 29.0 million (14.6%).

Sales of prescription drugs (Rx) grew by RUR 956.1 million (40.9%) from RUR 2,338.1 million in 2009 to RUR 3,294.2 million in 2010. The following drugs were the key contributors to the increase in sales of Rx drugs in 2010: Rastan® grew by RUR 253.5 million, Biosulin® R grew by RUR 150.4 million, Cocarboxylase Hydrochloride grew by RUR 106.4 million, Phosphogliv® grew by RUR 103.2 million, Combilipen® grew by RUR 83.8 million and Octolipen grew by 64.2 RUR million. In relative terms these increases amounted to 136.4%, 71.4%, 97.6%, 17.3%, 42.9% and 224.1% respectively.

In 2010, the value of the pharmaceutical market of the Russian Federation showed an increase of 7.8% which was driven entirely by the growth of the market in volume terms and accompanied by a certain decrease in the cost of packaging. This was due the regulation of selling prices for VEP introduced by the state which led to the transformation of the mode of consumption from stagnation to active growth due to thevincreased accessibility of pharmaceuticals for the population. Apart from that, there was a certain reduction in prices of pharmaceuticals not included in the VEP list compared to 2009 when the sole factor of growth for the majority of companies was an increase in prices.

It is noteworthy that in 2009, the year of the overall increase in prices for pharmaceuticals, the Company adopted a price control policy, which resulted in the increase of its sales volume by 14.4%. When, in 2010 the Company conducted a revision of its selling prices for medical preparations and decided to increase them, it led, in view of the above tendency and due to the price factor, to the increase of the sales value by 16.4%, despite a certain decrease in the volume of sales (6.5%).

MEDICAL EQUIPMENT

In 2010, the volume of sales of medical equipment and disposables decreased by RUR 58.2 million, or by 8,5%, and amounted to RUR 630 million vs RUR 688.7 million in 2009. There was a tendency for slowing down of the rate of the volume decrease in this segment (-8.5% in 2010 vs -36.0 in 2009). This segment is primarily financed through the state open auctions, and 2010 was a year when the situation with such financing improved.

COST OF SALES

Cost of sales comprises API and other material costs («materials and components»), third parties products for resale costs, overhead production costs, direct labour costs and amortization and depreciation.

The share of cost of sales in the total sales increased, in 2010, to 56.3% vs 51.3% in 2009.

In 2010, cost of sales grew by RUR 4,332.9 million or 35.0%, in relation to 2009, and amounted, in 2010, to RUR 16,700.8 million vs RUR 12,367.9 million in 2009. This was due to the increase in cost as described below.

The main expenditure items in the structure of cost of sales were "API and other materials" and "third parties products for resale costs" amounting in total to 89.4% of the overall costs of sales. A considerable share of the increase in the cost of sales was due to the growth of expenditure on "third parties products for resale": from RUR 4,973.1 million to RUR 8,272.4 million, or 66.3%, which resulted from the increase in the volume of pharmaceutical products purchased for subsequent resale.

The costs for "API and other materials" also showed growth, from RUR 5,697.0 million in 2009 to RUR 6,653.3 million in 2010, or 16.8%, primarily due to the increase in the volume of sales, the changes in the structure of the sales portfolio, and, to some extent, to the increase in the cost of raw materials, mainly caused by inflation.

The table below demonstrates the 'organic' changes in sales and cost of sales, excluding third party products sales:

	Year ended 31 December 2010		Year ended 31 December 2009	
	RUR in mln	%	RUR in mln	%
Sale of goods	19 792.8	100.0	17 939.0	100.0
Cost of sales	-8 428.5	42.6	-7 394.8	41.2

In 2010, cost of sales of Pharmstandard's own, i.e. 'organic', products in relation to the respective sales was 42.6% which is 1.3% higher than the corresponding 2009 figure. This change in cost is mainly attributable to the changes in the structure of the sales portfolio.

Below is a separate table specifically presenting the changes in the third parties products sales and cost of third parties products sales.

	Year ended 31 December 2010		Year ended 31 December 2009	
	RUR in mln	%	RUR in mln	%
Third parties products	9 893.8	100.0	6 156.4	100.0
Cost of sales	-8 272.4	83.6	-4 973.1	80.8

The increase in the cost of sales of third parties products in relation to their sales was caused by the changes in the sales portfolio structure during this period which was due to the following factors:

- three new preparations were included in the TPP portfolio: Coagil, (CJSC "Lekko", CJSC "Generium"), Prezista®, Intelence® (Janssen-Cilag S.p.A.);
- the selling price of some preparations increased;
- retail prices for certain preparations decreased, owing to the regulation of maximum prices.

Overall, the share of cost of sales in relation to the products sales, in percentage terms, in 2010 increased to 56.3% over 51.3% in 2009.

GROSS PROFIT

Gross profit of the Company increased by RUR 1,258.3 million (or 10.7%): from RUR 11,727.5 million in 2009 to RUR 12,985.8 in 2010. In relation to sales, total gross profit decreased from 48.7% in 2009 to 43.7% in 2010. This decrease was primarily due to a higher share of third parties products in the sales structure in 2010 in relation to 2009, and to their lower margin as compared to the Company's own products.

A review of the Company's organic sales (i.e. excluding third parties products sales) shows that 2010 gross profit was RUR 11,364.4 million, which is higher than the previous year's figure, RUR 10,544.2 million, by RUR 820.2 million, or 7.8%. Gross profit from the Company's organic sales in relation to the volume of sales amounted to 57.4% in 2010 in comparison to 58.8% in 2009. The specific reason for such a decrease was the changes in the sales structure during the review period.

Gross profit from the sales of TPP products in 2010 amounted to RUR 1,621.4 million which represents and increase of RUR 438.2 million (or 37%) over RUR 1,183.3 million in 2009. In relation to sales revenue, this is a decrease from 19.2% to 16.4%. This level of average gross profit from the whole range of TPP sales, is attributable primarily to the changes in the structure of TPP products sales (including the sales of new preparations) during the period of review.

In 2010, gross profit of the Company's pharmaceutical products segment was RUR 12,812.3 million, or 44.1% of pharmaceutical sales. In the segment of medical equipment and disposables gross profit in 2010 amounted to RUR 173.7 million, or 27.5% of this segment's sales volume, vs RUR 194.2 million, or 28.2% of the sales volume in 2009.

OPERATING EXPENSES

Operating expenses increased by RUR 633.8 million (20.0%) from RUR 3,174.4 million in 2009 to RUR 3,808.2 million in 2009. In relation to sales, in 2010 operating expenses decreased from 13.2% in 2009 to 12.8% in 2010.

Selling and distribution costs (S&D) in 2010 increased by RUR 453.1 million (18.4%) and amounted to RUR 2,916.2 million vs RUR 2,463.1 million in 2009, which represents 9.8% and 10.2% of sales in the respective years. Organic S&D (excluding third parties products expenses) in relation to sales amounted to 13.6% in 2010 over 13.0% in 2009.

Marketing, advertising and promotion expenses accounted for 48.9% of the total S&D expenses, amounting to RUR 1,427.3 million, which represents a decrease in relation to sales volume – from 5.7% in 2009 to 4.8% in 2010. It is worth noting that the amount of those expenses remained approximately the as in the previous year.

Labour costs totalled RUR 826.2 million, or 28.3% of S&D, which is an increase of RUR 240.2 million (41.0%) from RUR 585.9 million in 2009. This was mainly due to an increase in head count of medical representatives by 31.0% and a scheduled increase in payroll rates and bonuses to sales forces and other personnel for meeting their KPI (sales targets).

Other S&D expenses grew by RUR 151.0 million (29.5%) in relation to the previous year and amounted to RUR 662.6 million (22.7% of S&D). Expenses increased due to the following main factors:

- the growth of the volume of sales: the increase of expenses for the transportation and insurance of finished products of TPP, the increase in expenses for renting storage facilities, the increase in expenses for products certification;
- the increase in head count of medical representatives: expenses relating to training, travel and entertainment expenses;
- expenses relating to the care and maintenance of fixed assets.

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses (G&A) in 2010 increased by RUR 180.7 million (25.4%), from RUR 711.2 million in 2009 to RUR 891.9 million in 2010 (i.e. 3% of the overall sales volume).

Labour costs represented the greatest share of general and administrative expenses (61.8% of G&A) and increased by RUR 115.1 million (26.4%) from RUR 436.1 million in 2009 to RUR 551.2 million in 2010. This was primarily due to the increase in payroll rates, in headcount of qualified staff and in bonuses to administrative personnel for meeting their KPI. Other G&A expenses in 2010 increased by RUR 65.7 million and totalled RUR 340.8 million (38.2% of G&A). The increase was attributable to (1) services, legal, audit and consulting expenses due to the Company`s growth and (2) repairs of administrative facilities due to the expansion of space rented.

OPERATING PROFIT

Operating profit (defined a gross profit less operating expenses) grew by RUR 624.6 million (7.3%) from RUR 8,553.1 million in 2009 to RUR 9,177.6 million in 2010.

In relation to sales, our operating profit accounted for 30.9% of sales in 2010 as compared to 35.5% in 2009. We attribute this decrease in profitability mainly to the increase of the share of third parties products with lower margin in the Company's portfolio partly resulting, from the necessity to maintain competitive price for such high-cost products offered on the state open auctions.

Organic operating profit (without the contribution of TPP) amounted, in 2010, to 40.9% of total sales of Company's own products, compared to 43.4% in 2009.

OTHER EXPENSES (INCOME)

The net amount of 'Other Expenses' in 2010 was RUR 300.8 million (1.0% of sales).

The above amount included other income of RUR 188.0 million. The following is included in other income:

- the income from agent's commission for sales of TPP under the consignment scheme amounting to RUR 82.8 million (Altevir® from Pharmapark; Diaskintest from CJSC "Lekko");
- gain from buying and selling shares in JSC "Grindeks AS", Riga, Latvia amounted to RUR 47.5 million;
- reversal of impairment reserve in relation to the receivables due from "Genesis", amounted to RUR 28.8 million (this reserve was recorded as of 31 December 2008);
- due to the positive shift in demand in the market for adsorbents, Neosmektin trade-mark impairment was reversed in the amount of RUR 29.3 million.

Total other expenses amounted to RUR 488.8 million. The following is included in other expenses:

- expenses related to the construction of various elements of infrastructure of the R&D complex "NauchTechStroy Plus" LLC ("NTS+) which totalled RUR 248.3 million.

- expenses connected to the decision of the management to close down the production line of disposable products at OJSC "TZMOI" due to decline in demand: impairment of the production equipment worth RUR 76.0 million; expenses (RUR 7.4 million) with respect to the creation of reserves for payments resulting from staff reduction.
- expenses for banking services in connection with the delivery of supplies under the state open auctions amounted to RUR 32.4 million.

FINANCIAL INCOME AND FINANCIAL EXPENSE

Our financial expense decreased by RUR 98.3 million from RUR 145.9 million in 2009 to RUR 47.7 million in 2010. This was primarily due to the decrease in the balance of the Citibank syndicated loan, as per agreement concluded in 2006, scheduled for full repayment in 2011. Financial income in 2010 grew by RUR 182.3 million due to the gain in fair value of interest rate swap and also to the interest income from cash deposits.

INCOME TAX EXPENSE

In 2010, the Company incurred RUR 1,980.5 million of income tax expense compared to RUR 1,792.8 million in 2009. This increase in tax expense was due to the growth of profit prior to the tax assessment date.

PROFIT FOR THE YEAR AND NON-CONTROLLING INTEREST

In 2010, the Company's profit grew by RUR 311.3 million (4.5%) and amounted to RUR 7,163.8 million in comparison to RUR 6,852.4 million in 2009. These figures represent 24.1% and 28.4% of sales for the respective years. It is worth noting in this respect that the Company's profit without the contribution of TPP accounted for 31.2% of organic sales in 2010 vs 33.8% in 2009.

Profit from organic sales in the pharmaceutical segment amounted to RUR 6,167.4 million representing 32.2% of such sales.

In 2010, profit attributable to the equity holders of the Parent Company was RUR 7,149.5 million. Profit for the year due to non-controlling interests amounted to RUR 14.2 million payable to the minority shareholders of OJSC Pharmstandard-Tomskhimpharm with 9% voting shares.

LIQUIDITY AND CAPITAL RESOURCES

OVERVIEW

Our liquidity requirements arise primarily from the need to increase the Company's working capital, finance its capital investment programmes and expand its product portfolio through selective acquisitions of subsidiaries and intangible assets.

During the periods covered by the Company's Consolidated Financial Statements, we financed our operations and investments through free cash flow. In future, we also intend to fund acquisitions, if any, through free cash flow and borrowings.

The following table summarises our cash flows in 2010 and 2009:

Cash Flow	Year ended 31 December 2010, RUR, mln	Year ended 31 December 2009, RUR, mln
Net cash flow from operating activities	6,511.9	6,071.2
Net cash used in investing activities	(4,776.7)	(1,561.1)
Net cash used in financing activities	(377.1)	(1,698.7)
Cash and cash equivalents at the end of the period, net of bank overdraft	4,156.3	2,798.1

NET CASH FROM OPERATING ACTIVITIES

Substantially, all our cash flows from operating activities for the periods covered by the Company's Consolidated Financial Statements were generated from sales of pharmaceutical products and medical devices.

Standard commercial contracts that we sign with distributors provide for a 90–120 day credit period from the date of shipment, and we offer individual credit conditions to each distributor. For product supplies under the state Open auctions as well as product supplies within the framework of joint commercial projects with other, third-party, producers the credit period is determined individually for each contract and usually does not exceed 90 days from the moment of the Company's discharge of obligations

under the contract. Net cash flow from operating activities for 2009 and 2010 amounted to RUR 6,071 million and RUR 6,512 million respectively. The increase in net cash from the Company's operating activities in 2009 mainly resulted from an increase in sales through government Open auctions of the main and new brands of pharmaceuticals produced by Pharmstandard, such as Rabidly®, Amixin®, Afobazol®, Complivit®, Phosphogliv®, Rastan®, Biosulin®, Combilipen®, and also from the increase in sales and distribution through the state open auctions of third-party products, such as Velcade®, Coagil, Prezista®, Pulmozim®. The Company`s still exercises tight control over its operating expenses which include general and administrative expenses. The increase in operating costs in 2010 generally was in line with the Company's sales figures.

The reduction in cash outflow with respect to receivables in 2010 in comparison to 2009, was primarily connected to the payment, in 2010, of receivables recorded as of 31 December 2009, due to the flu and cold epidemic in the fourth quarter of 2009.

The increase in cash inflow with respect to payables in 2010 in comparison to 2009, was primarily connected to (i) the receipt of pre-payments related to the state open auctions which will be fully fulfilled by the Company in 2011 (ii) the increase in the Company's payables with respect to the supply of goods from third party manufacturers and to the contracts with raw material suppliers. This is connected to the general growth in the volume of its own production and the procurement of third-party products in accordance with the sales plan, including with respect to the state open auctions in 2011.

The increase in cash outflow with respect to the Company's resources in 2010 in comparison to 2009 is connected to the purchase of third-party products and to production output as well as to the sales plan for the first and second quarters of 2011, including the performance of obligations regarding product supply under the state open auctions.

NET CASH USED IN INVESTING ACTIVITIES

In 2009 and 2010 net cash used in investing activities amounted to RUR 1,561 million and RUR 4,777 million respectively. Within the above periods, the most significant investment activities included property acquisition, construction and modernisation of manufacturing facilities, construction of a R&D centre on the basis of a joint venture Nauchtechstroiplus Ltd, acquisition of equipment and intangible assets, prepayment for a new subsidiary in Ukraine as well as operations with short-term assets. In 2009 and 2010, we paid RUR 361,3 million and RUR 1,052, respectively, for acquisition of property and construction of manufacturing facilities and equipment. These acquisitions were primarily made for the development of the Company's production capacities, including the construction of new storage facilities, construction of a section for packaging and storage of thermolabile preparations and the increase in production capacities for Rastan® and Phosphogliv® in Ufa; acquisition of new equipment for the production of new tablet pharmaceuticals in Tomsk; construction of new storage facilities, acquisition of production sites for launching new preparations and substitution of exhausted equipment in Kursk.

In 2010, the Company paid RUR 806 million for the acquisition of the Acipol® trademark. In 2010, the Company made a partial prepayment which amounted to RUR 184 million for the purchase of the controlling interest in its subsidiary "Biolek" situated in Ukraine. In accordance with the terms of the contract, the outstanding amount was paid in 2011, upon closing the deal. In 2010, net cash used for purchase of financial assets, primarily promissory notes and short-term bank deposits, amounted to RUR 3,312 million (as compared to RUR 1,074 million in 2009). In 2010, the net cash inflow from operations with these financial instruments amounted to RUR 772 million (as compared to RUR 106 million in 2009).

NET CASH USED IN FINANCING ACTIVITIES

In 2009 and 2010, the net cash used in financing activities amounted to RUR 1,699 million and RUR 377 million, respectively.

These amounts were related to the repayment of a Citibank syndicated loan denominated in US dollars received in 2006. The decrease of the amount of net cash in 2010, in relation to 2009, resulted from the full repayment, in 2009, of one of the two tranches due for repayment, as per the terms of the credit agreement.

CONTRACTUAL OBLIGATIONS AND OTHER COMMITMENTS

As of 31 December 2010, the most significant contractual obligations of the Company were as follows: (i) an obligation amounting to RUR 1,377 million which arises from the advance payment from the Ministry of Health and Social Development of the Russian Federation in relation to the state open auctions with all the supplies under the open auctions having been fulfilled by the Company in

2011 (ii) obligations to third parties in relation to procurement of third party manufacturers, such as Velcade®, MabThera®, Pulmozyme, Mildronate®, Coagil amounting to RUR 6,717 million.

As of 31 December 2010, we had no other significant contractual obligations, except for certain liabilities incurred in the ordinary course of business, such as trade payables, wages and tax payables.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

OPERATING ENVIRONMENT

Russian economic reforms and the development of the legal, tax and regulatory framework in compliance with the market economy are in process. Future stability of the Russian economy to a large extent depends on these reforms and changes, as well as on the efficacy of economic, financial and monetary measures being undertaken by the government.

The Russian economy is vulnerable to global market downturns and economic slowdowns. In Russia, the global financial crisis has resulted in the reduction of gross domestic product, capital markets instability, significant deterioration of liquidity in the banking sector, and tighter credit conditions. While the Russian government has developed and introduced a range of stabilization measures to provide liquidity to Russian banks and companies, there is still no certainty regarding access to capital and the cost of capital for the Company and its counterparties, which can affect the financial position, performance and business prospects of the Group.

In 2009 and 2010, the Russian government has undertaken a range of measures to improve the situation of the pharmaceutical market. Among these measures are: the enacted Law on Circulation of Medicinal Products, introduction of mandatory registration of prices for Vital and Essential Medicinal Pharmaceuticals, tightening of control over manufacturers' and importers' pricing policy and distributors' and retailers' mark-up policy with respect to medicinal products. At present, a draft of the new law "On Protection of Health of Citizens of the Russian Federation" is under consideration. However, currently we do not expect these measures to greatly influence the sales structure and profitability of the Company, since the Company responds in a timely way to such changes and undertakes adequate measures.

CREDIT RISK

Our principal credit risk arises from the customers' possible failure to fulfill their payment obligations under sales contracts. In compliance with the Company's general principles for doing business, substantially all of our sales are made on credit terms. The credit terms depend on our credit and marketing practices with respect to a particular customer. We manage credit risk by relying on a policy which ensures that products are only sold to customers with an appropriate credit history. Moreover, we carry out daily monitoring of sales and receivables by means of effective internal control procedures. Our Credit Committee including CEO, CFO and CCO approves the Company's Credit Policy, which is revised in response to particular circumstances. According to the Company's Credit Policy, customers are generally divided into three categories: (i) the most reliable and reputable customers with maximum credit limit; (ii) customers with individual credit limit to be approved by the credit committee and (iii) customers with no credit limit, who have to make prepayments. The majority of our sales contracts are concluded with the customers who fall under the first category (in 2010, approximately 60% of the sales were made to our five major distributors). The carrying amount of the accounts receivable, net of provisions, represents the maximum amount of exposure to credit risk, at the end of each quarter. We believe that, other than the concentration with the five major customers, we have no significant concentrations of credit risk. Although collection of receivables can be influenced by various economic factors, the management believes that there is no significant risk of loss beyond the provisions stipulated by respective contracts.

CURRENCY RISK

A certain amount of our purchases is denominated in currencies other than the Russian rouble (the functional and reporting currency used in our Consolidated Financial Statements). We incur currency risk whenever we enter into transactions denominated in a currency other than our functional currency. Generally, our foreign currency transactions, which account for a substantial proportion of the Company's purchases of raw materials, as well as to borrowings and related interest payments thereon, are settled in US dollars and Euro. Therefore, our cost of sales, operating expenses presented in our Consolidated Financial Statements as well

as payables and borrowings reflected on the balance sheet of the Company, can be influenced by the foreign exchange rate fluctuations. We reduce the foreign exchange risk by monitoring changes in exchange rates in the currencies in which our cash, payables and borrowings are denominated. In particular, for the reduction of this risk we use up-to-date prediction methods and an individual approach to each deal in our contractual activity. Our well-designed budgeting system enables one to make timely management decisions related to all subsidiaries of the Company. At the beginning of 2009, the Russian rouble was devalued against certain currencies (primarily the US dollar and Euro). However, by the end of 2009, the Russian rouble had strengthened against those currencies essentially due to the positive changes in the Russian economy. After that, during the course of 2010, the Russian rouble-US dollar and Russian rouble-Euro exchange rates did not change significantly. We hope that during 2011 also, the rate of the Russian rouble will not change significantly in relation to the US dollar and Euro as compared with the rates as of the date of the Company's Consolidated Financial Statements issuance.

INTEREST RATE RISK

We are exposed to interest rate risk due to interest rate market fluctuations, since the majority of interest rates on our long-term borrowings are based on LIBOR. In September 2007, when LIBOR rate was approximately 5.7%, we entered into an Interest Rate Swap Agreement covering all interest payments on the Citibank loan, basically swapping the LIBOR rate interest obligations for a fixed rate of 4.932% per annum. In this manner, the Company protects itself against LIBOR rate fluctuations.

LIQUIDITY RISK

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

CAPITAL RISK MANAGEMENT

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

COMMODITY PRICE RISK

We do not think that the Company is subject to any significant material risk resulting from fluctuations in the prices of raw materials and supplies used in our production processes because, on the whole, our business does not significantly depend on any specific commodity and because there is no significant correlation between the rise and fall of the prices of different raw materials and supplies, as well as commodities for resale procured by the Company.

Pharmstandard

We care

for the health of a...


...future

Consolidated Financial Statements

for the year ended 31 December 2010

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Independent auditors' report

TO THE SHAREHOLDERS AND MANAGEMENT OF OJSC "PHARMSTANDARD"

We have audited the accompanying consolidated financial statements of OJSC "Pharmstandard" and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2010, and the consolidated statement of comprehensive income, consolidated cash flow statement and consolidated statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory information.

MANAGEMENT'S RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

AUDITORS' RESPONSIBILITY

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

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

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

OPINION

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2010, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young LLC

25 April 2011

Consolidated statement of financial position as at 31 December 2010

(in thousands of Russian Roubles)

	Notes	2010	2009
ASSETS			
Non-current assets			
Property, plant and equipment	11	4,168,079	3,685,845
Intangible assets	12	6,686,210	6,162,135
Prepayment for subsidiary acquisition	31	184,072	–
		11,038,361	**9,847,980**
CURRENT ASSETS			
Inventories	13	7,466,214	2,758,691
Trade and other receivables	14	12,376,059	9,289,082
VAT recoverable		480,142	258,932
Prepayments	15	219,621	136,729
Short-term financial assets	17	3,682,023	1,133,287
Cash and short term deposits	16	4,156,258	2,798,160
		28,380,317	**16,374,881**
Total assets		**39,418,678**	**26,222,861**
EQUITY AND LIABILITIES			
Equity attributable to equity holders of the parent			
Share capital	21	37,793	37,793
Treasury shares		–	(6)
Foreign currency translation reserve		(245)	–
Retained earnings		26,409,993	19,243,766
		26,447,541	**19,281,553**
Non-controlling interest		428,214	413,961
Total equity		**26,875,755**	**19,695,514**

	Notes	2010	2009
Non-current liabilities			
Long-term borrowings and loans	18	–	391,511
Deferred tax liability	28	642,334	807,062
Derivative financial instruments	18,30	11,249	34,751
Other non-current liabilities		–	24,197
		653,583	**1,257,521**
Current liabilities			
Trade and other payables and accruals and advances received	9,20	10,747,197	3,905,979
Current portion of long-term borrowings	18	395,823	391,360
Income tax payable		223,006	403,961
Other taxes payable	19	523,314	568,526
		11,889,340	**5,269,826**
Total liabilities		**12,542,923**	**6,527,347**
Total equity and liabilities		**39,418,678**	**26,222,861**

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

General Director **I. K. Krylov**

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

25 April 2011

The accompanying notes on pages 73–106 are an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income for the year ended 31 December 2010

(in thousands of Russian Roubles)

	Notes	2010	2009
Revenue	22	29,686,636	24,095,393
Cost of sales	23	(16,700,838)	(12,367,935)
Gross profit		**12,985,798**	**11,727,458**
Selling and distribution costs	24	(2,916,202)	(2,463,128)
General and administrative expenses	25	(891,954)	(711,245)
Other income	26	188,025	505,860
Other expenses	26	(488,852)	(400,603)
Financial income	27	315,167	132,878
Financial expense	27	(47,680)	(145,969)
Profit before income tax		**9,144,302**	**8,645,251**
Income tax expense	28	(1,980,506)	(1,792,810)
Profit for the year		**7,163,796**	**6,852,441**
OTHER COMPREHENSIVE INCOME			
Exchange differences on translation of foreign operations		(245)	–
Other comprehensive income for the year, net of tax		**(245)**	–
Total comprehensive income for the year, net of tax		**7,163,551**	**6,852,441**
PROFIT FOR THE YEAR			
Attributable to:			
Equity holders of the Parent		7,149,543	6,836,430
Non-controlling interest		14,253	16,011
		7,163,796	**6,852,441**

	Notes	2010	2009
TOTAL COMPREHENSIVE INCOME FOR THE YEAR, NET OF TAX			
Attributable to:			
Equity holders of the Parent		7,149,298	6,836,430
Non-controlling interest		14,253	16,011
		7,163,551	**6,852,441**
EARNINGS PER SHARE (IN RUSSIAN ROUBLES)			
- basic and diluted, for profit of the period attributable to equity holders of the parent	21	189.18	180.89

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General Director **I. K. Krylov**

Chief Financial Officer **E. V. Arkhangelskaya**
25 April 2011

The accompanying notes on pages 73–106 are an integral part of these consolidated financial statements.

Consolidated cash flow statement for the year ended 31 December 2010

(in thousands of Russian Roubles)

	Notes	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:			
Profit before income tax		9,144,302	8,645,251
Adjustments for:			
Depreciation and amortisation	11,12	792,016	752,058
Change in allowance for impairment of financial assets	14,26	(42,815)	(472,301)
Write-down of inventories to net realizable value	13	43,068	6,447
Gain recognised on sale of non-current assets classified as held for sale		–	(13,627)
(Reversal of impairment) impairment charge – intangible assets	12, 26	(29,258)	62,696
Impairment charge (reversal of impairment) – property, plant and equipment	11, 26	76,002	(13,374)
Loss from disposal of property, plant and equipment	26	5,311	7,578
Foreign exchange loss		4,412	138,589
Gain from disposal of financial assets	6,26	(47,487)	–
Expense related to the joint venture	26	248,298	–
Financial income	27	(315,167)	(132,878)
Financial expense	27	47,680	170,563
Operating cash flows before working capital changes		**9,926,362**	**9,151,002**
Increase in trade receivables	14	(2,956,557)	(4,062,775)
Increase in inventories	13	(4,750,590)	(280,229)
(Increase) decrease in VAT recoverable		(221,210)	67,276
Increase in trade prepayments	15	(82,892)	(63,185)
Increase in trade payables, advances received, other payables and accruals	20	6,815,907	2,586,467
(Decrease) increase in taxes payable other than income tax		(45,212)	229,219
Cash generated from operations		**8,685,808**	**7,627,775**
Income tax paid	28	(2,326,126)	(1,465,261)
Interest paid		(45,063)	(146,256)
Interest received		197,294	54,959
Net cash from operating activities		**6,511,913**	**6,071,217**

	Notes	2010	2009
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchase of property, plant and equipment	11	(1,051,934)	(361,270)
Purchase of intangible assets	7,12	(806,032)	(167,801)
Cash paid as prepayment for subsidiary acquisition	31	(184,072)	–
Cash paid for acquisition of non-controlling interests		–	(25,103)
Cash received from sale property, plant and equipment		5,783	10,487
Cash received from sale of short-term financial assets	17	772,048	106,105
Cash paid for short-term financial assets	17	(3,311,700)	(1,073,562)
Cash paid for other financial assets	6	(481,065)	–
Cash received from sale of other financial assets	6	528,552	–
Cash paid for acquisition of assets transferred to the joint venture	26	(248,298)	
Loans provided	17	–	(50,000)
Loans provided to related parties	10	(1,400,000)	–
Loans repaid by related parties	10	1,400,000	–
Net cash used in investing activities		**(4,776,718)**	**(1,561,144)**
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from loans and borrowings	18	1,300	–
Cash paid for treasury shares	5	–	(5,916)
Cash received from sale of treasury shares	5	16,690	–
Repayment of loans and borrowings	18	(395,087)	(1,692,821)
Net cash used in financing activities		**(377,097)**	**(1,698,737)**
Net increase in cash and cash equivalents, net of bank overdraft		**1,358,098**	**2,811,336**
Cash and cash equivalents at the beginning of the year, net of bank overdraft	**16**	**2,798,160**	**(13,176)**
Cash and cash equivalents at the end of the year, net of bank overdraft	**16**	**4,156,258**	**2,798,160**

The accompanying notes on pages 73–106 are an integral part of these consolidated financial statements.

Consolidated statement of changes in equity for the year ended 31 December 2010

(in thousands of Russian Roubles)

	Equity attributable to equity holders of the parent						
	Share capital	Treasury shares	Foreign currency translation reserve	Retained earnings	Total	Non-controling interest	Total equity
Balance at 31 December 2008	**37,793**	–	–	**12,413,396**	**12,451,189**	**163,203**	**12,614,392**
Profit for the year	–	–	–	6,836,430	6,836,430	16,011	6,852,441
Total comprehensive income for the year	–	–	–	**6,836,430**	**6,836,430**	**16,011**	**6,852,441**
Acquisition of treasury shares (Note 5)	–	(6)	–	(5,910)	(5,916)	–	(5,916)
Effect of sale of non-controlling interest in subsidiary	–	–	–	(150)	(150)	234,730	234,580
Recognition of non-controlling interest in MDR Pharmaceuticals	–	–	–	–	–	17	17
Balance at 31 December 2009	**37,793**	**(6)**	–	**19,243,766**	**19,281,553**	**413,961**	**19,695,514**
Profit for the year	–	–	–	7,149,543	7,149,543	14,253	7,163,796
Other comprehensive income for the year	–	–	(245)	–	(245)	–	(245)
Total comprehensive income for the year	–	–	**(245)**	**7,149,543**	**7,149,298**	**14,253**	**7,163,551**
Sales of treasury shares (Note 5)	–	6	–	16,684	16,690	–	16,690
Balance at 31 December 2010	**37,793**	–	**(245)**	**26,409,993**	**26,447,541**	**428,214**	**26,875,755**

The accompanying notes on pages 73–106 are an integral part of these consolidated financial statements.

Notes to the consolidated financial statements for the year ended 31 December 2010

1. CORPORATE INFORMATION

OJSC "Pharmstandard" ("the Company") and its subsidiaries ("the Group") principal activities are production and wholesale distribution of pharmaceutical and medical products. The Company is incorporated in the Russian Federation. Since May 2007, the Company's shares are publicly traded (Note 21). The Group's corporate office is in Dolgoprudny, Likhachevsky proezd, 5B, Moscow region, Russian Federation and its manufacturing facilities are located in Kursk, Tomsk, Ufa, Nizhny Novgorod and Tyumen. The Company controlled the following subsidiaries consolidated within the Group as at 31 December 2010 and 2009:

Entity	Country of incorporation	Activity	2010 % share	2009 % share
1. "Pharmstandard" LLC	Russian Federation	Central procurement	100	100
2. "Pharmstandard-Leksredstva" OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
3. "Pharmstandard-Tomskhimpharm" OJSC	Russian Federation	Manufacturing of pharmaceutical products	91	91
4. "Pharmstandard-Ufavita" OJSC	Russian Federation	Manufacturing of pharmaceutical products	100	100
5. "Pharmstandard-Phitofarm-NN" LLC	Russian Federation	Manufacturing of pharmaceutical products	99	99
6. "TZMOI" OJSC	Russian Federation	Manufacturing of medical equipment	100	100
7. Donelle Company Limited	Cyprus	Finance and holding Company*	89	89
8. Aphopharm CJSC	Russian Federation	Assets holder	89	89
9. MDR Pharmaceuticals	Cyprus	Assets holder	50.05	50.05
10. Vindexpharm CJSC	Russian Federation	Assets holder	100	–

In addition, the Group holds 50% of share capital in new joint venture "Nauchtechstroy Plus" LLC ("NTS+"). This research company was formed in February 2010 and it is in start up phase now (for more details see Note 8).

These consolidated financial statements were authorised for issue by the Board of Directors of OJSC "Pharmstandard" on 25 April 2011.

* Finance and holding company and assets holders generally do not conduct any business activities.

2. BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS

STATEMENT OF COMPLIANCE

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

BASIS OF ACCOUNTING

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

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

CHANGES IN ACCOUNTING POLICIES

The accounting policies adopted are consistent with those of the previous financial period except that the Group has adopted the following new and amended IFRS and IFRIC interpretations as of 1 January 2010.

- IFRS 3 (revised) *Business Combinations;*
- IAS 27 (revised) *Consolidated and Separate Financial Statements;*
- IFRIC 17 *Distributions of Non-cash Assets to Owners;*
- IAS 39 *Financial Instruments: Recognition and Measurement* - Eligible Hedged Items;
- Amendments to IFRS 2 Share-based Payments – Group Cash-settled Share-based Payment Transactions;
- "Improvements to IFRSs-2009" — a second collection of amendments to IFRSs that will not be included as part of another major project. The following table shows the list of IFRSs where amendments have been made that can result in accounting changes for presentation, recognition or measurement purposes and the topics addressed by these amendments:

IFRS (amended in 2009)	Subject of amendment
IFRS 2 *Share-based Payment*	Scope of IFRS 2 and revised IFRS 3 Business Combinations
IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*	Disclosures of non–current assets (or disposal groups) classified as held for sale or discontinued operations
IFRS 8 *Operating Segments*	Disclosure of information about segment assets
IAS 1 *Presentation of Financial Statements*	Current/noncurrent classification of convertible instruments
IAS 7 *Statement of Cash Flows*	Classification of expenditures on unrecognised assets
IAS 17 *Leases*	Classification of leases of land and buildings
IAS 18 *Revenue*	Determining whether an entity is acting as a principal or as an agent
IAS 36 *Impairments of Assets*	Unit of accounting for goodwill impairment test
IAS 38 *Intangible Assets*	Additional consequential amendments arising from revised IFRS 3 Measuring the fair value of an intangible asset acquired in a business combination
IAS 39 *Financial Instruments: Recognition and Measurement*	Treating loan prepayment penalties as closely related embedded derivatives Scope exemption for business combination contracts Cash flow hedge accounting
IFRIC 9 *Reassessment of Embedded Derivatives*	Scope of IFRIC 9 and revised IFRS 3
IFRIC 16 *Hedges of a Net Investment in a Foreign Operation*	Amendment to the restriction on the entity that can hold hedging instruments

The revised IFRS 3 *Business Combinations* ("IFRS 3R") is effective for periods beginning on or after 1 July 2009. IFRS 3R introduces changes in the accounting for business combinations that will impact the amount of goodwill recognised, the reported results in the period when an acquisition occurs and future reported results. A change to the scope of IFRS 3R increases the number of transactions to which it must be applied, by including combinations of mutual entities and combinations without consideration (e.g., dual listed shares). This revised standard has been adopted by the Group together with the revised IAS 27 *Consolidated and Separate Financial Statements*, including consequential amendments to IFRS 2, IFRS 7 and IAS 39.

IAS 27 (revised) *Consolidated and Separate Financial Statements* ("IAS 27R") is effective for periods beginning on or after 1 July 2009. This standard requires that a change in the ownership interest of a subsidiary (without loss of control) is accounted for as an equity transaction. Therefore, such transactions will no longer give rise to goodwill, nor will it give rise to a gain or loss. Furthermore, the amended standard changes the accounting for losses incurred by the subsidiary as well as the loss of control over a subsidiary. The amended standard has been adopted by the Group together with IFRS 3R, including consequential amendments to IFRS 5, IAS 7, IAS 21, IAS 28, IAS 31 and IAS 39.

IFRIC 17 *Distributions of Non-cash Assets to Owners* provides guidance on accounting for arrangements whereby an entity distributes non-cash assets to shareholders either as a distribution of reserves or as dividends. This interpretation is effective for annual periods beginning on or after 1 July 2009

The amendment to IAS 39 *Financial Instruments: Recognition and Measurement* – Eligible Hedged Items is effective for financial years beginning on or after 1 July 2009. This amendment addresses the designation of a one-sided risk in a hedged item, and the designation of inflation as a hedged risk or portion in particular situations.

Amendment to IFRS 2 *Share-based Payments* has been amended to clarify the accounting for group cash-settled share-based payment transactions, where a subsidiary receives goods or services from employees or suppliers but the parent or another entity in the group pays for those goods or services. . This amendment is effective for annual periods beginning on or after 1 January 2010 and supersedes IFRIC 8 and IFRIC 11.

There were no significant effects of above changes on accounting policies on the consolidated financial statements. However, the adoption of IFRS 3R and IAS 27R will affect the recognition of assets and liabilities and disclosures relating to future acquisition of businesses.

IFRSS AND IFRIC INTERPRETATIONS NOT YET EFFECTIVE

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

- IFRS 9 Financial Instruments, effective from 1 January 2013;
- Amendment to IFRS 1 *First-time Adoption of International Financial Reporting Standards* – Limited Exemption from Comparative IFRS 7 *Disclosures for First-time Adopters,* effective from 1 July 2010;
- Amendment to IAS 24 *Related Party Disclosures,* effective from 1 January 2011;
- Amendment to IAS 32 *Financial Instruments: Presentation* – Classification of rights issues denominated in a foreign currency, effective for annual periods beginning on or after 1 February 2010;
- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments,* effective for annual periods beginning on or after 1 July 2010;
- Amendment to IFRIC 14 IAS 19 – *The Limit on a Defined Benefit Asset, Minimum Funding Requirements and Their Interaction* – Prepayment of a minimum funding requirement, effective from 1 January 2011;
- Amendments to IFRS 7 *Financial instruments: Disclosures* – Transfers of financial assets;
- Amendments to IAS 12 *Income Taxes – s*et out in Deferred Tax: Recovery of Underlying Assets;
- Narrow amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards* – "The date of transition to IFRSs" and "Resume presenting financial statements" effective from 1 July 2011;
- "Improvements to IFRSs-2010", effective for annual periods beginning on or after 1 July 2010 or effective for annual periods beginning on or after 1 January 2011 — a new collection of amendments to IFRSs that will not be included as part of another major project. The following table shows the list of IFRSs where amendments have been made that can result in accounting changes for presentation, recognition or measurement purposes and the topics addressed by these amendments:

IFRS (amended in 2010)	Subject of amendment
IFRS 3R *Business Combinations,* effective from 1 July 2010	Transition requirements for contingent consideration from a business combination that occurred before the effective date of the revised IFRS
	Limiting the accounting policy choice to measure non–controlling interests upon initial recognition
	Un–replaced and voluntarily replaced share–based payment awards
IAS 27R *Consolidated and Separate Financial Statements,* effective from 1 July 2010	Clarifying that the amendments to IAS 21, IAS 28 and IAS 31 resulting from IAS 27R should be applied prospectively
IFRS 1 *First-time Adoption of IFRSs*	Accounting policy changes (IAS 8) in the year of adoption is not applicable
	Introducing guidance for entities that publish interim financial in the year of adoption
	Revaluation basis as deemed cost
	Use of deemed cost for operations subject to rate regulation
IFRS 7 *Financial Instruments: Disclosures*	Amending and removing existing disclosure requirements
IAS 1 *Presentation of Financial Statements*	Clarification of statement of changes in equity
IAS 34 *Interim Financial Reporting*	Events and transactions that require disclosure under IAS 34
IFRIC 13 *Customer Loyalty Programmes*	Clarification of fair value of award credits

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

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

3.1 PRINCIPLES OF CONSOLIDATION

Subsidiaries

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

Non-controlling interest is the equity in a subsidiary not attributable, directly or indirectly, to the Group. Non-controlling interest at the reporting date represents the minority shareholders' portion of the fair value of the identifiable assets and liabilities of the subsidiary at the acquisition date and the minorities' portion of movements in equity since the date of the combination. Losses within a subsidiary are attributed to the non-controlling interest even if that results in a deficit balance.

Non-controlling interest is presented as an equity item, separately from the equity of the owners of the parent.

Business combinations

From 1 January 2010, the acquisition method of accounting is used to account for business combinations by the Group. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any non-controlling interest. For each business combination, the Group measures the non-controlling interest in the acquired subsidiary at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses.

The excess of purchase consideration over the fair value of the Group's share of identifiable net assets is recorded as goodwill (Note 3.6). If the cost of the acquisition is less than the fair value of the Group's share of identifiable net assets of the subsidiary acquired the difference is recognised directly in the profit or loss.

Prior to 1 January 2010, business combinations were accounted for using the purchase method. Transaction costs directly attributable to the acquisition formed part of the acquisition costs. The non-controlling interest (formerly known as minority interest) was measured at the proportionate share of the acquiree's identifiable net assets.

Interest in a joint venture

The Group has an interest in a joint venture which is a jointly controlled entity, whereby the ventures have a contractual arrangement that establishes joint control over the economic activities of the entity. The Group recognises its interest in the joint venture using the proportionate consolidation method. The Group combines its proportionate share of each of the assets, liabilities, income and expenses of the joint venture with similar items, line by line, in its consolidated financial statements. The financial statements of the joint venture are prepared for the same reporting period as the parent company. Adjustments are made where necessary to bring the accounting policies in line with those of the Group.

Adjustments are made in the Group's consolidated financial statements to eliminate the Group's share of intra group balances, income and expenses and unrealised gains and losses on transactions between the Group and its jointly controlled entity. Losses on transactions are recognised immediately if the loss provides evidence of a reduction in the net realisable value of current assets or an impairment loss. The joint venture is proportionately consolidated until the date on which the Group ceases to have joint control over the joint venture.

Increases in ownership interests in subsidiaries

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

Acquisition of productive assets (single asset entities)

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

3.2 CASH AND SHORT-TERM DEPOSITS

Cash and short-term deposits in the statement of financial position comprise cash at banks and in hand, short-term deposits with an original maturity of three months or less and cash deposits placed to secure participation in the state tenders with an original maturity of three months or less.

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

Interest receivable on deposits is classified as other receivables.

3.3 VALUE ADDED TAX

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

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

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

3.4 INVENTORIES

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

3.5 PROPERTY, PLANT AND EQUIPMENT

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

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

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

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

3.6 GOODWILL

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

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

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

3.7 OTHER INTANGIBLE ASSETS

Intangible assets acquired separately from business combinations are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination are initially recognised at fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impair-

ment losses. Intangible assets with a finite life are amortised on a straight-line basis over the useful economic lives (for trade marks useful economic life is estimated between 15 and 20 years) and assessed for impairment whenever there is an indication that the intangible asset may be impaired. Amortisation periods and methods for intangible assets are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the profit or loss in the expense category consistent with the function of the intangible asset.

3.8 INVESTMENTS AND OTHER FINANCIAL ASSETS

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

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

Loans and receivables

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

Available-for-sale financial investments

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the two preceding categories. After initial measurement, available-for-sale financial assets are measured at fair value with unrealised gains or losses recognised directly in other comprehensive income until the investment is derecognised or determined to be impaired at which time the cumulative gain or loss previously recorded in other comprehensive income is recognised in the profit or loss.

Fair value

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

Amortised cost

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

Impairment of financial assets

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

Assets carried at amortised cost

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

Available-for-sale financial investments

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

3.9 BORROWINGS

Borrowings are initially recognised at the fair value of the consideration received less directly attributable transaction costs. After initial recognition, borrowings are measured at amortised cost using the effective interest method; any difference between the fair value of the consideration received (net of transaction costs) and the unwinding of discount is recognised as an interest expense over the period of the borrowings.

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

3.10 INCOME TAXES

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

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

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

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

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

The effect from a change in tax rates is recognised in profit or loss except to the extent that it relates to items previously charged or credited to other comprehensive income.

3.11 LEASES

Operating lease payments are recognised as an expense in the profit or loss on a straight line basis over the lease term.

3.12 DERECOGNITION OF FINANCIAL ASSETS AND LIABILITIES

Financial assets

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

Financial liabilities

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

3.13 PROVISIONS

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

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

3.14 EQUITY

Share capital

Ordinary shares are classified as equity.

Dividends

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

3.15 REVENUE RECOGNITION

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

3.16 EMPLOYEE BENEFITS

In 2010, under provision of the Russian legislation, social contributions are made through a social tax ("ST") calculated by the Group by the application of a ST rate 26% to the gross remuneration of each employee. The rate 26% was applicable only to the gross remuneration of each employee not more than RR 415 calculated from the beginning of the year. The Group allocates the ST to three social funds (state pension fund, social and medical insurance funds), where the rate of contributions to the pension fund was 20% depending on the annual gross salary of each employee. The Group's contributions relating to ST are expensed in the year to which they relate. Total contributions for ST amounted to RR 335,067 during the year ended 31 December 2010 (2009: RR 265,015) and they were classified as labour costs in these consolidated financial statements.

In addition, the Russian legislation provides for an increase the current ST rate from 26% to 34% effective from 1 January 2011. Furthermore, the new ST rate 34% will be applicable to the gross remuneration of each employee not more than RR 463 calculated from the beginning of the year.

3.17 FOREIGN CURRENCY TRANSACTIONS

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

At 31 December 2010, the exchange rates used for translation foreign currency balances were US$ 1 = 30.48 rubles; Euro 1 = 40.33 rubles (2009: USD 1 = 30.24 rubles; Euro 1= 43.39 rubles).

The functional currency of the foreign operations is the United States dollar (US$). As at the reporting date, the assets and liabilities of those subsidiaries are translated into the presentation currency of the Group (the Russian Rouble) at the rate of exchange ruling at the reporting date and its statement of comprehensive income is translated at the weighted average exchange rate for the year. The exchange differences arising on the translation are taken directly to a separate component of equity. In 2010 and 2009, the foreign subsidiaries did not perform any significant operations and held minor assets and liabilities, therefore its translation into the presentation currency had no significant effect on these consolidated financial statements.

3.18 IMPAIRMENT OF NON-FINANCIAL ASSETS

At each reporting date the Group assesses whether there is any indication that an asset or cash generating unit (CGU) may be impaired. The assets or CGUs subject to such assessment are primarily property, plant and equipment and trade marks. If any such indication exists, the Group makes an estimate of the asset's or CGU's recoverable amount. An asset's or CGU's re-

coverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use. Recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets. Where the carrying amount of an asset or CGU exceeds its recoverable amount, the asset or CGU is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessment of the time value of money and the risks specific to the assets or CGUs.

4. SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

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

USEFUL LIFE OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

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

IMPAIRMENT OF NON-FINANCIAL ASSETS

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

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

- *Property, plant and equipment:* changes in current competitive conditions, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, technological obsolescence, discontinuance of service, current replacement costs and other changes in circumstances that indicate impairment exists.
- *Trade marks:* changes in current competitive conditions, changes in the regulations, expectations of growth in the industry, increased cost of capital, changes in the future availability of financing, introduction of alternative products on the market and other changes in circumstances that indicate impairment exists.

IMPAIRMENT OF GOODWILL

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the value in use of the cash-generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at 31 December 2010 and 2009 was RR 1,180,469. More details are provided in Note 12.

ALLOWANCE FOR DOUBTFUL ACCOUNTS RECEIVABLE

The Group maintains an allowance for doubtful accounts receivable to account for estimated losses resulting from the inability of customers to make required payments. When evaluating the adequacy of an allowance for doubtful accounts receivable, management bases its estimates on the aging of accounts receivable balances and historical write-off experience, customer credit worthiness and changes in customer payment terms. If the financial condition of customers were to deteriorate, actual write-offs might be higher than expected. As at 31 December 2010, allowances for doubtful accounts receivable amounted to RR 48,781 (2009: RR 94,910). More details are provided in Note 14.

ALLOWANCE FOR WRITE-DOWN OF INVENTORIES TO NET REALIZABLE VALUE

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

FAIR VALUE OF DERIVATIVES

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

CURRENT TAXES

Russian tax, currency and customs legislation is subject to varying interpretations and changes occur frequently. Further, the interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Group's entities may not coincide with that of management. As a result, tax authorities may challenge transactions and the Group's entities may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods. As of 31 December 2010 management believes that its interpretation of the relevant legislation is appropriate and that it is probable that the Group's tax, currency and customs positions will be sustained. More details are provided in Note 29.

LEASES

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset.

5. REORGANIZATION OF GROUP'S STRUCTURE AND SALE OF SUBSIDIARY

REORGANIZATION OF GROUP'S STRUCTURE

In July 2009, the management approved a plan to reorganise the legal structure of some of the Group's subsidaries. This plan included a legal merger of OJSC "Pharmstandard-Octyabr" and CJSC "Masterlek" with OJSC "Pharmstandard". In November 2009, OJSC "Pharmstandard-Octyabr" and CJSC "Masterlek" were merged into OJSC "Pharmstandard".

OJSC "Pharmstandard-Oktyabr" and CJSC "Masterlek" did not conduct any operating activities during 2009. These subsidiaries had only minor assets and liabilities. The reorganization has improved the structure of Group's assets and liabilities and has enhanced the Group business efficiency.

In accordance with Russian legislation, shareholders have the right to unconditionally offer their shares for redemption by the Company, in the event of reorganization. In 2009, certain shareholders executed this right and the Company acquired 6,000 treasury shares with par value 1 (one) Russian Ruble. These shares comprise less than 0.02% of the authorized share capital. The difference between the nominal value of the treasury shares and consideration paid was debited directly to equity. In October 2010, these treasury shares were sold by the Company at the Russian Stock Exchange (MICEX). The difference between the nominal value of the treasury shares and consideration received, amounted to RR 16,684 was credited directly to equity.

SALE OF SUBSIDIARY

In 2009 the management approved a plan to dispose of "Black Bird Investment Enterprises Corp". This subsidiary did not conduct any business activities and had a loan balance payable and receivable. This subsidiary was sold during the 4th quarter of 2009 to a related party (Note 10) for a cash consideration of RR 13,770. This arrangement resulted in a gain amounting to RR 13,627 that was recognised in other income (Note 26).

6. ACQUISITION AND DISPOSAL OF ORDINARY SHARES OF JSC "GRINDEKS"

In April 2010, the Group acquired 1,090,844 ordinary shares representing 11.38%of share capital of JSC "Grindeks AS" ("Grindeks"), a company registered under the laws of Republic of Latvia, for a cash consideration of EURO 12,210 thousand (RR 481,065). The ordinary shares of Grindeks are listed on the stock exchange "NASDAQ OMX Riga". The Group has held strategic partnership with Grindeks in respect of distribution and promotion of its pharmaceutical product Mildronate® in the Russian Federation since January 2008. In 4th Quarter 2010, the Board of Directors of the Company accepted an offer to sell 1,090,844 ordinary shares of Grindeks to a third party. In October 2010, all ordinary shares of Grindeks were sold for cash consideration of EURO 12,447 thousand (RR 528,552). The gain from disposal of these financial assets amounting to RR 47,487 was recognized in profit and loss (Note 26).

7. ACQUISITION OF ACIPOL TRADE MARK

In August 2010 the Company signed a contract with shareholders of Vindexpharm CJSC ("Vindexpharm") with the purpose of acquiring Acipol trade mark through the purchase of all outstanding Vindexpharm's shares for a cash consideration of US$ 26,250 thousand (RR 806,032). On 2 September 2010 all shares of Vindexpharm were transferred to the Company.

Vindexpharm is a holder of Acipol trade mark being its the only asset. Therefore, the acquisition of Vindexpharm was accounted for as the acquisition of a single-asset entity. The consideration paid amounting to RR 806,032 was allocated fully to the value of trade mark (Note 12).

8. FOUNDATION OF JOINT VENTURE

In the 4th quarter of 2009, the management of the Group approved the plan for the foundation of a new joint venture. In February 2010, "NauchTechStroy Plus" LLC ("NTS+") was registered in the Russian Federation as a joint venture of the Company and another participant. Main purpose of "NTS+" is to build and commence its operations as a research and development center in Vladimir region of the Russian Federation specialized in bioengineering medical products and universal diagnostic researches. Commencement of its operation is scheduled in 2011.

The Group holds 50% interest in "NTS+" in the amount of RR 150,004, which was fully paid in cash. The Group also incurred certain expenditures on provision of financial assistance to "NTS+" presented as other expenses (Note 26).

The aggregate amounts of "NTS+" assets, liabilities, income and expenses proportionately included in the Group's consolidated financial statements are detailed below:

	2010
Current assets	156,831
Long-term assets	223,600
Current liabilities	(6,586)
Long-term liabilities	–
Income	–
Expenses	(16,160)

There were no any capital commitments of the Group in relation to its interests in "NTS+" as of 31 December 2010.

The share of the Group in the capital commitments of "NTS+" was equal to RR 11,948 as of 31 December 2010.

9. SEGMENT INFORMATION

For the management purposes, the Group is organised into two main reportable operating segments: (1) production and wholesale of pharmaceutical products and (2) production and wholesale of medical equipment and disposables. The medical equipment segment is primarily represented by OJSC "TZMOI", as production subsidiary, and by equipment department of OJSC "Pharmstandard", as managing and logistics division.

Management monitors sales, gross profits and segment results of these business segments separately for the purpose of making decisions about resource allocation and performance assessment. For the management purposes, budgets of income and expense are planned, made and analyzed for each of operating segments separately.

Segment result is segment revenue less segment expenses. Segment expenses consist of cost of sales, selling and distribution costs, general and administrative expenses and other income and expenses that can be directly attributed to the segment on a reasonable basis.

No operating segments have been aggregated to form the above reportable operating segments.

Segment assets consist primarily of property, plant and equipment, intangible assets, inventories, financial assets, receivables and operating cash. There were no assets unallocated to segments as of 31 December 2010 and 2009. Segment liabilities comprise operating liabilities and exclude items such as taxation and certain corporate liabilities. Capital expenditure comprises of additions to property, plant and equipment.

No significant intercompany transactions were entered to and between these operating segments.

The following table presents revenue and profit information regarding the Group's operating segments:

Year ended 31 December 2010	Production and wholesale of pharmaceutical products	Production and wholesale of medical equipment	Group
Sales to external customers	29,056,140	630,496	29,686,636
Total revenue	**29,056,140**	**630,496**	**29,686,636**
Gross profit	12,812,092	173,706	12,985,798
Segment result	**8,885,953**	**(9,138)**	**8,876,815**
Financial income, net			267,487
Profit before income tax			**9,144,302**
Income tax expense			(1,980,506)
Profit for the year			**7,163,796**
Segment assets	38,521,575	897,103	39,418,678
Total assets	**38,521,575**	**897,103**	**39,418,678**
Segment liabilities	11,224,770	45,741	11,270,511
Unallocated liabilities			1,272,412
Total liabilities			**12,542,923**
Acquisition of property, plant and equipment (Note 11)	1,032,007	18,125	1,050,132
Intangible assets acquisition (Note 12)	806,032	–	806,032
Depreciation and amortisation	738,026	53,990	792,016
Reversal of impairment of intangible assets (Note 12)	29,258	–	29,258
Impairment charge of property, plant and equipment (Note 11)	–	76,002	76,002

Year ended 31 December 2009	Production and wholesale of pharmaceutical products	Production and wholesale of medical equipment	Group
Sales to external customers	23,406,685	688,708	24,095,393
Total revenue	**23,406,685**	**688,708**	**24,095,393**
Gross profit	11,533,284	194,174	11,727,458
Segment result	**8,550,210**	**108,132**	**8,658,342**
Financial expense, net			(13,091)
Profit before income tax			**8,645,251**
Income tax expense			(1,792,810)
Profit for the year			**6,852,441**
Segment assets	25,215,141	1,007,720	26,222,861
Total assets	**25,215,141**	**1,007,720**	**26,222,861**
Segment liabilities	**4,466,577**	**32,125**	**4,498,702**
Unallocated liabilities			2,028,645
Total liabilities			**6,527,347**
Acquisition of property, plant and equipment (Note 11)	224,294	11,079	235,373
Intangible assets acquisition (Note 12)	167,801	–	167,801
Depreciation and amortisation	695,683	56,375	752,058
Impairment charge	62,696	–	62,696

Revenues from some individual customers in the pharmaceutical products segment exceeded 10% of total Group's segment revenue.

The table below shows the revenue from these customers:

Customer	2010	2009
The Ministry of health and social department (state tenders)[1]	3,102,226	3,905,778
Customer 1 (third party products, Note 22)	3,838,173	–
Customer 2	3,479,700	3,289,494
Customer 3	3,394,848	3,169,648

[1] Advances received recorded as of 31 December 2010 represented advances received from the Ministry of health and social department under state tenders (Note 20)

10. BALANCES AND TRANSACTIONS WITH RELATED PARTIES

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

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

The nature of the related party relationships for those related parties with whom the Group entered into transactions or had balances outstanding at 31 December 2010 and 2009 are detailed below.

Balances with related parties:

2010	Short-term financial assets (a)	Cash and short-term deposits-(a) Note 16	Other receivables-(a) Note 14	Trade payables, other payables and accruals – (b) Note 20
Other related parties[2]	632,000	3,887,404	53,699	770,545
Total	**632,000**	**3,887,404**	**53,699**	**770,545**

2009	Short-term financial assets (a)	Cash and short-term deposits (a) Note 16	Other receivables-(a) Note 14	Trade payables, other payables and accruals – (b) Note 20
Other related parties[2]	440,000	2,475,900	16,507	12,004
Total	**440,000**	**2,475,900**	**16,507**	**12,004**

(a) This balance primarily represented cash, short-term bank deposits and interest receivable at a bank controlled by a related party.

(b) This balance represented obligation for the license fee, payables for marketing services and payables for supply of the third-party products, described in section "Transactions with related parties" below.

Cash balances with the related bank carry no interest. Short-term financial assets at 31 December 2010 include cash deposits in the related bank and carry 8%-12.5% interest p.a. (for more details see Notes 16 and 17).

Significant transactions with related parties :

Statement of comprehensive income caption	Relationship	2010	2009
License fee (included in distribution costs) (A)	Other related parties	(30,341)	(30,401)
Warehouse rental expenses (included in distribution costs) (B)	Other related parties	(74,636)	(53,801)
Office rental expenses (included in general and administrative expenses) (B)	Other related parties	(26,671)	(15,654)
Marketing and advertising expenses (included in distribution costs) (C)	Other related parties	(80,658)	–
Cost of sales of third-party products (D)	Other related parties	(679,463)	–
Agency fee income (included in other income) (E)	Other related parties	–	4,779
Gain from disposal of subsidiary (F)	Other related parties	–	13,627
Interest income from loan provided to majority shareholder (G)	Majority shareholder	31,483	–

(A) License fee

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

(B) Rental expenses

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

[2] Other related parties, represent entities under control of the Company's shareholders having significant influence over the Company.

(C) Marketing and advertising expenses

In 2010, the Group acquired the results of clinical research related to one of the Group pharmaceutical products developed by a Russian scientific institute from a related party. This research was performed in 2007-2010 and the related party acted as an intermediary between the scientific institute and the Group. The Group plans to use the research result to promote the product on the market and, accordingly, related cost was classified as marketing and advertising expenses in the consolidated financial statements.

(D) Cost of sales of third-party products

In 2010, the Group signed purchase contracts for supply of third-party product Koagil VII manufactured by that related party. The amount includes the cost of this product sold by the Group through state tenders (Notes 22 and 23). As of 31 December 2010 the Group had no unsold inventory balances of Koagil VII.

(E) Agency fee income

In 2009, the Company held an agency contract with the related party for purchase of certain equipment on behalf of that party.

(F) Gain from disposal of subsidiary

This includes a gain received from disposal of a subsidiary to a related party (for more information see Note 5).

(G) Loans provided to the majority shareholder

In 2nd quarter 2010, the Company's majority shareholder "Augment Investments Limited" ("Augment"), a company registered under the laws of Cyprus (see Note 21), applied to the Company with request to provide short-term interest loan for the purpose of financing the current business activity of Augment not related to the Group. In accordance with the conditions of the syndicated borrowing organised by Citibank ("Citibank loan") (Note 18), the Group received written consent from the lenders of Citibank loan for the Augment's loan. In July 2010, the Group provided a short-term loan to Augment with maturity date not later than 15 January 2011 in the amount of RR 1,400,000 with fixed interest rate of 7.75% per annum. In October 2010, this loan was fully repaid by Augment. The interest income from this operation was recognised as financial income in profit or loss (Note 27).

ACQUISITION OF INTANGIBLE ASSETS

In 2009, the Group acquired an intangible asset (trade mark) for RR 90,050 from the related party.

Compensation to key management personnel

Key management personnel comprise 3 persons as at 31 December 2010 and 2009. Total compensation to key management personnel, amounted to RR 46,343 for the year ended 31 December 2010 (2009: RR 39,310). Such compensation represents the payroll and bonuses included in general and administrative expenses.

11. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following:

31 December 2010	Land	Buildings	Plant and machinery	Equipment and motor vehicles	Assets under construction	Total
COST						
Balance at 31 December 2009	32,986	2,204,001	2,518,059	282,375	205,512	5,242,933
Additions	–	3,867	81,951	132,931	831,383	1,050,132
Transfers	1,144	38,888	142,168	5,948	(188,148)	–
Disposals	(218)	(598)	(28,586)	(5,085)	(1,899)	(36,386)
Balance at 31 December 2010	**33,912**	**2,246,158**	**2,713,592**	**416,169**	**846,848**	**6,256,679**
ACCUMULATED DEPRECIATION AND IMPAIRMENT						
Balance at 31 December 2009	–	276,562	1,094,501	152,566	33,459	1,557,088
Depreciation charge	–	66,232	350,885	63,684	–	480,801
Disposals	–	(25)	(23,340)	(1,926)	–	(25,291)
Impairment (a)	–	–	73,800	–	2,202	76,002
Balance at 31 December 2010	–	**342,769**	**1,495,846**	**214,324**	**35,661**	**2,088,600**
NET BOOK VALUE						
Balance at 31 December 2009	**32,986**	**1,927,439**	**1,423,558**	**129,809**	**172,053**	**3,685,845**
Balance at 31 December 2010	**33,912**	**1,903,389**	**1,217,746**	**201,845**	**811,187**	**4,168,079**

31 December 2009	Land	Buildings	Plant and machinery	Equipment and motor vehicles	Assets under construction	Total
COST						
Balance at 31 December 2008	32,986	1,959,337	2,322,910	282,368	464,589	5,062,190
Additions	–	7,815	60,613	14,578	152,367	235,373
Transfers	–	238,754	165,850	2,531	(407,135)	–
Disposals	–	(1,905)	(31,314)	(17,102)	(4,309)	(54,630)
Balance at 31 December 2009	**32,986**	**2,204,001**	**2,518,059**	**282,375**	**205,512**	**5,242,933**
ACCUMULATED DEPRECIATION AND IMPAIRMENT						
Balance at 31 December 2008	–	213,249	794,702	103,671	33,459	1,145,081
Depreciation charge	–	64,367	336,824	60,756	–	461,947
Disposals	–	(1,054)	(23,651)	(11,861)	–	(36,566)
Reversal of impairment (b)	–	–	(13,374)	–	–	(13,374)
Balance at 31 December 2009	–	**276,562**	**1,094,501**	**152,566**	**33,459**	**1,557,088**
NET BOOK VALUE						
Balance at 31 December 2008	**32,986**	**1,746,088**	**1,528,208**	**178,697**	**431,130**	**3,917,109**
Balance at 31 December 2009	**32,986**	**1,927,439**	**1,423,558**	**129,809**	**172,053**	**3,685,845**

(a) Impaired assets represent equipment for production of medical disposables, including syringes, removed from active use due to decline in customer demand and low profitability of these disposables. The impairment charge equals to the carrying value of those equipment and assets under construction (Note 31).

(b) Due to changes in the market situation for medical devices during 2009 the Group resumed the production of syringes. As a result the previous impairment of the related equipment has been reversed.

In 2010 and 2009, the Group did not receive new borrowings and there were no new qualifying assets, therefore no interest expense was capitalized.

The Group assets include only a minor portion of land on which the Group's factories and buildings, comprising the Group's principal manufacturing facilities, are located, whilst the major portion of the land is held under operating lease agreements with the state municipal bodies. The lease agreements specify lease terms between 1 and 20 years with an option to prolong the lease term for another 10 years. In addition, the lease agreements include a purchase option after termination of the lease. Purchase price will be determined based on fair value of the land as determined by the municipal authorities. The total amount of rental payments for the use of the land during 2010 was RR 8,682 (2009: RR 8,187). Such payments are reassessed by the state authorities on an annual basis. No such reassessment has been completed for 2011 and beyond as of the date of approval of these consolidated financial statements for issue.

12. INTANGIBLE ASSETS

	Goodwill	Trademarks and patents	Total
COST			
Balance at 31 December 2009	1,180,469	5,924,109	7,104,578
Additions (a)	–	806,032	806,032
Balance at 31 December 2010	1,180,469	6,730,141	7,910,610
Accumulated Amortisation and Impairment			
Balance at 31 December 2009	–	942,443	942,443
Reversal of impairment (b)	–	(29,258)	(29,258)
Amortisation expense	–	311,215	311,215
Balance at 31 December 2010	–	**1,224,400**	**1,224,400**
NET BOOK VALUE			
Balance at 31 December 2009	**1,180,469**	**4,981,666**	**6,162,135**
Balance at 31 December 2010	**1,180,469**	**5,505,741**	**6,686,210**

	Goodwill	Trademarks and patents	Total
COST			
Balance at 31 December 2008	1,180,469	5,756,308	6,936,777
Additions (a)	–	167,801	167,801
Balance at 31 December 2009	1,180,469	5,924,109	7,104,578
Accumulated Amortisation and Impairment			
Balance at 31 December 2008	–	589,636	589,636
Impairment (c)	–	62,696	62,696
Amortisation expense	–	290,111	290,111
Balance at 31 December 2009	–	**942,443**	**942,443**
NET BOOK VALUE			
Balance at 31 December 2008	**1,180,469**	**5,166,672**	**6,347,141**
Balance at 31 December 2009	**1,180,469**	**4,981,666**	**6,162,135**

(a) Additions represents acquisition of Acipol trade mark (see Note 7). In 2009, there were acquisitions of a trade mark (see Note 10) and some patents (know-how).

(b) The reversal of impairment mainly relates to the increase in customer demand due to the pharmaceutical market growth and increase in consumption of certain pharmaceutical Group's products in 2010. The recoverable amount was determined based on a value in use calculation using cash flow projections developed on the basis of financial budgets approved by management covering a five-year period and cash flows beyond the five-year period are extrapolated using a 5% growth rate that is the mid-term average growth rate for pharmaceuticals market. The discount rate applied to cash flow projections is 14.7%.

(c) The impairment mainly relates to the decrease in customer demand due to the recent financial crisis. The recoverable amount was determined based on a value in use calculation using cash flow projections based on financial budgets approved by management covering a five-year period and cash flows beyond the five-year period are extrapolated using a 5% growth rate that is the mid-term average growth rate for pharmaceuticals market. The discount rate applied to cash flow projections was 16.4%.

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

	Carrying amount		Remaining amortization period (years)	
Name	**2010**	**2009**	**2010**	**2009**
Afobazol®	1,851,570	1,955,884	18	19
Arbidol®	1,611,825	1,715,258	15	16
Acipol®	788,120	–	15	–
Flucostat®	627,023	667,259	15	16

IMPAIRMENT TESTING OF GOODWILL

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

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

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

	Pharmaceuticals		Equipment		Total	
	2010	**2009**	**2010**	**2009**	**2010**	**2009**
Carrying amount of goodwill	961,615	961,615	218,854	218,854	1,180,469	1,180,469

The recoverable amount of the cash-generating units has been determined based on a value in use calculation using cash flow projections developed on the basis of financial budgets approved by management covering a five-year period and cash flows beyond the five-year period are extrapolated using a 5% growth rate that is the same as the mid-term average growth rate for pharmaceuticals and medical equipment market (2009: 5% for pharmaceuticals and medical equipment market). The discount rate applied to cash flow projections is 14.7% (2009: 16.4%).

KEY ASSUMPTION USED IN VALUE IN USE CALCULATIONS

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

- Discount rates;
- Raw material price inflation;
- Currency rates changes;
- Growth rate used to extrapolate cash flows beyond the budget period.

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

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

Currency exchange rates changes – estimated based on current trends on the foreign currency market.

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

SENSITIVITY TO CHANGES IN ASSUMPTIONS

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

13. INVENTORIES

Inventories consist of the following:

	2010	2009
Raw materials - at cost	1,931,686	1,448,918
Work in progress - at cost	304,338	330,508
Finished goods:		
- at cost	5,271,354	999,267
- at net realisable value (a)	5,230,190	979,265
	7,466,214	**2,758,691**

(a) On 31 December 2010, finished goods balance included third party products in the amount of RR 2,566,037 designated for sale under the terms of the state tenders won by the Company.

Movements in allowance for write-down of inventories to net realizable value were as follows:

	2010	2009
Balance at 1 January	20,002	24,479
Additional allowance	43,534	7,434
Unused amounts reversed	(466)	(987)
Utilised during the year	(21,906)	(10,924)
Balance at 31 December	**41,164**	**20,002**

14. TRADE AND OTHER RECEIVABLES

	2010	2009
Trade receivables (net of allowance for impairment of receivables of RR 48,781 (2009: RR 94,910))	12,271,212	8,994,926
Interest receivable (Note 10)	104,847	17,242
Other receivables (a)	–	276,914
	12,376,059	**9,289,082**

(a) Other receivables represented cash rebates on procurement.

At 31 December 2010 RR 153,236 of trade receivables were denominated in currencies other than Russian Roubles, primarily in US$ (2009: RR 52,584).

Movements in allowance for impairment of trade receivables were as follows:

	2010	2009
Balance at 1 January	94,910	568,676
Additional allowance	3,017	4,979
Unused amounts reversed	(45,832)	(477,279)
Utilised during the year	(3,314)	(1,466)
Balance at 31 December	48,781	94,910

In 2008 the Group recognized an allowance in the amount of RR 476,131 related to the bankruptcy of one of the Group's distributor, CJSC "Genesis". In 2009 and 2010, a successor of the distributor, agreed to pay almost the entire balance receivable that had been previously provided for. The reversal of the allowance for accounts receivable, included in "Unused

amount reversed" line, amounted to RR 28,460 (2009: RR 447,671) and recognised in profit or loss as other income (Note 26) and the remaining reversal amount was recognised in profit or loss as credit to cost of sales.

15. PREPAYMENTS

	2010	2009
Trade prepayments for services and materials	219,621	136,729
	219,621	**136,729**

16. CASH AND SHORT-TERM DEPOSITS

Cash and short-term deposits consist of the following:

	2010	2009
Cash in bank – Russian Roubles	3,898,237	1,604,760
Cash in bank – US$ and Euro	8,021	617,176
Short-term bank deposits with original maturity less than 90 days – Russian Roubles (a)	250,000	–
Cash deposits on tenders – Russian Roubles: - transferred to the Ministry of Health (b)	–	156,224
- placed in the related bank (c)	–	420,000
	4,156,258	**2,798,160**

(a) Short-term bank deposits bear an interest rate of 7% p.a. on average.
(b) This item represents cash deposits restricted for use placed to secure participation in tenders announced by the Government of the Russian Federation. Cash deposit transferred to the Ministry of Health is interest free.
(c) Cash deposits placed in the related bank carried an interest rate of 12.5% p.a.

17. SHORT-TERM FINANCIAL ASSETS

	2010	2009
Accounted for as loans and receivables: Promissory notes	614,700	331,120
Short-term bank deposits – Russian Roubles (Note 10)	2,697,000	440,000
Short-term bank deposits – US$	304,769	302,442
Short-term loans	50,000	45,500
Accounted for as available for sale: Securities	11,866	9,595
Other	3,688	4,630
	3,682,023	**1,133,287**

The promissory notes, deposits and loans bear interest rate within the range from 8% p.a. to 12.5% p.a.

18. BORROWINGS AND LOANS

	2010	2009
Long-term borrowings and loans		
(a) Citibank loan (Note 10)	394,523	782,871
Other loans	1,300	–
Less: Current portion of long-term borrowings and loans	(395,823)	(391,360)
	–	391,511

Long-term debt is repayable as follows:

	2010	2009
1 to 2 years	–	391,511
	–	391,511

As at 31 December 2010 and 2009 all the borrowings are US$ denominated. The foreign exchange risk in this respect is not covered by any derivative instruments.

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

- Facility A in the total amount of US$ 91 million with maturity period of 3 years (on 18 December 2009 this facility was repaid); and
- Facility B in the total amount of US$ 55 million with maturity period of 5 years.

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

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

In September 2007, when LIBOR rate interest was approximately 5.7%, the Group entered into an Interest Rate Swap agreement in respect to all interest payable under the Citibank loan swapping the LIBOR rate interest obligations into a fixed rate of 4.932% per annum. In this manner the Group protects itself against fluctuations of LIBOR rates. For more details see Note 30.

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

The Citibank loan agreement establishes certain financial ratios, restrictions on disposal of assets and distribution of dividends. There was no breach of these conditions by the Group.

The Citibank loan agreement also contains material adverse change clause.

In 2010, the Group repaid US$ 12,940 thousand (RR 395,087) of the Citibank loan (2009: US$ 53,385 thousand (RR 1,688,150)).

19. OTHER TAXES PAYABLE

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

	2010	2009
Value-added tax	445,634	520,305
Property and other taxes	77,680	48,221
	523,314	**568,526**

20. TRADE AND OTHER PAYABLES AND ACCRUALS, AND ADVANCES RECEIVED

	2010	2009
Trade payables	2,140,639	1,715,862
Payables for third parties products procurement	5,972,929	1,830,112
Payables for third parties products procurement and other payables – related parties (Note 10)	770,545	12,004
Advances received (Note 9)	1,337,032	
Other payables and accruals	526,052	348,001
	10,747,197	**3,905,979**

At 31 December 2010 RR 1,620,292 of trade payables were denominated in currencies other than Russian Rouble, primarily in US$ (2009: RR 1,253,586).

21. SHARE CAPITAL

In accordance with its charter documents the share capital of the Company is RR 37,793. The authorised number of ordinary shares is 37,792,603 with par value of 1 (one) Russian Rouble. All authorised shares are issued and fully paid. There were no other transactions with own shares during 2010 except for the sale of treasury shares (Note 5).

As at 31 December 2010 and 2009 more than half of voting shares of OJSC "Pharmstandard" were held by Augment controlled by Victor Kharitonin, a Russian citizen.

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

In 2008 and 2009, 969,815 ordinary shares representing 2.56% of share capital of the Company were sold by Augment and were offered at LSE. Also, in 2009 Augment reacquired 55,000 ordinary shares representing a minor part of share capital. After these transactions, 45.7% of share capital is publicly listed of which 27.6% is on the LSE.

In accordance with Russian legislation, dividends may only be declared from accumulated undistributed and unreserved earnings as shown in Russian statutory financial statements. The Company had approximately RR 14,179,754 (unaudited) of undistributed and unreserved earnings as at 31 December 2010 (2009: RR 8,911,487- unaudited). In addition, the Company's share in the undistributed and unreserved earnings of the subsidiaries and joint venture was approximately RR 11,809,047 (unaudited) as at 31 December 2010 (2009: RR 9,307,037- unaudited).

In accordance with the Citibank loan agreement (Note 18) the Group shall not pay, make or declare any dividend or other distribution without the prior written consent of the lenders.

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

EARNINGS PER SHARE

Earnings per share are as follows:

	2010	2009
Weighted average number of ordinary shares outstanding	37,792,603	37,792,603
Profit for the year attributable to the shareholders	7,149,543	6,836,430
Basic and diluted earnings per share, Russian Roubles	189.18	180.89

22. REVENUE

Sales breakdown by product groups comprised the following:

Product group	2010	2009
PHARMACEUTICAL PRODUCTS		
Over the Counter ("OTC")		
Branded	13,338,950	12,709,906
Non-branded	2,242,147	2,130,766
	15,581,097	**14,840,672**
Prescription		
Branded	2,806,909	2,022,368
Non-branded	487,271	315,741
	3,294,180	**2,338,109**
Third parties products (a)	9,893,825	6,156,359
Other	287,038	71,545
Total pharmaceutical products	**29,056,140**	**23,406,685**
MEDICAL EQUIPMENT AND DISPOSABLES	630,496	688,708
	29,686,636	**24,095,393**

(a) Third parties products sales include sales of branded pharmaceutical products such as Velcade®, Mildronate®, Coagil VII, IRS®-19, Imudon®, Prezista® and Pulmozyme® and other products manufactured by other pharmaceutical companies.

23. COST OF SALES

The components of cost of sales were as follows:

	2010	2009
Materials and components	6,653,267	5,697,714
Third parties products	8,272,386	4,973,093
Production overheads	813,178	790,751
Depreciation and amortisation	718,937	684,802
Direct labour costs	243,070	221,575
	16,700,838	**12,367,935**

24. SELLING AND DISTRIBUTION COSTS

Selling and distribution costs were as follows:

	2010	2009
Advertising	1,427,340	1,365,491
Labour costs	826,242	585,997
Freight, communication and insurance of goods in transit	164,331	150,738
Trainings and other services	43,413	25,641
Certification expenses	54,290	38,763
Rent	75,803	53,920
Commission and license fee	57,819	51,495
Materials, maintenance and utilities	96,739	58,006
Travel and entertainment	80,114	58,976
Depreciation	53,659	50,066
Other expenses	36,452	24,035
	2,916,202	**2,463,128**

The Group entered into a number of operating lease agreements for warehouses. Rental agreements are revised on an annual basis.

25. GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative expenses were as follows:

	2010	2009
Labour costs	551,189	436,082
Services, legal, audit and consulting expense	75,491	45,384
Travel and entertainment	20,712	16,315
Taxes other than income tax	16,353	15,347
Property insurance	17,275	13,981
Freight and communication	28,811	25,134
Depreciation	19,420	17,190
Rent	34,963	27,359
Materials, maintenance and utilities	91,524	71,428
Other	36,216	43,025
	891,954	**711,245**

The Group entered into a number of operating lease agreements for office premises. Rental agreements are revised on an annual basis.

26. OTHER INCOME AND OTHER EXPENSES

Other income comprised the following:

	2010	2009
Income from non-core operations (a)	82,820	31,188
Reversal of impairment – property, plant and equipment (Note 11)	–	13,374
Reversal of impairment – intangible assets (Note 12)	29,258	–
Reversal of impairment of receivables (b)	28,460	447,671
Gain from disposal financial assets (Note 6)	47,487	–
Gain from sale of subsidiary (Note 5)	–	13,627
	188,025	**505,860**

(a) Income from non-core operations primarily includes (i) agency fee incurred in respect of sale of certain third-parties products by the Group (ii) income from sale of materials and other assets not included in other categories (iii) income from other non-core services

(b) This amount represents reversal of impairment initially recorded to other expenses. The total reversal amount presented in Note 14 also included reversal of impairment initially recorded to cost of sales.

Other expenses comprised the following:

	2010	2009
Foreign exchange loss, net	16,393	226,329
Impairment of property, plant and equipment (Note 11 and 31)	76,002	–
Loss from disposal of property, plant and equipment	5,311	7,578
Impairment of intangible assets (Note 12)	–	62,696
Expense related to the joint venture – Note 8 (a)	248,298	–
Charity	22,425	13,992
Bank charges (b)	32,433	9,213
Other taxes	50,250	53,959
Expenses for personnel reduction incurred in connection with closure of disposables production (Note 31)	7,411	–
Fees for factoring	–	24,594
Other	30,329	2,242
	488,852	**400,603**

(a) In 2010, the Group made an additional cash contribution of RR 480,000 to the joint-venture. This contribution was provided by the Group to allow the joint venture to commence its research and development activities. The excess of the contribution over Group's interest in the joint venture in the amount of RR 240,000 was considered as non-refundable assistance to the joint venture and, accordingly, recognized as an expense in 2010

(b) Bank charges includes (i) commission for daily banking operations (ii) commission for certain bank guarantees obtained by the Group.

27. FINANCIAL INCOME AND EXPENSE

Financial income and expense comprised the following:

	2010	2009
INTEREST INCOME:		
Income from changes in fair value of Interest Rate Swap (Notes 18 and 30)	23,502	54,337
Interest income from loans and deposits	289,409	72,205
Other	2,256	6,336
	315,167	**132,878**
INTEREST EXPENSE:		
Loss from Interest Rate Swap (Notes 18 and 30)	29,736	74,074
Interest expense on borrowings and loans	17,944	71,895
	47,680	**145,969**

28. INCOME TAX

	2010	2009
Income tax expense – current	2,145,172	1,724,934
Deferred tax (benefit) expense – origination and reversal of temporary differences	(164,666)	67,876
Income tax expense	**1,980,506**	**1,792,810**

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

	2010	2009
Profit before income tax	9,144,302	8,645,251
Theoretical tax charge at statutory rate of 20%	1,828,860	1,729,050
Tax effect of items which are not deductible or assessable for taxation purposes:		
Non-deductible expenses	151,646	63,760
Income tax expense	**1,980,506**	**1,792,810**

Movements in deferred tax balances were as follows:

	31 December 2008	Temporary differences recognition and reversal	31 December 2009	Temporary differences recognition and reversal in profit and loss	Temporary differences recognition and reversal in other comprehensive income	31 December 2010
TAX EFFECTS OF DEDUCTIBLE TEMPORARY DIFFERENCES – ASSET (LIABILITY):						
Property, plant and equipment (Note 11)	(291,116)	(16,746)	(307,862)	21,905	–	(285,957)
Intangible assets (Note 12)	(554,433)	40,110	(514,323)	29,826	–	(484,497)
Trade and other receivables	121,241	(153,617)	(32,376)	56,347	–	23,971
Inventories	21,113	(8,782)	12,331	79,526	–	91,857
Trade and other payables and other taxes	(55,124)	71,482	16,358	(11,462)	–	4,896
Financial instruments	17,817	(10,867)	6,950	(4,700)	–	2,250
Other	1,316	10,544	11,860	(6,776)	62	5,146
Total net deferred tax liability	**(739,186)**	**(67,876)**	**(807,062)**	**164,666**	**62**	**(642,334)**

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

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

The aggregate amount of temporary differences associated with investments in subsidiaries and joint venture for which deferred tax liabilities have not been recognised was approximately RR 8,096,339 as at 31 December 2010 (2009: RR 5,839,675).

29. CONTINGENCIES, COMMITMENTS AND OPERATING RISKS

OPERATING ENVIRONMENT OF THE GROUP

Russia continues economic reforms and development of its legal, tax and regulatory frameworks as required by a market economy. The future stability of the Russian economy is largely dependent upon these reforms and developments and the effectiveness of economic, financial and monetary measures undertaken by the government.

The Russian economy is vulnerable to market downturns and economic slowdowns elsewhere in the world. In 2010, the Russian Government continued to take measures to support the economy in order to overcome the consequences of the global financial crisis. Despite some indications of recovery there continues to be uncertainty regarding further economic growth, access to capital and cost of capital, which could negatively affect the Group's future financial position, results of operations and business prospects.

While management believes it is taking appropriate measures to support the sustainability of the Group's business in the current circumstances, unexpected further deterioration in the areas described above could negatively affect the Group's results and financial position in a manner not currently determinable.

TAXATION

Russian tax, currency and customs legislation is subject to varying interpretations, and changes, which can occur frequently. Management's interpretation of such legislation as applied to the transactions and activity of the Group may be challenged by the relevant regional and federal authorities. Recent events within the Russian Federation suggest that the tax authorities are taking a more assertive position in its interpretation of the legislation and assessments and as a result, it is possible that transactions and activities that have not been challenged in the past may be challenged. As such, significant addi-

tional taxes, penalties and interest may be assessed. Fiscal periods remain open to review by the authorities in respect of taxes for three calendar years preceding the year of review. Under certain circumstances reviews may cover longer periods.

As at 31 December 2010 management believes that its interpretation of the relevant legislation is appropriate and that the Group's tax, currency and customs positions will be sustained.

Because of the uncertainties associated with the Russian tax and legal systems, the ultimate amount of taxes, penalties and interest assessed, if any, may be in excess of the amount expensed to date and accrued as of 31 December 2010. It is not practical to determine the amount of unasserted claims that may manifest, if any, or the likelihood of any unfavourable outcome. Should the Russian tax authorities decide to issue a claim and prove successful in the court, they would be entitled to recover the amount claimed, together with fines amounting to 20% of such amount and interest at the rate of 1/300 of the Central Bank of the Russian Federation rate for each day of delay for late payment of such amount. Management believes that it is not probable that the ultimate outcome of such matters would result in a liability. Therefore, no provision for these contingencies was recorded in these consolidated financial statements.

INSURANCE POLICIES

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

30. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

FAIR VALUES

Management believes that fair value of cash and cash equivalents, loans receivable, promissory notes, short-term deposits, prepayments for subsidiary acquisition, other receivable or payables and investments approximate their carrying amounts due to their short maturity.

Fair values of long-term borrowings and loans are approximately equal to their carrying value as they are based on variable interest rates (LIBOR). Fair value of derivative financial instruments has been calculated by discounting the expected future cash flows at prevailing interest rates.

FAIR VALUE HIERARCHY

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly;

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

The table below shows the assets measured at fair value as at 31 December 2010:

	Total	Level 1	Level 2	Level 3
ASSETS MEASURED AT FAIR VALUE				
Financial assets				
Securities (Note 17)	11,866	11,029	–	837
LIABILITIES MEASURED AT FAIR VALUE				
Interest rate swap	11,249	–	11,249	–

31 December 2009:

	Total	Level 1	Level 2	Level 3
ASSETS MEASURED AT FAIR VALUE				
Financial assets				
Securities (Note 17)	9,595	8,774	–	821
LIABILITIES MEASURED AT FAIR VALUE				
Interest rate swap	34,751	–	34,751	–

FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

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

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

INTEREST RATE RISK

The Group is exposed to interest rate risk through interest cash flow and market value fluctuations as the majority of interest rates on long-term borrowings are floating and based on LIBOR as disclosed in Note 18.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's profit before tax for one year assuming the parallel shifts in the yield curves (through the impact on floating rate borrowings and changes in fair value in respect of the Interest Rate Swap):

	Increase/decrease in basis points	Effect on profit or loss (interest expense)	Effect on profit or loss (due to fair value change)
AS AT 31 DECEMBER 2010			
	100	(2,440)	1,552
	(30)	**732**	**(469)**
AS AT 31 DECEMBER 2009			
	100	(7,829)	6,429
	(25)	**1,957**	**(1,711)**

FOREIGN EXCHANGE RISK

The Group has US dollar denominated long-term borrowings (see Note 18) and also certain US dollar denominated trade payables (Note 20), trade receivables (Note 14) and other liabilities. Therefore, the Group is exposed to foreign exchange risk.

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

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

	Increase/decrease in US$ rate	Effect on profit before tax
AS AT 31 DECEMBER 2010		
US$/Roubles exchange rate	+10%	(111,185)
US$/Roubles exchange rate	–10%	111,185
AS AT 31 DECEMBER 2009		
US$/Roubles exchange rate	+10%	(104,057)
US$/Roubles exchange rate	–10%	104,057

LIQUIDITY RISK

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

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

As at 31 December 2010	Total	Less than 3 months	3 to 6 months	6 to 12 months	
Borrowings (a)	400,499	100,975	100,399	199,125	
Other current liabilities	38,434	–	–	38,434	
Total	**438,933**	**100,975**	**100,399**	**237,559**	

As at 31 December 2009	Total	Less than 3 months	3 to 6 months	6 to 12 months	1 to 5 years
Borrowings (a)	804,921	102,039	102,039	204,078	396,765
Other non-current liabilities	67,018	–	–		67,018
Total	**871,939**	**102,039**	**102,039**	**204,078**	**463,783**

(a) The Citibank loan received in 2006 (see Note 18 for details) includes contractual principal amount of debt and interest rate calculated in accordance with corresponding terms of the loan agreement at 31 December 2010 and 2009.

CREDIT RISK

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

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

Cash is placed in the related bank (Note 10), which is considered to have minimal risk of default.

The table below summarises the Group's trade receivables aging.

	Total	Neither impaired nor past due	Not impaired but past due				
			less 1 month	1-2 months	2-3 months	3 to 6 months	> 6 months (a)
31 December 2010	**12,376,059**	**11,078,443**	**1,125,873**	**161,614**	**8,504**	**1,482**	**143**
31 December 2009	9,289,082	8,455,737	612,742	19,995	10,657	14,175	175,776

(a) At 31 December 2009 these receivables primarily represent the amount of restructured receivable of CJSC "Genesis". In 2009 and 2010, the Group reversed impairment against the receivable from CJSC "Genesis", which was recorded in 2008. They were collected in January-March 2010 (for more details see Note 14).

Sales concentration to a small group of customers

The Group works with five distributors that together represent more than 50% of the Group's revenue for 2010 and 2009. Given the Russian market structure limited number of large distributors is not unusual. The Group has no other significant concentrations of credit risk but is exposed to general risk of the global credit crisis and its effects on the Group's distributors.

Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital. The Group manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt (while taking into consideration terms and conditions set by the Citibank Loan Agreement, Note 18).

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

	2010	2009
Borrowings and loans	395,823	782,871
Trade and other payables	9,410,165	3,905,979
Less: cash and short-term deposits	(4,156,258)	(2,798,160)
Net debt	5,649,730	1,890,690
Equity	26,447,541	19,281,553
Capital and net debt	32,097,271	21,172,243
Gearing ratio	18%	9%

31. EVENTS AFTER THE REPORTING PERIOD

ACQUISITION OF SUBSIDIARY

In 4th quarter 2010 the Company signed contracts with shareholders of Private Joint Stock Company "Kharkiv Enterprise Imunobiological and Medical Substances Production "Biolik" ("Biolik") with the purpose to acquire 55% of the voting shares of "Biolik", a company located in Ukraine involved in the production of various pharmaceutical products for a cash consideration of RR 393,234 (US$ 13,086 thousand).

Of the total consideration amount, payment of RR 39,162 is contingent upon achievement by "Biolik" of certain operational and financial targets by 31 December 2011. On 18 January 2011, the acquired shares of "Biolik" were transferred to the Company. The primary reason for the acquisition was the Group's intent to extend its operations to the Ukrainian market.

The Group has not finalised the purchase price allocation for "Biolik" and the management of the Group is currently assessing the effect of acquisition on the consolidated financial statements.

OFFER FOR 4.9% OF COMPANY'S ORDINARY SHARES

On 18 January 2011, OJSC "Pharmstandard-Leksredstva" proposed voluntary offer to purchase up to 1,850,000 ordinary shares of the Company representing about 4.9% of the Company's authorized share capital. Under the terms of the offer, all Company's shareholders were invited to sell their ordinary shares of the Company at a price of 3,000 Russian Roubles per one share. On 18 February 2011, OJSC "Pharmstandard-Leksredstva" closed this offer to purchase up to 1,824,750 ordinary shares of the Company in the total amount of RR 5,474,250. The Company paid consideration for these treasury shares before the date of release of these consolidated financial statements.

CLOSURE OF DISPOSABLES PRODUCTION LINE

On 18 February 2011 the management of the Group approved the plan to discontinue the operations of production line of medical disposables, including syringes, because of low profitability and decline in customer demand of these products. Impairment of assets represented equipment for production of medical disposables amounted to RR 76,002 (Note 11) and expenses on personnel reduction amounted to RR 7,411 were recognised in profit and loss (Note 26).

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Contacts

INVESTOR RELATIONS

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

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

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

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

Investor Relations department is always glad to answer your questions. Your feedback is highly appreciated.

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COVERING ANALYSTS

Pharmstandard is followed by the analysts listed below. Please note that any opinions, estimates or forecasts regarding company's performance made by these analysts are theirs alone and do not represent opinions, forecasts or predictions of Pharmstandard Group or its management. Pharmstandard does not by its reference below or distribution imply its endorsement of or concurrence with such information, conclusions or recommendations.

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ABBREVIATIONS

ARVI acute respiratory viral infection

FRP Federal Reimbursement Programme

VED Vital and essential drugs

ONLC (Provision of Essential Pharmaceuticals Programme)

GMP Good Manufacturing Practice

INN International Not patented Names

CMR «Pharmexpert»Center of Marketing Researches

Rx Prescription drugs

OTC Non prescription drugs

TPP Third parties products

P&L profit and losses

SKU Stock Keeping Unit

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